RATING REPORT

Naveena Industries Limited

REPORT DATE:
January 15, 2024

RATING ANALYST:
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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	Stable		Negative	
Rating Date	January 15, 2024		December 30, 2022	
Rating Action	*Maintained*		*Maintained*	

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)
Applicable 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**

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, 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 fabric. 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.

Company Profile:

Naveena Industries Limited (NIL), incorporated in 1966, is primarily involved in the manufacturing and sale of fabric cloth. Around four-fifths 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. Moreover, the Company has recently established its Home Textile Division which will focus mainly on exports to the US and UK markets.

Key Rating Drivers

Business risk remains elevated amid weak macroeconomic environment, high-interest rates, inflationary pressures, rising raw material costs, ongoing energy crisis in the country, and a global slump in demand. All these factors pose a challenge to the sector in terms of margins sustainability and future growth.

Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21), however, in FY22 exports broke the threshold, clocking in at USD 32.4b. Textile sector contributes nearly one-fourth to industrial value-added segment and provides employment to about 40% of the industrial labor force[1]. Contributing around 8.5% to the country's gross domestic product (GDP), with an estimated market size of around Rs. 4.0tr, textile sector has maintained an average share of about 60% in national exports over the years.

The lingering effects of Covid-19 pandemic continue to shape the Pakistan's textile industry. Initially, as lockdowns lifted, the industry capitalized on opportunities, securing production contracts with western countries. This redirection of substantial volumes to Pakistan, was complemented by government import tax reductions and subsidized covid-related financing programs such Temporary Economic Refinance Facility (TERF), spurred robust export growth during FY22. However, a subsequent phase presented new challenges. Global interest rate hikes aimed at curbing post-pandemic inflation, coupled with geopolitical unrest such as the Ukraine conflict, led to supply chain disruptions and energy crisis. These factors led to a global demand slowdown in major textile economies, reflected in a 10% year-on-year decline in Pakistan's textile exports in FY23, totaling USD 16.7b (FY22: USD 18.5b). As per the data from Pakistan Bureau of Statistics (PBS), High Value-Added Segments made up over 82.2% (FY22: 80.7%) of the total textile exports in FY23.

Flash floods in Sindh and Southern Punjab monsoon wreaked havoc on the cotton crop last year. This catastrophe led to a historic low production level of 4 million bales of cotton in 2022, compared to a 12 million bales annual demand. Consequently, local cotton prices reached 12-year high of over Rs. 22,000 per 40kg during the year as well as import of raw cotton rose by ~20% in USD terms during FY22, as compared to the preceding year. This situation led to higher working capital requirements, adversely affecting profit margins and liquidity profile of textile entities, particularly spinners, weavers, and dyeing companies. Supported by favorable weather and timely government intervention, cotton production in the country is estimated to increase to 12.7 million bales during the current season (FY24). 4.0 million bales have already been produced during Q1FY24, marking an impressive 80.0% increase compared to the same period last year.

The industry is facing business risk due to weak macroeconomic environment both globally and locally, high-interest rates, inflationary pressures, rising raw material costs, ongoing energy crisis in the country, and a global slump in demand, primarily from North America and Europe.

Previously, the sector also enjoyed incentives provided by the government through a five-year textile policy (2020-25), including preferential energy rates, low-interest financing schemes, and timely payments of various refunds, easing liquidity constraints for local players. However, the prevailing economic instability along with advisory from the IMF led to the reduction or withdrawal of many of these fiscal supports. This along with contractionary monetary policy and political uncertainties in the country are the key business risk factors faced by the industry. In the long run, improvement in value addition, investment in technology and optimization of energy cost would define the future prospects of textile exports.

Margins demonstrate improvement despite a contraction in the top line in FY23.

The Company's topline witnessed a decline of ~4% in FY23, primarily due to sluggish demand amid an economic recession in both local and export markets. However, the gross and operating margins improved, reaching 16.7% (FY22: 14.4%) and 12.2% (FY22: 8.6%) respectively. This improvement is attributed to the timely purchase of raw materials, leveraging the rising price trend by accumulating inventories at lower costs. In 1QFY'24, gross margins remained stable at 16.7%, while operating margin slightly decreased to 11.9%.

Net margins in FY23 and 1QFY24 were constrained by elevated finance costs arising from heightened policy rates in the country, despite a decrease in debt utilization.

Capitalization indicators improved due to a reduction in debt drawdowns.

In FY23, the Company exhibited improvement in its capitalization indicators, as evidenced by gearing and leverage indicators at 1.6x (FY22: 1.9x) and 1.9x (FY22: 2.3x), respectively. This improvement is primarily attributed to decreased short-term borrowing resulting from lower working capital requirements. The Company had previously relied on higher short-term debt utilization due to an accumulation of stock in trade. The increase in finished goods in stock was due to delayed order pickups by international clients, reflecting reduced demand in their respective geographic regions. However, management has managed to limit fresh buildup of inventory, thus a decline has been observed of the same in FY23, leading to a lower drawdown of short-term facilities.

Liquidity profile adequate while debt service profile stressed by high finance burden. However, healthy cash reserves provide comfort to ratings.

The Company has continued to sustain an adequate liquidity profile, with the current ratio holding steady at 1.2x from FY21 to 1QFY24. Simultaneously, the cash ratio has seen a rise to 0.3x in 1QFY24, up from 0.2x in FY22, attributed to the Company's management of a healthy foreign currency account.

Meanwhile, the debt service coverage (DSCR) profile experienced deterioration in FY23 and subsequently in 1QFY24 due to significant pressure from finance costs amid an 825-bps increase in local interest rates during FY23. However, management plans on utilizing its healthy cash reserves to reduce its debt drawdown and ease pressure off of its coverage profile going forward. Moreover, inventory and trade debts provide sufficient cushion to short-term borrowings with a ratio of 1.2x in FY23 and 1QFY24 (FY22: 1.2x).

Key Considerations for future Ratings

Going forward, ratings will remain sensitive to the Company's ability to improve its coverage and capitalization profile in line with assigned ratings. Moreover, maintenance of key operational metrics will also continue to be important consideration for future ratings.

FINANCIAL SUMMARY				(PKR Millions)
BALANCE SHEET	**FY21**	**FY22**	**FY23**	**3MFY24**
Property, plant and equipment	3,216.9	4,828.6	4,705.3	4,626.8
Stock-in-trade	1,762.5	3,471.6	2,514.1	2,550.1
Trade debts	828.5	709.1	841.1	838.9
Cash and bank balances	822.4	941.9	1,281.7	1,364.2
Total Assets	7,184.8	10,774.4	9,830.0	9,883.6
Trade and Other Payables	809.6	1,135.7	886.3	1,081.5
Long-term Debt (incl. current portion)	1,005.7	2,080.1	2,026.2	1,985.7
Short-term Debt	1,693.4	3,578.4	2,804.0	2,810.6
Total Debt	2,699.1	5,658.5	4,830.3	4,796.3
Total Liabilities	3,591.0	6,951.2	5,939.3	6,013.4
Paid up Capital	199.6	199.6	199.6	199.6
Equity (excl. Revaluation Surplus)	2,812.3	3,041.7	3,109.2	3,088.8
INCOME STATEMENT	**FY21**	**FY22**	**FY23**	**3MFY24**
Net Sales	7,048.9	8,610.0	8,268.9	1,807.9
Gross Profit	951.6	1,243.9	1,384.6	302.5
Operating Profit	611.6	743.9	1,011.5	216.0
Finance Costs	106.7	371.7	830.0	190.9
Profit Before Tax	547.2	378.8	190.4	27.9
Profit After Tax	476.6	277.4	107.2	9.6
RATIO ANALYSIS	**FY21**	**FY22**	**FY23**	**3MFY24**
Gross Margin (%)	13.5%	14.4%	16.7%	16.7%
Net Margin (%)	6.8%	3.2%	1.3%	0.5%
Funds from Operation (FFO)	626.2	539.1	541.4	72.1
FFO to Total Debt* (%)	23.2%	9.5%	11.2%	6.0%
FFO to Long Term Debt* (%)	62.3%	25.9%	26.7%	14.5%
Gearing (x)	1.0	1.9	1.6	1.6
Leverage (x)	1.3	2.3	1.9	1.9
Debt Servicing Coverage Ratio* (x)	2.4	1.7	1.3	0.9
Current Ratio	1.4	1.2	1.2	1.2
(Stock in trade + trade debts) / STD (x)	1.5	1.2	1.2	1.2
Return on Average Assets* (%)	7.3%	3.1%	1.0%	0.4%
Return on Average Equity* (%)	16.0%	7.5%	2.8%	1.0%

**Annualized, if required*

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					
	15/01/2024	A-	A-2	Stable	Maintained	
	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.					
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Due Diligence Meetings Conducted	**S.No**	**Name**	**Designation**	**Date**		
	1	Mr. Muhammad Junaid	CFO	December 27, 2024		