ArihantCapital
Generating Wealth

Q2FY25 - Result Update
29th Oct 2024

# Firstsource Solutions Ltd

**Strong deal wins; Upward revision in guidance**

## CMP: INR 373

## Rating: Accumulate

## Target Price: INR 423

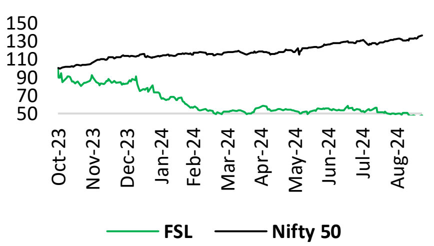
| Stock Info | |
|---|---|
| BSE | 532809 |
| NSE | FSL |
| Bloomberg | FSOL:IN |
| Reuters | FISO.BO |
| Sector | IT Enabled Services |
| Face Value (INR) | 10 |
| Equity Capital (INR Cr) | 697 |
| Mkt Cap (INR Cr) | 25,980 |
| 52w H/L (INR) | 378/154 |
| Avg Yearly Vol (in 000') | 161 |

**Shareholding Pattern %**
*(As on June, 2024)*

| | |
|---|---|
| Promoters | 53.66 |
| Public & Others | 44.11 |

| Stock Performance (%) | 1m | 3m | 12m |
|---|---|---|---|
| FSL | -7.03 | -2.0 | 27.7 |
| Nifty | 7.65 | 23.2 | 142.3 |

**FSL Vs Nifty**





Abhishek Jain
abhishek.jain@arihantcapital.com
022 67114851

Jyoti Singh
jyoti.singh@arihantcapital.com
022 67114834


**Firstsource Solutions Ltd (FSOL) in Q2FY25, FY25 constant currency revenue growth guidance raised to 19.5-20.5% from 11.5-13.5% in the previous quarter:Good top line and margin align with our estimates.The company reported revenue at INR 19,254 Mn (USD 230 mn above the estimate of USD 222 mn), y/y growth of 7.5% QoQ/+25.0% YoY in INR term above our estimate of INR 18,672 Mn. EBIT Margin at INR 2,081 Mn above our estimate of INR 2,017 Mn. Margin at 10.8% in line with our estimate of 10.8% (including one-time charges). PAT at INR 1,382 Mn below our estimate of INR 1,480 Mn. EPS of INR 1.96 vs of INR 1.92 in Q1FY25.**

**Synergy playing out well with Ascensos:** The Ascensos acquisition has strengthened the retail vertical, complementing traditional business from utilities companies. A healthy deal pipeline across both sectors is expected to drive broad-based growth in the coming quarters. Although organic revenues, excluding Ascensos, declined about 4% quarter-on-quarter due to significant cost pressures faced by UK companies, this has led to increased interest in offshore and nearshore delivery options. Ascensos enhances presence in the fast-growing retail and e-commerce segments, adding iconic UK brands to the client roster and improving delivery capabilities, particularly with its strategic location in South Africa.

**Remain positive sentiment In the BFS sector led by deal wins**: five new logos were added this quarter, reflecting strong expansion with both new and existing clients. While there is optimism about these developments and the outlook for the remainder of the FY25, the macro environment remains uncertain. Recent increases in 30-year mortgage rates, now at 6.44%, contrast with the Fed's rate cuts, highlighting ongoing challenges despite positive client growth. Overall, the sentiment in BFS remains positive amidst these uncertainties.

**Strong Deal Pipeline in Europe:** The pipeline in Europe remains robust, with several large strategic deals anticipated. Expectation is that deal wins from the first two quarters will begin to yield results in the H2FY25.

**Valuations**

The FY25 constant currency revenue growth guidance has been raised to 19.5-20.5%, including a 5% contribution from Ascensos The expectation for normalized FY25 EBIT margins, excluding one-time charges related to the acquisitions, is in the 11% to 11.5% range. There is optimism about achieving the $1 bn revenue milestone by Q4FY26.A mortgage-specific large accelerated plan and optical flow-through are in place to maintain margins. The goal is to improve margins by 50-75bps annually over the medium term until FY26.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/PAT to grow at a CAGR of 13.6%/17.7%/~21%, respectively, over FY24-27E. **We value FSL at a PE of 29x to its FY27e EPS of INR 14.6, which yields a target price of INR 423 per share (earlier target price; of INR 346 per share). We upgrade our rating to an Accumulate from Hold earlier on the stock.**

**Exhibit 1 Financial Performance**

| Particular | FY24 | FY25E | FY26E | FY27E |
|---|---|---|---|---|
| Sales | 6,336 | 7,656 | 8,835 | 10,038 |
| EBITDA | 956 | 1,181 | 1,414 | 1,636 |
| *EBIDTA Margin* | *15.1%* | *15.4%* | *16.0%* | *16.30%* |
| Reported PAT | 515 | 696 | 858 | 1,017 |
| PE (x) | *50.8* | *37.3* | *30.3* | *25.6* |
| EPS | 7.3 | 10.0 | 12.3 | 14.6 |

*Source: Arihant Research, Company Filings*

## Exhibit 2: Quarterly Performance (Consolidated)

| Consolidated (in INR Cr) | Q2FY25 | Q1FY25 | Q2FY24 | Q-o-Q | Y-o-Y |
|---|---|---|---|---|---|
| *Revenue (Mn USD)* | 230 | 215 | 186 | *7.0%* | *23.7%* |
| Net Revenue | 1,925 | 1,791 | 1,540 | *7.5%* | *25.0%* |
| Employee cost | 1,210 | 1,127 | 940 | *7.4%* | *28.8%* |
| Other Expenses | 428 | 394 | 371 | *8.4%* | *15.2%* |
| EBITDA | 287 | 270 | 229 | *6.4%* | *25.6%* |
| *EBITDA margin %* | *14.9%* | *15.1%* | *14.9%* | -15bps | 6bps |
| Depreciation | 79 | 73 | 65 | *8.2%* | *18.9%* |
| EBIT | 208.1 | 197.0 | 163.4 | *7.7%* | *10.1%* |
| *EBIT margin %* | 10.8% | 11.0% | 10.6% | -19bps | 20bps |
| Other Income | -3 | 2 | 17 | *-248.5%* | *-116.1%* |
| Finance costs | 34 | 32 | 26 | *8.6%* | *31.7%* |
| PBT | 171.0 | 167.3 | 154.3 | *2.3%* | *10.8%* |
| Exceptional item | - | - | - | | |
| PBT and share net profit | 171.028 | 167.256 | 154.303 | *2.3%* | *10.8%* |
| Tax Expense | 33 | 32 | 28 | *2.5%* | *18.1%* |
| Effective tax rate % | 19.2% | 19.1% | 18.0% | 5bps | 118bps |
| PAT | 138.2 | 135.2 | 126.5 | *2.2%* | *9.2%* |
| Non-controling intrest | - | - | - | | |
| Consolidated PAT | 138.211 | 135.249 | 126.509 | *2.2%* | *9.2%* |
| Reported PAT | 138.21 | 135.25 | 126.51 | *2.2%* | *9.2%* |
| Non - controlling interest | -0.01 | -0.00 | - | | |
| PAT | 138.21 | 135.25 | 126.51 | *2.2%* | *9.2%* |
| *PAT margin %* | *7.2%* | *7.6%* | *8.2%* | -37bps | -104bps |
| EPS (INR) | 2.01 | 1.97 | 1.85 | | |
| | | | | | |
| **Consolidated (in INR Cr)** | **Q2FY25** | **Q1FY25** | **Q2FY24** | ***Q-o-Q*** | ***Y-o-Y*** |
| Banking and Financial Services | 664 | 649 | 629 | *2.4%* | *5.6%* |
| Healthcare | 703 | 637 | 505 | *10.2%* | *39.2%* |
| Communication, Media and Technology | 412 | 398 | 327 | *3.6%* | *25.8%* |
| Diverse Industries | 154 | 101 | 81 | *53.4%* | *91.1%* |

*Source: Arihant Research, Company Filings*

- **Firstsource Solutions ltd – Q2FY25 Concall Highlights**

- The FY25 constant currency revenue growth guidance has been raised to 19.5-20.5%, including a 5% contribution from Ascensos The expectation for normalized FY25 EBIT margins, excluding one-time charges related to the acquisitions, is in the 11% to 11.5% range. There is optimism about achieving the $1 bn revenue milestone by Q4FY26.A mortgage-specific large accelerated plan and optical flow-through are in place to maintain margins. The goal is to improve margins by 50-75 basis points annually over the medium term until FY26.

- Revised business guidance is based on deal wins, including 13 new logos and the timeline for deal ramp-up. The focus is on building the business while minimizing macroeconomic impacts, with benefits continuing to be seen. Credit delinquency continues to rise due to changing U.S. customer behavior. Data provided is based on observable trends.

- In BFS, a 1% QoQ increase and a 3% overall growth were recorded, with 5 new logos added, including deals from top BFS companies. The macro environment remains uncertain, particularly with the Federal Reserve lowering interest rates. The UK business declined, excluding Ascensos.

- Ex-Ascensos, Q2 revenues grew 19.6% YoY cc. Fourth quarter of 3%+ QoQ revenue growth.

- Europe is expected to pick up in H2FY25, driven by strategic deals in AI/ML and partner ecosystems, along with regular RFPs. Notable deal wins have occurred in Europe, and strong relationships with top accounts are maintained.

- Ascensos, a leading UK-headquartered customer experience outsourcing partner for retail and eCommerce businesses, has been acquired. This acquisition strengthens nearshore capabilities, including in South Africa, and expands multilingual offerings while tapping into the thriving retail sector. Ascensos employs 2,500 individuals, all of whom are organic.

- A large deal secured from a leading telecom player in Australia and New Zealand, marking a new logo for FSL and the first major win for newly established ANZ operations.

- Strengthened relationships with one of the top 5 mortgage companies in the U.S. through a 5-year deal supporting their enterprise-wide transformation initiative.

- Expanded partnerships with a large cooperative financial institution in the UK for retail banking operations and customer interaction services.

- Additional business won from one of the top 5 healthcare insurance companies in the U.S. for claims processing services.

- Additional business secured from a leading not-for-profit healthcare provider in the U.S. for RCM services.

- A deal won from a leading online marketplace, a new logo for FSL, for customer experience services.

- A leading fintech player in the U.S. added as a client for first-party collection services.

- The deal pipeline remains healthy, with a large deal from the telecom sector and five large deals from mortgage companies. AI infusion is growing among customers, particularly in the mortgage industry, throughout FY25.

- Healthcare: strong growth qtr again, growth was well-distributed among payer and provider, added 5 new logos, delayed decision making seen amid , healthy and active pipeline in payer side.

- Two joint deals are in progress, though some delays may lead to significant impacts.

- In the UK retail digital sector, there are 2,500 employees across the UK and South Africa. Efforts are underway to increase the offshore and onshore footprint, supported by a healthy pipeline and significant tailwinds in verticals with potential for growth.

- The current environment presents typical uncertainty, with a broad-based portfolio in advanced stages. There is a focus on retaining existing subscribers while looking for a full transcript to change the business model. Over the last three weeks, 30-year mortgage rates have increased from an initial drop of 6.08% to 6.44%. About 80% of outstanding fixed-rate mortgage loans are at 5% or less from an interest rate standpoint. Overall, there is confidence in the logos added and existing clients from an expansion standpoint, despite ongoing macro uncertainty.

- UK business declined organically in Q2; Europe to pick up in H2; strategic deals within UK will ramp up in a phased manner rather than linear.

- Company expects payer segment to bounce back due to deals in advanced stages.

- Continue to broad-base provider sub-segment.

- Within Media, there is a pipeline for clients in newspapers and publishers

| Operating Metrics | Q2FY24 | Q3FY24 | Q4FY24 | Q1FY25 | Q2FY25 |
|---|---|---|---|---|---|
| **Revenue by Vertical** | | | | | |
| Banking & Financial Services | 40.80% | 38.30% | 37.30% | 36.40% | 34.40% |
| Healthcare | 32.70% | 33.50% | 32.90% | 35.70% | 36.30% |
| Communications Media & Tech | 21.20% | 22.50% | 23.60% | 22.30% | 21.30% |
| Diverse Industries | 5.30% | 5.70% | 6.20% | 5.60% | 8.00% |
| | | | | | |
| **Revenue by Geography** | | | | | |
| US | 65.10% | 65.40% | 65.00% | 68.20% | 68.50% |
| Europe, Middle East, and Africa | 34.80% | 34.50% | 34.90% | 31.80% | 1.40% |
| ROW | 0.10% | 0.10% | 0.10% | 0.00% | 0.10% |
| | | | | | |
| **Revenue by Delivery** | | | | | |
| Offshore | 26.70% | 30.30% | 31.40% | 35.00% | 35.80% |
| Onshore | 73.30% | 69.70% | 68.60% | 65.00% | 64.20% |
| | | | | | |
| **Top Clients Revenue** | | | | | |
| Top 5 clients (share of total revenues) | 35.00% | 35.80% | 36.70% | 34.60% | 32.50% |
| Top 10 clients (share of total revenues) | 51.30% | 52.00% | 52.60% | 51.50% | 48.60% |
| | | | | | |
| **Other Metrices** | | | | | |
| Total employees (end of period) | 23953 | 25947 | 27940 | 29231 | 32898 |
| Net Addition | 1569 | 1994 | 1993 | 1291 | 3667 |
| Attrition (TTM) | 39.80% | 37.70% | 35.40% | 32.00% | 30.90% |

*Source: Arihant Research, Company Filings*

## Key Financials

| Income Statement (INR Cr) | | | | |
|---|---|---|---|---|
| **Year End-March** | **FY24** | **FY25E** | **FY26E** | **FY27E** |
| **Revenue USD term** | **765.0** | **916.8** | **1039.4** | **1182.3** |
| *Change (%)* | 1.3% | 19.8% | 13.4% | 13.7% |
| **Revenues** | 6,336 | 7,656 | 8,835 | 10,038 |
| *Change (%)* | 5.2% | 20.8% | 15.4% | 13.6% |
| Employee costs | 3,909 | 4,907 | 5,610 | 6,344 |
| Other expenses | 1,470 | 1,568 | 1,811 | 2,058 |
| **Total Expenses** | **5,380** | **6,475** | **7,421** | **8,402** |
| **EBITDA** | **956** | **1,181** | **1,414** | **1,636** |
| **EBIDTA Margin** | **15.09%** | **15.42%** | **16.00%** | **16.30%** |
| Depreciation | 260 | 239 | 286 | 336 |
| **EBIT** | **696** | **941** | **1127** | **1300** |
| **EBIT Margin** | **10.99%** | **12.30%** | **12.76%** | **12.95%** |
| Interest | 103 | 105 | 102 | 101 |
| Other Income | 37 | 12 | 22 | 42 |
| **PBT** | **630** | **849** | **1,047** | **1,240** |
| Exceptional Items | - | - | - | - |
| **PBT after exceptional Items** | **630** | **849** | **1,047** | **1,240** |
| Tax | 115 | 153 | 188 | 223 |
| *Rate (%)* | *18.3%* | *18.0%* | *18.0%* | *18.0%* |
| **PAT** | **515** | **696** | **858** | **1,017** |
| **Margin** | **8%** | **9%** | **10%** | **10%** |
| **Consolidated PAT** | **515** | **696** | **858** | **1,017** |
| *Change (%)* | *0.2%* | *35.2%* | *23.3%* | *18.5%* |

| Balance Sheet (INR Cr) | | | | |
|---|---|---|---|---|
| **Year End-March** | **FY24** | **FY25E** | **FY26E** | **FY27E** |
| **Sources of Funds** | | | | |
| Share Capital | 697 | 697 | 697 | 697 |
| Reserves & Surplus | 3,003 | 3,456 | 4,070 | 4,843 |
| Non controlling interest | 0 | 0 | 0 | 0 |
| **Total Equity** | **3,701** | **4,153** | **4,767** | **5,540** |
| **Loan Funds** | **812** | **873** | **853** | **843** |
| Defered Tax Liability (Net) | 147 | 147 | 147 | 147 |
| **Total Liability** | **6,083** | **6,598** | **7,214** | **8,001** |
| **Application of Funds** | | | | |
| Gross Block | 1,221 | 1,286 | 1,586 | 1,886 |
| Less: Depreciation | 1,027 | 1,194 | 1,432 | 1,734 |
| Net Block | 194 | 92 | 154 | 152 |
| CWIP | 17 | 17 | 17 | 17 |
| Financial Assets | 1,488 | 2,423 | 2,912 | 3,622 |
| Investments | 30 | 30 | 30 | 30 |
| **Sundry debtors** | **1,161** | **1,161** | **1,161** | **1,161** |
| Cash and bank | 188 | 1,123 | 1,612 | 2,322 |
| Other Current Assets | 149 | 149 | 149 | 149 |
| Total Current assets | 1,537 | 2,471 | 2,961 | 3,671 |
| Total Current liabilities | 833 | 835 | 857 | 881 |
| Total Non-Current assets | **4,546** | **4,126** | **4,253** | **4,330** |
| **Capital Employed** | **6,083** | **6,598** | **7,214** | **8,001** |

| Cash Flow Statement (INR Cr) | | | | |
|---|---|---|---|---|
| **Year End-March** | **FY24** | **FY25E** | **FY26E** | **FY27E** |
| **PBT** | **630** | **849** | **1,047** | **1,240** |
| Cash From Operating Activities | 717 | 1,193 | 1,435 | 1,678 |
| Tax | 72 | 153 | 188 | 223 |
| Net Cash From Operations | 645 | 1,040 | 1,247 | 1,454 |
| **Capex** | **(85)** | **(66)** | **(300)** | **(300)** |
| Cash From Investing | (58) | (166) | (400) | (400) |
| Borrowings | (29) | (20) | (20) | (10) |
| **Finance cost paid** | **(101)** | **(105)** | **(102)** | **(101)** |
| Cash From Financing | (564) | 73 | (358) | (346) |
| **Net Increase/ Decrease in Cash** | **23** | **947** | **489** | **709** |
| **Cash at the beginning of the year** | **152** | **175** | **1,123** | **1,612** |
| Cash at the end of the year | 175 | 1,123 | 1,612 | 2,322 |

| Key Ratios | | | | |
|---|---|---|---|---|
| **Year End-March** | **FY24** | **FY25E** | **FY26E** | **FY27E** |
| **Per share (INR)** | | | | |
| EPS | 7.3 | 10.0 | 12.3 | 14.6 |
| BVPS | 53 | 60 | 68 | 79 |
| **Valuation (x)** | | | | |
| P/E | 50.8 | 37.3 | 30.3 | 25.6 |
| P/BV | 7.0 | 6.3 | 5.5 | 4.7 |
| EV/EBITDA | 27.8 | 21.8 | 17.9 | 15.0 |
| **Return ratio (%)** | | | | |
| EBIDTA Margin | 15.1% | 15.4% | 16.0% | 16.3% |
| EBIT Margin | 11.0% | 12.3% | 12.8% | 13.0% |
| PAT Margin | 8.1% | 9.1% | 9.7% | 10.1% |
| ROE | 13.9% | 16.8% | 18.0% | 18.4% |
| ROCE | 11.4% | 14.3% | 15.6% | 16.2% |
| **Leverage Ratio (%)** | | | | |
| Total D/E | 0.2 | 0.2 | 0.2 | 0.2 |
| **Turnover Ratios** | | | | |
| Asset Turnover (x) | 4.1 | 3.1 | 3.0 | 2.7 |
| Receivable Days | 63 | 55 | 48 | 42 |
| Payable days | 15 | 15 | 13 | 11 |

*Source: Arihant Research, Company Filings*

## Arihant Research Desk

Email: research@arihantcapital.com

Tel. : 022-42254800



| Head Office | Registered Office |
|---|---|
| #1011, Solitaire Corporate Park<br>Building No. 10, 1st Floor<br>Andheri Ghatkopar Link Road<br>Chakala, Andheri (E)<br>Mumbai – 400093<br>Tel: (91-22) 42254800<br>Fax: (91-22) 42254880 | 6 Lad Colony,<br>Y.N. Road,<br>Indore - 452003, (M.P.)<br>Fax: (91-731) 4217101 |


| 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% |

| Research Analyst Registration No. | Contact | Website | Email Id |
|---|---|---|---|
| INH000002764 | SMS: 'Arihant' to 56677 | www.arihantcapital.com | research@arihantcapital.com |




Arihant Capital Markets Ltd.
1011, Solitaire Corporate park, Building No. 10, 1st Floor,
Andheri Ghatkopar Link Road, Chakala, Andheri (E)
Tel. 022-42254800Fax. 022-42254880