RATING REPORT

Naveena Industries Limited (NIL)

REPORT DATE:

February 28, 2020

RATING ANALYST:

Narendar Shankar Lal
narendar.shankar@vis.com.pk

RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	BBB+	A-2	BBB+	A-2
Rating Outlook	Positive		Stable	
Rating Date	February 28, 2020		December 31, 2018	
Rating Action	*Maintained*		*Initial*	

COMPANY INFORMATION	
Incorporated in June 1989	**External auditors:** Ibrahim Shaikh & Co.
Public Unlisted Company	**Chairman:** Mr. Iftikhar Ahmed Khalid
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Shazad Khalid
Shazad Khalid (30%)	
Faisal Khalid (30%)	
Iftikhar Ahmed Khalid (25%)	
Yasmin Khalid (7.5%)	
Shazia Naveed (7.5%)	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria *Industrial Corporates (April 2019)*
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Naveena Industries Limited (NIL)

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Naveena Industries Limited (NIL) was incorporated as a Private Limited Company in March 1966. Later, the company was converted to unquoted public limited company in March 2011. The registered office of the company is situated in Karachi

The principal business of Naveena Industries Limited (NIL) includes manufacturing and export of grey cloth. NIL started commercial operations in 1966 as an embroidery unit (and later weaving) of Naveena Group which is involved in the business of spinning and weaving. The group also owns Ahmed Oriental Textile Mills Limited, which is engaged in production of yarn.

Production facilities

NIL's production facilities are located at F-130, SITE, Karachi and Mauza Kot, Kamoon Shah, Tehsil and District, Rahim Yar Khan. At present, the company operates a mix of airjet and shuttleless looms. Production details are mentioned in the following table:

Figure 1: Production Details

	FY18	FY19
Number of airjet looms	*330*	*330*
Number of shuttleless looms	*81*	*81*
Total number of looms	411	411
Installed capacity - fabric (million meters per annum)	49	49
Actual production - fabric (million meters per annum)	42	44
Capacity utilization	85.6%	88.6%

Capacity utilization increased during FY19 on account of higher actual production due to greater demand. Going forward, the management plans to conduct BMR by replacing its existing shuttleless looms based in Karachi with 72 airjet looms in Rahim Yar Khan. Facility in Karachi would be utilized to establish a processing and finishing unit.

Rating Drivers

Business risk profile is supported by favorable government policies for the textile sector and elevated demand on account of diversification efforts pursued by international players

Favorable policies & incentives of the government to enhance exports, which include provision of gas at a subsidized rate in Punjab and access to cheaper financing, bode well for the textile industry. Furthermore, ongoing diversification efforts of major international brands to reduce geographic concentration have translated to growth in demand for textile players in Pakistan. Initiatives given by the government to local exporters have also increased local demand for grey cloth for utilization in value added exports.

Topline has depicted sizeable growth on account of increase in average prices; client concentration remains on the higher side due to preference of the management to work with existing clients with sound and timely repayment history

Net sales increased by 22.6% to Rs. 6.4b (FY18: Rs. 5.3b) in FY19. Growth in sales was a function of increase in average prices as volumes were reported lower vis-à-vis the preceding year. Increase in average prices is attributed to limited supply vis-à-vis demand in the industry and rupee devaluation. Direct exports constituted around 78% (93%) of total gross sales in FY19, while the remaining sales included indirect export and local sales. Export sales were primarily geared towards to USA and European markets, while sales to China witnessed reduction due to better prices in the former markets. Client concentration is considered to be on the higher side with top 10 client accounting for 64.2% (FY18: 65.8%) of net sales in FY19. However, client concentration risk is partly mitigated due to long term association with clients.

Net Sales were reported at Rs. 3.6b at HY20. Going forward, growth in sales of the company is expected to be primarily driven by increase in average prices as the existing capacity utilization is already on the higher side. Sales mix in terms of exports and local sales is expected to remain similar level as FY19, with exports forming majority proportion of total sales.

Overall profitability profile supported by increasing topline and margins

Gross margins of the company increased to 13.8% (FY18: 11.1%) in FY19. Improvement in margins was a function of increase in average selling prices, efficient procurement of raw materials and cost savings in utilities expenses. Despite increase in production, gas expense was reported lower at Rs. 338.2m (FY18: Rs. 373.4m) due to subsidized rates provided by the government to textile companies in Punjab. Growth in topline and improvement in margins doubled the net profit of NIL to Rs. 338.2m (FY18: Rs. 169.2m) in FY19.

Improvement in margins continued to persist in HY20, with gross and net margins reported at 16.3% and 9.1%. Dividend payout ratio was reported at 14.5% (FY19: 5.9%; FY18: nil) in HY20. Going forward, growth momentum in sales is expected to improve profitability profile of NIL; however, the management expects the margins to sustain at similar level in FY19.

Improving leverage indicators

Equity base of the company was reported higher at Rs. 2.4b (FY19: Rs. 2.2b; FY18: Rs. 1.9b) at end-HY20 on account of profit retention. Total debt increased to Rs. 3.0b (FY19: Rs. 2.7b; FY18: Rs. 2.7b) due to higher utilization of short term borrowings to fund working capital requirements. Long term debt has decreased on timeline basis and primarily comprises Long Term Finance Facility (LTFF) borrowings. Going forward, management plans to acquire additional debt to fund its BMR activities. Resultantly, leverage indicators are expected to increase but will remain at manageable level.

Adequate liquidity profile

Overall liquidity profile of the company draws support from growing cash flows, sound debt coverage metrics and extended repayment period for additional long-term debt to be undertaken in future. Fund From Operations (FFO) has observed an upward trend owing to increase in profit before tax in HY20 and FY19. Resultantly, FFO in relation to long debt and FFO in relation to total debt improved to 96.7% (FY19: 64.0%; FY18: 29.5%) and 24.5% (FY19: 20.1%; FY18: 10.7%), respectively at end-HY20. Current ratio has remained over 1.0x on timeline basis. Inventory and trade debt provide adequate coverage for short term borrowings.

Corporate Governance framework depicts room for improvement

As the company is a family owned entity, Board comprises three family members including the CEO. Overall board composition and oversight has room for improvement through inclusion of independent directors. Furthermore, committees pertaining to audit and HR functions may also be established at Board level in line with best practices.

Financial Summary (amounts in PKR millions)				Appendix I
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**HY20**
Paid up Capital	199.6	199.6	199.6	199.6
Total Equity	1,728.8	1,897.9	2,216.1	2,451.4
INCOME STATEMENT	**FY17**	**FY18**	**FY19**	**HY20**
Net Sales	4,476.0	5,252.2	6,440.1	3,655.7
Profit Before Tax	147.5	161.7	402.1	312.1
Profit After Tax	100.4	169.2	338.2	275.1
RATIO ANALYSIS	**FY17**	**FY18**	**FY19**	**HY20**
FFO	257.7	287.4	550.6	373.1
FFO to Total Debt (%)	13.6%	10.7%	20.1%	24.5%
Current Ratio (x)	1.10	1.10	1.13	1.16
Gearing (x)	1.09	1.42	1.24	1.24
Leverage (x)	1.35	1.70	1.58	1.58

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix II

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 III**
Name of Rated Entity	Naveena Industries Limited (NIL)				
Sector	Textiles				
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		
	28/02/2020	BBB+	A-2	Positive	Maintained
	31/12/2018	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.				
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.				
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2020 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.				
Due Diligence Meetings Conducted		**Name**	**Designation**	**Date**	
	1	Mr. Muhammad Junaid	CFO	February 17, 2020	