RATING REPORT

Universal Leather (Private) Limited

REPORT DATE:
February 29, 2024

RATING ANALYSTS:
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RATING DETAILS		
Rating Category	**Latest Rating**	**Previous Rating**
Entity	BBB/A-3	BBB/A-3
Rating Date	*February 29, 2024*	*January 30, 2023*
Rating Outlook	*Positive*	*Stable*
Rating Action	Maintained	Upgrade

COMPANY INFORMATION	
Incorporated in 1968	**External auditors:** Mushtaq & Co Chartered Accountants
Public Limited Company	**Chief Executive Officer/Chairman:** Mr. Shakil Ahmed
Key Stakeholders (with stake 5% or more):	
Mr. Shakil Ahmed (19.2%)	
Mr. S.M. Saleem (10.0%)	
Mr. S.M. Naseem (10.0%)	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial 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

Universal Leather (Private) Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Universal Leather (Pvt.) Limited (ULPL) was incorporated in 1968 as a public listed company, which was further converted into a private limited company in 2004. The company's primary business operation includes tanning of cow and buffalo leather. The Company has its production facilities located in Karachi and Lahore.

Corporate Profile

Universal Leather (Private) Limited ('ULPL' or 'the Company') was incorporated in Pakistan on October 17, 1968 as a company limited by shares. The Company was later converted from public listed company to a private limited company on April 28, 2004. The principal business activity of the Company is tanning of leather from cow and buffalo hides. The manufacturing units of the Company are located at Korangi Industrial Area, Karachi and Halloky Road Kahna Kachha, Lahore while its registered office is situated at Korangi Industrial Area, Karachi.

The Company also has long term investments in associated companies (MIMA Leather and MIMA Knit) presently valued at PKR 122 mln, representing ~17.8% of its total assets base.

Operating Performance

The Company has two manufacturing facilities located in Karachi and Lahore, with cumulative installed production capacity of 4 mln sq. ft. per annum. Post FY20, reduction in installed capacity was the result of a shift in business model to focus on efficient product lines that benefit profitability. Capacity utilization currently stands at 57.4%.

Capacity Utilization %	FY19A	FY20A	FY21A	FY22A	FY23A
Installed Capacity Sq. Feet	5,200,000	5,200,000	4,000,000	4,000,000	4,000,000
Actual Production Sq. Feet	245,165	1,889,361	1,367,043	1,913,850	2,296,620
Capacity Utilization %	47.1%	36.3%	34.2%	47.8%	57.4%

Key Rating Drivers

Business risk profile is characterized by export-oriented nature and sensitivity to cyclicality in international economic trends.

The leather sector is ascribed a medium business risk profile, marked by its export-oriented nature which shields it from significant local economic factors such as currency depreciation and resultant inflation. In FY23, the leather sector exports saw a slight decline of ~7% to USD 887 mln (FY22: USD 953 mln) due to significant challenges in the export markets during this period. However, leather, a major raw material, is primarily sourced locally preventing the sector from exchange rate risks.

Going forward, sector performance is expected to face continuous challenges from rising gas tariffs, hike in electricity costs, and regional competition, particularly from, China and India, as well as escalating finance costs and high inflation in export markets such as USA and Europe. However, currency depreciation, and extension in the GSP+ status is expected to support export demand.

Exports shield from local economic shifts, although client concentration risk elevated.

Around 98.3% of the Company's topline is derived from export sales, which provides a measure of protection against economic volatility in Pakistan, specifically with from fluctuations in exchange rates. However, the Company faces significant client concentration risk in its portfolio with the top five clients contributing approximately 72%, with one client contributing 35% of the total sales. Nevertheless, this risk is partly mitigated by long-term association with most clients. As per management, collection issues in the local market have restrained them from targeting local market.

Improvement in profitability on back of higher topline, and net benefit of currency depreciation on margins.

The Company reported a 13.6% growth in its topline in FY23, primarily attributable to increase in average prices over time. Gross margin also showed an improvement reporting at 18.7% (FY22: 14.0%) in FY23. This improvement is on account of the net impact of currency depreciation being positive on the Company's financial performance, with much of their sales derived from exports while import of raw material is limited.

Coverage profile strengthened by improvement in operational profitability and cashflows.

As a result of aforementioned improvement in topline and operational margins, the Company's operational cashflows also reported an increase. Consequently, with nil long-term debt and minimal financial costs, the debt service coverage ratio (DSCR) strengthened to 6.7x (FY22L 2.6x) in FY23.

Improvement in the capitalization metrics on account of lower short-term debt drawdown.

In FY23, the Company generated sufficient cashflows, covering a significant portion of its working capital requirements. Consequently, the drawdown of short-term debt decreased to PKR 70 mln (FY22: PKR 166 mln), constituting the Company's overall debt profile. This resulted in an improvement in gearing and leverage ratios to 0.2x (FY22: 0.7x) and 1.4x (FY22: 2.0x), respectively.

Liquidity position strengthened on account of reduction in current obligations.

Historically, the Company maintains an adequate liquidity profile while maintaining a 5Y average current ratio of 1.04x. In FY23, the current ratio slightly improved to 1.1x (FY22: 1.0x) on account of significant decrease in the Company's current obligations.

Consideration for future review ratings

Going forward, ratings will remain sensitive to continued improvement in the Company's profitability, capitalization, coverage and liquidity profile.

REGULATORY DISCLOSURES Appendix I

Name of Rated Entity	Universal Leather (Private) Limited
Sector	Leather
Type of Relationship	Solicited
Purpose of Rating	Entity Rating

Rating History

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY			
02/29/2024	BBB/A-3	Positive	Maintained
01/30/2023	BBB/A-3	Stable	Upgrade
11/18/2021	BBB-/A-3	Positive	Maintained
10/01/2020	BBB-/A-3	Negative	Maintained
05/09/2019	BBB-/A-3	Stable	Downgrade
10/16/2017	BBB/A-3	Negative	Downgrade
05/20/2016	BBB+/A-3	Stable	Reaffirmed
05/04/2015	BBB+/A-3	Stable	Reaffirmed
04/09/2014	BBB+/A-3	Stable	Reaffirmed
04/08/2013	BBB+/A-3	Stable	Reaffirmed
02/13/2012	BBB+/A-3	Stable	Reaffirmed

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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Waqas Shakil	Chief Operating Officer	14 February 2024