RATING REPORT

Union Fabrics (Private) Limited

REPORT DATE:
January 6, 2021

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-2	A-	A-2
Rating Date	*January 6, 2021*		*April 24, 2020*	
Rating Outlook	Stable		Rating Watch-Developing	
Outlook Date	*January 6, 2021*		*April 24, 2020*	

COMPANY INFORMATION	
Incorporated in 1992	**External auditors:** Horwath Hussain Chaudhury & Co.
Private Limited Company	**Chairman of the Board:** Mr. M Asif Siddiq
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. M Asif Siddiq
Mr. M. Asif Siddiq (30.56%)	
Mr. Faisal Amin (13.09%)	
Mr. Khurram Arif (10.90%)	
Mr. Ahmed Amin (10.30%)	
Ms. Sana Ali Shah (8.89%)	
Ms. Sania Khalid (5.45%)	
Mr. M. Amin Siddiq (5.41%)	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Corporates (May 2019) ***https://www.vis.com.pk/kc-meth.aspx***

Union Fabrics (Pvt) Limited

OVERVIEW OF THE INSTITUTION

Union Fabrics (Pvt) Limited (UFPL) commenced operations in 1992 as a small scale weaving unit and currently operates in the home textiles, processing and value added business lines in addition to weaving of greige fabric.

The company has 4 plants situated in S.I.T.E area. The company's greige fabric product and various home textile products form a significant part of its export sales.

The management team of the company is spearheaded by the sponsor- Mr. Asif Siddiq himself. Mr. Asif holds a Bachelor's degree in Electrical & Electronics Engineering from University of Florida and an MBA degree in Finance and MIS from University of South Florida.

Certifications held by UFPL include GOTS (Global Organic Textile Standard), OEKO-TEX (Class I and II) which is an international testing and certification system for textiles for limiting use of hazardous chemicals and substances in the textile product, and ISO 9001:2008 and ISO 14001:2004 relating to Quality Management Systems for customer satisfaction and Environment Management System for environmental performance, respectively.

RATING RATIONALE

Union Fabrics (Pvt) Limited (UFPL) deals in the weaving and finishing business segment of greige fabric and home textile product line with more than four-fifth of the sales geared towards the export market. Capacity utilization levels of sizing, weaving, stitching and processing segments continued to rise and stood above 90% during the outgoing and ongoing fiscal year. UFPL is has revamped its information technology infrastructure with implementation of SAP enterprise resource planning software which shall support scaling up of operations. Moreover, overall corporate governance framework depicts room for improvement given status of a private limited company.

Favorable government policies for enhancing exports and improving country's perception and law & order situation bode well for the textile sector. Key risk factor include rising cost of doing business (increasing electricity and gas tariff and rising local cotton prices). Even though implications of Covid-19's second wave remain elevated, we expect the order book for the industry to remain strong in the ongoing year, easing our business risk concerns.

Textile exports depicted growth of 9.3% during FY20 driven largely by sizeable currency devaluation in the outgoing year. Overall growth emanated from the value added segment. Favorable government policies for enhancing exports and improving country's perception and law & order situation bode well for the textile sector. Conversely, increasing cost of doing business and reduction in rebate rates may impact margins for selected players. Even though implications of Covid-19's second wave remain elevated, we expect the order book for the industry to remain strong in the ongoing year, easing our business risk concerns.

Overall profitability profile is supported by improving gross margins contributed by currency devaluation, higher volumetric growth and value-added pricing. Going forward, management envisages profitability to improve in the backdrop of higher projected revenue and margins from the value added segment.

Sales revenue of the company witnessed an increase of 26% during FY20. This significant escalation in topline was largely on account of introduction of specialized product categories, geographical diversification and pricing benefit from value added segment. Given sufficient orders in hand, sales revenue is projected to depict growth in FY21. As per management, the textile industry witnessed an increasing demand of home textiles as a result of COVID-19. Gross profit margins were reported higher at 14.7% (FY19: 12.8%) during FY20 on account of sizeable currency devaluation, higher volumetric growth and value-added pricing. However due to higher cost of raw material, gross profit margins declined to 13.0% during 1QFY21. Higher finance cost of the company due to elevated debt levels and absence of one-off gain on disposal of fixed assets, net margin of the company declined during FY20. Net margins were reported higher at 6.7% (FY20: 5.1%; FY19; 5.8%) during 1QFY21. Going forward, management envisages profitability to improve in the backdrop of higher projected revenue and margins from the value added segment.

Liquidity profile of the company is considered adequate in relation to outstanding obligations. Going forward, with improving profitability and limited additional long-term debt drawdown, liquidity profile is expected to strengthen.

Liquidity profile of the company has improved during FY20 with adequate coverage of cash flows in relation to outstanding obligations, manageable ageing of trade debts and sound debt servicing ability. Trade debts in relation to sales have depicted a noticeable rise during FY20 on account of higher dues receivable from the subsidiary-UAPL. Timely recovery of inter-company dues is considered important from a ratings perspective. Going forward, with improving profitability and limited additional long-term debt drawdown, liquidity profile is expected to strengthen.

Equity base of the company witnessed an increase owing to equity injection and profit retention. Leverage indicators have increased in the ongoing year due debt drawdown to fund capex and working capital requirement. Given projected increase in profitability and limited additional long-term debt drawdown, capitalization indicators are expected to improve going forward.

Equity base has increased on account of profit retention and issuance of right shares for funding expansion (1QFY21: Rs. 3.2b; FY20: 3.0b; FY19: 2.4b). Further equity injection planned by sponsors during ongoing fiscal year will support capitalization levels of the company. During the ongoing year, long-term debt and short-term debt increased on account of introduction of new machinery and increase in net working capital requirement, respectively. Gearing and leverage indicators remain on the higher side at 1.58x (FY20: 1.34x, FY19: 1.57x) and 2.1x (FY20: 1.9x, FY19: 2.0x), respectively at end-Sep'20. Given projected increase in profitability and limited additional long-term debt drawdown, capitalization indicators are expected to improve going forward.

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	Union Fabrics (Pvt) Ltd
Sector	Textile
Type of Relationship	Solicited
Purpose of Rating	Entity Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
6/1/2021	A-	A-2	Stable	Maintained
24/4/2020	A-	A-2	Rating Watch-Developing	Maintained
17/12/2019	A-	A-2	Stable	Reaffirmed
26/12/2018	A-	A-2	Stable	Reaffirmed
21/11/2017	A-	A-2	Stable	Initial

Instrument Structure	N/A
Statement by the Rating Team	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.
Probability of Default	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.
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Due Diligence Meetings

Name	Designation	Date
Tufail Kasbati	CFO	16-Dec-2020
M. Asif Siddiq	CEO	16-Dec-2020