

CMP: INR 208

Rating: Accumulate

Target Price: INR 238

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)	14,476
52w H/L (INR)	229/112
Avg Yearly Vol (in 000')	208

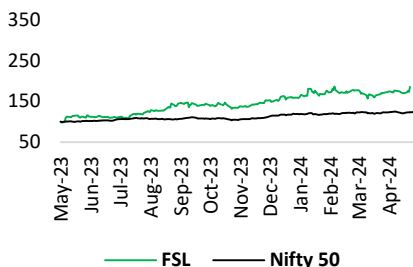
Shareholding Pattern %

(As on March, 2024)

Promoters	53.66
Public & Others	44.11

Stock Performance (%)	1m	3m	12m
FSL	2.9	4.2	76.3
Nifty	0.18	2.85	24.2

FSL Vs Nifty



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Firstsource Solutions Ltd (FSOL) in Q4FY24, above with estimates. Company has approved the acquisition of 100% ownership in Quintessence Business Solutions & Services (QBSS) for a consideration not exceeding INR 328 Cr transaction to be completed by 5 May 2024. The company reported revenue at INR 1670 Cr (US\$ 201 mn against an estimate of US \$ 194 mn), YoY growth of 4.7% QoQ/5.8% YoY% (Above with the estimate of INR 1,620 Cr). Segments: Banking and Financial Services was flat YoY (+2.1%QoQ). While growth seen in diverse Industries was up (59.9%YoY/13.8% QoQ) followed by Communication, Media, and Technology (up 13.3%YoY/9.7% QoQ), Healthcare (6.3% YoY/2.7%QoQ). EBIT at INR 183 Cr and Margin at 11% our estimate of 10.7% led by cost management and strong pipeline. PAT at INR 133.5 Cr against our estimate of INR 158 Cr. EPS of INR 1.9 vs of INR 1.88 in Q3FY24. Net increase by 1993 employee net headcount at 27,940 employees. Attrition: Offshore attrition declined by 300 bps QoQ to 33.80% & onshore attrition declined by 80 bps QoQ to 42.5%.

Integration of QBSS with FSOL aims to leverage synergies.: FSOL has acquired Quintessence Business Solutions (QBSS), specializing in healthcare RCM, for \$39.2 mn, with an upfront payment of \$25.9 million, deferred compensation of \$5.6 million, and an earn-out base payment of \$7.8 million, expected to finalize by May 15th, 2024. This aligns with FSOL's strategy to broaden its service portfolio and capture a larger MS in the expanding revenue cycle management sector. Moreover, FSOL anticipates capitalizing on opportunities arising from the consolidation of the CX market, targeting both major players facing concentration risks and smaller competitors encountering challenges in the competitive landscape. The transaction is valued at 2.6x P/S. Revenues for QBSS in FY24 stood at \$14.8mn, growing at a CAGR of 24% over FY22-FY24. This acquisition will be both margin and EPS accretive for FSOL

Strong collections Business, company focus on expanding geography: Positive momentum observed in collection services with card issuers, driven by record-high credit card spending and delinquencies, fostering growth in client acquisition. Renewals and transformational deals with longstanding clients in retail in US& UK and commercial banking reinforce the company's expansion strategy.

Valuations

For FY25, the company has Revenue growth of 10-13% expected for FY25, aiming for a USD 1 Bn exit run rate by FY '26 with EBIT margin expansion of 50-75 basis points over 3-4 years. The company plans strategic investments while maintaining an EBIT margin guidance of 11-12% for FY25. We anticipate that robust execution and securing deals with both current and new clients will drive growth momentum, while closely monitoring the Mortgage and Provider sectors for potential acceleration, which is crucial for sustained robust growth. We expect FSL revenue, EBITDA, and PAT to grow at a CAGR of ~11%, ~14%, and 17%, respectively, over FY24-27E. **We value FSL at a PE of 20x to its FY27e EPS of INR 11.9, which yields a target price of INR 238 per share (earlier target price; of INR 254 per share). We downgrade our rating to Accumulate from Buy on the stock.**

Exhibit 1 Financial Performance

Particular	FY23	FY24	FY25E	FY26E	FY27E
Sales	6,022	6,336	7,272	8,022	8,784
EBITDA	827	956	1,121	1,268	1,405
EBIDTA Margin	13.7%	15.1%	15.4%	15.8%	16.00%
Reported PAT	514	515	648	739	828
PE (x)	28.4	28.3	22.4	19.6	17.5
EPS	7.3	7.3	9.3	10.6	11.9

Source: Arihant Research, Company Filings

Exhibit 2: Quarterly Performance (Consolidated)

Consolidated (in INR Cr)	Q4FY24	Q3FY24	Q4FY23	Q-o-Q	Y-o-Y
Revenue (Mn USD)	201	192	190	4.7%	5.8%
Net Revenue	1,670	1,597	1,557	4.6%	7.3%
Employee cost	1,056	989	969	6.7%	9.0%
Other Expenses	364	370	344	-1.6%	6.0%
EBITDA	250	237	244	5.6%	2.5%
EBITDA margin %	15.0%	14.9%	15.7%	13bps	-70bps
Depreciation	67	66	64	1.6%	4.8%
EBIT	183.0	170.9	179.9	7.1%	1.7%
EBIT margin %	11.0%	10.7%	11.6%	25bps	-60bps
Other Income	3	15	13	-81.7%	-77.8%
Finance costs	27	25	21	4.3%	28.3%
PBT	159.3	160.8	171.9	-0.9%	-7.3%
Exceptional item	-	-	-		
PBT and share net profit	159.290	160.790	171.87	-0.9%	-7.3%
Tax Expense	26	32	31	-19.6%	-15.6%
Effective tax rate %	16.2%	19.9%	17.8%	-375bps	-160bps
PAT	133.5	128.7	141.30	3.7%	-5.5%
Non-controlling intrest	-	-0	-0		
Consolidated PAT	133.502	128.629	141.304	3.8%	-5.5%
Reported PAT	133.50	128.63	141.30	3.8%	-5.5%
PAT margin %	8.0%	8.1%	9.1%	-6bps	-108bps
EPS (INR)	1.94	1.88	2.1	3.2%	-6.3%

Consolidated (in INR Cr)	Q4FY24	Q3FY24	Q4FY23	Q-o-Q	Y-o-Y
Banking and Financial Services	623	610	628	2.1%	-0.7%
Healthcare	550	535	517	2.7%	6.3%
Communication, Media and Technology	393	358	347	9.7%	13.3%
Diverse Industries	103	91	65	13.8%	59.9%

Source: Arian Research, Company Filings

Concall Highlights**Banking and Financial Services Vertical:**

- In Q4FY24, BFS vertical experienced a 1.7% QoQ growth in constant currency terms. However, this growth was down 3.3% YoY, primarily due to the base effect in the mortgage portfolio.
- The company is investing in strengthening its sales and solutions teams in this vertical to expand its footprint in existing clients and adjacent segments.
- The technology-led proposition is resonating well with mortgage customers exploring non-linear execution models to prepare for potential cyclicality.
- The company saw increased volumes in collections services for credit card issuers and added 6 new logos in the BFS vertical during Q4FY24.

Healthcare Vertical:

- The healthcare vertical grew 5% YoY and 3% QoQ in constant currency terms in Q4FY24.
- Two large deals from existing customers in Q3FY24 ramped up well in Q4FY24, and 2 new logos were added in the vertical.
- The US healthcare market is in a transition phase, driving up costs and affecting revenue for providers, creating opportunities for revenue cycle management solutions.
- The acquisition of QBSS expands the company's scale in the mid and back-office revenue cycle management market, which is growing at a double-digit CAGR.
- The combination with QBSS allows the company to offer technology-led, end-to-end revenue cycle management services and disrupt traditional players.

Communications, Media, and Technology Vertical:

- The CMT vertical grew 9% YoY and 8% QoQ in constant currency terms in Q4FY24.
- Growth was strong outside the top client as well, across telecom and digital media, edtech, and consumer tech sub-segments.
- The engagement with ETS in the edtech segment is scaling well, and the company is actively engaging with multiple providers globally.
- In consumer tech, the company is expanding its footprint among market-leading logos with a non-traditional service proposition.

Diversified Vertical (Energy and Utilities):

- The diversified vertical, comprising energy and utilities, grew nearly 50% YoY and 7% QoQ in constant currency terms in Q4FY24.
- The company continues to see strong demand in the utilities and energy market and is making fresh inroads with existing clients in this vertical.

Deal Wins:

- The company added 41 new clients in FY24, including 9 in Q4FY24.
- Notable deal wins in Q4FY24 included a large cooperative financial institution in the UK, a major player in the US healthcare delivery system, and an existing retail bank client for customer support and back-office services.

Operational Updates:

- The company added 1,993 new employees in Q4FY24, bringing the total count to 27,940 as of 31st March 2024.
- Trailing 12-month attrition rates stood at 30.8% offshore and 42.5% onsite in Q4FY24, trending downwards due to employee value-focused initiatives
- Initiatives were taken to intensify the First Source brand, including a new brand positioning and increased engagement with industry analysts and advisors.

Geographic Performance:

- Growth was well-distributed across the US and Europe, with both geographies growing at 4% QoQ in constant currency terms in Q4FY24.
- The company expects broad-based growth across both geographies in the coming quarters, given strong deal pipelines.
- Efforts are underway to strengthen sales teams in the US and Europe, focusing on client acquisition and expanding wallet share.
- In the UK, the company is targeting the public services sector and making selective moves in continental Europe to support European operations of large UK clients.

Automation and Efficiency Initiatives:

- Technology, AI, and automation are being actively explored across the life cycle of an engagement to drive further efficiency.
- Optimization of sourcing and staffing strategies, right-shoring of resources across operations and support functions, and increased use of technology, AI, and automation are underway to drive efficiency and margin expansion.
- Centralization, automation, and offshoring of roles in support functions are being explored as additional levers for margin expansion.

Operating Metrics	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24
Revenue by Vertical								
Banking & Financial Services	46.30%	43.40%	41.80%	40.30%	40.80%	40.80%	38.30%	37.30%
Healthcare	32.10%	34.50%	34.20%	33.20%	32.60%	32.70%	33.50%	32.90%
Communications Media & Tech	20.20%	20.20%	21.60%	22.30%	21.80%	21.20%	22.50%	23.60%
Diverse Industries	1.40%	1.90%	2.40%	4.20%	4.80%	5.30%	5.70%	6.20%
Revenue by Service Lines								
Digitally Empowered Contact Centre	46.60%	47.70%	50.40%	52.60%	51.80%	52.90%	53.50%	54.90%
Intelligent Back Office	32.70%	30.90%	29.20%	27.00%	27.00%	21.9%	25.80%	25.80%
Platforms, Automation & Analytics	20.70%	21.40%	20.40%	20.40%	21.20%	21.20%	20.70%	19.30%
Revenue by Geography								
US	68.40%	67.20%	64.90%	63.30%	63.50%	65.10%	65.40%	65.00%
UK	30.10%	31.30%	34.10%	36.30%	36.40%	34.80%	34.50%	34.90%
ROW	1.50%	1.50%	1.00%	0.40%	0.10%	0.10%	0.10%	0.10%
Revenue by Delivery								
Offshore	27.40%	25.90%	25.10%	24.60%	25.60%	26.70%	30.30%	31.40%
Onshore	72.60%	74.10%	74.90%	75.40%	74.40%	73.30%	69.70%	68.60%
Top Clients Revenue								
Top client %	15.20%	14.90%	15.80%	15.40%	14.60%	12.70%	13.70%	14.90%
Top 5 client %	36.40%	36.60%	38.50%	37.40%	37.20%	35.00%	35.80%	36.70%
Other Metrics								
Total employees (end of period)	25234	23932	23627	23018	22384	23953	25947	27940
Employees in India	14769	13431	12489	12395	12457	14437	16269	17987
Employees outside India	10465	10501	11138	10623	9927	9516	9678	9953
Net Addition	-1323	-1302	-305	-609	-634	1569	1994	1993
Offshore Attrition (180 days+)	43.80%	45.70%	44.40%	44.90%	39.10%	36.10%	33.80%	30.80%
Onshore Attrition (180 days+)	56.90%	52.00%	47.20%	42.30%	45.30%	44.80%	43.30%	42.50%

Source: Arianth Research, Company Filings

Key Financials

Considering revenue guidance and the addition of QBSS acquisition growth, we have adjusted our revenue growth estimates upwards by 2%-4% respectively. With an optimistic view on cost optimization and improved margin commentary, our OPM estimates have been revised upwards by 50bps-52bps.

Income Statement (INR Cr)					
Year End-March	FY23	FY24	FY25E	FY26E	FY27E
Revenue USD term	751	765.0	865.7	955.0	1045.7
Change (%)	281.2%	1.9%	13.2%	10.3%	9.5%
Revenues	6,022	6,336	7,272	8,022	8,784
Change (%)	1.7%	5.2%	14.8%	10.3%	9.5%
Employee costs	3,867	3,909	4,661	5,110	5,578
Other expenses	1,328	1,470	1,489	1,645	1,801
Total Expenses	5,196	5,380	6,151	6,755	7,378
EBITDA	827	956	1,121	1,268	1,405
EBIDTA Margin	13.72%	15.09%	15.42%	15.80%	16.00%
Depreciation	263	260	239	286	336
EBIT	563	696	882	981	1069
EBIT Margin	9.35%	10.99%	12.13%	12.23%	12.17%
Interest	79	103	105	102	101
Other Income	131	37	12	22	42
PBT	615	630	790	901	1,010
Exceptional Items	-	-	-	-	-
PBT after exceptional Items	615	630	790	901	1,010
Tax	102	115	142	162	182
Rate (%)	16.5%	18.3%	18.0%	18.0%	18.0%
PAT	514	515	648	739	828
Margin	9%	8%	9%	9%	9%
Consolidated PAT	514	515	648	739	828
Change (%)	-4.3%	0.2%	25.8%	14.1%	12.1%

Cash Flow Statement (INR Cr)					
Year End-March	FY23	FY24	FY25E	FY26E	FY27E
PBT	615	630	790	901	1,010
Cash From Operating Activities	861	717	1,133	1,289	1,447
Tax	66	72	142	162	182
Net Cash From Operations	795	645	991	1,127	1,265
Capex	-54	-85	-66	-300	-300
Cash From Investing	16	-58	-166	-400	-400
Borrowings	-235	-29	-20	-20	-10
Finance cost paid	-79	-101	-105	-102	-101
Cash From Financing	-743	-564	73	-358	-346
Net Increase/ Decrease in Cash	68	23	899	369	520
Cash at the beginning of the year	83	152	175	1,074	1,444
Cash at the end of the year	152	175	1,074	1,444	1,964

Balance Sheet (INR Cr)					
Year End-March	FY23	FY24	FY25E	FY26E	FY27E
Sources of Funds					
Share Capital	697	697	697	697	697
Reserves & Surplus	2,670	3,003	3,407	3,902	4,486
Non controlling interest	0	0	0	0	0
Total Equity	3,367	3,701	4,104	4,599	5,183
Loan Funds	827	812	873	853	843
Deferred Tax Liability (Net)	120	147	147	147	147
Total Liability	5,664	6,083	6,549	7,046	7,643
Application of Funds					
Gross Block	1,156	1,221	1,286	1,586	1,886
Less: Depreciation	880	1,027	1,194	1,432	1,734
Net Block	276	194	92	154	152
CWIP	3	17	17	17	17
Financial Assets	1,341	1,488	2,374	2,744	3,264
Investments	60	30	30	30	30
Sundry debtors	1,038	1,161	1,161	1,161	1,161
Cash and bank	156	188	1,074	1,444	1,964
Other Current Assets	151	149	149	149	149
Total Current assets	1,408	1,537	2,423	2,793	3,313
Total Current liabilities	872	833	835	857	881
Total Non-Current assets	4,256	4,546	4,126	4,253	4,330
Capital Employed	5,664	6,083	6,549	7,046	7,643

Key Ratios					
Year End-March	FY23	FY24	FY25E	FY26E	FY27E
Per share (INR)					
EPS	7.3	7.3	9.3	10.6	11.9
BVPS	48	53	59	66	74
Valuation (x)					
P/E	28.4	28.3	22.4	19.6	17.5
P/BV	4.3	3.9	3.5	3.2	2.8
EV/EBITDA	18.4	15.8	12.7	11.0	9.5
Return ratio (%)					
EBIDTA Margin	13.7%	15.1%	15.4%	15.8%	16.0%
EBIT Margin	9.4%	11.0%	12.1%	12.2%	12.2%
PAT Margin	8.5%	8.1%	8.9%	9.2%	9.4%
ROE	15.3%	13.9%	15.8%	16.1%	16.0%
ROCE	9.9%	11.4%	13.5%	13.9%	14.0%
Leverage Ratio (%)					
Total D/E	0.2	0.2	0.2	0.2	0.2
Turnover Ratios					
Asset Turnover (x)	4.3	4.1	3.0	2.9	2.7
Receivable Days	61	63	58	53	48
Payable days	12	15	15	14	13

Source: Arihant 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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