RATING REPORT

Union Apparel (Private) Limited

REPORT DATE:
March 04, 2024

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-2	A-	A-2
Rating Date	*March 04, 2024*		*January 18, 2023*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION

Incorporated in 2016	**External auditors:** Crowe 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. Khurram Arif
Union Fabrics (Private) Limited – 100%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria *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

Union Apparel (Private) Limited

OVERVIEW OF THE INSTITUTION

Incorporated in 2016, Union Apparel (Private) Limited (UAPL) is a wholly-owned subsidiary of Union Fabrics (Private) Limited (UFPL). UAPL is engaged in manufacture and sale of fabric to the domestic market.

Chairman of the Company- Mr. Asif Siddiq 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.

The management team of the company is spearheaded by one of the directors of the parent company- Mr. Khurram Arif. He has been associated with Union fabrics since the past 18 years. Mr. Khurram holds a degree in Mechanical Engineering from England.

RATING RATIONALE

Company Profile

Setup in 2016, Union Apparel (Private) Limited (UAPL or 'the Company') is a wholly-owned subsidiary of Union Fabrics (Private) Limited (UFPL), engaged in manufacture and sale of fabric to leading brands in the local market. UAPL possesses necessary information technology infrastructure utilizing SAP enterprise resource planning software which provides operational efficiency.

In order to meet increasing demand of existing clientele, reduce dependence on outside purchases, and to improve lead time, the Company had implemented expansion in the weaving division, which entailed installation of 12 electronic jacquard looms along with 132 Picanol air-jet looms with complete back process enhancing production capacity from 6m meters/annum to 24m meters/annum at Nooriabad, Karachi. The project has been operational since July-2023.

Sector Update

The business risk profile of the textile sector in Pakistan is characterized by high level of exposure to economic cyclicality and intense competition. This sector's performance is significantly influenced by the broader economic conditions in the country, making it inherently vulnerable to fluctuations in demand driven by economic factors.

Pakistan's textile industry spans the entire value chain, from the production of raw materials like cotton to the manufacturing of finished textile products such as apparel and home textiles. Many companies operate as integrated units, controlling multiple stages of production to ensure quality, efficiency, and cost-effectiveness.

During FY23, Pakistan's yarn production registered a substantial decline, primarily due to reduced availability of cotton, as a result of crop damage and import restrictions. The sector's profitability was constrained by factors such as higher production costs, increased raw material costs, and rising energy expenses, all of which constrained the sector's profit margin. The industry's performance is closely intertwined with the outlook of the cotton and textile industries, both of which were affected in FY23. Global economic slowdown and contractionary economic policies led to a decrease in demand for textile products and, consequently, cotton yarn.

While the global outlook for cotton production is expected to rebound, local challenges persist. These challenges include high interest rates, increasing energy costs, and persistent inflationary pressures. These factors are likely to result in continued sluggish performance for the spinning sector in FY24.

Key Rating Drivers

The increase in unit prices drives topline growth and boosts gross margin, while elevated finance cost negatively impact net margin in FY23

The topline is primarily supported by local sales, contributing ~97.0%, while export sales constitute ~3.0% of total sales. The top-3 client concentration decreased to ~50.0% during FY23 (FY22: 61.6%). This illustrates management's strong association with reputed brands in the market, while maintaining focus to keep lowering the concentration risk.

In FY23, the sales revenue increased by ~15.0%, owing to a rise in unit prices, though there was a contraction of ~8.0% in sales volumes. The gross profit registered a growth of ~25.4% in FY23, while the gross margin rose to 16.2% (FY22: 14.7%). The Company incurred an increase in finance costs of ~46.1% compared to previous year due to an elevated monetary policy rate. Consequently, the net profit declined, while the net margin significantly contracted to 4.2% (FY22: 8.6%).

During 1QFY24, the profitability metrics improved further as both gross and net margins increased to 17.5% and 4.5% (FY23: 16.2% and 4.3%). The management indicated that sufficient orders have been secured till April 2024 and the sales revenue is projected to increase further by the end of FY24.

Going forward, the management expects that the commencement of operations at the new weaving unit in Nooriabad since July 2023, would increase the Company's capacity to meet additional orders, thereby increasing sales. The net margin is anticipated to be ~5.0% by the end of FY24, owing to higher finance charges and increased local competition.

Liquidity improves backed by a higher FFO and increased cash flow coverages; however, the same has room for further improvement

During FY23, the Funds from Operations (FFO) increased owing to higher operating profitability. Consequently, the Debt-Service-Coverage ratio (DSCR) improved to 1.72x (FY22: 1.14x), owing to higher FFO, while the FFO/Total Debt and FFO/Long-term Debt ratios exhibited favorable trends, rising to 0.16x and 0.28x (FY22: 0.05x and 0.09x) respectively. The current ratio of the Company remained relatively stable at 0.97x (FY22: 0.93x), while the cash conversion cycle remained steady at 55 days (FY22: 54 days), indicating adequate liquidity position.

During 1QFY24, FFO decreased, primarily due to increase financial charges. As a result, DSCR reduced to 1.20x (FY23: 1.72x) and both FFO/Total Debt and FFO/Long-term Debt ratios deteriorated to 0.08x and 0.14x (FY23: 0.16x and 0.28x) respectively. The current ratio improved marginally to 1.00x (FY23: 0.97x), indicating room for further improvement. The cash conversion cycle increased to 61 days (FY23: 55 days); the days payables outstanding rose significantly to 381 days (FY23: 239 days) on account of higher trade payables, resulting from extensive procurement of raw materials, particularly yarn, in 1HFY24 to fulfill rising customer orders for FY24. Going forward, improvement of liquidity profile along with maintenance of cash flow coverage indicators will remain important for the assigned ratings.

Capitalization indicators improve on account of debt reduction and equity base expansion in FY23

To save the bottom line from facing finance cost pressures, the Company reduced short-term debt by Rs. 0.06 bn and repaid long-term debt of Rs. 0.05 bn. As a result, short-term borrowings amounted to Rs. 1.25 bn as at Jun'23 (Jun'22: Rs. 1.31 bn) and long-term debt reduced to Rs. 1.73 bn as at Jun'23 (Jun'22: Rs. 1.78 bn). The equity base grew by ~12.4%, reaching Rs. 2.00 bn as at Jun'23 (Jun'22: Rs. 1.78 bn), owing to higher retention of profits. The proportionate increase in equity relative to total debt and liabilities, resulted in both gearing and leverage ratios improving to 1.50x and 2.97x (FY22: 1.73x and 3.34x) respectively.

During 1QFY24, the gearing ratio improved further to 1.46x (FY23: 1.50x), while the leverage ratio worsened to 3.74x (FY23: 2.97x) as the Company's current portion of total liabilities, relative to total equity, increased on account of higher trade payables commensurate to extensive buying of raw materials, yarn. Going forward, improving the capitalization profile will remain important for the assigned ratings.

Assessing UAPL's governance presents opportunities for further strengthening of corporate structure

The position of CEO at UAPL is held by Mr. Khurram Arif, with Mr. Tufail Kasbati serving as the Secretary. Mr. Mahmood Hussain acts as the Company's legal advisor. The Company operates without board committees, as it is overseen by three brothers, facilitating meetings in a family setting. Additionally, the Company's auditor, Crowe Hussain Chaudhury & Co., is included in the State Bank of Pakistan's approved panel, holding an 'A' category, indicating professional competence and credibility.

REGULATORY DISCLOSURES					Appendix I
Name of Rated Entity	Union Apparel (Private) Limited				
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				
	04/03/2024	A-	A-2	Stable	Reaffirmed
	18/01/2023	A-	A-2	Stable	Reaffirmed
	7/12/2021	A-	A-2	Stable	Reaffirmed
	6/1/2021	A-	A-2	Stable	Upgrade
	24/4/2020	BBB	A-2	Rating Watch-Negative	Maintained
	17/12/2019	BBB	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.				
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Due Diligence Meetings	**Name**	**Designation**	**Date**		
	Mr. Tufail Kasbati	CFO	06-Feb-2024		