



The Pakistan Credit Rating Agency Limited

Rating Report

US Apparel & Textiles (Pvt.) Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
04-Mar-2023	A+	A1	Stable	Maintain	-
04-Mar-2022	A+	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

US Apparel & Textiles (Private) Limited (US Apparel) is a prominent textile venture of US Group. The group companies operate under the umbrella of AJ holdings – the flagship HoldCo of the group. The group leveraging is nil, which is much of a conscious group decision. Sponsors exercise oversight of the businesses and professional management, are well-equipped and well-experienced, and spearhead the individual companies. Strategic direction is meticulously worked out and rigorously followed once decided and finalized. The Company is principally engaged in the manufacturing and export of ready-made garments. The Company’s management has experienced professionals, aided by comprehensive reporting, where operations of the Company are supervised with complete autonomy. Its established business profile emanates from a strong presence in the broader value chain; enabling the company to manage volatility in the textile industry. The rating reflects a steady revenue base in recent years. The top line primarily consists of exports. The company’s top line improved to PKR 44.7bln (FY21: PKR 30.7bln). Margins remained largely sustained where growth was recorded in revenue. US Apparel continues to maintain a favorable capital structure and strong coverages signifying a robust financial profile. During the year Company enhanced its capacity by 15,000 Pcs per day. This will cater to expansion in the revenue base and strengthen the business profile of the company. This will cater to expansion in the revenue base and strengthen the business profile of the company. During 7MFY23, the textile exports were valued at \$10.08bln compared to \$10.93bln, reflecting an 8% decline YoY – the declining trend has been recorded in the last few months. The decline in exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand for yarn in international markets is also a challenge. The analysis of 5MFY23 reveals that among value-added items, bedwear has witnessed the largest decline of 19% (on an MoM basis), down to \$217 million. Knitwear remained on the downward path in October 2022 and declined by 10% to \$392 million. Among non-value-added items, the cotton yarn has shown the largest decline of 35%. Moreover, a slowdown is prevailing in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries. The demand pattern is expected to improve post-Jun-23.

The ratings are dependent on the Company’s ability to maintain a strong business profile amidst current circumstances. Preserving low-leveraged capital structure and sound coverages remain imperative.

Disclosure

Name of Rated Entity	US Apparel & Textiles (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-22),Methodology Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology Rating Modifiers(Jun-22)
Related Research	Sector Study Composite and Garments(Dec-21)
Rating Analysts	Iram Shahzadi iram.shahzadi@pacra.com +92-42-35869504



Composite and Garments

The Pakistan Credit Rating Agency Limited

Profile

Legal Structure US Apparel & Textiles (Private) Limited (US Apparel) was incorporated on February 18, 1987 as a private limited company.

Background US Apparel & Textiles (Private) Limited is the flagship business venture of the US Group.

Operations US Apparel & Textiles (Private) Limited is principally engaged in the manufacturing and export of ready-made denim garments. The Company has five production units.

Ownership

Ownership Structure US Apparel is a wholly-owned subsidiary of AJ Holdings (Private) Limited. The holding company exercises its control over the company's board by virtue of its 100% stake in the Company.

Stability The Group ownership is divided between the two families Javed Arshad Bhatti & family & Mian Muhammad Ahsan & family. The Group's holding Company, AJ Holdings Limited, primarily manages investments in subsidiary and associated companies and this bodes fairly well for the stability of the overall structure.

Business Acumen US Group is one of the oldest business conglomerates in Pakistan with considerable interest in textiles. The group has developed quite good expertise in the textile garments sector, over the years, and enjoys long-term association with several customers abroad. The group's presence has been limited to the textile sector but sustained volatility effectively over the years. Apart from garment business, US Group also has a Denim weaving Mill namely, US Denim Mills Limited, involved in weaving. This has assisted the Company in expanding its operations despite challenging market dynamics.

Financial Strength The presence of the holding company and details of business profile and operations of almost all group companies, reflects the strong financial strength of sponsors. This indicates sponsors' ability and willingness to support the flagship company of the group in case of need.

Governance

Board Structure The Company has a ten-member board with the presence of sponsors and their families. The position of CEO designate is vested with Mr. M. Salman Hafeez Malik.

Members' Profile The members of the Board have relevant stature and extensive experience of over three decades of the textile industry. Currently, there are no independent directors on the board.

Board Effectiveness The board meetings are held regularly in which discussion on various aspects is also formally documented in minutes.

Financial Transparency EY Ford Rhodes Chartered Accountants, who are in the category 'A' of SBP and have a QCR rating by ICAP, are the external auditors of the company. They have expressed an unqualified opinion on the financial statements of the company for the year ending June 30th, 2022.

Management

Organizational Structure US Apparel is further divided into sub-business units. The sBU-USA and sBU-UK/EU have five garment manufacturing units with capacity to produce 25 mln units annually. The Manufacturing Unit 2 & Unit 5 fall under sBU USA and Unit 1-R, Unit 3 & Unit 4 fall in sBU UK/EU. The Manufacturing Unit US Denim Mills, third sBU is a fabric mill that produces 40 mln meters of fabric annually. Each sBU divided into functional departments, namely: (i) Finance & IT (F&I), (ii) Marketing, (iii) Production, (iv) Supply Chain and Corporate Sourcing (v) Admin & HR. All departments report to respective MD(s) who are responsible to deliver the bottom line and agreed goals & targets of sBU's. MD's, CFO, Director Projects, Director HR, Director IR report to CEO designate.

Management Team Mr. Muhammad Salman Hafeez Malik is the CEO designate of the Company. He carries twenty-five years of professional experience and is a Chartered Accountant. He has been working with this group since 2019. Mr. Afnan Mansoor, CFO of the Company, has been associated since the year 2009. He is a Chartered Accountant.

Effectiveness The management meetings are held on periodic basis with follow-up points to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations. These meetings are headed by the CEO.

MIS The Company's daily and monthly MIS comprises comprehensive performance reports which are reviewed frequently by senior management. Recognizing the need for quality information systems to control and maintain the efficiency of operations, the company has implemented an Oracle based ERP solution - Oracle E business suite, Harmony version 4.

Control Environment US Apparel & Textiles utilize management systems as their mechanism for ensuring control. There is clear evidence of these systems being audited and certified externally. The Company has attained ISO 14001, 45001, 9001 SA8000, WRAP, Sedex, ISO 9001, OekoTex, GRS, RCS, OCS, SLCP light, STEP, CR 360, Higg FEM 3.0, and GOTS certification.

Business Risk

Industry Dynamics During 7MFY23, the textile exports were valued at \$10.08bln compared to \$10.93bln, reflecting an 8% decline YoY – the declining trend has been recorded in the last few months. The decline in exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand for yarn in international markets is also a challenge. The analysis of 5MFY23 reveals that among value-added items, bedwear has witnessed the largest decline of 19% (on an MoM basis), down to \$217 million. Knitwear remained on the downward path in October 2022 and declined by 10% to \$392 million. Among non-value-added items, cotton yarn has shown the largest decline of 35%. Moreover, a slowdown is prevailing in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries. The demand pattern is expected to improve post-Jun-23.

Relative Position US Apparel & Textiles (Private) Limited is principally engaged in the manufacturing and export of ready-made garments. In Pakistan's denim sector, US Apparel is one of the top exporters.

Revenues During FY22, the Company's top line has improved to PKR 44.7bln (FY21: PKR 30.7bln); an uptick of 45% YoY. The major portion of the revenue base is derived from exports. The main export destinations in FY22 were the US, UK, and European countries. During FY22, the Company's gross profits enhanced to PKR 10.3bln (FY21: PKR 6.9bln). Hence, the net profitability exhibited a sizeable growth and clocked at PKR 5.2bln (FY21: PKR 2.6bln).

Margins During FY22, the gross profit margin stood at 23.2% (FY21: 22.7%) attributable to the rationalization of cost structure and improved pricing. The management closely monitors operating expenses, translating into an improved operating profit margin of 16.2% (FY21: 15.6%). Hence, the net profit margin clocked at 11.7% (FY21: 8.4%).

Sustainability During the year Company enhanced its capacity by 15,000 Pcs per day. This will cater to expansion in the revenue base and strengthen the business profile of the company.

Financial Risk

Working Capital During FY22, the Company's net working capital cycle remains largely the same at 30days (FY21: 30days) attributable to slight attrition in inventory days (FY22: 36days, FY21: 40days) and movement in receivable days (FY22: 33days; FY21: 28days). The Company's net trade assets increased by 53% to clock in at PKR 12.97bln (FY21: PKR 8.46bln) which reflects a good cushion in trade assets.

Coverages Free Cash Flows from Operations (FCFO) increased in FY22 and clocked in at PKR 6,092mln on the back of higher EBITDA YoY. The Company has a lease liability of PKR 91mln in FY22. Hence, the coverage of the Company is very strong because the Company has no borrowing.

Capitalization The capital structure of the Company is strong. Equity of the Company is at PKR 14.8bln (FY21: PKR 12.4bln). The Company has no on-balance sheet borrowing. The leveraging stems from the funded & non-funded facilities kept by the Company from different institutions.



The Pakistan Credit Rating Agency Limited

US Apparel & Textiles (Pvt.) Limited Garments	Jun-22 12M	Jun-21 12M	Jun-20 12M
A BALANCE SHEET			
5 Total Assets	23,606	17,542	16,499
10 Net Assets	14,776	12,382	11,515
11 Shareholders' Equity	14,776	12,382	11,515
B INCOME STATEMENT			
1 Sales	44,660	30,686	29,655
4 Profit or (Loss) before Interest and Tax	6,168	3,149	2,710
6 Net Income Or (Loss)	5,212	2,589	2,204
C CASH FLOW STATEMENT			
a Free Cash Flows from Operations (FCFO)	7,173	4,141	4,074
b Net Cash from Operating Activities before Working Capital Changes	5,735	3,050	3,188
c Changes in Working Capital	(1,666)	(1,089)	581
1 Net Cash provided by Operating Activities	4,070	1,961	3,769
2 Net Cash (Used in) or Available From Investing Activities	(2,246)	(326)	(1,450)
3 Net Cash (Used in) or Available From Financing Activities	(3,298)	(1,813)	(2,795)
4 Net Cash generated or (Used) during the period	(1,475)	(178)	(475)
D RATIO ANALYSIS			
1 Performance			
a Sales Growth (for the period)	45.5%	3.5%	-2.0%
b Gross Profit Margin	23.2%	22.7%	21.5%
c Net Profit Margin	11.7%	8.4%	7.4%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	12.3%	9.9%	15.7%
2 Working Capital Management			
a Gross Working Capital (Average Days)	69	68	66
b Net Working Capital (Average Days)	30	30	32

Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	Very high credit quality. Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
AA-	
A+	
A	High credit quality. Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
A-	
BBB+	
BBB	Good credit quality. Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BBB-	
BB+	
BB	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
BB-	
B+	
B	High credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
B-	
CCC	
CC	Very high credit risk. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



*The correlation shown is indicative and, in certain cases, may not hold.

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

- a) Broker Entity Rating
- b) Corporate Rating
- c) Debt Instrument Rating
- d) Financial Institution Rating
- e) Holding Company Rating
- f) Independent Power Producer Rating
- g) Microfinance Institution Rating
- h) Non-Banking Finance Companies Rating

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Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions

- (3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
- (5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
- (11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(F-VII)

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