

May 30, 2022

Zensar Technologies Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/Short-term - Fund-based/Non-fund based	177.00	177.00	[ICRA]AA+(Stable)/[ICRA]A1+; reaffirmed
Long-term - Non-fund based	14.00	14.00	[ICRA]AA+(Stable); reaffirmed
Total	191.00	191.00	

*Instrument details are provided in Annexure-1

Rationale

The rating reaffirmation factors in Zensar Technologies Limited's (Zensar) established business position in the IT services industry and steady performance in FY2022. Zensar posted ~13.1% of YoY core revenue¹ growth in constant currency terms in FY2022, supported by accelerated demand for digital services (cloud and digital transformation). The company's core revenue contribution from digital services grew to 70.8% as of FY2022 from 54.5% in FY2020. The company reported sizeable order booking of TCV² worth \$575 million in FY2022 maintaining a healthy mix of large and mid-sized deals supported by multiple wins across verticals. Coupled with growth prospects of digital and cloud infrastructure services, and a focused effort to scale up contribution from top-tier clients, this provides revenue visibility for Zensar in the medium term.

The ratings also factor in Zensar's healthy financial profile, characterised by recurring free cash flows, strong capital structure and comfortable liquidity position. The liquidity profile remains supported by sizeable cash and investments of \$155.7 million (Rs. 1,180 crore) as on March 31, 2022. Zensar recorded OPM of 15.5% in FY2022 versus 18.1% in FY2021, mainly due to increased cost of delivery because of increased cost of hires to support growth as well as attrition rates and high wage hikes for the last fiscal, coupled with investment in sales and marketing. Margins are likely to witness continued pressure in the near term owing to wage cost inflation and normalisation of operational overheads. However, attrition levels are expected to start tapering from the end of the current fiscal, as record net employee addition at the industry level in FY2022 is likely to address the demand-supply gaps to a large extent. This coupled with better realisation and operational efficiencies is likely to support the profit margins over the medium term.

The ratings remain constrained by the relatively moderate scale of operations and concentration on the US market (70.5% of revenue in FY2022) compared to large domestic IT players. While increasing the scale and the size of its operations, a leveraged funding structure for future acquisitions could materially impact the company's financial risk profile. Further, a large cross-border acquisition would entail careful integration of operations to realise likely synergies. The company also faces stiff competition from other prominent players in the global IT services industry, leading to limited pricing flexibility. Additionally, industry participants, including Zensar, continue to face challenges in the form of foreign currency fluctuations, talent acquisition and retention. The demand for IT services remains exposed to macro-economic uncertainties in Zensar's key operating markets of the US, Europe and South Africa.

The Stable outlook on the rating reflects ICRA's opinion that Zensar will continue to benefit from its established business profile, healthy order book position and favourable demand outlook of the industry.

¹ Adjusted for Third Party Maintenance (TPM) business which was sold off in FY2021

² TCV- Total Contract value

Key rating drivers and their description

Credit strengths

Diversified presence across various service lines and verticals – The company’s revenues are diversified across various service offerings, such as the digital application services (DAS) and digital foundation services (DFS). Further, its clientele is distributed across the manufacturing (industrial and hi-tech), consumer services, and banking and financial services (BFSI) domains, resulting in sectoral diversification. The BFSI and consumer services verticals reported healthy growth of 24% and 27% YoY, respectively, supported by healthy industry demand for digitalisation, investment in sales and marketing teams and strengthening of client engagement across major accounts. Growth in Zensar’s manufacturing vertical (generated 49% of total revenues in FY2022), meanwhile, was moderate at 4% YoY owing to project closures and stable revenue from its top client.

Part of a large, established, and diversified Group imparts financial flexibility – Zensar is part of the ~Rs. 263 billion (FY2021 revenues) RPG Group, which has a diversified presence in infrastructure, tyres, technology and pharmaceuticals. It derives financial flexibility and benefits from the strong management lineage of the Group.

Healthy order book and favourable industry demand outlook provides revenue visibility – Supported by the healthy demand, the company secured sizeable new orders in FY2022, translating into TCV worth \$576 million in FY2022. The order inflow has a healthy mix of large and mid-sized deals supported by multiple wins across verticals. Also, in Q4 FY2022, ~40% of the deal wins were from new clients. Coupled with healthy demand outlook for digital and cloud-based services, this provides revenue visibility to the company.

Strong financial profile characterised by healthy cash flow generation, robust capital structure and comfortable liquidity profile – The company’s financial profile remains strong as reflected in its high operating profitability, strong capital structure and robust liquidity position in the form of a strong cash and investment balance of \$155.7 million (Rs. 1,180 crore) as on March 31, 2022. Zensar posted ~13.1% of YoY core revenue growth in constant currency terms and healthy operating margin of 15.5% in FY2022, supported by accelerated demand for digital services (cloud and digital transformation). Going forward, the financial metrics are expected to be in line with past trends and remain healthy backed by revenue growth and healthy liquidity position.

Credit challenges

Relatively moderate scale of operations and geographical concentration risk compared to large IT companies – With revenues of Rs. 4,243.8 crore in FY2022, Zensar’s scale of operations remains more moderate than some large domestic IT players, thereby restricting its pricing flexibility and margins. Zensar’s geographical revenue trend is in line with the global IT services industry, with the US being its largest revenue generator. With 70.5% of its revenues being derived from the US market in FY2022, followed by Europe (18.1%) and Africa (11.5%), Zensar’s revenues and earnings are exposed to the structural and region-specific challenges in the US.

Industry specific challenges like intense competition, forex risk, high employee attrition and exposure to policies in key operating markets – Given the intense competition in the industry, Zensar’s profit margins are susceptible to pricing pressures and wage inflation. Further, much of the revenues and margins are exposed to forex risks, although the company’s hedging mechanisms mitigate the same to an extent. Being in a highly labour-intensive business, the availability and retention of a skilled workforce are the key challenges. Zensar’s margin has been impacted in FY2022, owing to increased cost of delivery

because of considerable wage cost inflation. The LTM³ attrition as on March 31, 2022 was 27.9%. However, attrition levels are expected to start tapering from the end of the current fiscal, as record net employee addition at the industry level in FY2022 is likely to address the demand-supply gaps to a large extent. Zensar is also exposed to macroeconomic uncertainties and any adverse regulatory/ legislative changes in its key operating markets of USA, Europe and South Africa.

Liquidity position: Strong

Zensar's liquidity is **strong** with healthy estimated fund flow from operations (FFO) of Rs. 500-530 crore in FY2023, aided by steady revenue growth and operating profitability. The liquidity is also strengthened by sizeable cash/liquid investments of \$155.7 million (~Rs. 1,180 crore), healthy unutilised working capital limits as on March 31, 2022, and with no debt repayment liability. ICRA expects the company to continue to scout for investment/acquisition opportunities to support its inorganic growth initiatives. The impact, if any, of the same on Zensar's credit and liquidity profile will depend on the ticket size of these investments/acquisitions and their operational and financial synergies.

Rating sensitivities

Positive factors- A rating upgrade for Zensar is unlikely in the medium term given the moderate scale of operations. However, the ratings could be upgraded if the company demonstrates significant improvement in its scale of business, supported by growth across verticals.

Negative factors - Negative pressure on Zensar's ratings could arise in case of sizeable debt-funded acquisitions, which could significantly impact the financial profile and liquidity position. Specific credit metrics that could lead to a downgrade of Zensar's ratings include Total Debt/OPBITDA (debt including lease liability) exceeding 1.25 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Information Technology(IT) Services Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Zensar. As on March 31, 2022, the company had 15 subsidiaries, which are listed in Annexure-2.

About the company

Zensar is a mid-size IT software and infrastructure services and solutions provider with industry expertise across manufacturing (Hitech and Industrial), retail, insurance, banking and financial services. The company delivers comprehensive services for mission-critical applications, enterprise applications, business intelligence and analytics, business process management and digital services. Zensar has operations across the US, the UK, Europe and South Africa. Zensar is a part of the diversified RPG Group with a presence in infrastructure, Tyres, technology, and pharmaceuticals.

Zensar's comprehensive range of software services and solutions enable its more than 140 customers to cross new thresholds of business performance. The company is present across the whole value chain of IT and IT enabled services from IT consulting, application development and maintenance to package implementation and BPO operations.

³ Last twelve months

Key financial indicators (audited)

Zensar - Consolidated	FY2021	FY2022
Operating Income (Rs. crore)	3,781.4	4,243.8
PAT (Rs. crore)	307.0	421.7
OPBDIT/OI (%)	18.1%	15.5%
PAT/OI (%)	8.1%	9.9%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.4
Total Debt/OPBDIT (times)	0.5	0.5
Interest Coverage (times)	12.8	18.6

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Note: PAT is after exceptional losses and Debt includes lease liability

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current Rating (FY2023)				Chronology of Rating History for the past 3 years				
	Type	Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31, 2022 (Rs. crore)	Date & Rating in	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020		
				May 30, 2022			Feb 25, 2020	Dec 27, 2019	
1	Fund based/Non-fund based	Long-term and short term	177.0	-	[ICRA]AA+ (Stable) / [ICRA]A1+	-	[ICRA]AA+ (Stable) / [ICRA]A1+	[ICRA]AA+ (Negative) / [ICRA]A1+	[ICRA]AA+ (Stable) / [ICRA]A1+
2	Non-fund based	Long-term	14.0	--	[ICRA]AA+ (Stable)	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)

Complexity level of the rated instrument

Instrument	Complexity Indicator
Fund based/Non-fund based	Simple
Non-fund based	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analyzing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term/Short-term Fund based/ Non-fund based	NA	NA	NA	177.0	[ICRA]AA+(Stable)/ [ICRA]A1+
NA	Long-term - Non-fund based	NA	NA	NA	14.0	[ICRA]AA+(Stable)

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

Annexure-2: List of entities considered for consolidated analysis

Company Name	ZENSAR Ownership	Consolidation Approach
Zensar Technologies Inc.	100%	Full Consolidation
Zensar Technologies (UK) Ltd.	100%	Full Consolidation
Zensar (Africa) Holdings (Pty) Ltd.	100%	Full Consolidation
Zensar (South Africa) (Pty) Ltd.	75%	Full Consolidation
Zensar Technologies (Singapore) Pte. Ltd.	100%	Full Consolidation
Foolproof Ltd., UK	100%	Full Consolidation
Foolproof (SG) Pte. Ltd.	100%	Full Consolidation
Cynosure Interface Services Private Limited	100%	Full Consolidation
Keystone Logic Mexico S. DE R.L. DE C.V	100%	Full Consolidation
Zensar Technologies GMBH	100%	Full Consolidation
Zensar Technologies (Canada) Inc.	100%	Full Consolidation
Zensar information technology B.V	100%	Full Consolidation
M3Bi India Private Limited	100%	Full Consolidation
M3Bi LLC	100%	Full Consolidation
Zensar Colombia S.A.S	100%	Full Consolidation

Source: Company data

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About ICRA Limited:

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