RATING REPORT

Utopia Industries (Private) Limited

REPORT DATE:
September 10, 2024

RATING ANALYSTS:
Zunain Arif
zunain.arif@vis.com.pk

M. Amin Hamdani
amin.hamdani@vis.com.pk

RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook/Rating Watch	Stable		Stable	
Rating Action	Reaffirmed		Initial	
Rating Date	*September 10, 2024*		*June 06, 2023*	

COMPANY INFORMATION	
Incorporated in 2018	**External Auditors:** Kreston Hyder Bhimji & Co Chartered Accountants
Private Limited Company	**CEO:** Mr. Adnan Niaz
Key Shareholders (with stake 5% or more):	
Mr. Adnan Niaz ~ 50%	
Mr. Jabran Niaz ~ 50%	

APPLICABLE METHODOLOGY(IES)
VIS Entity 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*

Utopia Industries (Private) Limited

OVERVIEW OF THE INSTITUTION

Utopia Industries (Private) Limited (UIPL) was incorporated on April 6 2018, as a private limited company. Registered office is situated at S.I.T.E, Superhighway, Karachi.

Profile of CEO

Mr. Adnan Niaz is the CEO & Co-Founder of Utopia Industries. With a tech-savvy background, he leads 15+ years across diverse core functions. He also previously worked as a Sr. Consultant at Barclays Capital-USA & Bank of America. He holds MS degree from Alborg University, Denmark.

RATING RATIONALE

Corporate Profile:

Utopia Industries (Private) Limited ('UIPL' or 'the Company'), a division of Utopia Group, operates under the ownership and active participation of two Pakistani brothers. UIPL specializes in the manufacturing and export of a diverse range of products such as terry towels, pillows, comforters, mattress toppers, mattress encasements and protectors, bed sheets, cookware, plastic products, and personal care items. The registered office and all factory units are located on SITE, Superhighway, Karachi, Sindh, Pakistan.

The Company currently has 6 operating units producing different ranges from textile products to plastic and kitchen ware. Details of different units are presented below:

- **Unit 1:** Manufacturing of various miscellaneous textile products including fabric, apparel, and home textiles.
- **Unit 2:** Head office building, Specialized in dyeing yarn, micro fabric, para-dyeing, as well as knitting and weaving fabrics, Paper printing, Cut 2 Pack production of Garments & Towel Products.
- **Unit 3:** Waterjet weaving of microfiber fabric, Cut 2 pack production of Bedding products.
- **Unit 4:** Manufacturing of Plastic & Metal products including polybags, comforter bags, fry pans, metal containers, water bottles and lunch boxes, shaker bottles. Machine manufacturing for Compost Bin, Utensil Holder & machine spare parts.
- **Unit 5:** Manufacturing of cartons and producing various types of pillows & cushions.
- **Unit 6:** Producing polyester staple fiber, Draw Texturized Yarn (DTY), and Cut 2 Pack production of comforters.

Sector Update

The business risk profile of the textile sector in Pakistan is characterized by a 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. In FY23, the textile sector faced challenges due to various economic and environmental factors. These included damage to the cotton crop resulting from flooding in 1HFY23, escalating inflation, and import restrictions due to diminishing foreign exchange reserves.

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. Reduction in cotton supply, coupled with 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 inflationary pressures. Additionally, the sector's vulnerability to global market dynamics and the domestic economic landscape further contribute to its high business risk profile. However, there is optimism as an anticipated bigger cotton crop in FY24 is expected to alleviate some pressure on input costs and margins.

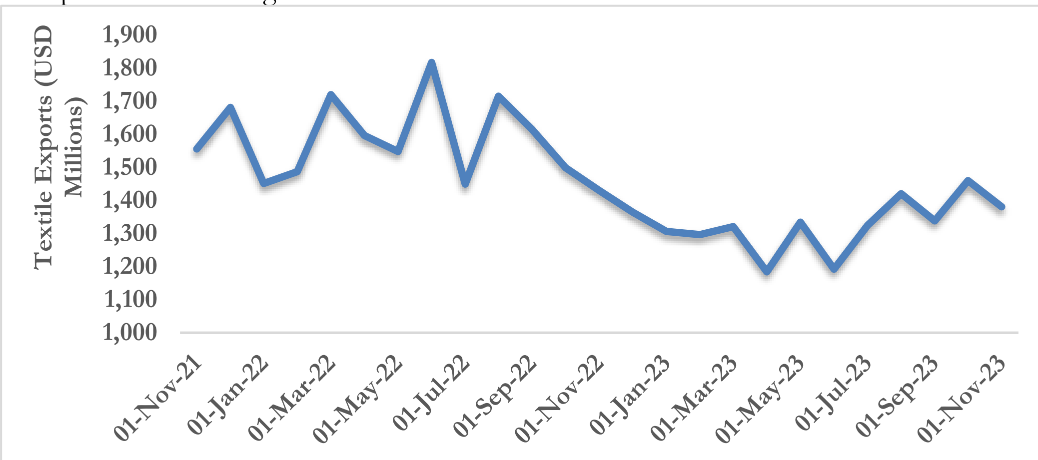

Figure 1: MoM Textile Exports (In USD' Millions) | Source: SBP

<u>Operational Update and Capacity Utilization:</u> Property, Plant, and Equipment (PPE) increased to Rs. 17.6b (FY23: Rs. 15.7b; FY22: Rs. 6.3b) at ended FY24. During FY23 and FY24, the Company added Rs. 1.7b and Rs. 2.68b to PP&E respectively, out of which major additions include waterjet looms, bio-mass fuel (pallets) based boiler, PSF production plant, Cookware plant, Air jet looms, as well as other miscellaneous items. This resulted in enhancement of capacities of different departments. The entire capex has been done through internal cash. As of end-Jun'24, textile segments contributed 91% to the topline, while remaining is contributed by plastic and kitchen ware. Due to the increased export demands, the Company has recently increased its capacities in textile, plastic and kitchen ware segments. In the textile segment, capacity utilization improved in FY24 to 87.9% (FY23: 76.7%; FY22: 96.8%), with production notably increasing to 42.9m kgs (FY23: 29.9m kgs; FY22: 26.7m kgs). The plastic and kitchen ware segments followed the same trend, with installed capacities and actual production increasing vis-a-vis FY22. The current energy requirements of the Company are fulfilled through K-electric and bio-mass, while the Company has also recently installed 4MW of solar panels.

(in millions)	FY22	FY23	FY24
Textile			
Installed Capacity (kgs)	27.62	39.05	48.81
Actual Production (kgs)	26.73	29.94	42.91
Capacity Utilization	***96.8%***	***76.7%***	***87.9%***
Plastic Ware			
Installed Capacity (lbs)	3.92	5.15	6.18
Actual Production (lbs)	3.39	3.82	4.89
Capacity Utilization	***86.5%***	***74.1%***	***79.1%***
Kitchen Ware			
Installed Capacity (kgs)	0.05	0.22	0.29

Actual Production (kgs)	0.04	0.21	0.27
Capacity Utilization	***80.0%***	***94.9%***	***94.4%***

Key Rating Drivers

Strong Topline Growth in FY23 and FY24 driven by higher selling prices; however, margins remain under pressure owing to increased costs of production and freight.
Topline increased by 40.1% in FY23, with net sales recorded higher at Rs. 36.6b (FY22: Rs. 26.2b) due to higher selling prices (in USD) despite slightly lower volumetric sales. Almost 99% (FY22: 99%) of sales emanated from export sales. The Company sells products on Amazon through its sister company Utopia Towels Inc. USA. Regional export sales were dominated by USA which constituted around 75% (FY22: 76%) of total net sales. Amidst higher raw material and fuel prices, gross profit of the Company declined to Rs. 7.4b (FY22: Rs. 8.9b), with gross margins declining to 20.3% (FY22: 34.2%). Finance costs increased to Rs. 474.5m (FY22: Rs. 170.4m), amid higher borrowings in FY23. Accounting for taxation, the bottom line recorded a net profit of Rs. 2.1b vis-à-vis Rs. 1.9b in FY22, with net margins declining to 5.6% (FY22: 7.3%).

During FY24, net sales increased by approximately 31.54% Y/Y amounting to Rs. 48.2b as compared to Rs. 36.6b in FY23. Being an export-oriented company, export sales constituted 97% of the sales mix, with USA continuing to take major share. Gross profit for FY24 was Rs. 7.13b (FY23: Rs. 7.4b), with gross margins further declining to 14.8% (FY23: 20.3%). Operating expenses decreased to Rs. 4.75b (FY23: Rs. 4.88b), due to lower distribution charges. Finance cost was recorded at Rs. 508.7m (FY23: Rs. 474.5m), which mainly constituted of Musharakah and bank charges. Due to considerable growth in cost of sales, and an increase in the finance cost and taxation, along with a reduction in other income, the net profit declined to Rs 1.7b (FY23: Rs 2.1b). As a result, the net margin declined to 3.5% during FY24(FY23: 5.6%).

Adequate liquidity profile with sound cashflow and debt coverages
Liquidity profile improved during the review period, with funds from operations (FFO) recorded at Rs. 4.4b (FY22: Rs. 3.2b) at end-FY23. This increase in FFO is primarily attributed to higher operating profit. At end-FY24, FFO was recorded at Rs. 3.4b. FFO to long-term debt stood at 0.46x (FY23: 2.76x; FY22: 2.51x) and FFO to total debt at 0.29x (FY23: 0.54x; FY22: 0.55x) at end-FY24. During the review period, debt service coverage ratio (DSCR) registered a decline, although it remained sound at 5.71x (FY23: 8.70x; FY22: 19.07x). The decline in DSCR was driven by higher long-term repayments. Current ratio remained intact at 1.34x (FY23: 1.35x; FY22: 1.28x) at end FY24. Net operating cycle registered continuous improvement, reducing to 51 days (FY23: 72 days; FY22: 74 days) at end FY24, on the back of better terms with clients and efficient inventory management. Going forward, maintaining liquidity and cashflow profile will remain an important rating trigger.

Growth in equity on the back of internal capital generation, with improved gearing and leverage ratios due to reduced borrowing levels.
Equity (adjusted for surplus) grew significantly amounting to Rs. 7.4b (FY23: Rs. 5.4b; FY22: Rs. 3.1b) at endFY24, due to higher retained earnings driven by profitability. During FY23, the Company issued ~300m bonus shares, thereby converting retained earning into share-capital. Hence total paid-up capital increased to Rs. 3.0b (from Rs. 1.0 in FY22). Total debt of the Company amounted to Rs. 5.9b as of June'24, compared to Rs. 8.1b in Jun'23 and Rs. 5.7b in Jun'22. The Company also mobilizes sponsors loan; however, due to the non-interest-

bearing nature of the loan, it is not treated as debt.. Gearing and leverage further improved to 0.45x (FY23: 0.72x; FY22: 0.75x) and 0.81x (FY23: 1.11x; FY22: 1.15x), respectively on the back of an increase in equity base and decrease reliance on debt. During the rating horizon, the management expects to mobilize Rs. 2.0b in order to install water jet looms and solar plant to increase total solar capacity to 7MW. Looking ahead, maintaining capitalization indicators is important from ratings perspective.

Utopia Industries (Private) Limited — Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**FY21**	**FY22**	**FY23**	**FY24**
Property, Plant and Equipment	4,151	6,493	15,886	17,879
Stock-in-Trade	3,629	7,300	5,770	7,765
Stores and Spares	35	246	313	229
Trade Debts	19	715	6,114	1,382
Advances, deposits and Prepayments	702	1,170	1,646	1,682
Cash & Bank Balances	350	223	678	1,118
Other Assets	113	167	433	735
Total Assets	8,999	16,315	30,840	30,790
Long Term Borrowings (inc. current portion)*	148	1,261	1,599	1,389
Sponsors Loan	3,774	4,468	5,884	5,884
Short Term Borrowings	0	4,453	6,539	4,549
Total Debt	148	5,714	8,137	5,937
Trade and Other Payables	3,881	3,008	4,020	4,386
Other Liabilities	0	7	320	413
Total Liabilities	7,803	13,197	18,361	16,621
Paid up capital	1	1	3,000	3,000
Tier-1 Equity	1,197	3,118	5,371	7,424
Total Equity	1,197	3,118	12,479	14,169
INCOME STATEMENT	**FY21**	**FY22**	**FY23**	**FY24**
Net Sales	7,986	26,151	36,633	48,188
Gross Profit	1,598	8,950	7,439	7,126
Operating Profit	1,180	3,451	2,561	2,376
Profit Before Tax	1,188	2,177	2,575	2,360
Profit After Tax	1,111	1,922	2,062	1,690
RATIO ANALYSIS	**FY21**	**FY22**	**FY23**	**FY24**
Gross Margin (%)	20.0%	34.2%	20.3%	14.8%
Net Margin (%)	13.9%	7.3%	5.6%	3.5%
Gearing (x)	0.12	1.83	1.52	0.80
Adjusted Gearing (x)	0.03	0.75	0.72	0.45
Leverage (x)	6.52	4.23	3.42	2.24
Adjusted Leverage (x)	0.81	1.15	1.11	0.81
FFO	1,173	3,159	4,418	3,370
FFO to Long Term Debt (%)	7.93	2.51	2.76	2.43
FFO to Total Debt (%)	7.93	0.55	0.54	0.57
Debt Servicing Coverage Ratio (x)	32.61	19.07	8.70	5.71
ROAA (%)	19.9%	15.2%	8.7%	5.5%
ROAE (%)	173.4%	89.1%	48.6%	26.4%
Current Ratio (x)	1.23	1.28	1.35	1.34
(Stock in trade + Trade debts)/ST borrowings (x)	#DIV/0!	1.80	1.82	2.01

**Adjusted for sponsor loan*

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	Utopia Industries (Private) Limited
Sector	Textile
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
Rating Type: Entity				
10-09-2024	A-	A-2	Stable	Reaffirmed
06-06-2023	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.
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Due Diligence Meeting Conducted

Name	Designation	Date
Mr. Shahid Mahfooz	Finance Manager	24th May, 2024
Mr. Abdul Hannan	Senior Manager- Financial Reporting	
Mr. Rashid Bhatti	Head of Finance	