



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-2024	A	A1	Stable	Upgrade	-
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 that specializes in the manufacturing and marketing of radial tyres for trucks & buses. SLM Tyres is the first All-Steel Radial Tyres manufacturing facility in Pakistan incorporated as a result of a joint venture arrangement between Service Industries Limited (SIL), Chaoyang Long March Tyre Company Limited (LM), and Mr. Shabir Ahmad offering a complete transfer of technology from the commencement of the project. The ratings draw comfort from the longstanding position of SIL in Pakistan and LM in China – a leading Chinese manufacturer of all-steel radial tyres. The manufacturing facility is being set up in three phases: Phase 1 with annual tyre production of 0.74mln has been completed. Phase 2, aiming at enhancing the capacity to 1.6mln is in progress, while Phase 3 is planned to expand the capacity to 3.5mln eventually. During 9MFY24, the company achieved capacity utilisation of ~90% (based on the installed capacity of 0.74mln tyres per annum) which is expected to further increase to ~100% by the end of FY24 resulting in an impressive market share of ~50%. The capacity is likely to ramp up in upcoming years considering the solid expansion plans and rising demand for radial tyres for the trucks & buses segment in Pakistan. Tyre demand is primarily governed by the replacement market followed by automobile OEMs. Intense competition from imported and grey market tyres necessitates high-quality products at affordable prices. SLM Tyres intends to expand its clientele base across the globe by offering high-quality radial tyres and utilising multi-brand names under its sponsorship. The project has been set up in S.I.T.E Area, Nooriabad, Sindh. The Company commenced its commercial production in March 2022. Since then, the Company has been able to build a nationwide marketing and distribution channel to serve the local demand for radial tyres along with the development of a considerable clientele in the export segment seeking benefits from export avenues to multiple countries. During 9MFY24, the company's topline registered an impressive growth of ~122.1% and clocked in at PKR 26,841mln where ~35% was contributed by exports. Moreover, the ratings also take into account the considerable improvement in the profitability matrix signified by a GP Margin of ~23.5% (FY23, 8.3%) and NP Margin of ~15.7% (FY23, -3.4%). The Financial risk profile is demonstrated by an improved capital cycle, adequate coverages, & a moderately leveraged capital structure comprising both STB and LTB. The company has also availed borrowings at a concessionary rate. Going forward, the funding requirements for the expansion of the project are planned to be met through a mix of debt and internally generated cashflows.

The ratings depend on the Company's ability to sustain the growth trajectory along with robust financial discipline. Significant developments have been observed in the financial and non-financial performance of the company, which are expected to positively impact the ratings in future.

Disclosure

Name of Rated Entity	Service Long March Tyres (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology Rating Modifiers(Apr-24),Methodology Corporate Rating(Jul-23)
Related Research	Sector Study Tyres(Oct-23)
Rating Analysts	Sohail Ahmed Qureshi sohail.ahmed@pacra.com +92-42-35869504

Profile

Legal Structure Service Long March Tyres (Private) Limited ('SLM Tyres' or 'the Company') was incorporated in Pakistan on January 7th, 2020 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 the latest technology known as All Steel Radial manufacturing with complete in-house research facilities and the capability to manufacture finished products 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 phases 2 and 3, the Company plans to complete them in the coming years. Currently, SLM Tyres capacity utilization has been reported to be around 90%.

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 The ownership structure seems stable as no major change in the pattern of shareholding is expected in the near future. A 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 several decades.

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

Governance

Board Structure The board of SLM Tyres comprises nine members, including the Chairman – Mr. Jin Yongsheng, 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. Li Qingwen. There are no independent directors on the board.

Members' Profile Five members involved in the business are representatives of Service Group whereas the 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 the period ending June 30th, 2023.

Management

Organizational Structure A well-defined organizational structure exists within 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 and on the boards of various private and public companies in the past. The other key members involved in the business are also thorough professionals with substantial experience in diversified sectors.

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

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

Business Risk

Industry Dynamics The estimated market size of the Tyres Sector in FY23 stood at PKR~198.3bln (FY22: PKR~158.2bln). Key players in the tyre sector include Ghandhara Tyre and Rubber Company, Panther Tyres Ltd, Service Industries Ltd and Service Long March Tyres Pvt Ltd. The demand drivers of the tyre sector in Pakistan can be broadly segmented into the OEM and replacement markets where the average share of the replacement market is ~80%. The major raw material used in the production of tyres is rubber, both natural and synthetic. 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 has emerged as an important import substitution in the country's radial tyres market for commercial vehicles.

Revenues The commercial production of the project commenced in March 2022 when its first phase came online, the Company has grown exponentially over the past year and reported a topline of PKR 26,841mln in 9MFY24 (FY23, PKR 16,116mln) exhibiting a significant growth of ~122% during the period, primarily driven by the increase in volumes. Exports contributed ~35% to the topline of the company.

Margins During 9MFY24, the Company's gross margin improved to 23.5% with gross profit reported at PKR 6,317mln (FY23: PKR 1,332mln). That trickled down to an increased bottom line of PKR 4,213mln (FY23: negative 547mln) reflecting a healthy net profit margin of 15.7% (FY23: -3.4%) signifying that the company has achieved economies of scale.

Sustainability The radial tyres market in Pakistan is highly competitive owing to tyres smuggled through grey channels and the large no. of radial tyres imported every year, but SLM Tyres is expected to gain its market share by successfully reaching its full plant capacity in the coming years. A joint venture with Chaoyang Long March Tyre Company shall bring additional support at all levels. The Company intends to expand its footprint 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 9MFY24, gross working capital days were reduced to ~80 (FY23: ~145 days). Subsequently, the net working capital cycle stood at ~64 days at the end Mar'24 (FY23: ~105 days) reflecting improved working capital management through optimization of inventory and receivables cycle.

Coverages During 9MFY24, the Company's free cash flows from operations (FCFO) clocked in at PKR 5,464mln (FY23: PKR 1,815mln) on account of increased gross profit incurred during corresponding years. During the period, the interest coverage ratio of the Company stood at 5.6x (FY23: 1.4x) whereas the core-debt coverage ratio stood at 3.4x (FY23: 0.7x).

Capitalization During 9MFY24, the Company held a moderately leveraged capital structure as reflected by the ratio of ~38.7% (FY23: ~55.9%). The total borrowings were recorded at PKR 11,223mln (FY23: PKR 15,273mln). 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.



The Pakistan Credit Rating Agency Limited

Service Long March Tyres (Pvt.) Limited Tyres & Tubes	Mar-24 9M	Jun-23 12M	Jun-22 12M	Jun-21 12M
A BALANCE SHEET				
1 Non-Current Assets	20,744	20,368	19,759	11,343
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	12,296	11,172	7,036	3,760
<i>a Inventories</i>	4,070	5,307	2,604	-
<i>b Trade Receivables</i>	2,672	3,642	1,255	-
5 Total Assets	33,040	31,540	26,795	15,102
6 Current Liabilities	2,580	2,640	3,095	1,259
<i>a Trade Payables</i>	1,688	1,378	2,159	939
7 Borrowings	11,223	15,273	10,634	4,834
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	1,484	1,602	1,867	1,431
10 Net Assets	17,753	12,026	11,198	7,578
11 Shareholders' Equity	17,753	12,026	11,198	7,578
B INCOME STATEMENT				
1 Sales	26,841	16,116	2,127	-
<i>a Cost of Good Sold</i>	(20,524)	(14,784)	(2,028)	-
2 Gross Profit	6,317	1,332	99	-
<i>a Operating Expenses</i>	(867)	(573)	(180)	(15)
3 Operating Profit	5,451	759	(81)	(15)
<i>a Non Operating Income or (Expense)</i>	(233)	76	67	93
4 Profit or (Loss) before Interest and Tax	5,218	835	(14)	78
<i>a Total Finance Cost</i>	(1,004)	(1,350)	(144)	(0)
<i>b Taxation</i>	-	(32)	(176)	(22)
6 Net Income Or (Loss)	4,213	(547)	(334)	55
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	5,464	1,815	205	(42)
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	4,127	789	205	(43)
<i>c Changes in Working Capital</i>	(120)	(5,992)	(3,376)	687
1 Net Cash provided by Operating Activities	4,008	(5,203)	(3,171)	645
2 Net Cash (Used in) or Available From Investing Activities	(660)	(1,595)	(8,553)	(10,442)
3 Net Cash (Used in) or Available From Financing Activities	(2,752)	5,720	10,075	12,522
4 Net Cash generated or (Used) during the period	595	(1,078)	(1,648)	2,724
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	122.1%	657.6%	N/A	N/A
<i>b Gross Profit Margin</i>	23.5%	8.3%	4.7%	N/A
<i>c Net Profit Margin</i>	15.7%	-3.4%	-15.7%	N/A
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	19.9%	-25.9%	-149.1%	N/A
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	37.7%	-4.7%	-3.6%	1.2%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	80	145	662	N/A
<i>b Net Working Capital (Average Days)</i>	64	105	396	N/A
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	4.8	4.2	2.3	3.0
3 Coverages				
<i>a EBITDA / Finance Cost</i>	5.6	1.4	1.5	N/A
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	3.4	0.7	0.6	N/A
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	1.1	17.0	113.6	-115.1
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	38.7%	55.9%	48.7%	38.9%
<i>b Interest or Markup Payable (Days)</i>	32.4	123.9	338.4	N/A
<i>c Entity Average Borrowing Rate</i>	9.7%	9.9%	1.7%	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.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

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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2) Conflict of Interest

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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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(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)

(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

(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)

(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)

(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)

(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)

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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 | 17-(a)

(19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

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