RATING REPORT

Service Sales Corporation (Private) Limited

REPORT DATE:
May 20, 2024

RATING ANALYSTS:
Saeb Muhammad Jafri
saeb.jafri@vis.com.pk

Shaheryar Khan Mangan
shaheryar@vis.com.pk

RATING DETAILS		
Rating Category	**Initial Rating**	
	Long-term	**Short-term**
Entity	A-	A-2
Rating Outlook	Stable	
Rating Action	Initial	
Rating Date	*May 20, 2024*	

COMPANY INFORMATION	
Incorporated in 1965	**External auditors:** UHY Hassan Naeem & Co., Chartered Accountants
Private Limited Company	**Chief Executive Officer:** Mr. Shahid Hussain
Key Shareholders (with stake 5% or more):	
Mr. Shahid Hussain - 41.21%	
Ms. Ayesha Nazar - 13.18%	
Ms. Farida Shahid Kardar - 9.85%	
Ms. Uzma Hussain Hyat - 7.90%	
Ms. Saeeda Nazar - 7.65%	
Mr. Hamid Hussain - 5.00%	
Mr. Ahmed Shahid Hussain - 5.00%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Corporates:
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Service Sales Corporation (Private) Limited — Appendix I

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Service Sales Corporation (Private) Limited ('SSCPL' or 'the Company') *was incorporated in 1965 as a private limited company. The principal activity of the Company is retail and wholesale of footwear products and related accessories. The head office of the Company is situated on the 2nd Floor, EFU House, 6-D, Main Gulberg, Jail Road, Lahore.*

Profile of CEO

Mr. Shahid Hussain *is the Chief Executive Officer as well as Director of Servcie Sales Corporation (Pvt) Limited, Shoe Planet (Pvt) Limited, while serving as only a Director at SSC Manufacturing (Pvt) Limited. Mr. Shahid Hussain has over 40 years of experience. He has also served as the Chief Executive Officer of Service Industries Limited till 2011.*

Company Profile:

Service Sales Corporation (Private) Limited ('SSCPL' or 'the Company') was incorporated in 1965 as a private limited company. The principal activity of the Company is retail and wholesale of footwear products and related accessories. The head office of the Company is situated on the 2nd Floor, EFU House, 6-D, Main Gulberg, Jail Road, Lahore.

SSCPL's retail segment comprises over 330 retail stores under the brand name Ndure, representing approximately 82% of the total business. All retail outlets are operated by the Company, including 13 stores situated on company-owned properties, while the remainder are leased. The wholesale segment encompasses the Calza and Liza brands, distributed through 800 independent retailers across Pakistan, supported by 8 Wholesale Business Centers and E-commerce channels. These brands collectively contribute to around 14% of the total business. Whereas 4% of the total business originates from E-commerce channel.

Related Parties:

SSCPL has two wholly owned subsidiaries namely SSC Manufacturing (Pvt.) Limited ('SSCM' or 'the First Subsidiary') and Shoe Planet (Pvt.) Limited ('SPPL' or 'the Second Subsidiary'). SSCM and SPPL manufacture about 61% of the Company's products, while the rest are obtained from other local suppliers.

<u>Key Rating Drivers:</u>

Business risk profile is considered medium to high characterized by high cyclicality and competition within the market along with low regulatory and technological risk factors.

VIS has characterized the business risk profile of the footwear industry as medium to high. Demand for footwear is primarily driven by consumer preference and household income, resulting in susceptibility to economic cyclicality. Moreover, competition puts further stress on the business risk profile. However, the industry faces low regulatory and technological risks, which provides some support to the overall business risk profile.

About 30% of the overall market size is managed by the branded market. Within the branded market, the Company has an approximate market share of 16% in the local footwear industry.

Going forward, although some improvements have been observed in macroeconomic conditions, persistent issues such as high energy costs, inflation, and interest rates will remain a constraint on the industry's growth.

Sustained growth in sales, gross margins improved while net margins depict weakening.

The Company's revenue has exhibited growth at a 4-year Compound Annual Growth Rate (CAGR) of 2.28% (FY19-FY23), albeit with a drop in sales noted in the COVID-impacted FY20. During FY23, the growth in topline was reported at 7.62%. This growth was driven by higher prices albeit a contraction in the volumetric sales amid weak economic environment. The sales of the Company are predominantly in the local market.

Simultaneously, increasing prices benefited the Company's margins in FY23, with gross and operating margins improving to 42.54% (FY22: 39.67%) and 10.96% (FY22: 10.64%), respectively. The Company successfully passed on the impact of increasing input costs to the customer. However, heightened finance burden from a significant surge in local policy rates and increased debt utilization levels dragged down net margins, which declined to 3.13% (FY22: 4.18%).

Elevated capitalization profile, characterized by 71% of rental operating leases in Total Debt, provides support to assigned rating.

In working out the capitalization profile, Total Debt is considered inclusive of Lease Liability-Property (Requirement of IFRS-16), which is 71% of the Total Debt. Lease Liability- Property represents the operational rental leases, which can be terminated at any time without any penalty.

The Company Total Debt (inclusive of Lease Liability- Property) has maintained an elevated capitalization profile between FY20-FY22, with an average gearing and leverage ratio of 1.61x and 2.00x. During FY23, the gearing and leverage indicators (inclusive of Lease Liability-Property) witnessed increase to 1.71x (FY22: 1.66x) and 2.14x (FY22: 2.08x). Assigned ratings are supported by the nature of Lease Liability- Property as operational leases.

The debt mix of SSCPL is ~74% (FY22: ~75%) overall long-term financing including lease labilities and ~26% (FY22: ~25%) short-term debt. During FY23, short-term borrowings increased by ~13% to bridge their widening working capital gap, providing support to assigned ratings.

Adequate coverage profile

The Company's coverage profile experienced contraction in FY23, attributed to a decline in the Funds from Operations (FFO) due to increased financial charges, influenced by a surge in local interest rates during the year. The debt servicing coverage ratio (DSCR) weakened to 1.43x (FY22: 1.64x), although it remains at a healthy level. Similarly, the short-term debt coverage also declined to 1.62x (FY22: 1.69x), albeit remaining sufficient for assigned ratings.

Adequate liquidity profile

The Company maintains an adequate liquidity profile, with a 3-year average current ratio of 1.16x. In FY23, the current ratio was reported at 1.17x. Meanwhile, the cash conversion cycle increased to 49 days (FY22: 42 days), mainly due to a slight increase in the inventory period to 110 days (FY22: 105 days) together with a slight increase in the payable cycle to 90 days (FY22: 83). Elevated inventory and payable days are a result of the nature of their business, being a distribution company. The Company maintains approximately six months of inventory across all its stores as per the management.

Considerations for Future Reviews

Going forward, ratings are sensitive and consider the planned alignment of capitalization and debt service metrics with assigned ratings, which are regarded to be relatively elevated. Moreover, ratings will also consider support of consistent growth in export sales of subsidiaries as an important consideration going forward.

<table>
<tr><th>REGULATORY DISCLOSURES</th><th>Appendix I</th></tr>
<tr><td>Name of Rated Entity</td><td>Service Sales Corporation (Private) Limited</td></tr>
<tr><td>Sector</td><td></td></tr>
<tr><td>Type of Relationship</td><td>Solicited</td></tr>
<tr><td>Purpose of Rating</td><td>Entity Rating</td></tr>
<tr><td>Rating History</td><td>
<table>
<tr><th>Rating Date</th><th>Current Rating</th><th></th><th>Rating Outlook</th><th>Rating Action</th></tr>
<tr><td colspan="5">RATING TYPE: ENTITY</td></tr>
<tr><td>05/20/2024</td><td>A-</td><td>A-2</td><td>Stable</td><td>Initial</td></tr>
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</td></tr>
<tr><td>Instrument Structure</td><td>N/A</td></tr>
<tr><td>Statement by the Rating Team</td><td>VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.</td></tr>
<tr><td>Probability of Default</td><td>VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.</td></tr>
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<tr><td>Due Diligence Meetings Conducted</td><td>
<table>
<tr><th>Name</th><th>Designation</th><th>Date</th></tr>
<tr><td>Mr. Tabish Sharif</td><td>CFO</td><td>April 30, 2024</td></tr>
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