

CMP: INR 164

Rating: Accumulate

Target Price: INR 188

Stock Info

BSE	532809
NSE	FSL
Bloomberg	FSOL:IN
Reuters	FISO.BO
Sector	IT Enabled Services
Face Value (INR)	10
Equity Capital (INR Cr)	697
Mkt Cap (INR Cr)	113,748
52w H/L (INR)	176/96
Avg Yearly Vol (in 000')	145

Shareholding Pattern %

(As on Sept, 2023)

Promoters	53.66
Public & Others	44.11

Stock Performance (%)

	1m	3m	12m
FSL	-2.36	11.3	48.01
Nifty	-0.38	1.2	6.91

FSL Vs Nifty



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Firstsource Solutions Ltd (FSL) in Q2FY24, In-line with estimates. Revenues at INR 15,400 Mn (US\$ 186 mn), up 3.5% YoY (in-line with our estimate INR 15,370 Mn) EBIT at INR 1,634 mn or 10.6% of revenues, up 30.3% YoY (in-line with our estimate INR 1630 Mn). PAT at INR 1,265 mn or 8.2% of revenues, down 2.2% YoY. The company is anticipating a constant currency revenue growth in the range of 0-2% for FY24, along with an EBIT margin between 11% and 11.5%. It expects that the ramp-up of certain deals will contribute to robust revenue growth in the second half of FY24

Sustained Growth in Collections Business Throughout Q2: In Q2, collections business saw steady growth fueled by new logo acquisitions and expansion in existing accounts. Company emphasis remains on expanding the digital collections platform and diversifying into non-financial sectors. With significant client additions in financial services, a robust deal pipeline, enhanced execution capabilities in Mexico, and entry into a major Nordic bank for U.K. collections, the focus on customer experience remains paramount.

Strong Growth Prospects in Healthcare: Health plans navigate a stable macroeconomic environment, leveraging cost optimization and acquisitions for membership expansion. The strategic emphasis on disruptive solutions and partnerships strengthens competitiveness throughout the value chain. Q2 success in vendor consolidations and key account strategy positions the for robust H2FY24 revenue growth, complemented by expanding Digital Process Automation offerings and strong prospects in the payer segment

Strategic Unveiling: A Seven-Pronged Approach with a Focus on Near-Term Challenges: The recently revealed strategy, encompassing organizational simplification, cross-selling and up-selling, capability expansion, brand enhancement, and more, aims to propel the company toward top-quartile growth and improved profitability in the medium term.

Valuations

FY24 revenue guidance adjusted in light of macro uncertainty from 2%-5% CC Growth to 0-2%, operating margins revised to 11-11.5% (from 11%-12%) a noteworthy shift. Despite this, the company anticipates strong H2FY24 revenue growth, fueled by the ramp-up of key Deals. Robust business pipeline identified in large banks in CX Landscape and emerging segments. Committed to Cost Optimization, Acquisitions, and Strategic Partnerships for Sustained Expansion. **We value FSL at a PE of 16x to its FY26e EPS of INR 9.9, which yields a target price of INR 188 per share (earlier target price; of INR 125 per share). We upgrade our rating to Accumulate from Hold earlier**

Exhibit 1 Financial Performance

Particular	FY23	FY24E	FY25E	FY26E
Sales	6,022	6,228	6,729	7,317
EBITDA	827	950	1,044	1,145
EBITDA Margin	13.7%	15.3%	15.5%	15.7%
Reported PAT	514	534	615	688
PE (x)	22.4	21.3	18.5	16.6
EPS	7.3	7.7	8.8	9.9

Source: Arihant Research, Company Filings

Exhibit 2: Quarterly Performance (Consolidated)

Consolidated (in INR Cr)	Q2FY24	Q1FY24	Q2FY23	Q-o-Q	Y-o-Y
Revenue (Mn USD)	186	186	187	0.0%	-0.5%
Net Revenue	1,540	1,529	1,488	0.7%	3.5%
Employee cost	940	924	953	1.8%	-1.3%
Other Expenses	371	365	344	1.6%	8.0%
EBITDA	229	240	192	-4.7%	19.3%
EBITDA margin %	14.9%	15.7%	12.9%	-85bps	197bps
Depreciation	65	61	66	6.7%	-1.4%
EBIT	163.4	178.9	125	-8.7%	30.3%
EBIT margin %	10.6%	11.7%	8.4%	-109bps	218bps
Other Income	17	2	49	878.9%	-65.7%
Finance costs	26	25	20	2.7%	31.1%
PBT	154.3	155.3	154.92	-0.6%	-0.4%
Exceptional item	-	-	-		
PBT and share net profit	154.303	155	155	-0.6%	-0.4%
Tax Expense	28	29	26	-5.2%	8.9%
Effective tax rate %	18.0%	18.9%	16.5%	-86bps	154bps
PAT	126.5	126.0	129.4	0.4%	-2.2%
Non-controlling interest	-	-0	-0	-100.0%	-100.0%
Consolidated PAT	126.509	125.982	129.40	0.4%	-2.2%
Reported PAT	126.51	125.98	129.40	0.4%	-2.2%
PAT margin %	8.2%	8.2%	8.7%	-2bps	-48bps
EPS (INR)	1.85	1.85	1.90	0.0%	-2.6%

Consolidated (in INR Cr)	Q2FY24	Q1FY24	Q2FY23	Q-o-Q	Y-o-Y
Banking and Financial Services	629	623	639	-0.7%	-7.3%
Healthcare	505	498	508	-3.8%	6.7%
Communication, Media and Technology	327	332	296	-4.2%	13.6%
Diverse Industries	81	73	30	13.4%	256.6%

Source: Arihant Research, Company Filings

Concall Highlights

The company is anticipating a constant currency revenue growth in the range of 0-2% for FY24, along with an EBIT margin between 11% and 11.5%. It expects that the ramp-up of certain deals will contribute to robust revenue growth in the H2FY24.

- The company has a strong physical presence in the U.S. and the U.K., and it has expanded its services with a top-5 U.S. healthcare insurance provider, offering digital intake and provider data management services.
- The company is strategically organizing its service portfolio into five key areas, encompassing both established services like collections and customer experience, as well as emerging and high-growth segments like consulting, trust and safety, and data and analytics, while also focusing on cross-selling and upselling to existing clients and anticipating modest growth in H2 compared to H1.
- Margin:** The company remains committed to seeking cost optimization and potential acquisitions to fuel member expansion, actively exploring partnership opportunities.
- Attrition:** TTM employee attrition at 44.8% for onshore and 36.1% for offshore.
- QoQ net headcount addition of 1,569; India employee base higher by 1,980; RoW lower by 411.
- Collections business** In Q2, the company maintained a consistent growth trajectory, attributed to acquiring new clients and expanding existing accounts. Their strategic emphasis is on extending their presence through the digital collections platform and venturing into diverse industry verticals beyond financial services.
- Clients:** The company successfully onboarded five new clients in the financial services sector and has a promising deal pipeline. They also increased their operational capabilities in Mexico, now servicing two collections clients from that region. Additionally, they initiated a partnership with one of the largest Nordic banks to support their collections business in the U.K. and enhance customer experience.
- Order pipeline:** The company is seeing a strong business pipeline across large banks in the CX landscape and in the emerging segments.
- BFS vertical:** The company has seen success with auto finance, continue to split capabilities in risk and compliance, and they informed a bunch of partnerships in this space, either on the gen AI side or with leaders in areas like credit data services to power digital verification.
- Healthcare:** Two key wins in Q2, gradual volume increase due to system transition, hospitals preparing for funding normalization post-PHE through cost restructuring.
- Gen AI:** In Q2, they launched First Sense AI, proprietary framework to accelerate clients AI deployment.

Operating Metrics	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Revenue by Vertical										
Banking & Financial Services	51.70%	48.90%	48.30%	49.00%	46.30%	43.40%	41.80%	40.30%	40.80%	40.80%
Healthcare	26.70%	29.60%	30.30%	30.30%	32.10%	34.50%	34.20%	33.20%	32.60%	32.70%
Communications Media & Tech	19.60%	19.50%	19.60%	19.00%	20.20%	20.20%	21.60%	22.30%	21.80%	21.20%
Diverse Industries	2.00%	2.00%	1.80%	1.70%	1.40%	1.90%	2.40%	4.20%	4.80%	5.30%
Revenue by Service Lines										
Digitally Empowered Contact Centre	46.30%	46.80%	45.90%	44.40%	46.60%	47.70%	50.40%	52.60%	51.80%	52.90%
Intelligent Back Office	47.60%	45.60%	44.00%	36.50%	32.70%	30.90%	29.20%	27.00%	27.00%	21.9%
Platforms, Automation & Analytics	6.10%	7.60%	10.10%	19.10%	20.70%	21.40%	20.40%	20.40%	21.20%	21.20%
Revenue by Geography										
US	67.60%	68.40%	69.80%	70.70%	68.40%	67.20%	64.90%	63.30%	63.50%	65.10%
UK	31.10%	30.10%	28.50%	27.50%	30.10%	31.30%	34.10%	36.30%	36.40%	34.80%
ROW	1.30%	1.50%	1.70%	1.80%	1.50%	1.50%	1.00%	0.40%	0.10%	0.10%
Revenue by Delivery										
Offshore	29.30%	31.00%	30.80%	27.00%	27.40%	25.90%	25.10%	24.60%	25.60%	26.70%
Onshore	70.70%	69.00%	69.20%	73.00%	72.60%	74.10%	74.90%	75.40%	74.40%	73.30%
Top Clients Revenue										
Top client %	16.30%	15.80%	15.20%	14.80%	15.20%	14.90%	15.80%	15.40%	14.60%	12.70%
Top 5 client %	42.00%	41.20%	37.60%	35.90%	36.40%	36.60%	38.50%	37.40%	37.20%	35.00%
Other Metrics										
Total employees (end of period)	27916	27835	27398	26557	25234	23932	23627	23018	22384	23953
Employees in India	16677	16976	16826	16045	14769	13431	12489	12395	12457	14437
Employees outside India	11239	10859	10572	10512	10465	10501	11138	10623	9927	9516
Net Addition	-88	-81	-437	-841	-1323	-1302	-305	-609	-634	1569
Offshore Attrition (180 days+)	29.20%	36.20%	45.20%	45.90%	43.80%	45.70%	44.40%	44.90%	39.10%	36.10%
Onshore Attrition (180 days+)	54.80%	68.80%	59.50%	50.20%	56.90%	52.00%	47.20%	42.30%	45.30%	44.80%

Source: Arianth Research, Company Filings

Exhibit 3: Revenue Split by Verticals-Increase mix in Diverse industries

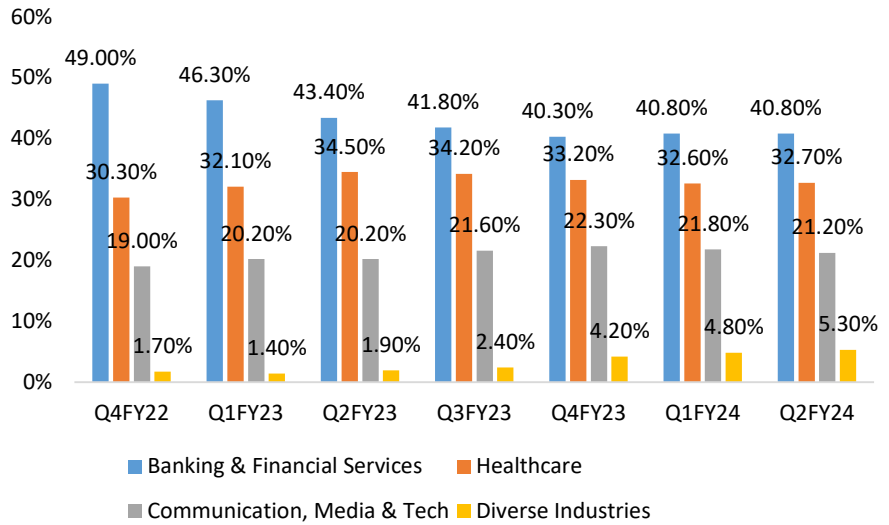


Exhibit 4: Revenue Split by Service line trend

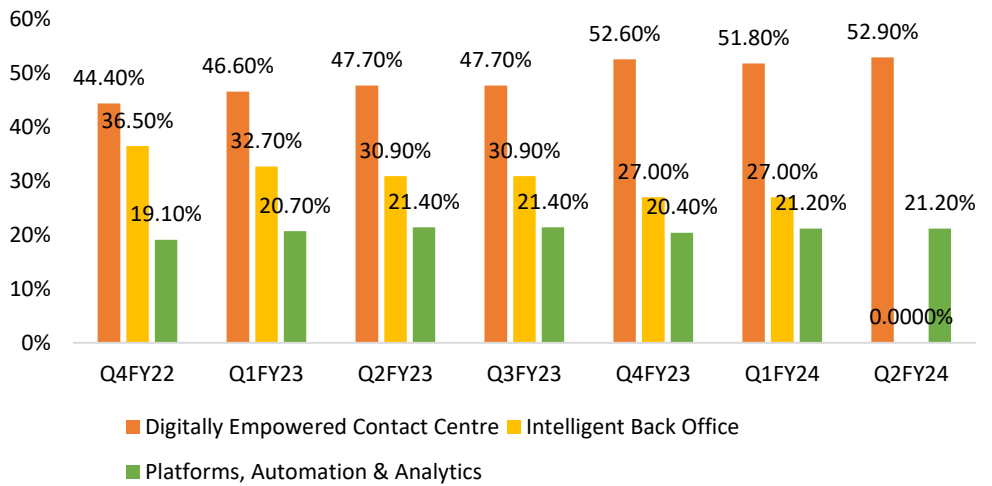
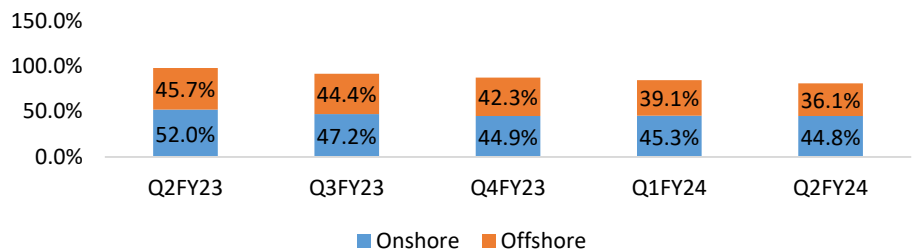


Exhibit 5: The company is adding new clients and by growing existing signature accounts

Attrition



Source: Arianth Research, Company Filings

Key Financials

Income Statement (INR Cr)					Balance Sheet (INR Cr)				
Year End-March	FY23	FY24E	FY25E	FY26E	Year End-March	FY23	FY24E	FY25E	FY26E
Revenue USD term	751	757.7	818.6	890.1	Sources of Funds				
<i>Change (%)</i>	281.2%	0.9%	8.1%	8.7%	Share Capital	697	697	697	697
Revenues	6,022	6,228	6,729	7,317	Reserves & Surplus	2,670	2,960	3,331	3,775
<i>Change (%)</i>	1.7%	3.4%	8.1%	8.7%	Non controlling interest	0	0	0	0
Employee costs	3,867	3,986	4,307	4,672	Total Equity	3,367	3,657	4,028	4,472
Other expenses	1,328	1,292	1,378	1,500	Loan Funds	827	721	671	620
Total Expenses	5,196	5,278	5,685	6,172	Deferred Tax Liability (Net)	120	120	120	120
EBITDA	827	950	1,044	1,145	Total Liability	5,664	5,809	6,167	6,601
EBITDA Margin	13.72%	15.25%	15.52%	15.65%	Application of Funds				
Depreciation	263	266	239	251	Gross Block	1,156	1,221	1,286	1,353
EBIT	563	684	805	894	Less: Depreciation	880	1,027	1,194	1,397
EBIT Margin	9.35%	10.98%	11.97%	12.21%	Net Block	276	194	92	(44)
Interest	79	65	60	62	CWIP	3	3	3	3
Other Income	131	33	5	8	Financial Assets	1,341	1,715	2,133	2,637
PBT	615	651	750	839	Investments	60	60	60	60
Exceptional Items	-	-	-	-	Sundry debtors	1,038	938	1,014	1,103
PBT after exceptional Items	615	651	750	839	Cash and bank	156	630	973	1,388
Tax	102	117	135	151	Other Current Assets	151	151	151	151
<i>Rate (%)</i>	18.0%	18.0%	18.0%	18.0%	Total Current assets	1,408	1,783	2,201	2,705
PAT	514	534	615	688	Total Current liabilities	872	851	888	928
Margin	9%	9%	9%	9%	Total Non-Current assets	4,256	4,026	3,966	3,896
Consolidated PAT	514	534	615	688	Capital Employed	5,664	5,809	6,167	6,601
<i>Change (%)</i>	-4.3%	4.0%	15.1%	12.0%					

Cash Flow Statement (INR Cr)				
Year End-March	FY23	FY24E	FY25E	FY26E
PBT	615	651	750	839
Cash From Operating Activities	861	1,039	989	1,082
Tax	66	117	135	151
Net Cash From Operations	795	921	854	931
Capex	(54)	(65)	(66)	(67)
Cash From Investing	16	(165)	(166)	(168)
Borrowings	(235)	(50)	(50)	(51)
Finance cost paid	(79)	(65)	(60)	(62)
Cash From Financing	(743)	(279)	(346)	(349)
Net Increase/ Decrease in Cash	68	478	342	415
Cash at the beginning of the year	83	152	630	973
Cash at the end of the year	152	630	973	1,388

Key Ratios				
Year End-March	FY23	FY24E	FY25E	FY26E
Per share (INR)				
EPS	7.3	7.7	8.8	9.9
BVPS	48	52	58	64
Valuation (x)				
P/E	22.4	21.3	18.5	16.6
P/BV	3.4	3.1	2.8	2.5
EV/EBITDA	14.6	12.1	10.6	9.3
Return ratio (%)				
EBITDA Margin	13.7%	15.3%	15.5%	15.7%
EBIT Margin	9.4%	11.0%	12.0%	12.2%
PAT Margin	8.5%	8.6%	9.1%	9.4%
ROE	15.3%	14.6%	15.3%	15.4%
ROCE	9.9%	11.8%	13.1%	13.5%
Leverage Ratio (%)				
Total D/E	0.2	0.2	0.2	0.1
Turnover Ratios				
Asset Turnover (x)	4.3	3.5	3.1	2.7
Receivable Days	58	55	55	55
Payable days	11	11	11	11

Source: Arianth Research, Company Filings

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Stock Rating Scale	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	-5% to -12%
SELL	<-12%

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