Trucks & Buses

An Overview

December 2020

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TRUCKS & BUSES|GLOBAL INDUSTRY

Executive Summary

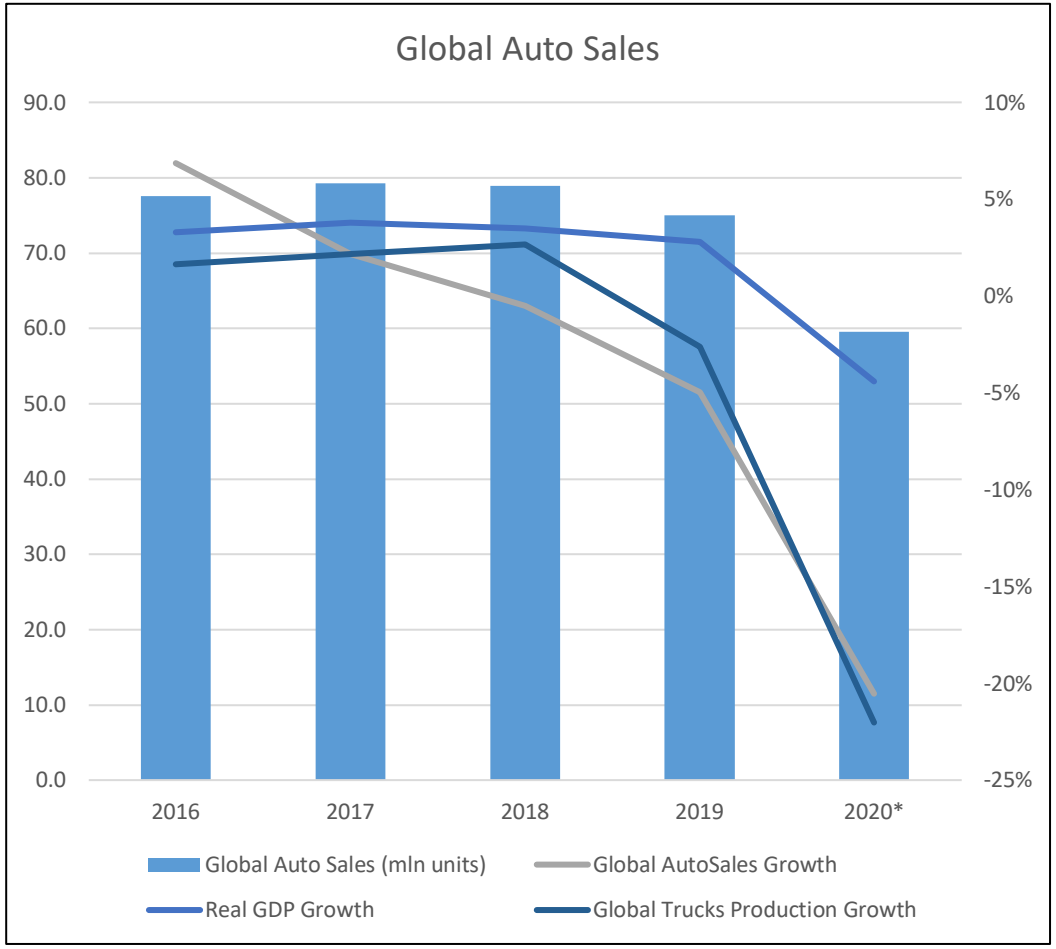
- The **Trucks & Buses** sector comprises entities that are involved in manufacturing, assembling, marketing and distribution of Trucks and Buses.
- The Global Trucks and Buses market generated a revenue of USD~380bln in CY19 contributing ~0.3% to the global GDP.

Trucks:

- Globally, the truck industry is highly concentrated. In the US, the top 20 companies make up ~95% of the entire industry's revenue. Every industry relies on trucking for the delivery of materials. Businesses of all sizes depend on the trucking industry to maintain fast delivery times and deliver products safely. Trucks are responsible for 68% of all freight tonnage in the U.S.

Buses:

- Buses and coaches, across the globe, are one of the prime sources for urban commute and intercity transport. Public transport plays an important role in minimizing the cost of congestion and maximizing economic productivity. By providing an alternative means of travel to private vehicles, public transport has a critical role to play in reducing carbon emissions.



**CY20 figures have been prorated on the basis on 9MCY20 figures.

Source: Macrotrends, Time, Globe News Wire

Region Wise Production

Region wise Production of Commercial Vehicles (units mln)									
Region	CY15		CY16		CY17		CY18		CY19	
China*	5.6	31.1%	5.7	31.1%	5.7	30.5%	5.4	28.1%	5.3	28.3%
North America	4.0	22.2%	4.3	23.5%	4.4	23.5%	4.6	24.0%	4.7	25.1%
Europe	3.2	17.8%	3.4	18.6%	3.5	18.7%	3.6	18.8%	3.5	18.7%
South Asia	2.4	13.3%	2.3	12.6%	2.4	12.8%	2.8	14.6%	2.5	13.4%
Japan & Korea	1.6	8.9%	1.5	8.2%	1.5	8.0%	1.5	7.8%	1.5	8.0%
South America	0.7	3.9%	0.7	3.8%	0.8	4.3%	0.8	4.2%	0.7	3.7%
Middle East & Africa	0.5	2.8%	0.4	2.2%	0.4	2.1%	0.5	2.6%	0.5	2.7%
Total	18.0	100.0%	18.3	100.0%	18.7	100.0%	19.2	100.0%	18.7	100.0%

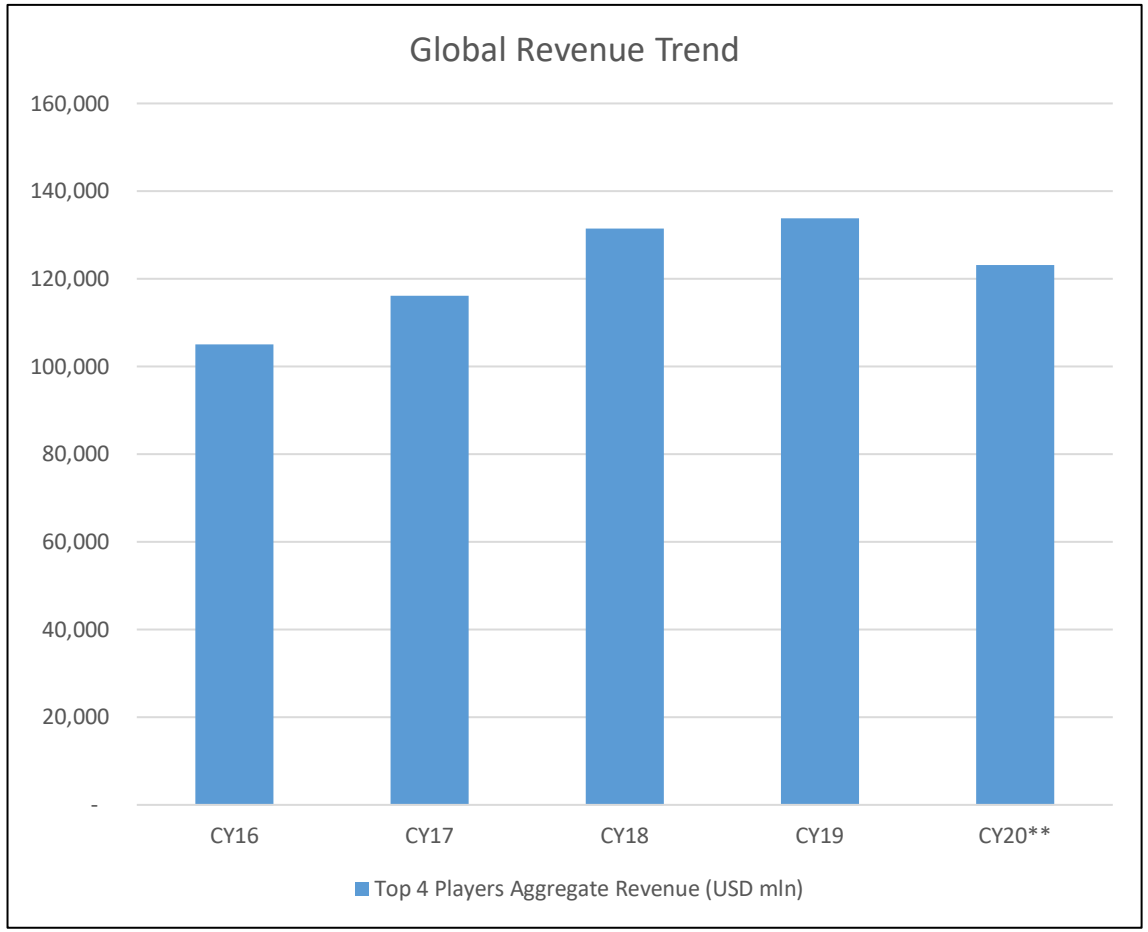
- Trucks and Buses witnessed a production CAGR of 0.77% from CY15 to CY19. Production volumes are forecast to decline by 22% YoY basis in consequence of COVID-19 pandemic.
- In general, most American transit systems expect their buses to have a useful life of 12 years and 250,000 miles. This is because after 12 years, they are eligible to receive replacement bus funding from the federal government. In China bus life expectancy is up to 9 years. Life expectancy is longer in developing countries.

*Includes Macau, Taiwan & Hong Kong

Source: ACEA, Link Springer

Global Market Share

- The global trucks and buses industry is dominated by four major players: Daimler AG (Germany), Volvo Trucks Corporation (Sweden), Volkswagen (Germany)and PACCAR (USA).
- Aggregate revenue of the top 4 players had a sizeable contribution of ~30% to the global trucks and buses market.
- All four top players are aggressively working towards developing environment friendly low emission trucks and buses. Moreover, electric trucks and buses have also been under focus.
- Daimler is leading in battery-electric trucks and has electric trucks in customer use in all segments.



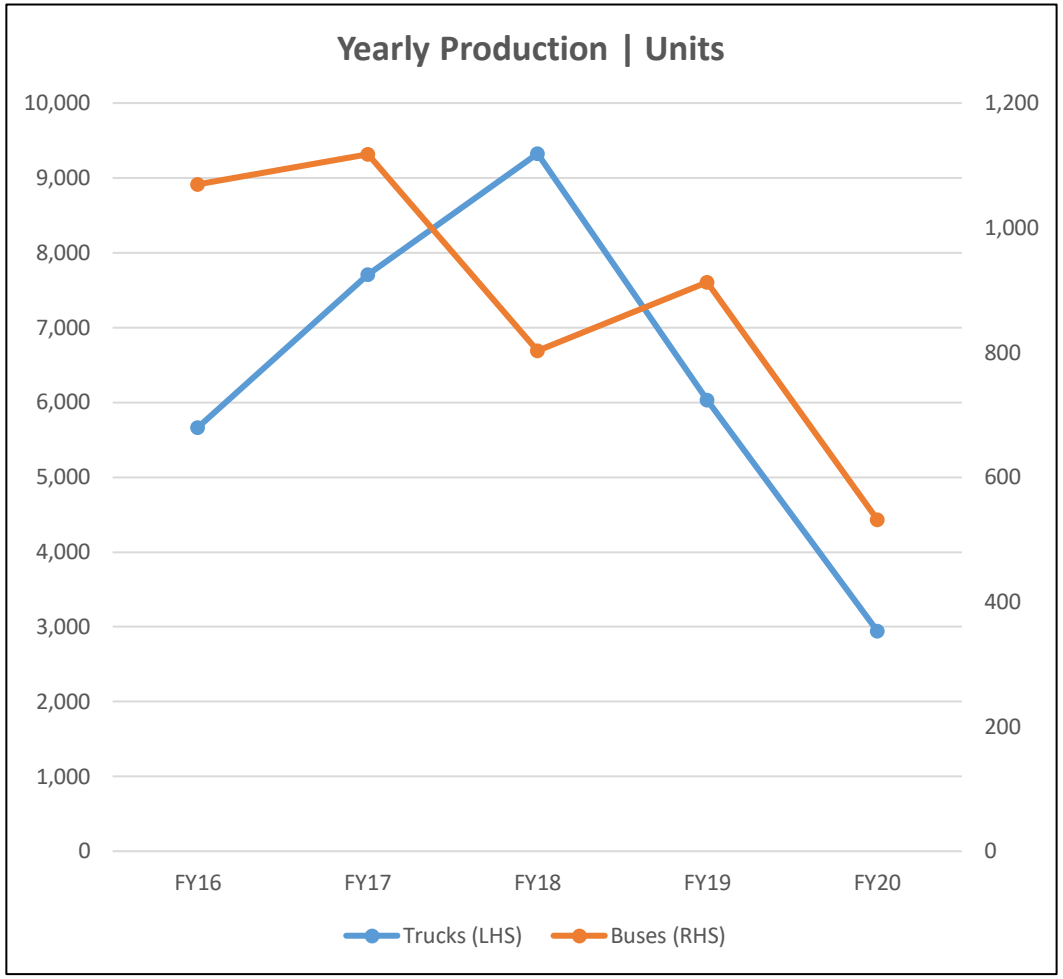
Source: Financial Statements

TRUCKS & BUSES|LOCAL INDUSTRY

Executive Summary

Vehicles On Roads	FY16	FY17	FY18	FY19	FY20*
Trucks	263,800	276,200	280,000	291,200	304,900
Buses	150,600	156,300	159,200	165,600	164,000
Total	**414,400**	**432,500**	**439,200**	**456,800**	**468,900**
**provisional*					

- Large-Scale Manufacturing (LSM) has a contribution of 9.5% to the national GDP (FY20) (~10.2% in FY19). The automobile sector weighs 4.613 in the country's LSM.
- Automobile Sector has been under distress since FY19 due to unfavorable socio-economic indicators which were further aggravated on the outbreak of Covid-19 pandemic in FY20.
- The Trucks and Buses Industry is dominated by top ~7-8 players.
- Despite its economic significance, the growth in trucks and buses industry has remained historically laggard. Trucks and buses are either imported in the country as Completely Built Units (CBU) or imported in parts and assembled locally (Completely knocked down units (CKD)). Localization levels in this segment are still the lowest as compared to other segments of the automobile Industry.



Source: PAMA, Pakistan Economic Survey

Local Players

- All the major players have taken licenses from various international brands and are their authorized assemblers and distributors in Pakistan:
  - Ghandhara Nissan Ltd. is the authorized assembler and manufacturer of Dongfeng, JAC and Renault Trucks vehicles in Pakistan. It previously manufactured Nissan Trucks as well before they were discontinued globally. Ghandhara Industries Ltd. is the authorized assembler and manufacturer of Isuzu vehicles in Pakistan.
  - Hinopak Motors Ltd. is the authorized assembler and manufacturer of Hino vehicles in Pakistan.
  - Master Motors Corporation is the authorized assembler and manufacturer of Daimler Fuso, Foton, Iveco Trucks & Yutong Buses in Pakistan.
  - Al-Haj FAW Motors Ltd. is a subsidiary of Chinese assembler and manufacturer FAW Group.
  - Afzal Motors Ltd. is a distributor and manufacturer of Daewoo, JAC and KING LONG trucks and buses in Pakistan.

DONGFENG Trucks · YUTONG · JAC MOTORS · RENAULT TRUCKS · ISUZU · DAEWOO · HINO

Key Features – Production & Sales

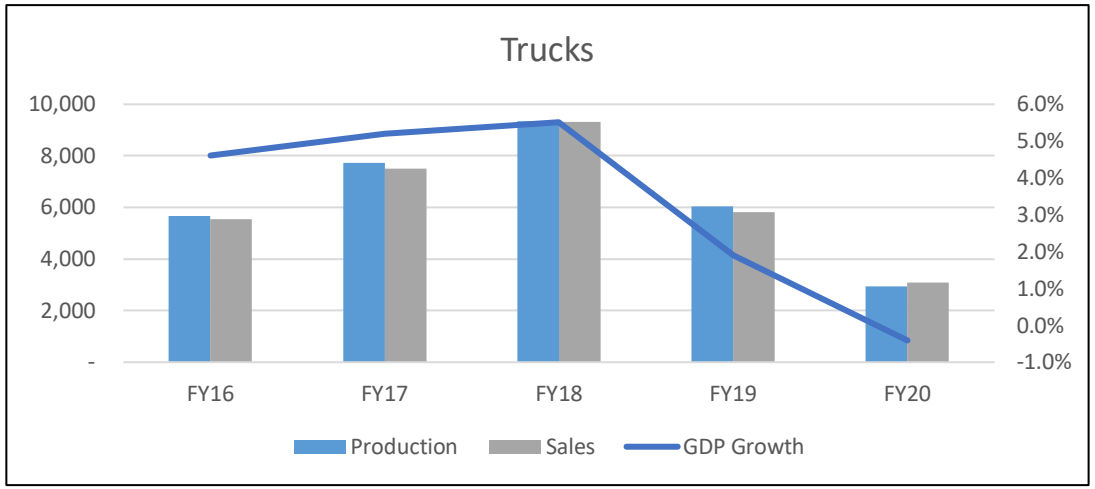
Trucks:

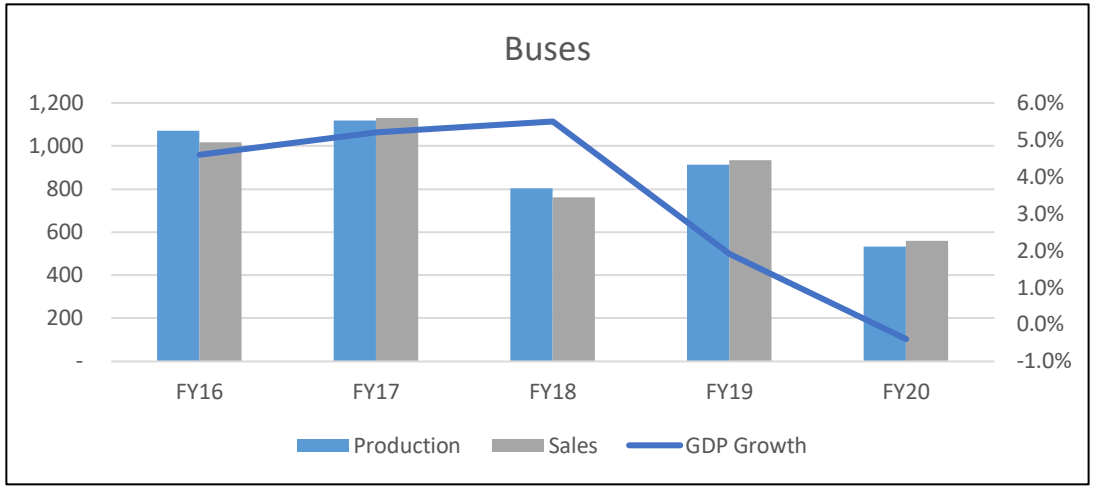
- Production and sales of Trucks reflect a similar pattern to the GDP growth in Pakistan due to their demand arising from growth in development and industrial activities. The production and sales were severely hampered in FY20 due to overall slowdown in the economy activities (~46% decline in 9MFY20 from SPLY). Moreover, the supply of trucks and their respective payments were disrupted due to a halt in government projects. The low capacity utilization among both segments is a result of overall low demand in the country and reliance on imports in CBU form.

Buses:

- Production and sales of buses, however, is largely linked to the growth in travel and tourism Industry. The production and sales witnessed a severe decline of ~33% in terms of production in FY18. This was mainly due to influx of bus imports in Completely Built Unit (CBU) form. The situation improved in FY19 and then took a dip in FY20 owing to COVID-19 (~29% dip in 9MFY20 from SPLY).

		FY18	FY19	9MFY20
Trucks	Installed Capacity	28,500	28,500	28,500
	Capacity Utilized	24%	18%	10%
Buses	Installed Capacity	5,000	5,000	5,000
	Capacity Utilized	11%	13%	9%

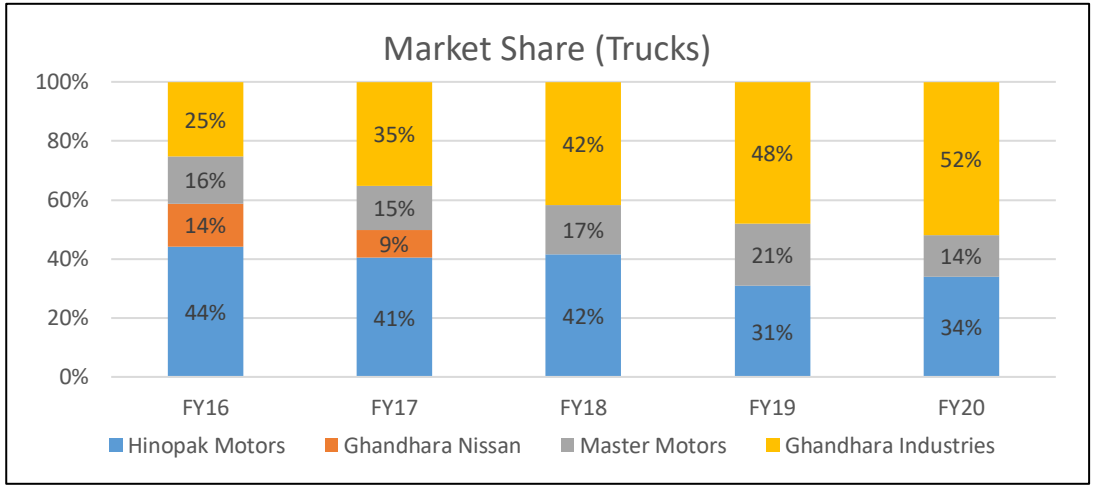


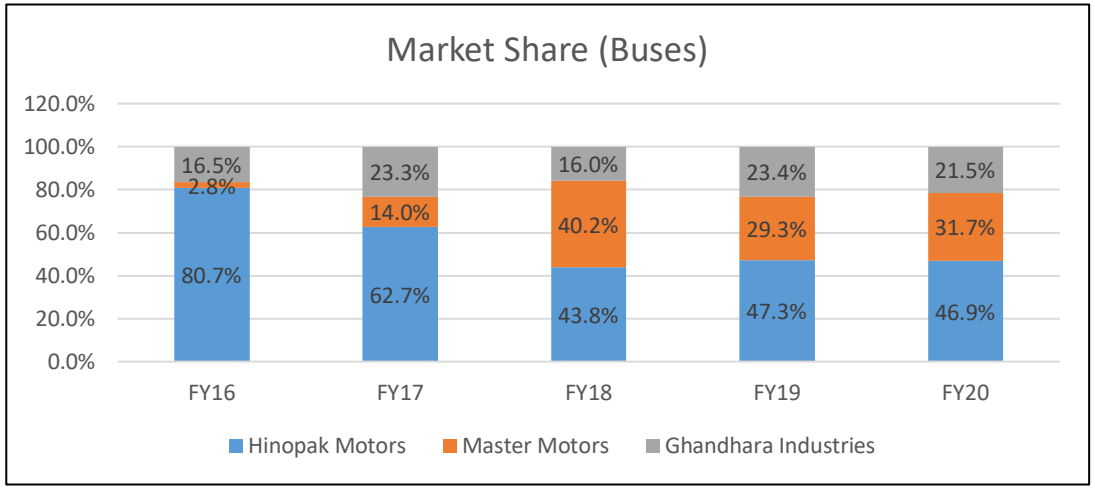


Source: PAMA, Pakistan Economic Survey

Key Features – Competitive Landscape

- Pakistan's trucks and buses industry, like passenger car industry, is dominated by a handful of players including Hinopak Motors, Ghandara Nissan, Ghandara Industries and Master Motors which cumulatively enjoy a sizable market share. Barriers to entry are mainly of technological and capital-intensive nature.
- Ghandhara Industries occupies the highest share in the industry followed by HinoPak and Master Motors.
- Ghandhara Nissan Ltd. terminated assembly of Nissan PKD Trucks in FY17 owing to its discontinuation globally.
- Hinopak has witnessed a decline in its market share as Master and ISUZU Trucks steadily increased their market shares.
- In terms of sales of buses, Hinopak saw a steady decline in production and market share and this too was captured by Master Motors. Although, Hinopak's production declined by almost 50%, it still manages to carry the highest market share buses.





Source: PAMA

Operating Environment - Duties & Taxes

- The sector is regulated by Pakistan Standards and Quality Control Authority. It is an autonomous body subordinate to the Ministry of Science and Technology of the Government of Pakistan.
- Four of the major players are members of the Pakistan Automotive Manufacturers Association which is a trade group of automobile manufacturers that operate in Pakistan. It is the leading advocacy group for the auto industry in Pakistan and is licensed by the Ministry of Commerce under the Trade Organizations Ordinance 2007.
- Custom Duty for Electric truck components and CBUs were introduced recently in the beginning of FY21.
- With respect to income tax, the industry is under Normal Tax Regime (NTR). Further, minimum tax @1.5% of turnover is applicable if tax liability under NTR is lower than minimum tax.

PCT Code	Description	Custom Duty	
Trucks		**FY21**	**FY20**
4011.2011	New pneumatic tires	16%	16%
4013.1010	Inner Tubes	3%	3%
8426.1110	Works trucks fitted with a crane (Not Exceeding 400 metric ton)	11%	11%
8427.1000	Self- propelled trucks powered by an electric motor	0%	0%
8704.1010	Components for assembly/manufacture of Dump trucks designed for off highway use	30%	30%
8704.9020	Components for the assembly / manufacture of Electric trucks, in any kit form	30%	
8704.9030	Electric trucks (CBU)	30%	
Buses			
8702.9020	Components for assembly / manufacture of Fully dedicated LNG/ LPG or CNG buses	20%	20%
8702.9030	Fully dedicated LNG buses (CBU)	20%	20%
8702.9040	Fully dedicated LPG buses (CBU)	20%	20%
8702.9050	Fully dedicated CNG buses (CBU)	20%	20%
8708.2920	Long members for frame	35%	35%

Source: FBR

TRUCKS & BUSES|LOCAL INDUSTRY

Operating Environment – Localization Lagging Behind

- Trucks and buses in Pakistan have the lowest localization levels compared to other segments of the Automobile Industry.
- Both trucks and buses are either only assembled in Pakistan or directly imported in Completely Built-Up form (CBU).
- This is mainly due to the fact that demand for trucks and buses is low on a national level and setting up production plants would require intensive capital investment. This is also partially because of the earlier reliance on policies which promoted an import led economic growth.
- Moreover, the trucks and buses industry has historically been dominated by a few players which have focused primarily on assembling and distribution rather than enhancing local production. However, new entrants in the market in the previous years are expected to lead and promote a greater level of localization among trucks and buses.

Imports and Local Assembling

		FY16	FY17	FY18	FY19	FY20*
Trucks	Imports-CBU	1,398	1,929	1,098	518	175
	Local Assembling (CKD)	5,666	7,712	9,187	6,035	2,732
	Total	**7,064**	**9,641**	**10,285**	**6,553**	**2,907**
Buses	Imports-CBU	1,234	720	685	611	239
	Local Assembling (CKD)	1,070	1,118	784	913	462
	Total	**2,304**	**1,838**	**1,469**	**1,524**	**701**

Localization Levels in Assembling Process

Trucks/Buses	30%
Passenger Cars & LCVs	50-60%
Tractors	85%
Motorcycles	90%

*Provisional

Source: Pakistan Economic Survey

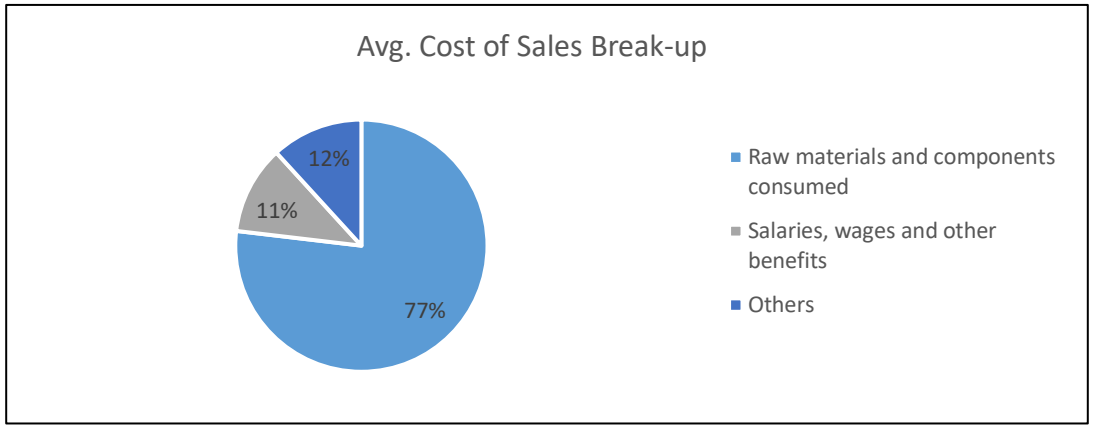
Demand Dynamics

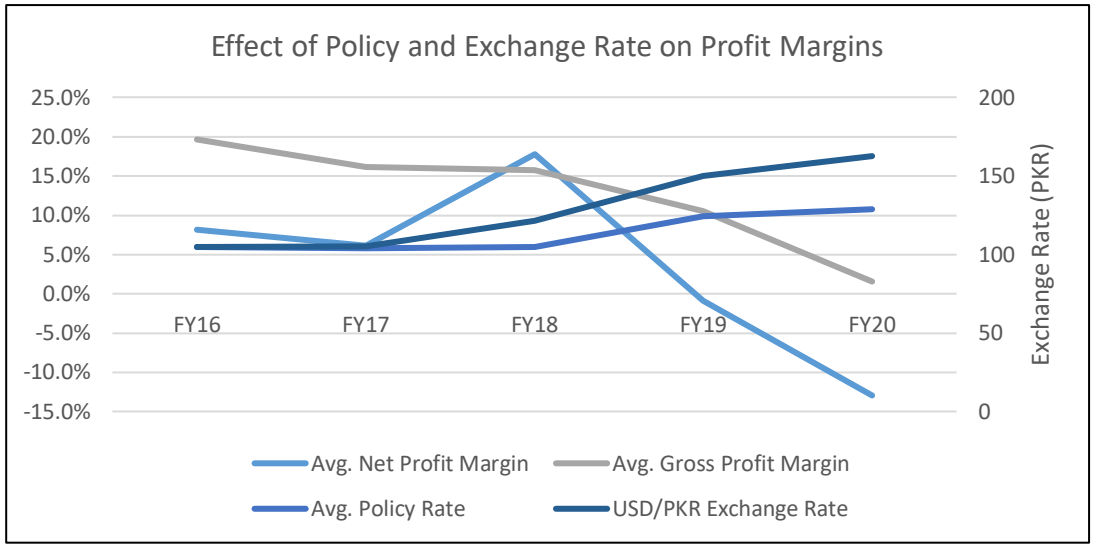
- Demand for buses is driven by investment in public transportation systems. Pakistan is likely to receive funds worth USD 50mln to launch a Green Bus Rapid Transport (BRT) network to run buses on bio-methane that would greatly help reduce air pollution from the port city of Karachi. Another factor that contributes to demand of buses is inter-city transport.
- Demand for trucks at the highest level is impacted by the overall economy. GDP growth, industrial production, retail spending and consumption, inventory restocking, agricultural demand (e.g. produce seasons) and auto production are all factors that drive the demand for trucks.
- The contraction in GDP of -0.4% in FY20 owing to COVID-19 and continued halt in government projects led to a decline of ~40% in production and sales of trucks and buses. However, the production of trucks is expected to rise due to increased economic activity in the country to meet CPEC related material and freight transport needs.
- Owing to the incentives offered by Pakistan Auto Policy 2016-21, more than 12 automakers announced to collaborate with different companies in Pakistan, under the Greenfield as well as Brownfield investment categories. Some of them were not able to materialize and a few were put on hold due to various reasons including country's volatile economic conditions, depreciating exchange rate. Nonetheless, the new entrants are expected to increase level of localization by introducing a more extensive product line.
- SAIC Motors, the largest automotive company in China, recently launched HONGYAN heavy duty trucks in Pakistan as well as Renault in partnership with Ghandhara Nissan Ltd.

Source: Green Climate Fund, PAMA, Pakistan Economic Survey

Business Risk

- The top 4 local Trucks and Buses manufacturers registered an aggregate revenue of PKR~32bln in FY20 (down by ~24% YoY due to slower demand amidst Covid-19 pandemic), and contributed ~7% to the listed automobile sector.
- **Operating Risk:** The most significant risk the trucks and buses manufacturers face is the increase in cost of imported parts used in assembly and production. As the industry is dependent on international markets, rising exchange rate has had negative repercussions on the cost of production. The Industry had an average GP margin of ~20% in FY16 which fell massively over the years to ~11% in FY19 and nosedived to ~2% in FY20.
- **Sales Risk:** The overall economic slowdown owing to high interest rates along with reduced CPEC activity during CY19 had a toll on the overall Large Scale Manufacturing of the country. Production of trucks and buses was also affected, and this was further amplified by the outbreak of COVID-19 and resulting lockdown.
- Roadshows and marketing campaigns which have had substantial impact in supporting sales have been reduced owing to restrictions to follow SOPs.
- During 1QFY21, revenue of the top 3 players* witnessed a dip of ~22% from SPLY. However, margins witnessed a significant improvement. GP margin increased by 225%, while Net loss reduced by ~67%.





*Includes Ghandhara Industries, Ghandhara Nissan and Hino Pak

Source: Financial Statements

Financial Risk

- The sector's financial risk profile has been under stress prior to pandemic times too due to unfavorable macro indicators such as high policy rate and devalued PKR against USD. Demand evaporation, on the other side, due to redefined policies and slow economic activities in the country had further hampered the performance of the Sector. These factors, in combination with Covid-19 outbreak, had the following impact on the financial risk profile of the sector players:

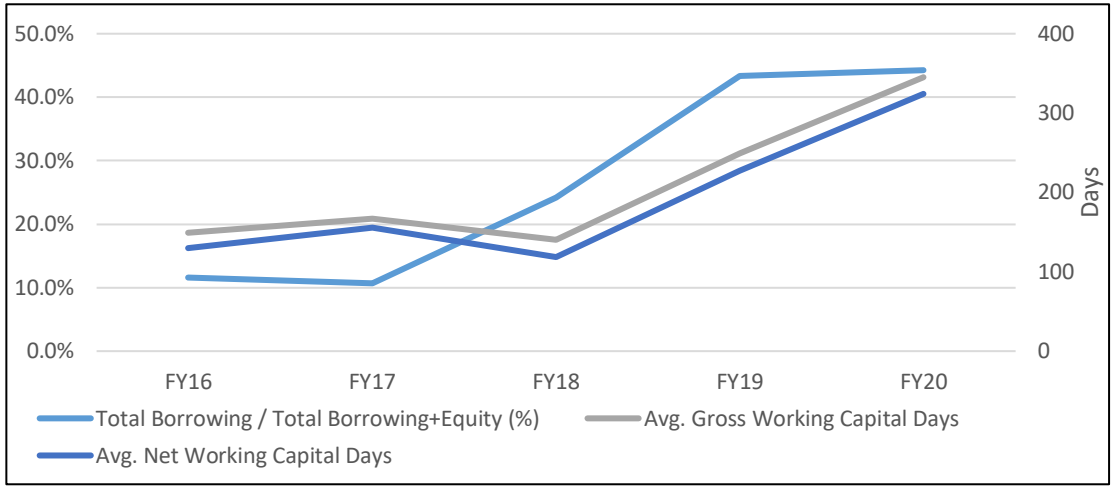
❖ Inventory Pile up due to lower orders and delays in Recoveries from Customers.

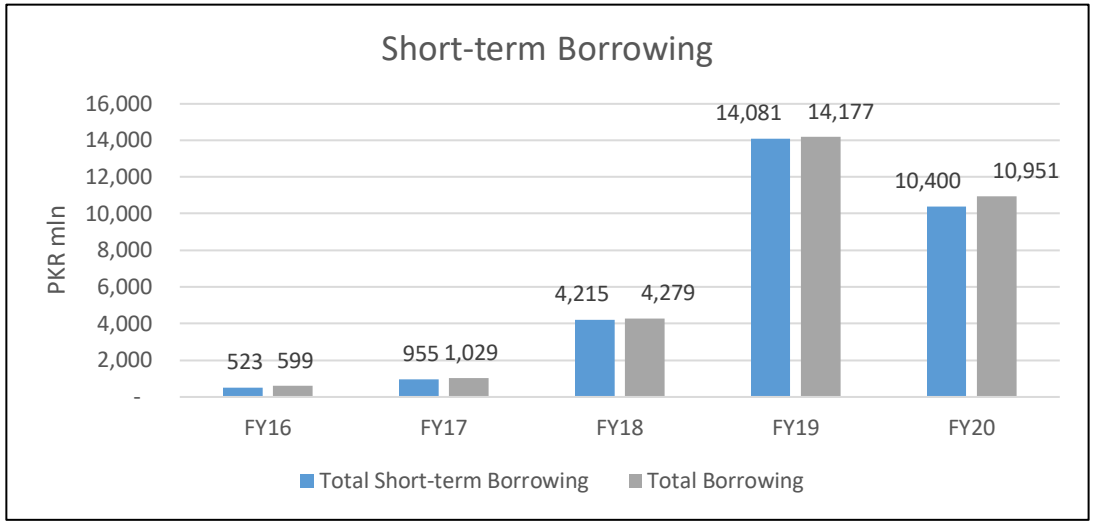
❖ Increase in Short Term Borrowings for Working Capital Management.

❖ Elevated Financing Cost due to increased borrowings.

❖ Squeeze in margins due to low sales volumes and high costs.

- The Sector's borrowing book stood at PKR~11bln as at June'20 (PKR~14bln – June'19), down by ~21% YoY. Most of the Borrowings are STBs. Overall leveraging of the Sector has dramatically increased in the past couple of years, however, still remains in the moderate range (40%-45%)



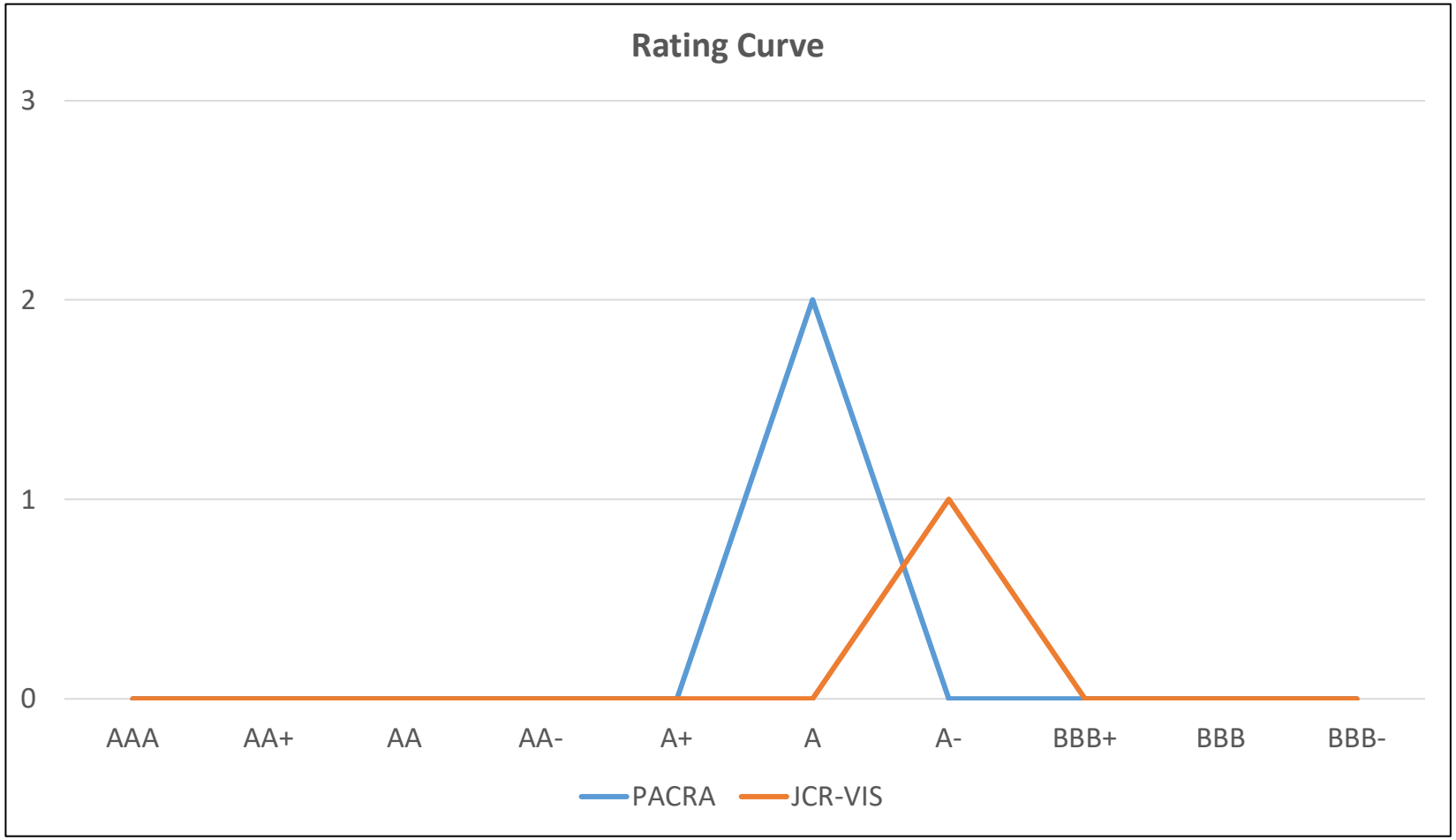


*Analysis is based on four players' financials – Ghandhara Industries, Ghandhara Nissan, Hino Pak and Master Motors

Source: Financial Statements

TRUCKS & BUSES|LOCAL INDUSTRY

Rating Curve



Total Market Capitalization: PKR~22bln

Rated Market Capitalization: PKR~19bln

Market Capitalization Rated by PACRA: PKR~17bln

Market Share Rated by PACRA: ~35%

SWOT Analysis

- Introduction of New Product Line by existing players.
- Strong ties with international parent companies/suppliers.

- Majority of Cost of Sales dependent on imports
- Recent devaluation of rupee led to financial distress on margins

- Exchange Rate volatility
- Development of ML-1 under CPEC will provide an alternative for freight and transport

- Incentives for both green-field and brown-field investments in Automotive Development Policy (ADP) 2016-21
- Resumption CPEC related activities and increase in LSM has been witnessed since easing of lockdown

TRUCKS & BUSES|CONCLUSION

OUTLOOK: STABLE

- On the global front, there has been a rising market interest in electric trucks and buses. It is anticipated that sales of Electric Medium and Heavy-Duty Vehicles (eMHDVs) will rise at a CAGR of 9% till 2030.

Trucks:

- On the local front, significant devaluation of Pakistani Rupee, along with rising interest rates severely impacted the operational and financial capacity of the sector. Even before the COVID-19 lockdowns completely hampered operations across the industry, macroeconomic indicators and change in government policies had put the Trucks industry in a tough situation.
- Resumption of CPEC related activities and stability of policy and exchange rate are key drivers for the future progress of the sector. The government is paying keen attention to revival and resumption of CPEC related projects which are key drivers for the trucks industry in Pakistan.
- Under the Automotive Development Policy (ADP) 2016- 2021, it was intended to increase production of trucks and buses to 12,000 and 2,200 by 2021 respectively. This does not seem achievable in the current scenario but reflects government's commitment to improving the sector. Furthermore, increasing competition due to new Chinese entrants in the market will improve quality and increase price sensitivity of the products addressing low localization levels of trucks in Pakistan.
- During 4MFY21, production and sales of trucks was recorded at 1,052 and 1,104 units respectively (1,175 and 1,114 units – 4MFY20), showing the sector has caught pace and improving economic conditions would stabilize the offset of COVID-19 gradually.

Buses:

- Tourism, over the past few years has increased, owing to the government's consistent effort in its promotion. As the effects of COVID-19 subside and tourism resumes rising pace, buses are expected to see an increase in demand.
- During 4MFY21, production and sales of buses was recorded at 160 and 186 units respectively (207 and 259 units – 4MFY20).

With the recent stability achieved in exchange rate along with low policy rate compared to the preceding year, the overall situation in the trucks & buses industry of Pakistan expected to improve on a gradual basis.

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