Firstsource Solutions Limited

December 18, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term / Short-term bank facilities	351.00	CARE A+; Stable / CARE A1+	Reaffirmed
Commercial paper@	50.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1. @Carved out of working capital limits.

Rationale and key rating drivers

The reaffirmation of the ratings assigned to the bank facilities/instrument of Firstsource Solutions Limited (FSL), continues to derive strength from the company's strong brand recall and established position in the business process management (BPM) industry, especially in the overseas markets, along with its well-diversified revenue profile spread across multiple verticals and geographies.

During the past five years, FSL's consolidated revenues have grown at a Compounded Annual Growth Rate (CAGR) of around 11 percent (Rupee-denominated growth), however; during FY23 (Refers to period from April 01 to March 31) revenues increased by around 2 percent on a year-on-year (Y-o-Y) basis. The slowdown in the pace of growth was largely attributed to the decline in revenues from the banking and financial services (BFS), which in turn was impacted with the slowdown in the US mortgage segment, owing to higher interest rate cycle. On the other hand, the healthcare and the Communications Media & Tech (CMT) verticals continued to record positive growth.

For the fiscal FY23, the revenues from operations have contracted by 1.1 percent on a constant currency (CC) basis. BFS (43 percent of revenue contribution) has declined by around 20 percent while Healthcare (34 percent of revenue contribution) and CMT (21 percent of revenue contribution) have each grown by 8.7 percent and 14 percent respectively (on CC basis). During the last few quarters, the company has seen good client additions in the healthcare and CMT business, including on boarding of a few big-ticket clients. This, in addition to continued business from the existing client base, may help the company to generate stable revenues.

Acquisitions done in FY22 includes ARSI and the Stonehill group. ARSI, being in collections business, has helped the company in revenue improvement, resulting in higher growth in non-mortgage business. The Stonehill Group acquisition has witnessed the impact on the mortgage business, recording net loss for the period. However, CARE Ratings Limited (CARE Ratings) foresees the degree of risk emanating from frequent acquisitions is relatively low, as the company focuses on small ticket size acquisitions as compared to its annual cash accruals.

The ratings further take into consideration the relatively less volatility in the profitability margins which have been consistently maintained in the range of 14-17% over the last few fiscals, resulting in healthy cash flow from operating activity of more than ₹. 500 crore (in absolute terms) annually.

The capital structure of the company remains robust with total outside liabilities (TOL)/total net worth (TNW) and overall gearing at 0.65x and 0.43x as on March 31, 2023, considering the lease liability component. The company avails terms loans largely for acquisition purposes, which are paid out in the next 2-3 years. In addition, the company has consistently maintained cash and liquid investments above ₹200 crore over the last three fiscals. For FY24 (P), the company has minimal debt repayments of ₹160 crore as against adjusted gross cash accruals of ₹662 crore. Maximum overall gearing for the company over the last five fiscals has been comfortable at 0.60x.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

The rating strengths are however, tempered by FSL's exposure to intense competition in the BPM industry, risk associated with high attrition rates, customer and geographical concentration risk, impact of protectionist policies by US/UK and foreign exchange fluctuation risks.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Total debt (excluding lease) by gross cash accruals below 1.0x on a sustained basis
- On a consolidated basis, improvement in profit after tax (PAT) margins above 10% along-with return on capital employed over 20% on a sustained basis.
- Current ratio greater than 1.50x on a sustained basis.

Negative factors

- Any large-sized debt-funded capex, mergers or acquisitions or unrelated diversification.
- Decline in revenues to below ₹5,500 crore, emanating from technological disruption or any non-renewal of key customer contract.
- PAT margin less than 5% on a sustained basis

Analytical approach:

Consolidated approach as the subsidiaries are into the same line of business and are operating under the common management. Details of the subsidiary and associate companies included for consolidated approach is below:

List of subsidiaries/associates	% Shareholding (As on Mar 31, 2023)
Firstsource Solutions UK Limited (FSL UK)	100.00%
Firstsource Solutions S.A. (FSL-Arg)	99.98%
Firstsource BPO Ireland Limited (FSL Ireland)	100.00%
Firstsource Dialog Solutions (Private) Limited	74.00%
Firstsource Process Management Services Limited (FPMSL)	100.00%
Firstsource Group USA, Inc. (FG US)	100.00%
Firstsource Business Process Services, LLC (FBPS)	100.00%
Firstsource Advantage LLC (FAL)	100.00%
One Advantage LLC (OAL)	100.00%
Medassist Holding LLC (MedAssist)	100.00%
Firstsource Solutions USA LLC	100.00%
Firstsource Health Plans and Healthcare Services, LLC	100.00%
Sourcepoint, Inc	100.00%
Sourcepoint Fulfillment Services, Inc.	100.00%
PatientMatters, LLC (PM)	100.00%
Medical Advocacy Services for Healthcare, Inc (MASH)	100.00%
Kramer Technologies LLC (KT)	100.00%
The StoneHill Group, Inc	100.00%
American Recovery Service Incorporated	100.00%
Firstsource Solutions México, S. de R.L. de C.V	99.00%
Firstsource Solutions Jamaica Limited	100%
Firstsource Employee Benefit Trust	100.00%
Nanobi Data and Analytics Private Limited (Nanobi)	21.79%

Outlook: Stable

Though we do not expect any drastic recovery in the mortgage segment in FY24, the business performance is expected to be stable given diversified revenue streams and additional business from the existing and new clients. The financial profile of the company remains strong as the term debt repayments can be comfortably met through internal accruals.

Detailed description of the key rating drivers:

Key strengths

Established track record with experienced management

FSL was promoted by ICICI Bank Ltd in 2001. In FY12, Spen Liq Pvt Ltd, a wholly owned subsidiary of CESC Ltd (part of the RP-Sanjiv Goenka group) acquired 56.82% stake in FSL to become the majority shareholder. Following restructuring in the RP Sanjiv Goenka group, majority ownership of 53.66% in FSL now vests with the group.

With presence in the international markets since long decades, FSL has established a strong footing in overseas markets reflected in more than 95% of the revenue from USA and UK markets. The management continues to explore options via inorganic growth with past two acquisitions done in the period September-December 2021. The new CEO (effective September 01, 2023), Ritesh Idnani has come in with around three decades of experience, including senior role at Tech Mahindra.

Steady profitability and operational performance

During FY23, the consolidated revenue from operations contracted by 1.1% YoY in FY23 and contracted by 1.4% YoY in H1FY24. Overall, BFS segment has been down 12% YoY in FY23 and down by 4.5% YoY in H1FY24. New mortgage originations have declined is USA due to higher interest rates. However, this decline in the mortgage segment has been partly offset by the growth in the collections segment. Excluding mortgage, BFS segment had organic constant currency growth of 18.3% in FY23. We expect mortgage segment to gradually improve in CY24 as the interest rate hikes seems to have peaked. Healthcare business has climbed 17% YoY (8.7% on constant currency basis) in FY23 and had degrowth of 2.8% YoY in H1FY24. This business is primarily divided into provider segment (e.g. hospitals) and payer segment (e.g. health plan providers, Medicaid). The company has seen good client additions in this segment in Q2FY24 and expects good growth in H2FY24. On the other hand, CMT business also has improved by 10.8% in FY23 (4% in UK and 56% in USA) due to rapid scaling up of the US- CMT business.

Additionally, the profit before interest, lease rentals, depreciation and tax (PBILDT) margins have consistently stayed healthy in the range 14-17% over the last five fiscals, despite turbulent times in some of the key customer segments. This has been possible due to long-term nature of contracts with clients which enables steady revenue streams.

Comfortable capital structure and debt coverage indicators

The financial risk profile of the company is comfortable aided by healthy cash accruals on the back of stable operating profitability. The company has engaged in acquisitions in the past within its domain to adapt to the rapidly evolving technologies. These acquisitions have usually been done with mix of debt and equity. Post the acquisition of ARSI and Stonehill group in FY22, the overall gearing had climbed to 0.60x as on March 31, 2022 from 0.43x as on Mar 31, 2021. Currently, the overall gearing has again come down to 0.43x as on March 31, 2023. The debt coverage indicators remain strong due to size of the acquisitions being small compared to the company’s gross cash accruals. Resultantly, interest coverage ratio stands at 7.76x for FY23 and total debt by PBILDT at 1.69x as on March 31, 2023. Also, the overall gearing excluding lease liabilities stands at 0.24x as on September 30, 2023, which is in quite comfortable range.

Diversified revenue profile and strong client base

FSL provides business process outsourcing (BPO) services mainly across three verticals: BFSI, healthcare and CMT. The verticals contributed 41%, 33% and 21% respectively to the company’s revenue during H1FY24. US healthcare and US BFS business contribute more than 60% of revenues. Rest of the revenues primarily comes from CMT and BFS business in UK. The company has more than 100 clients spanning across varied industries. Additionally, a significant portion of FSL's clients are Fortune 500 and FTSE 100 companies with strong financial profiles leading to low counterparty risk. The company's client profiles include top general-purpose credit card issuers, retail banks, motor insurers, private insurance companies, pay TV and mobile service operators, internet service providers and over 1,000 hospitals in the US.

Global delivery capabilities

FSL has presence across geographies and services its clients through its global delivery centres. As on March 31, 2023, the company along with its 21 subsidiaries has 48 global delivery centers of which 11 are in India, 24 in the USA, 10 in the UK, two in the Philippines and one in Mexico. The global delivery capability enables FSL to deliver wide range of services and gives the company proximity to its clients. Furthermore, the presence of its delivery centres across various geographies enables FSL to use locations and skills most appropriate for delivering BPO services to clients located across various geographies.

Key weaknesses

Customer concentration risk

Although improved, FSL derived 15% of its total revenue for FY23 from its top client. However, the average tenure of the contract with the top client is long term with more than 10 years. The company's top five clients contributed 37% of its revenue for FY23 thus exposing it to customer concentration risk. Non-renewal of key customer contracts if any were to occur would impact the revenues of the company significantly. However, comfort is drawn from long standing association of FSL with these clients and ability to get repeat business over the years from these clients.

Increasing industry competition

With the rapid evolution of the Indian IT-enabled services (ITeS) sector, competition is intense as companies compete for a share of the outsourcing pie. The competitive risk comes from BPOs (like Hinduja Global Solutions, Genpact), BPM divisions of global IT companies (TCS, Accenture, Infosys), Local/onshore BPM providers in the US and Europe and in-house captives of potential clients. Also, there is shared services (where-in the client themselves flip their backend solutions to offshore location). This reduces the potential client base for the BPO companies.

FSL also faces competition from other low-cost outsourcing geographies like China, Philippines, Mexico, and Brazil. However, the company has an established brand name in the industry and has long relationships with its clientele which help ity to face the competition. Pressure from clients to cut costs through automation hurts revenue and the entry of large IT players into BPO has further intensified competition as more clients look for integrated IT-BPO deals. However, the company has an established brand name in the industry and has long relationships with its clientele which help the company to navigate the competition. Furthermore, the inherently high attrition rate in the BPO business poses few challenges on operational productivity. However, the attrition rate has improved for onshore business from 52% in Q2FY23 to 36% in Q2FY24.

Foreign exchange fluctuation risk

FSL is exposed to foreign exchange fluctuation risk on cross-currency exposure (revenues and cost in different currencies) wherein the company caters to international customers from the delivery centres in India (primarily). The company has a policy to hedge its exposure on a 12-month rolling basis through forward cover contracts and options. However, the company is still exposed to foreign exchange fluctuation risk for any unhedged exposure.

Impact of protectionist policies in developed countries

The operations remain exposed to government policies and preferences with respect to factors such as local supply, duties, protectionism stance adopted by foreign countries. To partly mitigate against this risk, the company has developed significant local presence in US and UK. As on March 31, 2023, 41% of the employees are in US and UK locations, where the revenue for the company is mainly derived.

Liquidity: Adequate

Liquidity profile remains adequate with cash and liquid investments of ₹220.44 crore as on September 30, 2023. The current ratio for the company is 0.9x as on March 31, 2023 and has consistently stayed in this range. This is due to current lease obligations and usage of unsecured working capital borrowings (line of credit from banks). On the other hand, FSL has modest long-term debt repayments for FY24 which can be comfortably met through its internal accruals.

Assumptions/Covenants Not applicable

Environment, social, and governance (ESG) risks

	Risk factors
Environmental	**GHG emissions: Low** Total Scope 1 & Scope 2 GHG (greenhouse gas) emissions per rupee of turnover has been reduced by ~9% (as compared to FY22) due to increased use of renewable energy mix. **Energy consumption: Increased** The increased energy consumption in FY23 as compared to FY22 may be the result of WFH to work from office transition. However, around 20% of the energy consumption has been from non-renewable sources.
Social	**Gender diversity: Adequate** Around 35% women in workforce (employees and workers), 10% representation in board, 33% representation in key management personnel. **LTIFR: Moderate** Lost time injury frequency rate (per 1 million person per hour worked) has been 0.22 in FY23 for non-permanent employees due to five work-related injuries recorded. **Attrition rate: High** Attrition rate has been inherently high in the industry but has come down in the onshore segment from 52% in Q2FY23 to 36% in Q2FY24.
Governance	**Board independence: Equally Balanced** 50% of the majority comprises independent directors. **Data governance risk: Moderate** The industry is inherently exposed to risks related to cybersecurity, information security and data privacy. Adequate data-governance practices with various operational centres being certified with ISO 27001 (which is international standard for Information security management system).

Applicable criteria

Policy on default recognition
Consolidation
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Service Sector Companies
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Information technology	Information technology	IT - Services	IT-enabled services

FSL is a leading global provider of BPM services through end-to-end customer life cycle management across different industry verticals i.e. telecom & media, BFSI and healthcare. The company, on a consolidated basis had 48 global delivery centers as on March 31, 2023 located in India, US, UK, Mexico and Philippines.
FSL was promoted as ICICI Infotech Upstream Limited on December 6, 2001 by ICICI Bank Limited. In 2012-13, the RP-Sanjiv Goenka Group acquired 56.82% shares of FSL through, wholly-owned subsidiary of CESC Limited (rated CARE AA; Negative/ CARE A1+), Spen Liq Private Limited (SLPL). Following restructuring in the RP Sanjiv Goenka group, majority ownership of 53.66% in FSL now vests with the group. The RP-Sanjiv Goenka group has interests across diverse business sectors such as power & natural resources, infrastructure, carbon black, retail, education and media & entertainment.

Brief Financials (₹ crore)	FY2022 (A)	FY2023 (A)	H1FY2024 (UA)
Total operating income	5921.15	6022.32	3069.18
PBILDT	979.70	855.07	487.66
PAT	536.53	513.71	252.49
Overall gearing (times)	0.60	0.43	0.44
Interest coverage (times)	11.33	7.76	9.48

A: Audited UA: Unaudited; Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Commercial paper-Commercial paper (Standalone)*		Not yet placed	Not yet placed	7 days to 1 year	50.00	CARE A1+
Fund-based/Non-fund-based-LT/ST		-	-	-	351.00	CARE A+; Stable / CARE A1+

*Carved out of working capital limits.

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Commercial paper-Commercial paper (Standalone)	ST	50.00	CARE A1+	-	1)CARE A1+ (19-Dec-22)	1)CARE A1+ (20-Dec-21)	1)CARE A1+ (21-Dec-20) 2)CARE A1+ (06-Apr-20)
2	Fund-based/Non-fund-based-LT/ST	LT/ST*	351.00	CARE A+; Stable / CARE A1+	-	1)CARE A+; Stable / CARE A1+ (19-Dec-22)	1)CARE A+; Stable / CARE A1+ (20-Dec-21)	1)CARE A+; Stable / CARE A1+ (21-Dec-20) 2)CARE A+; Stable / CARE A1+ (24-Apr-20) 3)CARE A+; Stable / CARE A1+ (06-Apr-20)
3	Non-fund-based - ST-BG/LC	ST	-	-	-	1)Withdrawn (19-Dec-22)	1)CARE A1+ (20-Dec-21)	1)CARE A1+ (21-Dec-20) 2)CARE A1+ (24-Apr-20) 3)CARE A1+ (06-Apr-20)

*Long term/Short term.

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities- Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Commercial paper-Commercial paper (Standalone)	Simple
2	Fund-based/Non-fund-based-LT/ST	Simple

Annexure-5: Lender details

To view the lender-wise details of bank facilities please click here

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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