



The Pakistan Credit Rating Agency Limited

Rating Report

US Denim Mills (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
20-Mar-2024	A	A1	Stable	Maintain	-
20-Mar-2023	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The rating emanate from the prominent profile of US Denim Mills (Private) Limited (“UDML”, or “the Company”) in the weaving industry of Pakistan and is one of the textile ventures of the US group. The rating takes comfort from the presence of AJ Holding Limited as a sponsoring group and two Companies primarily operate under its umbrella which includes US Apparel & Textiles (Pvt) Limited & US Denim Mills (Private) Limited. The sponsors exercise oversight over individual enterprises, oversee professional management, and are well-equipped and experienced. Strategic direction is meticulously worked out and rigorously followed once decided and finalized. The Company’s management has experienced professionals, aided by comprehensive reporting, where operations of the Company are supervised with complete autonomy. US Denim has a subsidiary in Turkey, with name of Us Fashion Turkey Tekstil Ticaret Anonim Sirketi to augment accessibility in international markets by exploring multiple export avenues mainly in Europe. The Company product slate is dedicated to denim fabric with quality yield derived ranges from 07 to 12 yarn count. The top line of the Company stood at PKR 22bln during FY23 (FY22: 23bln) predominately stemming from indirect exports, constituting 68% of its total revenue and 30% from direct exports to multiple destinations including Bangladesh, Sri Lanka, Egypt, Morocco, Turkey & Italy etc. The margins of the Company have shown a notable upswing during FY23, based on pricing competitiveness which depicts a strategic shift by international manufacturers as they enacted a close-to-needle approach. In recent times, the Company has shifted their energy mix to boilers to manage energy cost risk. US Denim maintain a favorable capital structure, sufficient cashflows and strong coverages signifying a robust financial profile. The Company has planned CAPEX for backward vertical integration in the spinning segment. The management of the Company is mindful to keep align their performance with financial projections.

During FY23, the size of the textile industry stood at PKR 2.9trn mainly supplemented by PKR 1,584bln from composite and garments, and PKR 775bln from spinning and PKR 637bln from weaving. The weaving industry has 9,000 looms in working with an export cotton cloth volume of 2,012mln Sq. Meter and amount of PKR 499bln. The availability of raw materials like cotton yarn, inflated finance costs and energy tariffs are prime challenges specific to the industry.

The ratings are dependent on the Company’s ability to maintain a strong business profile amidst current circumstances while continue to generate sufficient cashflows, stable topline and profitability. The adherence of debt matrix at an optimal level and maintaining sound coverages remain vital for assigned ratings.

Disclosure

Name of Rated Entity	US Denim Mills (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jul-23),Methodology Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology Rating Modifiers(Apr-23)
Related Research	Sector Study Weaving(Aug-23)
Rating Analysts	Muhammad Harris Ghaffar harris.ghaffar@pacra.com +92-42-35869504

Profile

Legal Structure US Denim (Private) Limited (US Denim, The Company) was incorporated on January 18, 2005, as a private limited company.

Background The Company is a vital business venture of the US Group. Moreover, the company is associated with A.J Group since its inception.

Operations US Denim is principally engaged in the manufacturing and sale of denim fabric. The Company's total energy requirement is 553,761 units and the sources to meet the requirement - captive (Coal, Gas, Furnace Oil), WAPDA etc. US Denim has also installed 1.9 M. W Solar Power Generation at full capacity.

Ownership

Ownership Structure The Company 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 associations with several customers abroad. The group's presence has been limited to the textile sector but sustained volatility effectively over the years. Apart from the garment business, US Group also has a Denim weaving Mill namely, US Denim Mills Limited, engaged 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 the 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. Currently, there are no independent directors on the board.

Members' Profile Members of the Board have long association with the board and relevant stature and extensive experience. The position of CEO is vested with Mr. M. Irfan Nazir Ahmed.

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

Financial Transparency KPMG Taseer Hadi & Co. 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, 2023.

Management

Organizational Structure The organizational structure of the company is divided into several functional departments, namely: (i) Finance, (ii) Marketing, (iii) Quality Assurance, (iv) Operations, (v) Information Technology, (vi) Supply Chain, and (vii) HR & Admin, and procurement functions. All departments report to respective GM(s) who are responsible to deliver the bottom line and agreed goals & targets. All the GMs report to CEO.

Management Team Mr. Irfan Nazir Ahmad, the CEO, holds an MBA qualification and boasts 25 years of ample experience in the Textile & Apparel Industry, covering Sales & Marketing, General Management, Production Management, and Supply Chain. His tenure includes roles at Reshi Textiles, Azgard 9 Ltd, US Denim, and US Apparel, with an ongoing association with the group since 2014. Mr. Farrukh, the CFO, has been associated with the group since 2001. He is a Chartered Management Accountant.

Effectiveness The management meetings are held periodically with follow-up points to resolve or proactively address operational issues, if any, eventually ensuring a 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 Denim utilizes management systems as its mechanism for ensuring control. There is clear evidence of these systems being audited and certified externally. Examples of this include ISO 14001, GOTS, C2C at the gold level, AWS, OCS, GRS, RCS, Higg FEM 3.0, SLCP, ICS Environment, BSCI, and Oeko-Tex.

Business Risk

Industry Dynamics During FY23, the size of the textile industry stood at PKR 2.9trn mainly supplemented by PKR 1,584bln from composite and garments, and PKR 775bln from spinning and PKR 637bln from weaving. The weaving industry has 9,000 looms in working with an export cotton cloth volume of 2,012mln Sq. Meter and amount of PKR 499bln. The availability of raw materials like cotton yarn, inflated finance costs and energy tariffs are prime challenges specific to the industry.

Relative Position US Denim has a prominent profile in the dedicated denim fabric export from Pakistan. The Company operates with a capacity of 229 Air Jet looms and 20 power looms.

Revenues As of FY23, the Company reported a net revenue of PKR 22.059bln, reflecting a decline of 4.6% on YoY basis. (FY22: PKR 23.120bln) and 14.994bln during 6MFY24. Exports sales accounted for ~30% of the total sales revenue in FY23. The Company exports fabric to various countries, prominently Bangladesh, Egypt, Turkey, and Sri Lanka.

Margins The margins of the Company have shown a notable upswing during FY23, based on pricing competitiveness which depicts a strategic shift by international manufacturers as they enacted a close-to-needle approach. In FY23, the company achieved a gross profit of PKR 4.395bln, (FY22: PKR 2.707bln), with a gross profit margin of 19.9%. Net income surged by 93%, amounting to PKR 2.876bln, resulting in a net profit margin of 13%, compared to 6.4% in FY22. Furthermore, during 6MFY2024, the company recorded a net income of PKR 1.528bln with a net profit margin of 10.2%.

Sustainability The Company has planned CAPEX for backward vertical integration in the spinning segment. The management of the Company is mindful to keep align their performance with financial projections.

Financial Risk

Working Capital In FY23, a surge in the Company's net working capital cycle was observed, reaching 43 days compared to 36 days in FY22. This increase was driven by rises in both inventory days, which climbed to 50 days from 38 days in FY22, and receivable days, which extended to 77 days from 64 days in FY22. Furthermore, payable days were also extended, from 65 days in FY22 to 84 days in FY23. The Company's net trade assets remained steady at PKR 8.771bln, reflecting a commendable cushion in trade assets. The company's Working Capital requirements are predominantly met through internal cash generation, supplemented by interest-free financing acquired from other group companies.

Coverages In FY23, the company experienced a significant increase in its FCFO, increased notably by 76% to reach PKR 3.354bln. This surge is attributable to the improved profitability, leading to higher (EBITDA), which in turn led to growth in free cash flow from operations. The coverage of the Company is very strong as the Company has no borrowings.

Capitalization The capital structure is reflecting a comfortable position. 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 equity base of the Company is at PKR 8.4bln (FY22: PKR 8bln) and 8.6bln in 6MFY24. Further strengthening of the equity base shall improve risk absorption capacity, going forward.



The Pakistan Credit Rating Agency Limited

US Denim Mills (Pvt.) Limited Weaving	Jun-23 12M	Jun-22 12M	Jun-21 12M
A BALANCE SHEET			
1 Non-Current Assets	4,938	5,285	5,284
2 Investments	-	-	-
3 Related Party Exposure	363	1	1
4 Current Assets	9,325	9,374	6,700
a Inventories	3,071	2,943	1,871
b Trade Receivables	4,633	4,630	3,424
5 Total Assets	14,626	14,661	11,985
6 Current Liabilities	5,382	5,267	3,556
a Trade Payables	5,077	5,025	3,248
7 Borrowings	-	-	-
8 Related Party Exposure	837	1,323	896
9 Non-Current Liabilities	-	69	44
10 Net Assets	8,407	8,003	7,490
11 Shareholders' Equity	8,407	8,003	7,490
B INCOME STATEMENT			
1 Sales	22,059	23,120	17,376
a Cost of Good Sold	(17,664)	(20,413)	(15,547)
2 Gross Profit	4,395	2,707	1,828
a Operating Expenses	(1,056)	(885)	(818)
3 Operating Profit	3,339	1,822	1,010
a Non Operating Income or (Expense)	(253)	(114)	(283)
4 Profit or (Loss) before Interest and Tax	3,086	1,708	727
a Total Finance Cost	(36)	(26)	(22)
b Taxation	(175)	(194)	(117)
6 Net Income Or (Loss)	2,876	1,489	588
C CASH FLOW STATEMENT			
a Free Cash Flows from Operations (FCFO)	3,354	1,909	922
b Net Cash from Operating Activities before Working Capital Changes	3,354	1,906	919
c Changes in Working Capital	(85)	(878)	(160)
1 Net Cash provided by Operating Activities	3,269	1,028	758
2 Net Cash (Used in) or Available From Investing Activities	(31)	(366)	(31)
3 Net Cash (Used in) or Available From Financing Activities	(3,356)	(546)	(777)
4 Net Cash generated or (Used) during the period	(118)	116	(50)
D RATIO ANALYSIS			
1 Performance			
a Sales Growth (for the period)	-4.6%	33.1%	23.5%
b Gross Profit Margin	19.9%	11.7%	10.5%
c Net Profit Margin	13.0%	6.4%	3.4%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	14.8%	4.5%	4.4%
e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]	35.0%	19.2%	8.2%
2 Working Capital Management			
a Gross Working Capital (Average Days)	126	102	98
b Net Working Capital (Average Days)	43	36	45
c Current Ratio (Current Assets / Current Liabilities)	1.7	1.8	1.9
3 Coverages			
a EBITDA / Finance Cost	N/A	N/A	N/A
b FCFO / Finance Cost+CMLTB+Excess STB	N/A	N/A	N/A
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.2	0.7	1.0
4 Capital Structure			
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	8.8%	14.2%	10.7%
b Interest or Markup Payable (Days)	N/A	N/A	N/A
c Entity Average Borrowing Rate	0.0%	0.0%	0.0%

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.

Long-term Rating	Short-term Rating
AAA	A1+
AA+	A1
AA	A2
AA-	A3
A+	A4
A	
A-	
BBB+	
BBB	
BBB-	
BB+	
BB	
BB-	
B+	
B	
B-	
CCC	
CC	
C	

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

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(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

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- (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

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- (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).
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- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
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- (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)
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- (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)
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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 | 17-(a)
- (19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

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