September 30, 2024

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	95.00	135.00	[ICRA]A+ (Stable)/ [ICRA]A1; reaffirmed/assigned
Total	**95.00**	**135.00**	

**Instrument details are provided in Annexure-I*

Rationale

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

The ratings action factors in the Group's established business position as the third-largest domestic player in the fragmented manpower staffing industry, and its reputed and diversified client base of large companies across end-user industries like telecom, BFSI (Banking, Financial Services and Insurance), ITeS, retail, e-commerce, etc. The Group reported a modest revenue growth of ~2% in FY2024, primarily due to demand decline across the global technology solution (GTS) segment (mainly IT staffing) and modest growth in the general staffing segment. The GTS segment's share in the overall revenues declined to 7% in FY2024 from 11% in the previous year due to reduced hiring by IT sector clients amid slowdown in growth momentum of the industry. Consequently, the operating margins also moderated to 1.9% in FY2024 from 2.9% in the previous year as the margins of the GTS segment are significantly higher than the general staffing segment. Notwithstanding the same, the company continued to maintain its healthy financial profile, characterised by negative net debt position, comfortable debt protection metrics and strong liquidity position. ICRA expects the Group to sustain its revenue growth and margins over the medium term, while maintaining strong credit metrics, supported by the overall growth in the Indian economy, leading to an increase in employment levels, especially in the organised markets. Moreover, to support future growth and augment its service offerings/sectoral presence, the Group is expected to continue to spend on its inorganic growth initiatives. ICRA has also noted the risks arising out of the expected planned acquisitions by the Group and the likely cash outflow to fund those acquisitions. As the same are expected to be funded through existing surplus funds, the capital structure and the debt protection metrics are unlikely to be affected.

Additionally, ICRA has noted the receipt of the NCLT (National Company Law Tribunal) order by the Group to merge some of its subsidiaries, which once completed, is expected to result in some operational and cost synergies.

However, the ratings are constrained by the inherently low profit margins and high attrition in the general staffing segment (contributes ~90% to the Group's total revenues), and intense competition in the fragmented manpower outsourcing industry as a major portion is provided by the unorganised sector, constraining pricing flexibility to an extent. However, increasing compliances toward regulatory requirements led companies to move towards the organised sector, which provides better revenue visibility. ICRA has also noted the risks arising out of inorganic expansions as the company continues to look for acquisitions. ICRA notes that some other leading industry participants have received notices from the income tax (IT) department towards disallowance of benefits under section 80JJAA of the IT Act, 1961. Any future action of similar nature by the department under this section on the Group or across the industry, will remain a key monitorable.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company and the Group will maintain its strong credit profile and liquidity position, supported by healthy internal accrual generation and continued net debt-free status.

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 a market share of 1.7%[1] 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 1,21,218 as on March 31, 2024. The Group has a pan-India presence with over 50 branch offices for sourcing and recruitment in 75 cities. Going forward, a steady growth in the employee base, increased focus towards the more margin-accretive IT and professional/industrial staffing and planned inorganic growth acquisitions are expected to support the Group's revenue increase and margin expansion.

Diversified and established client base – The Group has a diversified geographical footprint with its client base consisting of top multinational firms from diversified industries such as telecom, BFSI, retail and e-commerce, etc. As on March 31, 2024, it serves 1,261 clients across industries in the domestic market. Under the general staffing segment, the Group has adopted the collect-and-pay model (for ~60% of its billing) for most of its customers, wherein the salaries of the associate employees deployed to its customers are collected in advance and are then paid to them. If credit period is allowed to customers (IT staffing), the Group has an understanding with most of its customers that it will not do funding for the second month. This reduces the risk of bad debt and lowers the Group's working capital requirements.

Healthy financial profile of the Group – The Group reported some moderation in revenue growth and the operating margins in FY2024. Notwithstanding the same, its financial risk profile remained healthy, supported by its strong net worth of Rs. 519.8 crore as on March 31, 2024, net debt negative status and comfortable liquidity position, as marked by sizeable cash/bank balances and cushion in the form of undrawn bank lines. Going forward, ICRA expects the overall financial profile to remain healthy, given higher revenue growth, healthy cash and bank balance, supported by stable cash flow generation, and no material increase in its leverage levels despite payouts against planned acquisitions.

Credit challenges

Inherently thin operating margin in general staffing business – The Group's operating margins are inherently thin (1.9% in FY2024) due to the high share of revenues from the general staffing segment (90% of revenue), wherein the Group mainly adopts cost-plus mark-up model for pricing its customers. The mark-up is usually 4-5% on the employee cost or on a per-employee basis. Due to low mark-up in the general staffing industry, players generally have a low gross margin of about 4-5% and an operating margin of 1.5-2%. Further, intense competition limits pricing flexibility in the general staffing business. However, the margins are considerably higher in the specialised staffing segments like IT staffing, which generates 7-8% of the Group's revenue.

Intense competition in the fragmented manpower outsourcing industry and high attrition risks – The staffing industry is a fragmented market, where the top five players together have a market share of 13.8%[1], and includes considerable number of unorganised players, which offer services at low prices. Consequently, competition continues 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 Group, which is the third-largest organised player in the staffing industry. Inherent to the industry, the Group witnesses high employee attrition owing to low skill/entry level and the temporary nature of the jobs.

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[1] *Source: DRHP of First Meridian*

Liquidity position: Strong

The Group's liquidity is strong with healthy cash flow from operations, no long-term debt repayment obligations and healthy cash and cash equivalent of ~Rs. 234 crore and unutilised bank limits of ~Rs. 85 crore as on July 31, 2024. The utilisation increases during mid-month for paying associate salaries under the cost-and-pay model, which moderates the liquidity buffer to an extent during that period. Overall, ICRA expects the Group's liquidity position to remain strong, despite an expected cash outflow of Rs. 70-80 crore in FY2025 towards planned acquisitions.

Rating sensitivities

Positive factors – The ratings could be upgraded, if the company demonstrates a healthy revenue growth, led by diversification in its business profile with improvement in margins on a sustained basis, while maintaining healthy credit metrics and liquidity position.

Negative factors – Pressure on the ratings could arise, if there is any significant contraction in revenues and margins or any debt-funded acquisition that could lead to a deterioration in its liquidity and debt protection metrics, on a sustained basis. Specific credit metrics that could lead to ratings downgrade include Net Debt/OPBITDA of more than 1.5 times, on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not applicable
Consolidation/Standalone	Consolidated

About the company

First Meridian was formed on 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 five subsidiaries and two step-down subsidiaries.

The Group provides a 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-term 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 was acquired by First Meridian in June 2018. The company is mainly involved 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)

First Meridian Business – Consolidated	FY2023	FY2024*
Operating income	3606.3	3689.5
PAT	81.0	27.4
OPBDIT/OI	2.8%	1.9%
PAT/OI	2.2%	0.7%
Total outside liabilities/Tangible net worth (times)	1.2	1.0
Total debt/OPBDIT (times)	0.8	0.8
Interest coverage (times)	14.7	9.7

*Source: Company, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore*

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 year			Chronology of rating history for the past 3 years					
	FY2025			FY2024		FY2023		FY2022	
	Type	Amount Rated (Rs Crore)	Sep 30, 2024	Date	Rating	Date	Rating	Date	Rating
Fund Based Working Capital	Long-term/ Short - term	135.00	[ICRA]A+ (Stable)/ [ICRA]A1	Jun 12, 2023	[ICRA]A+ (Stable)/ [ICRA]A1	Jun 23, 2022	[ICRA]A (Stable)/ [ICRA]A1	Apr 08, 2021	[ICRA]A (Stable)/ [ICRA]A1

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/ Short -term – Fund Based Working Capital	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	**Working Capital**	NA	NA	NA	135.00	[ICRA]A+ (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	First Meridian Ownership	Consolidation Approach
Innovsource Services Private Limited	100.0% (Rated entity)	Full Consolidation
Innovsource Facilities Private Limited	100.0%	Full Consolidation
FirstMeridian Global Services Private Limited (formerly known as V5 Global Services Private Limited)	100.0%	Full Consolidation
Affluent Global Services Private Limited	100.0%	Full Consolidation
CBSI India Private Limited	100.0%	Full Consolidation
Rlabs Enterprise Services Limited	100.0%	Full Consolidation
Surge Forth Technologies Private Limited	51.0%	Full Consolidation

Source: Company data

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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.

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