

June 23, 2022

Innovsource Services Private Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/ Short-term – Fund Based Working Capital	50.00	95.00	[ICRA]A (Stable)/ [ICRA]A1; reaffirmed/assigned
Total	50.00	95.00	

*Instrument details are provided in Annexure-1;

Rationale

While arriving at the ratings of Innovsource Services Private Limited (ISPL), ICRA has taken the consolidated financial of First Meridian Business Private Limited (First Meridian or the Group; the group holding company of ISPL), which includes its subsidiaries and step-down subsidiaries, given their common management, significant operational and financial linkages.

The rating action factors in the Group's steady performance in FY2022, as marked by healthy revenue growth and improvement in accrual generation, aided by considerable increase in the Group's associate base (118,082 as on March 31, 2022 against 95,228 as on March 31, 2021) and increase in salaries across industries during the fiscal. Moreover, equity infusion of Rs. 120.0 crore by the promoters during this fiscal has strengthened the Group's net worth to Rs. 398.0 crore¹ as of March 31, 2022. Coupled with low debt levels, this has continued to result in comfortable leverage levels and strong debt protection metrics for the Group. ICRA notes that the Group has filed DRHP² for its planned IPO³, as it plans to raise Rs. 50 crore through fresh issue, and its existing promoters have also planned an offer for sale of Rs. 750 crore. ICRA expects the fresh issue to further strengthen the capital structure of the Group. Its liquidity remains strong supported by cash and cash equivalent of Rs. 277 crore as on March 31, 2022 and no long-term debt repayment liability. The ratings also continue to factor in the Group's established brand equity, strong market share as the third largest domestic player in the fragmented staffing industry, and its established client base of reputed companies across industries. The end-user industries include telecom, BFSI, infrastructure, e-commerce, etc. The ratings also consider the Group's diversified, domestic, geographical footprint and customer base with ~47% of its total revenues derived from its top 10 customers in 9M FY2022.

However, its ratings remain constrained by the inherently low profit margins and high attrition in the general staffing segment, which currently contributes ~91% to the Group's total revenues. ICRA expects moderate improvement in margin over the medium term, with increase in revenue share of IT and professional/ industrial staffing. The ratings remain constrained by the intense competition in the fragmented manpower outsourcing industry as a major portion is provided by the unorganised sector, leading to weaker pricing flexibility. However, the increasing compliances toward regulatory requirement has led companies to move towards the organised sector, which provides better revenue visibility. ICRA has also taken note of the risks arising out of the expected planned acquisition by the Group and the expected cash outflow to fund those acquisitions.

The Stable outlook on the [ICRA]A rating reflects ICRA's opinion that the Group will continue to benefit from its track record of operations, established client base and healthy financial risk profile.

¹ As per provisional financials

² Draft Red Herring Prospectus

³ Initial public offering

Key rating drivers and their description

Credit strengths

Established presence and strong market share in staffing business – The First Meridian Group is the third largest player with market share of 1.5% in the fragmented domestic staffing industry, supported by a strong brand equity and increasing formalisation of the industry. Through various acquisitions, the Group has built a strong presence in general staffing and IT staffing, with a total associate strength of 118,082 as on March 31, 2022. The Group has a pan India presence with over 50 branch offices for sourcing and recruitment in 75 cities. Going forward, steady increase in the employee base, increased focus toward the more margin accretive IT and professional/industrial staffing and steady demand outlook are expected to support the Group's revenue growth and margin expansion.

Diversified and established client base; includes reputed names – The Group has a diversified geographical footprint with its client base consisting of top multinationals. firms from diversified industries such as telecom, BFSI, infrastructure and e-commerce. At present, it serves over 1,273 clients across industries in the domestic market. Under the general staffing segment, the Group adopts the collect-and-pay model (for ~59% of its billing) for most of its customers, wherein the salaries of the associate employees deployed to its customers are collected in advance and then paid to the associate employees. In case where credit period is allowed to customers, the Group have an understanding with most of its customers that it will not do funding for second month. This reduces the risk of bad debts and lowers the Group's working capital requirements.

Healthy financial profile of the Group – The Group reported healthy revenue growth of 36% YoY in FY2022 supported by sizeable increase in associates (118,082 as on March 31, 2022 versus 95,228 as on March 31, 2021) and an increase in salaries across industries. ICRA expects healthy revenue growth in the medium term supported by steady requirement for staffing across key sectors (Telecommunication, Retail, IT and ecommerce) and full year revenue from Rlabs Enterprise Services Private Limited⁴ (acquired in February 2022) and other inorganic acquisitions. The Group's capital structure and coverage metrics remain healthy supported by no external long-term debt and strong network of ~Rs 398 crore as on March 31, 2022. The network was supported by equity infusion of Rs 120 crore by promoters in March 2022 by way of a right issue. ICRA expects the overall financial profile to remain comfortable with healthy revenue growth and stable cash flows.

Credit challenges

Inherently thin operating margin in general staffing business – The Group's operating margins are inherently thin (2.2% in FY2022) due to the high share of revenues from the general staffing segment (~91.0% of revenue), wherein the Group mainly adopts cost-plus mark-up model for pricing its customers. The mark-up is usually around 4-5% on the employee cost or on per employee basis. Due to low mark-up in the general staffing industry, players generally have low gross margin of about 4-5% and EBITDA margin of 1.5-2.0%. Further, competitive intensity limits the pricing flexibility in the general staffing business. However, the margins are considerably higher in specialised staffing segments like IT staffing, which generates about 9% of the Group's revenue. ICRA expects moderate improvement in margin in the medium term supported by healthy growth in revenues and higher share of revenue from IT staffing segment.

Intense competition in the fragmented manpower outsourcing industry and high attrition risks – The staffing industry is a fragmented market, with top five players combinedly have market share of 12% and includes a lot of unorganised players, who offers services at a low price. Consequently, competitive pressures continue to limit the Group's pricing power and scope for margin expansion in these segments. However, with increasing focus on compliance and the expected streamlining of labour codes, the organised sector is likely to improve its market share, going forward. This should further support the growth of the

⁴ It is in the business of IT staffing and consultancy, providing staff augmentation, IT consultation and managed services solutions to customers.

Group, which is the third largest organised player in the staffing industry. Inherent to the industry, the Group witness's high employee attrition owing to low skill/entry level and the temporary nature of the jobs.

Liquidity position: Strong

The Group is expected to generate cash flow from operations (FFOs) of Rs. 70-80 crore in FY2023, supported by healthy cash accruals. The Group's liquidity position is strong, supported by healthy cash and cash equivalent of Rs. 277.0 crore as on March 31, 2022, and no long-term debt repayment liability.

Overall, ICRA expects the Group's liquidity position to remain strong, supported by a healthy cash balance and a comfortable working capital position despite its plans to grow inorganically.

Rating sensitivities

Positive factors – The rating could be upgraded if there is steady scale up in operations coupled with improvement in profitability indicators driven by increasing share of higher margin business.

Negative factors – Negative pressure on the ratings could arise if there is a significant contraction in revenues and margins or any debt-funded acquisition that could lead to increase in debt levels of the Group. Specific credit metrics that could lead to a rating downgrade include Net Debt /OPBITDA of more than 2.0 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Consolidation and Rating Approach
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of First Meridian Business Private Limited. As on March 31, 2022, the Group had five subsidiaries and one step-down subsidiary.

About the Company

First Meridian Business Private Limited was formed in February 20, 2018, backed by the three PE investors, Samara Capital, Janchor Partners Pan-Asian Master Fund (Hong Kong), and Emerald Strategic Holdings PTE. The Group is the holding company of the five subsidiaries and one step-down subsidiary.

The Group provides wide range of services comprising:

- **General staffing and allied services:** contract staffing solutions, workforce automation solutions and trade marketing solutions
- **Global technology solutions (IT staffing):** short and long-term technology contract staffing solutions
- **Other HR services:** permanent recruitment, recruitment process outsourcing, pharmaceutical and healthcare staffing and facility management

ISPL was incorporated in March 2016 and acquired by First Meridian in June 2018. The company is mainly engaged in providing general staffing services. General staffing is primarily manpower outsourcing on a skill requirement basis or project completion basis for a limited period.

Key financial indicators (audited)

Name of first meridian	FY2020	FY2021	9M FY2022
Operating Income (Rs. crore)	2058.4	2110.3	2,069.4
PAT (Rs. crore)	-19.6	-33.7	21.4
OPBDIT/OI (%)	1.6%	1.7%	2.1%
PAT/OI (%)	-1.0%	-1.6%	1.0%
Total Outside Liabilities/Tangible Net Worth (times)	1.4	1.7	1.9
Total Debt/OPBDIT (times)	1.1	0.9	0.6
Interest Coverage (times)	18.1	12.3	16.3

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

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 March 31, 2022 (Rs. crore)	Date & Rating in	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					Jun 23, 2022	Apr 8, 2021	-	-
1	Fund based Working Capital facilities*	Long-term and short term	80.0	-	[ICRA]A(Stable)/[ICRA]A1	[ICRA]A(Stable)/[ICRA]A1	-	-
2	Fund based Working Capital facilities	Long-term and short term	15.0	-	[ICRA]A(Stable)/[ICRA]A1	[ICRA]A(Stable)/[ICRA]A1		

*Co-borrower includes Affluent Global Services Private Limited, V5 Global Services Private Limited and CBSI India Private Limited

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/Short term Fund-based	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	Working capital Limits	NA	NA	NA	95.0	[ICRA]A(Stable)/ [ICRA]A1

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	First Meridian Ownership	Consolidation Approach
Innovsource Services Private Limited	100.0% (rated entity)	Full Consolidation
Innovsource Facilities Private Limited	100.0%	Full Consolidation
V5 Global Services Private Limited	100.0%	Full Consolidation
Affluent Global Services Private Limited	100.0%	Full Consolidation
CBSI India Limited	100.0%	Full Consolidation
Rlabs Business systems Private Limited	75.0%	Full Consolidation

Source: Company data

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About ICRA Limited:

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Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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