

CMP: ₹ 338

Target: ₹ 400 (18%)

Target Period: 12 months

BUY

October 30, 2024

Strong Performance continues!

About the stock: Firstsource Solutions (FSL) provides business process services to BFSI, communication, media, tech and healthcare.

- Company generates ~69% revenues from the US and 31.4% from the UK
- FSL is a domain driven BPM services company which has 200+ global clients, including 19 Fortune-500 companies & 3 FTSE-100 companies.

Q2FY25 Performance: FSL reported its revenue at ₹1,932.6 crore, up by 8.3% QoQ/25.3% YoY. In US\$ terms revenue came at US\$ 230 mn, up by 7% QoQ/23.6% YoY (6.9% QoQ/22.7% YoY in CC terms). The organic CC growth was 4.2% QoQ. EBIT margin was at 10.8%, down by ~20 bps QoQ.

Investment Rationale:

- **Revenue guidance revised upwards:** Given strong Q2 and Ascencos integration, FSL revised its revenue growth guidance to 19.5-20.5% in CC terms (vs. 11.5-13.5% earlier, including ~5% contribution from Ascencos over 7 months in FY25). Further FSL reiterated its target to achieve US\$ 1 billion exit revenue run rate by FY26. The upward revision, however, implies a flattish organic growth for the next two quarters which seems a little conservative considering the healthy growth witnessed in Q2 & the strong deal pipeline. **We have revised our estimates & baked in 16.9% CAGR in revenues over FY24-27E to US\$ 1,223 mn.**
- **Sustained margin expansion likely over medium term:** FSL was able to keep its margins stable in Q2 within its guided band, despite annual wage hikes. However, it has narrowed its FY25 EBIT margin guidance to 11-11.5% (vs 11-12%) earlier. Nonetheless, it has maintained its aspiration of margin expansion of 50-75 bps annually over the medium term from FY26. Accordingly, **we have baked in EBIT margins of 11.4%, 12.2% and 13% for FY25/FY26/27E. Healthy revenue growth coupled with margins expansion to drive ~26.9% earnings CAGR over FY24-27E.**
- **Broad-based deal & client wins/GenAI:** FSL won 3 large deals, consecutively for the second time and added 30 new logos in Q2. It has healthy deal pipeline and expects to maintain the same going forward. It has highlighted that on the GenAI front they're building a specialized LLM for the US mortgage model and have made accelerated progress with their RelAI suite of AI offerings, solutions & platforms.

Rating and Target Price

- FSL is well placed to sustain its medium and long-term growth momentum driven by new logo addition and GenAI enhancement initiatives.
- **We maintain BUY, with a revised target price of ₹400; at 29x P/E on average of FY26 & FY27E EPS.**

Key Financial Summary

₹ crore	FY22	FY23	FY24	5 year			3 year	
				CAGR (FY19-24)	FY25E	FY26E	FY27E	CAGR (FY24-27E)
Net Sales	5,921	6,022	6,336	10.6%	7,845	9,039	10,351	17.8%
EBITDA	960	827	956	12.3%	1,222	1,471	1,760	22.5%
EBITDA Margins (%)	16.2	13.7	15.1		15.6	16.3	17.0	
Net Profit	537	514	515	6.4%	621	829	1,051	26.9%
EPS (₹)	7.6	7.6	7.6		9.1	12.2	15.4	
P/E	42.8	44.8	44.7		37.0	27.7	21.9	
RoNW (%)	17.7	15.3	13.9		15.4	18.5	20.8	
RoCE (%)	14.5	14.5	14.0		16.2	19.3	22.2	

Source: Company, ICICI Direct Research



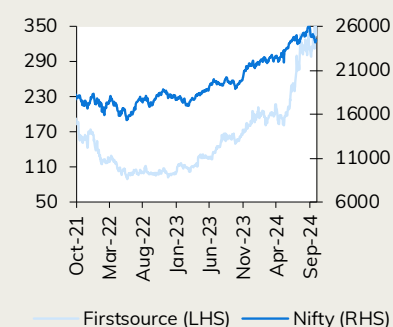
Particulars

Particular	Amount
Market Cap (₹ Crore)	23,337.8
Total Debt (₹ Crore)	812.3
Cash (₹ Crore)	218.5
EV (₹ Crore)	23,931.6
52 week H/L	378/ 154
Equity capital	697.0
Face value	10.0

Shareholding pattern

	Dec-23	Mar-24	Jun-24	Sep-24
Promoters	53.7	53.7	53.7	53.7
FII	9.9	9.6	9.4	11.6
DII	18.2	19.3	19.5	18.6
Other	18.3	17.5	17.5	16.1

Price Chart



Key risks

- Further delay in the deal ramp up in UK
- Lower than expected margin growth

Research Analyst

Bhupendra Tiwary, CFA
bhupendra.tiwary@icicisecurities.com

CA Anjini Sharma
anjini.sharma@icicisecurities.com

Deep Thosani
deep.thosani@icicisecurities.com

Performance highlights and outlook

- Revenue Performance:** Firstsource Solutions (FSL) in CC terms reported a revenue growth of 6.9% QoQ & 22.7% YoY. In dollar terms it reported a revenue of US\$ 230 mn, up by 7% QoQ & 23.6% YoY. In rupee terms FSL reported revenue of INR 1,932.6 crore, up by 8.3% QoQ & 25.3% YoY.
- Geography performance:** All the geographies improved sequentially with US (69% of mix) seeing an uptick of 7.4% QoQ & UK region (31.4% of mix) by 5.6% QoQ. The UK region, however, faces cost pressures which has caused the delay in ramp up of some important deals. However, the company expect the revenue growth in the region to improve over the next two quarters.
- Segment wise Performance and outlook:** Segment wise, all the verticals reported a sequential growth with, Others (8% of mix) reporting a growth of 52.8% QoQ (led by inorganic growth), followed by healthcare (36% of the mix), CMT (21% of the mix), BFSI (34% of the mix) which grew by 8.8%, 2.2%, 1.1% respectively.
 - BFSI Segment:** For the quarter, the company added 5 new logos in this vertical and has a balanced mix of new client addition and existing client expansion. Further, the Fed rate cuts could bolster the confidence of the company in this segment's future performance.
 - Diverse Portfolio (Others):** This segment reported a solid growth both sequentially and on a YoY basis. This growth was aided by the inorganic contribution of the Retail segment that came through the Ascensos acquisition and FSL's traditional business from utilities company. The management stated that they see a healthy deal pipeline in both these sub segments, should translate for a broad-based growth moving forward.
- Guidance:** FSL for FY25 revised its revenue growth guidance to 19.5% - 20.5% in CC terms (vs 11.5-13.5% earlier, including ~5% contribution from Ascensos over seven months in FY25). It, however, narrowed its EBIT margin guidance to 11-11.5% range (vs 11-12% earlier) but maintained its aspiration of margin expansion of 50-75 bps annually, over the medium term from FY26. **We note that the upward revision implies a flattish organic growth for the next two quarters which seems a little conservative considering the healthy growth witnessed in Q2 & the strong deal pipeline.**
- GenAI/AI:** On the AI front, the company has partnered with Microsoft to leverage Azure Open AI services to provide GenAI powered solutions and platforms to its clients. It is also investing in **building its domain centric large language model specifically for the mortgage industry**. The management mentioned that they're making accelerated progress with relAI their suite of AI led offerings, solutions and platforms.
- Deal Wins:** The company reported its **highest ever new logo addition over the past two years by adding 30 new logos in the quarter**. Additionally, it has **signed 3 large deals** consecutively for the second time from its 1 deal a year back.
- Attrition & Employee addition:** The company during the quarter added 3,667 net new employees (of which 2.5k are from the Ascensos acquisition), taking its employee base to 32,898 employees. The attrition for the quarter stood at 30.9% down ~110 bps QoQ.
- Ascensos Acquisition:** As per the company, the acquisition will help the company in establishing its presence in the retail and e-commerce segment which has a TAM of US\$ 35 bn. (~ ₹2,94,000 crore). Ascensos presence in the South Africa region will bolster FSL's position with its UK

based clients who are actively exploring outsourcing capacities in the same time zone. As a result, the company's clients have awarded them with additional business in South Africa post the acquisition. The acquisition will also provide the company with delivery capabilities in 11 non-English languages.

Exhibit 1: Quarter Performance

₹ crore	Q2FY25	Q2FY24	YoY (%)	Q1FY25	QoQ (%)	Comments
Revenue	1,925.4	1,540.0	25.0	1,791.1	7.5	Revenue grew by 6.9% QoQ in CC terms & 7% in dollar terms
Employee expenses	1,210.4	940.0	31.6	1,126.8	8.2	
Gross Margin	714.9	600.0	19.2	664.3	7.6	
Gross margin (%)	37.1	39.0	-183 bps	37.1	4 bps	
SG&A expenses	427.7	371.2	15.2	394.4	8.4	
EBITDA	287.3	228.8	25.6	269.9	6.4	
EBITDA Margin (%)	14.9	14.9	6 bps	15.1	-15 bps	
Depreciation & amortisation	79.2	65.4	21.1	72.9	8.7	
EBIT	208.1	163.4	27.3	197.0	5.6	
EBIT Margin (%)	10.8	10.6	20 bps	11.0	-19 bps	Margins remained within the guided range despite wage hikes
Other income (less interest)	-37.1	-9.1	306.2	-29.8	24.5	
PBT	171.0	154.3	10.8	167.3	2.3	
Tax paid	32.8	27.8	18.1	32.0	2.5	
PAT	138.2	126.5	9.2	135.3	2.2	

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 2: Profit and loss statement ₹ crore

(Year-end March)	FY24	FY25E	FY26E	FY27E
Total Revenues	6,336	7,845	9,039	10,351
Growth (%)	5.2	23.8	15.2	14.5
Employee expenses	3,909	4,897	5,604	6,366
Other Expenses	1,471	1,726	1,963	2,225
EBITDA	956	1,222	1,471	1,760
Growth (%)	15.7	27.8	20.4	19.6
Depreciation & Amortization	260	325	371	414
Other Income	37	5	23	32
Interest	103	134	100	80
PBT before Exceptional Item	630	768	1,024	1,298
Growth (%)	2.4	21.9	33.4	26.7
Tax	115	146	195	247
PAT before Excp Items	515	621	829	1,051
Exceptional items				
PAT before MI	515	621	829	1,051
Minority Int & Pft. from asso.	(0)	(0)	-	-
PAT	515	621	829	1,051
Growth (%)	0.2	20.7	33.5	26.7
EPS	7.6	9.1	12.2	15.4
EPS (Growth %)	0.2	20.7	33.5	26.7

Source: Company, ICICI Direct Research

Exhibit 3: Cash flow statement ₹ crore

(Year-end March)	FY24	FY25E	FY26E	FY27E
Profit before Tax	630	768	1,024	1,298
Dep & Amortization	260	325	371	414
WC changes	(240)	(204)	(160)	(177)
Other non cash adju.	(5)	(18)	(118)	(199)
CF from operations	645	871	1,116	1,336
Capital expenditure	(85)	(235)	(90)	(103)
Δ in investments	36	-	-	-
Other investing cash flow	1	5	23	32
CF from Inv Activities	(58)	(230)	(67)	(71)
Issue of equity	(52)	-	-	-
Δ in debt funds	128	-	(200)	(200)
Dividends paid	(241)	(298)	(373)	(473)
Other financing cash flow	(101)	(134)	(100)	(80)
CF from Fin Activities	(564)	(525)	(766)	(846)
Δ in cash and cash bank	23	116	283	419
Effect of exchange rate changes				
Opening cash	156	188	305	588
Closing cash	188	305	588	1,006

Source: Company, ICICI Direct Research

Exhibit 4: Balance Sheet ₹ crore

(Year-end March)	FY24	FY25E	FY26E	FY27E
Equity	697	697	697	697
Reserves & Surplus	3,003	3,326	3,783	4,361
Networth	3,700	4,023	4,480	5,058
Minority Interest	0	0	0	0
LT liabilities & provisions	737	737	737	737
Total Debt	812	812	612	412
Source of funds	5,250	5,573	5,829	6,207
Net fixed assets	800	802	615	397
CWIP	17	17	17	17
Goodwill	2,988	2,988	2,988	2,988
Other non current assets	740	829	898	975
Loans and advances	-	-	-	-
Current Investments	30	30	30	30
Debtors	1,161	1,437	1,654	1,894
Cash & Cash equivalents	188	305	588	1,006
Other current assets	158	196	225	258
Trade payables	306	378	435	499
Current liabilities	460	569	655	750
Provisions	67	83	96	110
Application of funds	5,250	5,573	5,829	6,207

Source: Company, ICICI Direct Research

Exhibit 5: Key ratios

(Year-end March)	FY24	FY25E	FY26E	FY27E
Per share data (₹)				
EPS	7.6	9.1	12.2	15.4
DPS	3.5	4.2	5.3	-
BV	54.4	59.1	65.8	74.3
Operating Ratios (%)				
EBITDA Margin	15.1	15.6	16.3	17.0
PBT Margin	9.9	9.8	11.3	12.5
PAT Margin	8.1	7.9	9.2	10.2
Return Ratios (%)				
RoNW	13.9	15.4	18.5	20.8
RoCE	14.0	16.2	19.3	22.2
Valuation Ratios (x)				
P/E	44.7	37.0	27.7	21.9
EV / EBITDA	24.7	19.2	15.6	12.7
Price to Book Value	6.2	5.7	5.1	4.5
EV / Net Sales	3.7	3.0	2.5	2.2
Mcap / Net Sales	3.6	2.9	2.5	2.2
Turnover Ratios				
Debtor days	67	67	67	67
Creditors days	18	18	18	18
Solvency Ratios				
Total Debt / Equity	0.2	0.2	0.1	0.1
Current Ratio	1.6	1.6	1.6	1.6
Quick Ratio	1.6	1.6	1.6	1.6
Net Debt / EBITDA	0.6	0.4	(0.0)	(0.4)

Source: Company, ICICI Direct Research

RATING RATIONALE

ICICI Direct endeavours to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

ICICI Direct Research Desk,
ICICI Securities Limited,
Third Floor, Brillanto House,
Road No 13, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

ANALYST CERTIFICATION

I/We, Bhupendra Tiwary, CFA, MBA (Finance), Anjini Sharma, CA, Deep Thosani, MBA (Finance), Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products.

ICICI Securities is Sebi registered stock broker, merchant banker, investment adviser, portfolio manager and Research Analyst. ICICI Securities is registered with Insurance Regulatory Development Authority of India Limited (IRDAI) as a composite corporate agent and with PFRDA as a Point of Presence. ICICI Securities Limited Research Analyst SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. Registered Office Address: ICICI Venture House, Appasaheb Marathe Marg, Prabhadevi, Mumbai - 400 025. CIN: L67120MH1995PLC086241, Tel: (91 22) 6807 7100. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on www.icicibank.com.

Investments in securities market are subject to market risks. Read all the related documents carefully before investing.

Registration granted by Sebi and certification from NISM in no way guarantee performance of the intermediary or provide any assurance of returns to investors. None of the research recommendations promise or guarantee any assured, minimum or risk-free return to the investors.

Name of the Compliance officer (Research Analyst): Mr. Atul Agrawal

Contact number: 022-40701000 E-mail Address: complianceofficer@icicisecurities.com

For any queries or grievances: Mr. Bhavesh Soni Email address: headservicequality@icicidirect.com Contact Number: 18601231122

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities and its analysts, persons reporting to analysts and their relatives are generally prohibited from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit icicidirect.com to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Retail Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, and target price of the Institutional Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities and ICICI Securities as a entity are engaged in various financial service businesses, they might have financial interests or actual/beneficial ownership of one percent or more or other material conflict of interest various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.