# RATING REPORT

# Naveena Industries Limited (NIL)

**REPORT DATE:**

December 30, 2022

**RATING ANALYST:**

Shaheryar Khan Mangan
*shaheryar@vis.com.pk*

Sara Ahmed
*sara.ahmed@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** | Negative | | Stable | |
| **Rating Date** | December 30, 2022 | | December 31, 2021 | |
| **Rating Action** | *Maintained* | | *Upgrade* | |

**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 |
| Naveena Holdings Limited (99.9%) | |

**APPLICABLE METHODOLOGY(IES)**

**VIS Entity Rating Criteria Methodology – Industrial Corporates (August 2021)**
**https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf**

# Naveena Industries Limited (NIL)

**OVERVIEW OF THE INSTITUTION**

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

*External auditors of the company lie in Category C of the SBP Panel of Auditors.*

**RATING RATIONALE**

Naveena Industries Limited (NIL), incorporated in 1966, is primarily involved in the manufacturing and sale of grey cloth. Around four-fifth of the company's sales comprise exports sales, as it has signed a manufacturing bond, requiring it to export around 80% of the yearly output. NIL's holding entity, Naveena Holdings also owns a spinning unit by the name of Ahmed Oriental Textile Mills Limited. Such a vertically integrated structure helps the company to benefit from economies of scale and ensure improved operational efficiency.

### Production Facilities

NIL's production facilities are located in Karachi and Rahim Yar Khan. At present, the Company operates a mix of air-jet and shuttle-less looms. Production details are mentioned in the following table:

*Table 1: Production details*

| | FY20 | FY21 | FY22 |
|---|---|---|---|
| TOTAL NUMBER OF LOOMS | 411 | 411 | 414 |
| INSTALLED CAPACITY (MILLION METERS PER ANNUM) | 45 | 45 | 45 |
| ACTUAL PRODUCTION (MILLION METERS PER ANNUM) | 36 | 37 | 33 |
| CAPACITY UTILIZATION | 80% | 82% | 73% |

Capacity utilization decreased during FY22 on account of lower demand led by the slowdown in the market.

### Sector Update

- Pakistan's export growth came in at 14% and 27% in FY21 and FY22 respectively. Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21), however, in FY22 exports finally broke the threshold, coming in at USD 32.4b.

- As illustrated in the table below, the composition of textile exports has depicted improvement in, with contribution from higher value added segment increasing from 77.2% in FY20 to 80.8% in FY22 of aggregate textile exports.

*Table 2: Segment-wise textile Exports (All Figures in USD' Millions, except for percentages)*

| | FY20 | FY21 | FY22 | 1Q'FY22 | 1Q'FY23 | FY20 | FY21 | FY22 | 1Q'FY22 | 1Q'FY22 |
|---|---|---|---|---|---|---|---|---|---|---|
| **High Value-Added Segment** | **9,669** | **12,427** | **15,605** | **3,561** | **3,749** | **77.2%** | **80.7%** | **80.7%** | **80.6%** | **81.8%** |
| - Knitwear | 2,794 | 3,815 | 5,121 | 1,145 | 1,321 | 22.3% | 24.8% | 26.5% | 25.9% | 28.8% |
| - Readymade Garments | 2,552 | 3,033 | 3,905 | 861 | 912 | 20.4% | 19.7% | 20.2% | 19.5% | 19.9% |
| - Bed wear | 2,151 | 2,772 | 3,293 | 803 | 780 | 17.2% | 18.0% | 17.0% | 18.2% | 17.0% |
| - Towels | 711 | 938 | 1,111 | 241 | 237 | 5.7% | 6.1% | 5.8% | 5.5% | 5.2% |

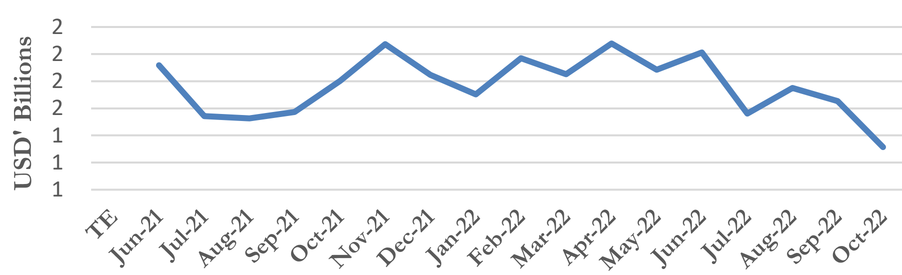
| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| - Made-up Articles (Excl. towels & bed wear) | 591 | 756 | 849 | 197 | 180 | 4.7% | 4.9% | 4.4% | 4.5% | 3.9% |
| - Art, Silk & Synthetic Textile | 315 | 370 | 460 | 108 | 108 | 2.5% | 2.4% | 2.4% | 2.4% | 2.4% |
| - Others | 555 | 743 | 866 | 206 | 211 | 4.4% | 4.8% | 4.5% | 4.7% | 4.6% |
| **Low to Medium Value-added Segment** | **2,858** | **2,972** | **3,717** | **860** | **835** | **22.8%** | **19.3%** | **19.2%** | **19.4%** | **18.2%** |
| - Cotton Cloth | 1,830 | 1,921 | 2,438 | 557 | 581 | 14.6% | 12.5% | 12.6% | 12.6% | 12.7% |
| - Cotton Yarn | 984 | 1,017 | 1,207 | 289 | 236 | 7.9% | 6.6% | 6.2% | 6.5% | 5.2% |
| - Others | 43 | 34 | 72 | 14 | 18 | 0.3% | 0.2% | 0.4% | 0.3% | 0.4% |
| **Total** | **12,527** | **15,399** | **19,332** | **4,421** | **4,584** | | | | | |

**Source: PBS**

- After posting windfall margins in FY21 and H1'FY22, margins of textile operators, particularly spinners, weavers and dying units, have come under pressure during the period Jan-Sep'2022, mainly on account of higher input costs and recessionary trend in export markets.

- The recessionary trend in Pakistan's major export textile export markets, mainly North America and EU, has started to materialize in Pakistan's MoM export proceeds, with receipts for October 2022 (at USD 1.36b) being lower by 11% and 15% vis-à-vis preceding month and corresponding period last year respectively, as also illustrated in the table below.

*Figure 1: MoM Textile Exports (TE) (In USD' Billions)*




- Given expected industrial gas load shedding during the period Dec-Feb'22, and prevailing recession in major export markets and peak inventory levels, textile export proceeds are expected to fall by ~10% in FY23. Furthermore, profitability margins of textile operators, particularly spinners, weavers and dying companies, are expected to remain under pressure given higher input and financial costs.

## Rating Drivers

**Growth in top-line supported by price increase. Volumes depict decline.**

- Net sales of the Company increased by 22% to Rs.8.6b (FY21: Rs.7.0b). The increase is attributable to a blend of a higher average selling price and currency devaluation, albeit volume of sales declined in FY22. Volume sales in FY22 were down by 18% while price increase was recorded at 50%.

- Sales of the Company encompass 76.8% direct exports, 17.3% indirect exports and 6% in local sales. Share direct exports remained at the same level vis-à-vis previous year. Top ten Customer concentration diluted in FY22 to 81.25% (FY22: 94.74%), albeit it remains on the higher side.

- During 1QFY'23, sales of the Company stood at Rs.2.5b (1QFY'22: Rs.1.8b), higher than comparative period last year, primarily supported by currency devaluation. Volumes have remained under pressure amid economic slowdown in international markets. The Company had reduced its capacity in the last few months in line with the slower demand however, some pace has picked up in the current month with capacity operating at 80% plus.

**Margins of the Company have deteriorated. Improvement in the same will remain critical, going forward**

- Despite gross margins improving on account of currency gains, net margins have been impacted adversely due to higher financial cost largely contributed by exchange loss on FE loans. Net margins in Q1'23 were recorded at 1.7%.

- Going forward with increase in the borrowing in FY22, its impact is going to be materialized in the future. Hence, the rising finance cost will continue to be a drag on the profitability of the Company.

**Adequate liquidity profile.**

- As a result of lower profitability, funds from operations (FFO) for FY22 and Q1'23 have declined, consequently impacting FFO coverages. In addition, debt profile has also elevated with new Long term loan drawdowns and higher working capital requirement. FFO to Total debt and was 2.2% in 1QFY'23.

- Liquidity profile remains adequate for now with current ratio at 1.21x, and Short term debt coverage at 0.9x in 1QFY'23. Working capital cycle however reflects an increase on account of inventory buildup as a result of slowdown in market demand. In case the slowdown is extended, liquidity may come under pressure. Improving liquidity profile will remain a key rating driver.

- Debt servicing is manageable for now however, it remains vulnerable to continued dismal market conditions.

**Capitalization indicators elevated as a result of expansion. Profit retention will be critical.**

- Gearing levels were higher at FY22 end and Q1'23 due to drawdowns related to capacity expansion as well as working capital requirements. In addition, dividend payout of Rs.39m was made in FY22 as well as Q1'23, resulting in equity base unchanged at Rs.3b. We expect pressure on gearing to continue and therefore retention of profitability in the Company for improvement in capitalization indicators will be critical. Management does not expect any further capex related borrowings in the future.

- Gearing levels were higher at FY22 end and Q1'23 due to drawdowns related to capacity expansion as well as working capital requirements. In addition, dividend payout of Rs.39m was made in FY22 as well as Q1'23, resulting in equity base unchanged at Rs.3b. We expect pressure on gearing to continue and therefore retention of profitability in the Company for improvement in capitalization indicators will be critical. Management does not expect any further capex related borrowings in the future.

## Financial Summary (amounts in PKR millions) — Appendix I

| BALANCE SHEET | FY19 | FY20 | FY21 | FY22 | 1QFY'23 |
|---|---|---|---|---|---|
| Fixed Assets | 2,483.8 | 2,329.7 | 3,271.6 | 4,875.3 | 4,805.1 |
| Stock-in-Trade | 1,602.6 | 1,608.8 | 1,762.5 | 3,471.6 | 3,355.3 |
| Trade Debts | 474.5 | 636.7 | 828.5 | 709.1 | 863.3 |
| Cash & Bank Balances | 804.6 | 852.4 | 822.4 | 941.9 | 940.2 |
| Refunds Due from Government and Other Receivables | 288.1 | 298.7 | 291.0 | 609.2 | 517.7 |
| Total Assets | 5,720.5 | 5,814.2 | 7,184.8 | 10,774.4 | 10,775.1 |
| Trade and Other Payables | 651.8 | 703.7 | 809.6 | 1,135.7 | 1,176.8 |
| Long Term Debt (including current maturity) | 860.2 | 751.7 | 1,005.7 | 2,080.1 | 2,153.3 |
| Short Term Debt | 1,885.3 | 1,901.8 | 1,693.4 | 3,578.4 | 3,538.2 |
| Total Debt | 2,745.5 | 2,653.5 | 2,699.1 | 5,658.5 | 5,691.5 |
| Total Liabilities | 3,504.4 | 3,451.5 | 3,591.0 | 6,951.2 | 6,941.4 |
| Paid up Capital | 199.6 | 199.6 | 199.6 | 199.6 | 199.6 |
| Total Equity (without surplus on revaluation) | 2,216.1 | 2,362.7 | 2,812.3 | 3,041.7 | 3,052.2 |

| INCOME STATEMENT | FY19 | FY20 | FY21 | FY22 | 1QFY'23 |
|---|---|---|---|---|---|
| Net Sales | 6,440.1 | 6,681.9 | 7,048.9 | 8,610.0 | 2,539.3 |
| Gross Profit | 887.6 | 884.0 | 951.6 | 1,243.9 | 449.7 |
| Profit Before Tax | 402.1 | 357.5 | 547.2 | 378.8 | 68.0 |
| Profit After Tax | 338.2 | 292.0 | 476.6 | 277.4 | 42.3 |

| RATIO ANALYSIS | FY19 | FY20 | FY21 | FY22 | 1QFY'23 |
|---|---|---|---|---|---|
| Gross Margin (%) | 13.8% | 13.2% | 13.5% | 14.4% | 17.7% |
| Net Profit Margin | 5.3% | 4.4% | 6.8% | 3.2% | 1.7% |
| FFO | 550.6 | 461.2 | 626.2 | 539.1 | 123.5 |
| FFO to Total Debt (%) | 20.1% | 17.4% | 23.2% | 9.5% | 2.2% |
| FFO to Long Term Debt (%) | 64.0% | 61.3% | 62.3% | 25.9% | 5.7% |
| Debt Servicing Coverage Ratio (x) | 2.0 | 1.5 | 3.6 | 1.7 | 0.9 |
| ROAA (%) | 6.2% | 5.1% | 7.3% | 10.3% | 1.6% |
| ROAE (%) | 16.4% | 12.8% | 16.0% | 29.0% | 4.4% |
| Gearing (x) | 1.24 | 1.12 | 0.96 | 1.86 | 1.86 |
| Leverage (x) | 1.58 | 1.46 | 1.28 | 2.29 | 2.27 |
| Current Ratio (x) | 1.13 | 1.25 | 1.41 | 1.17 | 1.21 |
| (Stock in trade + Trade Debts) / Short Term Borrowings (%) | 110.2% | 118.1% | 153.0% | 116.8% | 119.2% |

## ISSUE/ISSUER RATING SCALE &DEFINITIONS — Appendix I

**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 II |
|---|---|---|---|---|---|---|
| **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** | | | | | |
| | 30/12/2022 | A- | A-2 | Negative | Maintained | |
| | 31/12/2021 | A- | A-2 | Stable | Upgrade | |
| | 20/11/2020 | BBB+ | A-2 | Stable | Maintained | |
| | 24/04/2020 | BBB+ | A-2 | Rating Watch - Negative | Maintained | |
| | 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. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2022 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS. | | | | | |
| **Due Diligence Meetings Conducted** | **S.No** | **Name** | **Designation** | **Date** | | |
| | 1 | Mr. Muhammad Junaid | CFO | December 12, 2022 | | |
| | 2 | Mr. Hasan Saleem | General Manager Finance & Accounts | December 12, 2022 | | |