

October 06, 2023

Mphasis 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 – Others	1,600.00	1,600.00	[ICRA]AA+ (Stable)/ [ICRA]A1+; Reaffirmed
Total	1,600.00	1,600.00	

*Instrument details are provided in Annexure-I

Rationale

The reaffirmation of ratings of Mphasis Limited (Mphasis) factors in its established position in the Information Technology (IT) and IT-enabled services (ITeS) industry, its presence across diverse business segments and its strong financial profile. Further, the company has a strong execution track record along with well established relationships with a strong customer base. Mphasis reported 15.4% YoY growth in its operating income to Rs. 13,798.5 crore in FY2023. However, softness in mortgage and banking segments (accounts for more than 50% of annual revenues) in the US market in recent quarters, led to minor degrowth in the company's revenue in Q1 FY2024. Nevertheless, it reported record Total Contract Value (TCV) wins of \$707 million during the quarter, which enhance its overall order book position and provide revenue visibility. While some recovery in growth for Mphasis is likely from H2 FY2024, overall growth in FY2024 is expected to be considerably lower than FY2023, in line with the industry trend, due to lower discretionary spending by clients. Nevertheless, the company's financial profile is expected to remain strong, marked by steady accrual generation, strong liquidity position and comfortable capital structure and coverage metrics.

The ratings, however, remain tempered by Mphasis' relatively moderate scale of operations and concentration on the US market (82% of revenues in FY2023) as compared to some large domestic IT services companies. ICRA also notes the competition faced by the company from other prominent players in the global IT services industry, which limits pricing flexibility to an extent. Moreover, the industry is susceptible to challenges in the form of foreign currency fluctuations, talent acquisition and retention. Also, the demand for IT services remains exposed to macro-economic uncertainties in Mphasis' key operating markets of the US, Europe and India. Further, Mphasis has made steady pay-outs in the form of dividends or share buybacks to support repayments on debt raised by the erstwhile holding company (Marble Pte II Limited). In addition, the company has sizeable contingent liabilities, especially with respect to income tax related matters. Any higher than anticipated dividend payout or materialisation of contingent liabilities, impacting the company's liquidity or credit profile on a sustained basis will remain a key monitorable.

The Stable outlook on the rating reflects ICRA's opinion that despite some moderation in growth momentum in the near term, Mphasis's credit profile will continue to remain strong, supported by its established position in the industry, healthy cash flow generation from operations and strong liquidity position.

Key rating drivers and their description

Credit strengths

Established operational track record and presence in the industry – Mphasis is a mid-sized player catering to the IT/ ITeS/ BPO industry in various domains such as banking and capital markets, communication, insurance, etc. The company has strong domain expertise and offers a wide range of services. Based on its expertise, the company continues to add new clients, which aided its top line growth in recent years. Mphasis serves marquee customers across the globe, including global banks, mortgage lenders and top global insurance companies, among others.

Improving momentum from direct business – Over the years, the company’s share of direct business has increased considerably supported by mining of existing clients, acquisition of new clients across verticals based on domain expertise, and from deals from the clientele of the Blackstone Group. The direct business accounted for ~94% in Q1 FY2024. Further, the company reported record TCW wins of \$707 million in Q1 FY2024, which enhance future revenue visibility. Moreover, its recent strategic initiatives such as alliance with Kore.ai. and incremental business from acquisition of eBECS are likely to support future growth.

Access to Blackstone’s clientele – Given the Blackstone Group’s parentage, Mphasis has access to its investment portfolio, which it has leveraged since its acquisition. With Blackstone expanding its assets under management across verticals and geographies, new opportunities for client wins shall continue for Mphasis. Also, with Abu Dhabi Investment Authority (ADIA) and University of California (UC) Investments picking up stake in Mphasis in April 2021, the company will continue to gain access to the investment portfolios of these investors as well.

Strong financial profile characterised by strong earnings and net debt-free status — Mphasis’ financial profile continues to remain strong, aided by healthy revenue growth and internal accrual generation, strong liquidity position, comfortable capital structure and robust debt protection metrics. Mphasis posted healthy revenue growth in FY2023, supported by accelerated demand for digital services (cloud and digital transformation). However, ICRA expects moderation in revenue growth in FY2024 for industry participants, including Mphasis (reported 4.7% YoY degrowth in Q1 FY2024 primarily due to softness in demand from the banking segment), owing to the base effect and persistent uncertainty in key markets leading to a cautious stand by customers as reflected in their lower discretionary spending. However, Mphasis’s debt protection metrics are expected to remain healthy, supported by strong cash flows and relatively stable margins, despite some slowdown in revenue growth.

Credit challenges

Relatively moderate scale of operations and geographical concentration risk compared to large IT services companies — Despite a healthy top-line growth of 15.4% to Rs. 13,798.5 crore in FY2023, Mphasis’s scale of operations continue to remain relatively moderate as compared to some large domestic IT services companies, thereby restricting its pricing flexibility and margins to some extent. Moreover, in line with global industry trends, Mphasis derives a significant share (~80-82%) of its revenues from the US market. This exposes its revenues and earnings to the structural and region-specific challenges of the US.

Industry specific challenges like intense competition, forex risk, high employee attrition and exposure to policies in key operating markets— Mphasis’ profit margins remain susceptible to the pricing pressures and wage inflation because it operates in the intensely competitive IT services industry. Moreover, its revenues and margins are exposed to forex risks as revenues are derived from the international market. Nonetheless, its hedging mechanisms mitigate this risk to some extent. Further, being in a highly labour-intensive business, the availability and retention of a skilled workforce continues to remain a key challenge. Moreover, Mphasis derived about 58-59% of its revenues from its top 10 clients during FY2023 and Q1 FY2024, thereby signifying moderate customer concentration risk. However, its established and strategic association with its clients mitigates the concentration risks to an extent. Also, the company’s engagement with its clients span across multiple projects, which provides further protection from concentration risks.

Liquidity position: Strong

Mphasis’ liquidity position is **strong**, supported by healthy internal accrual generation, sizeable cash and liquid investment of ~Rs. 2,781 crore, as on June 30, 2023. Moreover, the company has significant buffer in the form of undrawn working capital limits (as of August 2023). Despite the high dividend pay-outs and share buybacks, the company’s liquidity position has remained strong on the back of healthy operating cash flows.

ESG and Social Risk

Environmental concerns — Given its service-oriented business, Mphasis’ direct exposure to environmental risks as well as those emanating from regulations or policy changes is not material.

Social concerns — Like other Indian IT service companies, Mphasis faces the risk of data breaches and cyber-attacks that could affect the large volumes of customer data that it manages. Any material lapses on this front could result in substantive liabilities, fines, or penalties and reputational impact. Also, the company remains exposed to the risk of changes in immigration laws in the key developed markets where it provides its services. Any such changes could have the effect of heightening the competition among IT players for skilled workforce, leading to higher attrition rates and may have an adverse impact on profitability. Managing various facets of human capital, including skills, compensation, and training, is in any case a key differentiating factor among IT companies.

Rating sensitivities

Positive factors – Improvement in the scale of operations coupled with sustained improvement in earnings, while maintaining its credit metrics, would be a positive trigger.

Negative factors – Sharp deterioration in its financial profile emanating from weak end-user demand and/or higher than expected dividend outflow, or any strategic acquisition will be a trigger for a rating downgrade. Specific credit metrics that could lead to a rating downgrade 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 –Information Technology (Services)
Parent/Group support	Not Applicable
Consolidation/Standalone	ICRA has considered the consolidated financials of Mphasis for arriving at the ratings.

About the company

Mphasis is a mid-sized IT company primarily engaged in providing IT/ ITeS/ BPO services to clients in the banking and capital markets, emerging industries, information technology, communication, logistics, entertainment, and insurance sectors. The company derives its revenues primarily from software services and projects, licensing arrangements and application services, infrastructure outsourcing services, as well as from BPO operations. Headquartered in Bangalore, the company enjoys a presence across US, Europe, Australia, Asia Pacific, Japan and India.

The company was incorporated in August 1992 as BFL Software Limited. It was renamed as Mphasis BFL Limited in July 2000, after the merger of the US-based IT consulting company, Mphasis Corporation (founded in 1998), and BFL Software Limited. In June 2006, Electronic Data Systems Corporation (EDS) acquired Mphasis; and later when EDS was acquired by Hewlett-Packard (HP), Mphasis became a 60.47% subsidiary of HP. However, in September 2016, the global private equity major, the Blackstone Group, acquired HP’s stake for a consideration of Rs. 7,071 crore through an SPV—Marble Pte II Limited. In Q1 FY2018, Blackstone reduced its stake to 52.3% before increasing it to 56.12% in Q4 FY2020. In FY2022, Marble Pte II Limited’s stake was acquired by another entity of the Blackstone Group, BCP Topco IX Pte. Ltd. As of June 30, 2023, the Blackstone Group held 55.58% stake in Mphasis through the same entity.

Key financial indicators (audited)

Mphasis - consolidated	FY2022	FY2023
Operating income	11,961.4	13,798.5
PAT	1,430.9	1,637.9
OPBDIT/OI	17.7%	17.6%
PAT/OI	12.0%	11.9%
Total outside liabilities/Tangible net worth (times)	0.5	0.4
Total debt/OPBDIT (times)	0.6	0.4
Interest coverage (times)	28.5	25.0

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; Note: PAT is after exceptional losses and Debt includes lease liability; Financial ratios in the report are ICRA adjusted figures and may not be directly comparable with results reported by the company in some instances

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2024)		Chronology of rating history for the past 3 years					
		Amount rated (Rs. crore)	Amount outstanding as of Sep 15, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022		Date & rating in FY2021	
				Oct 06, 2023	Aug 29, 2022	Sep 30, 2021	Jun 17, 2021	Apr 7, 2020	
1	Fund based/Non-fund based facilities	Long term and short term	1,600.0	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	-
2	Non-fund based facilities	Long term and short term	-	-	-	-	-	-	[ICRA]AA+ (Stable)/ [ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/ Short -term – Fund-based/Non-fund Based Facilities	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 analysing 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 are available on ICRA's website: [Click Here](#)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund based/Non-fund based facilities	NA	NA	NA	1,600.0	[ICRA]AA+(Stable)/ [ICRA]A1+

Source: Company

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

Annexure II: List of entities considered for consolidated analysis

Company Name	Mphasis Ownership	Consolidation Approach
Mphasis Corporation	100%	Full Consolidation
Mphasis Deutschland GmbH	91%	Full Consolidation
Mphasis Australia Pty. Ltd	100%	Full Consolidation
Mphasis (Shanghai) Software & Services Company Ltd	100%	Full Consolidation
Mphasis Consulting Limited	100%	Full Consolidation
Mphasis Belgium BV	100%	Full Consolidation
Mphasis Europe BV	100%	Full Consolidation
Mphasis Pte Limited	100%	Full Consolidation
Mphasis UK Limited	100%	Full Consolidation
Mphasis Software and Services (India) Private Limited	100%	Full Consolidation
Msource Mauritius Inc	100%	Full Consolidation
Msource (India) Private Limited	100%	Full Consolidation
Mphasis Ireland Limited	100%	Full Consolidation
Mphasis Lanka (Private) Limited	100%	Full Consolidation
Mphasis Infrastructure Services Inc	100%	Full Consolidation
Mphasis Poland s.p.z.o.o.	100%	Full Consolidation
PT. Mphasis Indonesia	100%	Full Consolidation
Mphasis Wyde Inc.	100%	Full Consolidation
Wyde Corporation Inc.	100%	Full Consolidation
Mphasis Wyde SASU	100%	Full Consolidation
Wyde Solutions Canada Inc.	100%	Full Consolidation
Mphasis Philippines Inc	100%	Full Consolidation
Digital Risk LLC.	100%	Full Consolidation
Digital Risk Mortgage Services LLC	100%	Full Consolidation
Investor Services, LLC	100%	Full Consolidation
Digital Risk Valuation Services, LLC	100%	Full Consolidation
Stelligent Systems, LLC	100%	Full Consolidation
Datalytx Limited	100%	Full Consolidation
Datalytx MSS Limited	100%	Full Consolidation
Dynamyx Limited	100%	Full Consolidation
Blink Interactive, Inc	100%	Full Consolidation
Mphasis Solutions Services Corporation	100%	Full Consolidation
Mrald Limited	51%	Full Consolidation
Mrald Services Limited	100%	Full Consolidation
Mphasis Digi Information Technology Services (Shanghai) Limited	100%	Full Consolidation

Source: Mphasis Limited Annual Report – FY2023

Note: ICRA has taken a consolidated view of the parent (Mphasis), its subsidiaries and associates while assigning the ratings.

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About ICRA Limited:

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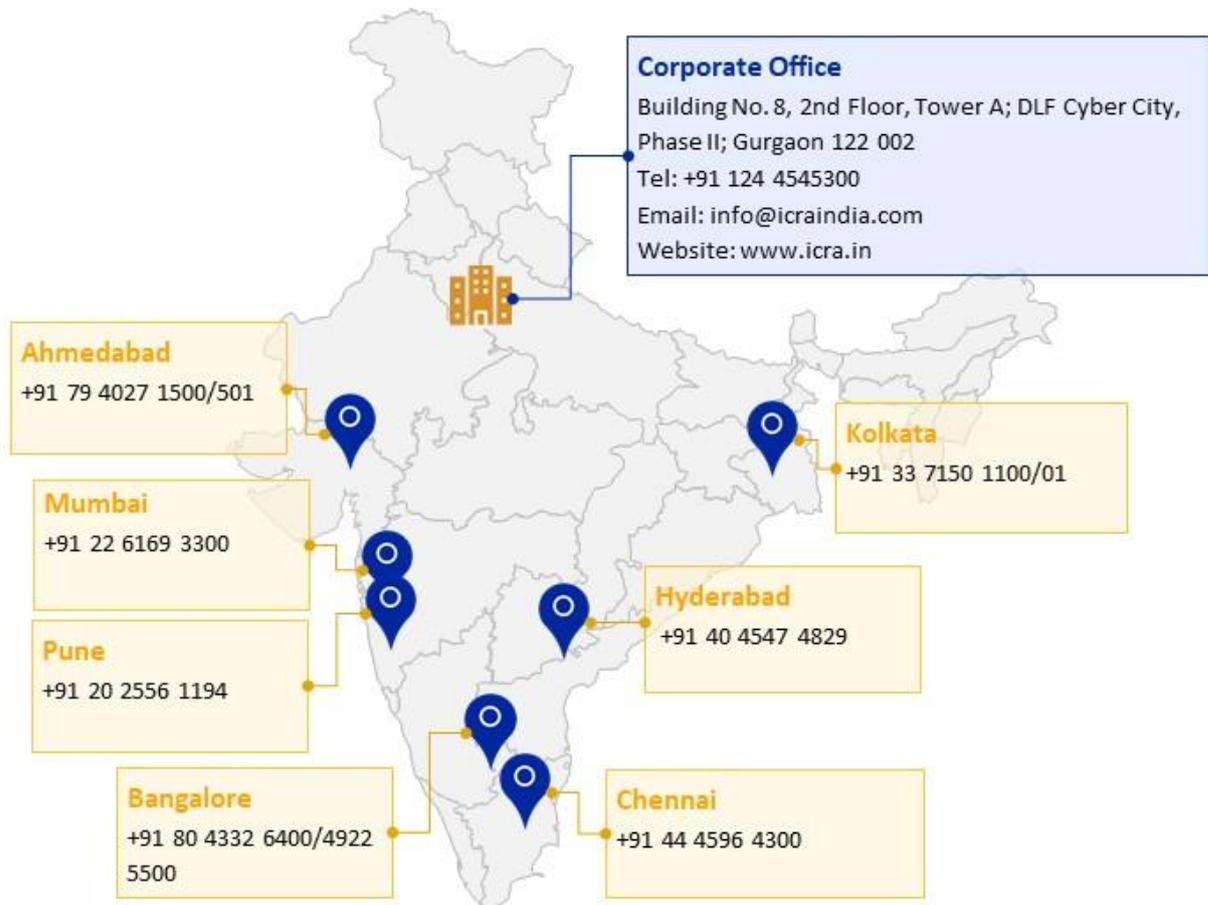
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