PRESS RELEASE
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Indian IT services industry to record muted revenue growth of 4-6% in FY2025: ICRA

- ***Nevertheless, industry's operating profit margin (OPM) to remain healthy at ~22% in FY2025***

ICRA expects the Indian IT services industry to see a second consecutive year of mild revenue growth, estimated at 4-6% in FY2025. Despite persisting challenges, ICRA projects the industry's operating profit margin (OPM) to remain healthy at ~22% in FY2025, with attrition levels having declined considerably and expected to stabilise over the near term. Despite expectations of continued subdued growth, ICRA maintains its Stable outlook on the Indian IT services industry, led by a well-established business position, expectation of healthy earnings and cash flow generation, and strong balance sheets of the industry players.

Commenting on the near-term expectations of industry performance, **Deepak Jotwani, Vice President & Sector Head – Corporate Ratings, ICRA**, said: *"ICRA expects FY2025 to be the second consecutive year of muted revenue growth (for its sample set companies), estimated at 4-6%, given the lower discretionary technological spends by clients amidst persistent macro-economic uncertainty in the key markets of the US and Europe. Higher inflation and interest costs have exerted pressure on clients across key industries, with an increasing focus on cost optimisation/ business critical projects, and deferment of large discretionary spends. Though the revenue conversion of the orders has slowed down, the order book and deal pipeline of most IT services companies remains strong. This, coupled with the increasing prominence of technological spend by clients as part of their overall capital allocation strategy, is expected to support the growth momentum once the macroeconomic headwinds subside over the medium term*."

Revenue growth for the Indian IT services companies has remained tepid in the last five-six quarters as the industry continues to face challenges from macro-economic headwinds in key markets. Accordingly, ICRA's sample set companies[1] recorded a modest YoY growth of ~5.5% in revenues in USD terms in FY2024, against 9.2% in FY2023.

"*Despite tepid revenue growth*, *ICRA expects the OPM for its sample set companies to remain healthy at ~22% in FY2025, supported by easing out of wage cost inflation and optimisation of operational efficiencies",* **Jotwani** said.

In terms of geographic split of revenues, the Indian IT services industry generates a lion's share from the US, followed by Europe and the Rest of the World (RoW) markets. ICRA's sample set companies generated 55-60% of its Q1 FY2025 revenues from the US, 22-25% from Europe, and the balance from the RoW markets. Thus, the industry remains susceptible to macroeconomic uncertainties and any adverse regulatory changes in these markets, for example, the revenue growth from the US witnessed a sharp moderation in recent quarters as macroeconomic headwinds continue to intensify. However, despite the moderation, growth in Europe has been more resilient compared to the US.

Higher adoption of generative AI (Gen-AI) remains a key monitorable for the industry, over the medium to long term. Leading Indian IT services companies have trained a sizeable portion of their employee base in Gen-AI skills and have already started ramping up their capability and service offerings, to deliver AI-based solutions to their clients. While the order book or revenue contribution from Gen-AI deals so far is limited, it is likely to pick up over the medium term as overall technology adoption is more pervasive.

[1] Leading 15 large and medium sized listed Indian IT services companies

Moderation in demand, coupled with the increase in utilisation of excess manpower capacity added in FY2023 has exerted pressure on hiring by IT services companies in recent times. This is demonstrated by negative net addition for the past seven quarters for the sample set companies. While the level of negative net addition declined considerably in Q1 FY2025, ICRA expects hiring to remain muted in the near term until the growth momentum picks up materially. Earlier, hiring by IT services companies was at an all-time high in FY2022 and H1 FY2023, buoyed by strong demand for digital technologies and to combat the surge in attrition levels. Moreover, there has been a steady decline in the last twelve-month (LTM) attrition for ICRA's sample set companies over the last five quarters. "*The LTM attrition for ICRA's sample set companies tapered significantly to 13.1% in Q1 FY2025 from 23.2% in Q2 FY2023 as the overall slowdown in growth momentum and strong hiring in the previous fiscal corrected the demand-supply mismatch witnessed earlier. ICRA expects attrition levels to stabilise at a long-term average of 12-13% in FY2025,*" **Jotwani** added.

Despite continued substantial dividend pay-outs/share buybacks and inorganic investments, ICRA expects the financial profile of the majority of the industry players to remain strong, supported by healthy cash flow generation, lower debt, and robust liquidity.

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