



The Pakistan Credit Rating Agency Limited

Rating Report

Service Long March Tyres (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jun-2023	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Service Long March Tyres (Private) Limited ('SLM Tyres' or 'the Company') is a private limited concern specialized in the manufacturing and marketing of radial tyres for trucks & buses. SLM Tyres is the first All-Steel Radial Tyres manufacturing facility in Pakistan with complete transfer of technology from the commencement of the project. The Company is a joint venture arrangement between Service Industries Limited (SIL), Chaoyang Long March Tyre Company Limited (LM), and Myco Corporation Pakistan. The ratings draw direct comfort from longstanding position of SIL in Pakistan and LM in China – a leading Chinese manufacturer of all-steel radial tyres. Total estimated cost of project stands at USD 300mln with targeted production capacity of 2.4mln tyres per annum. The manufacturing facility is being set up in three phases: phase 1 with annual tyre production of 0.74mln, phase 2 of 1.2mln, and phase 3 of 2.4mln. At present, its production capacity utilization stands at ~30pc. The capacity is likely to ramp up in upcoming years considering the solid expansion plans and rising demand of radial tyres for trucks & buses segment in Pakistan. Tyre demand is primarily governed by replacement market followed by automobile OEMs. Intense competition from imported tyres necessitates high quality products at affordable prices. SLM Tyres intends to build its clientele base across the globe through channeling high-quality radial tyres and affirmation of multi-brand names under its sponsorship. The project has been set up in S.I.T.E Area, Nooriabad, Sindh. During Mar'22, the Company officially commenced its commercial production to serve local demand of radial tyres along with seeking benefits from export avenues to multiple countries. SLM Tyres has built a nationwide marketing and distribution channel. In radial tyres segment, the Company faces direct competition from imported and grey market tyres. With successful completion of Phase 1, the Company has registered significant growth of ~570.2% with topline clocked at ~PKR 10.7bln during end of 9MFY23. Its profitability matrix shall start to materialize in near future with each step towards running operations and completion of project. Financial risk profile is demonstrated by adequate capital cycle, low coverages, & leveraged capital structure. Going forward, the cash flows requirement for the development of project is planned to be met through direct support from Sponsors and working capital lines from banks. As of now, SLM Tyres has availed loans at concessionary rates to support project growth.

The ratings are dependent on the Company's ability to maintain a robust financial discipline. Moreover, the achievement of breakeven point and commensurate profit growth shall remain imperative.

Disclosure

Name of Rated Entity	Service Long March Tyres (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-22),Methodology Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology Rating Modifiers(Jun-22)
Related Research	Sector Study Tyres(Oct-22)
Rating Analysts	Iqra Toqeer iqra.toqeer@pacra.com +92-42-35869504

Profile

Legal Structure Service Long March Tyres (Private) Limited ('SLM Tyres' or 'the Company') was incorporated on January 7th, 2020 in Pakistan as a private limited entity under the Companies Act, 2017. SLM Tyres is the first greenfield project in Pakistan to manufacture All-Steel Radial Tyres. The Company's registered office is located at Service House, Main Gulberg, Lahore.

Background SLM Tyres is a subsidiary entity of Service Industries Limited (SIL). SIL entered into a joint venture agreement with Chaoyang Long March Tyre Company Limited – a Chinese Company and with Mr. Shabir Ahmad of Myco Corporation, Pakistan to establish Pakistan's first Radial Tyres manufacturing facility in Sindh Industrial Trading Estate (S.I.T.E), Nooriabad, Sindh. Commercial production of the project commenced in March 2022.

Operations The Company uses latest technology known as All Steel Radial manufacturing with complete in-house research facilities and capability to manufacture finished product from scratch. The Company's manufacturing facility is being developed in three phases with a total annual production capacity of 2.4 million tyres. Phase 1 has an annual production capacity of 0.74 million tyres, which has already been completed and is operational. In terms of phase 2 and 3, the Company plans to complete them in coming years. As of now, SLM Tyres capacity utilization has been reported to be around 30%.

Ownership

Ownership Structure SLM Tyres is a joint venture between Chaoyang Long March Tyre Company Limited (~44%), Service Industries Limited (~32.09%), Service Global Footwear Limited (~18.91%), and Mr. Shabir Ahmad (~5.0%).

Stability Ownership structure seems stable as no major change in the pattern of shareholding is expected in near future. Major stake of ~51% rests with the entities of Service Group.

Business Acumen Service Group and Chaoyang Long March Tyre Co. Ltd. (prime sponsors of SLM Tyres) are considered to have strong business acumen. Both of them have been operating in and outside their regions for a number of decades.

Financial Strength SLM Tyres being the entity of Service Group maintains healthy financial profile with substantial access to domestic and international markets. This indicates Sponsors' ability to provide support is considered good, if need arises.

Governance

Board Structure The board of SLM Tyres comprises nine members, including Chairman – Mr. Li Qingwen, CEO – Mr. Omar Saeed, and seven Non-Executive Directors – Mr. Arif Saeed, Mr. Hassan Javed, Mr. Chaudhry Ahmed Javed, Mr. Badar Ul Hassan, Mr. Zhang Xingyou, Mr. Yang Shuping, and Mr. Jin Yongsheng. There are no independent directors on the board.

Members' Profile Five members involved in the business are representatives of Service Group whereas remaining four members are representatives of Chaoyang Long March Tyre Company – a leading Chinese manufacturer of radial tyres. All the directors on the board have related industry exposure of more than two decades.

Board Effectiveness The board has formed no sub-committees, thus hampering effective governance. However, board meetings are held quarterly in compliance with the principles of corporate governance, and all meeting minutes are documented properly.

Financial Transparency M/S. Riaz Ahmad and Co., SBP category 'A' auditor, is the external auditor of the Company. The auditors expressed an unqualified opinion on the Company's financial statements for period ending June 30th, 2022.

Management

Organizational Structure A well-defined organizational structure exists in the Company. All the functions are reporting directly or indirectly to the CEO. These are : 1) Commercial & Sales, 2) Technical, 3) Production Operations, 4) Finance & Accounts, and 5) Support Services. Each department is headed by a qualified HOD.

Management Team Mr. Omar Saeed, the CEO of SLM Tyres, is a graduate of Brown University and he did his Master's in Business Administration from Harvard Business School. Mr. Omar has also served as the CEO of Service Industries Limited (SIL) from 2011 to 2018 Boards of various private and public companies in the past. The other key members involved in the business are also thorough professionals with multiple years of experiences in diversified sectors.

Effectiveness With the support of an experienced team of professionals, SLM Tyres is building up the business strengths and increasing its foot print across different cities of Pakistan, and also tends to reach export markets in near future.

MIS The Company is presently using Oracle EBS ERP. It has multiple operational modules to keep track of daily and monthly reports required by the management to ensure level of effectiveness.

Control Environment For operational efficiency and appraisal of internal controls, the Company has in-house team of qualified professionals at all levels to implement and monitor the policies and procedures. SLM Tyres has an effective mechanism for identification, assessment and reporting of all types of risk arising out of the business operations.

Business Risk

Industry Dynamics In FY22, Pakistan's tyre sector made an estimated sale of ~44mln units (FY21: ~41mln units), depicting a growth rate of ~8% YoY. The tyres sector in Pakistan can be broadly segmented into the OEM and replacement markets. The average share of replacement market is ~80%. The major raw material used in the production of tyres is rubber, both natural and synthetic. In FY22, rubber imports grew exorbitantly by ~57% quantity wise, while in PKR terms, the imports went up by ~23%. The market for radial tyres in Pakistan's trucks and buses segment has been experiencing steady growth over the years. The sector is experiencing a gradual shift towards radial tyres due to their superior performance, longer lifespan, better fuel efficiency, and improved safety.

Relative Position Service Long March Tyres (Pvt.) Limited is Pakistan's first All-Steel Radial Trucks & Buses Tyres manufacturer to successfully launch a greenfield project. The Company is emerging its presence in the country's radial tyres market for commercial vehicles.

Revenues The commercial production of the project commenced in March, 2022. With its first phase came online, the Company reported topline of PKR 2,127mln in FY22 whereas it has registered significant growth of ~570.2% at end of 9MFY23 with topline clocked at PKR 10,694mln.

Margins During 9MFY23, the Company's gross margin stood at 4.0% with gross profit reported at PKR 430mln (FY22: PKR 99mln). For 9MFY23, the bottom-line of the Company stands at negative PKR 860mln (FY22: negative 334mln). Net margin stood at -8.0% (FY22: -15.7%).

Sustainability Radial tyres market in Pakistan is highly competitive owing to tyres smuggled through grey channels and large no. of radial tyres imported every year, but SLM Tyres is expected to gain its market share through successfully reaching to its full plant capacity in coming years. A joint venture with Chaoyang Long March Tyre Company shall bring additional support at all levels. The Company intends to emerge its presence as an exporter of radial tyres for commercial MVs.

Financial Risk

Working Capital The Company's capital needs emanate from financing inventories and trade receivables for which it relies initially on both debt and equity. During 9MFY23, gross working capital days stood at ~161 (FY22: ~662 days). Subsequently, net working capital cycle stood at ~116 days at end Mar'23 (FY22: ~396 days).

Coverages During 9MFY23, the Company's free cash flows from operations (FCFO) marked at PKR 796mln (FY22: PKR 205mln) on account of gross profit incurred during corresponding years. As at end Mar'23, interest coverage ratio of the Company stood at 1.0x (FY22: 1.5x) whereas core-debt coverage ratio stood at 0.7x (FY22: 0.6x).

Capitalization As at end Mar'23, the Company held a leveraged capital structure with a ratio of ~54.7% (FY22: ~48.7%) with total borrowings recorded at PKR 14,150mln (FY22: PKR 10,634mln). The Company's debt book is a mix of both long-term and short-term borrowings. The Company has also availed SBP Loans at concessionary rates to support its expansion plans.



Service Long March Tyres (Pvt.) Ltd. Tyres & Tubes	Mar-23	Jun-22	Jun-21	Jun-20
	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	19,307	19,759	11,343	783
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	10,825	7,036	3,760	740
<i>a Inventories</i>	4,618	2,604	-	-
<i>b Trade Receivables</i>	4,074	1,255	-	-
5 Total Assets	30,132	26,795	15,102	1,523
6 Current Liabilities	2,416	3,095	1,259	4
<i>a Trade Payables</i>	1,364	2,159	939	-
7 Borrowings	14,150	10,634	4,834	-
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	1,854	1,867	1,431	-
10 Net Assets	11,713	11,198	7,578	1,519
11 Shareholders' Equity	11,713	11,198	7,578	1,519
B INCOME STATEMENT				
1 Sales	10,694	2,127	-	-
<i>a Cost of Good Sold</i>	(10,263)	(2,028)	-	-
2 Gross Profit	430	99	-	-
<i>a Operating Expenses</i>	(421)	(180)	(15)	(6)
3 Operating Profit	10	(81)	(15)	(6)
<i>a Non Operating Income or (Expense)</i>	7	67	93	32
4 Profit or (Loss) before Interest and Tax	17	(14)	78	26
<i>a Total Finance Cost</i>	(877)	(144)	(0)	(0)
<i>b Taxation</i>	-	(176)	(22)	(8)
6 Net Income Or (Loss)	(860)	(334)	55	18
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	796	205	(42)	(10)
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	796	205	(43)	(10)
<i>c Changes in Working Capital</i>	(6,014)	(3,376)	687	0
1 Net Cash provided by Operating Activities	(5,218)	(3,171)	645	(10)
2 Net Cash (Used in) or Available From Investing Activities	(1,046)	(8,553)	(10,442)	(756)
3 Net Cash (Used in) or Available From Financing Activities	4,860	10,075	12,522	1,501
4 Net Cash generated or (Used) during the period	(1,404)	(1,648)	2,724	735
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	570.2%	N/A	N/A	N/A
<i>b Gross Profit Margin</i>	4.0%	4.7%	N/A	N/A
<i>c Net Profit Margin</i>	-8.0%	-15.7%	N/A	N/A
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	-48.8%	-149.1%	N/A	N/A
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	-10.0%	-3.6%	1.2%	1.2%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	161	662	N/A	N/A
<i>b Net Working Capital (Average Days)</i>	116	396	N/A	N/A
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	4.5	2.3	3.0	199.6
3 Coverages				
<i>a EBITDA / Finance Cost</i>	1.0	1.5	N/A	N/A
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	0.7	0.6	N/A	N/A
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	-286.4	113.6	-115.1	0.0
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	54.7%	48.7%	38.9%	0.0%
<i>b Interest or Markup Payable (Days)</i>	75.5	338.4	N/A	N/A
<i>c Entity Average Borrowing Rate</i>	8.8%	1.7%	0.0%	0.0%

Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	Very high credit quality. Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
AA-	
A+	
A	High credit quality. Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
A-	
BBB+	
BBB	Good credit quality. Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BBB-	
BB+	
BB	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
BB-	
B+	
B	High credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
B-	
CCC	
CC	Very high credit risk. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



*The correlation shown is indicative and, in certain cases, may not hold.

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults, or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

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Note. This scale is applicable to the following methodology(s):
 a) Broker Entity Rating
 b) Corporate Rating
 c) Debt Instrument Rating
 d) Financial Institution Rating
 e) Holding Company Rating
 f) Independent Power Producer Rating
 g) Microfinance Institution Rating
 h) Non-Banking Finance Companies Rating

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ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)

iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).

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(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)

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(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity

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(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)

(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)

(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)

(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(F-VII)

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