RATING REPORT

Naveena Exports Limited

REPORT DATE:
February 25, 2022

RATING ANALYST:

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RATING DETAILS				
	Latest Ratings		Previous Ratings	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	A	A-1	A	A-1
Rating Date	*February 25, 2022*		*February 23, 2021*	
Rating Action	Maintained		Maintained	
Rating Outlook	Positive		Stable	

COMPANY INFORMATION	
Incorporated in 1989	**External auditors:** Ibrahim, Shaikh & Co. Chartered Accountants
Public Unlisted Company	**Chairman of the Board:** Mr. Asif Riaz
Key Shareholding (more than 5%)	**Chief Executive Officer:** Mr. Masood Riaz
Naveena Group (Private) Limited – 99.99%	**Director:** Mr. Saqib Riaz

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Corporates (August,2021)
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Naveena Exports Limited

OVERVIEW OF THE INSTITUTION

Incorporated in 1989, Naveena Exports Limited (NEL) is a wholly owned subsidiary of Naveena Group managed by three brothers: Mr. Asif Riaz (Chairman), Mr. Masood Riaz (Chief Executive Officer) and Mr. Saqib Riaz (Director).

NEL is fully compliant with International Social and Environmental & Quality standards. The company has a liaison office in Bangladesh with sales representatives in US, South America, Europe and Turkey

Profile of Chairman

Mr. Asif Riaz possesses over 30 years of experience in the textile sector. He currently is Chairman of Pakistan Denim Manufacturers and Exporters Association. He has been associated with Naveena since its inception.

RATING RATIONALE

Naveena Exports Limited ('NEL' or 'the Company') has completed 32 years in the business of manufacturing and sale of yarn and denim fabric. Headquartered in Karachi, the Company has its manufacturing facilities located in Karachi and Lahore with total annual installed capacity of 49.28m (Lbs) of spinning yarn and 35.5m (Mtr) of denim production.

Expansion

The management has planned to enhance its spinning capacity by almost 100% (new spindles to be installed: 39,504); for which land has already been purchased in Nooriabad area. Total cost of the project is estimated at Rs 7.3b; of which three-fourth will be funded through LTFF financing facility and the remaining will be financed by internal capital generation. 70% L/Cs for machinery has already been established. Timeline for the completion of this expansion project is FY24.

Group Formation

During FY 2020-21, a Scheme of Arrangement (Scheme) was filed by the Company before the Honorable Sindh High Court (SHC), after getting the required approvals from the Board of Directors and shareholders to transfer Company's investment in Naveena Steel Mills (Private) Limited (NSMPL) amounting to Rs. 5,999,999,000 to Naveena Group (Private) Limited. This scheme was approved by the court on December 01, 2021 and accordingly shares of NSMPL were transferred to Naveena Group (Private) Limited on December 20, 2021.

Further, as part of Group formation, Naveena Exports Limited has now became wholly owned subsidiary of Naveena Group (Private) Limited as of December 31, 2021.

Sector Update

- Subsequent to posting export contraction in FY20 - owing to the pandemic-induced slowdown experienced in H2'FY20 – Pakistan's export base grew by 14% in FY21, which is partly attributable to a low base effect. Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21). So the uptick is largely aligned with historical numbers and is not considered material.

- Share of textile exports in total exports has oscillated in the range of 54-59%, coming in at 57% during the past 2-years (FY20-21). In FY21, owing to the similar low-base effect, as discussed above, textile exports were up 13%.

- In USD' terms textile exports have grown at a CAGR of 4.4% during the past 3-year period (FY19-FY21), despite depreciation in average USD/PKR parity of 24%, 16%, and 1% in FY19, FY20 and FY21 respectively.

- Textile exports in H1'FY22 were 34% higher than SPLY. With additional capacities coming online in January 2022, textile exports for FY22 are likely to exceed the annualized figure of USD 18b.

- The composition of textile exports has depicted improvement in the last 4-yar period, as contribution from lower to medium value added segment has been decreasing from 27.1% in FY18 to 19.3% in FY21 of aggregate textile exports.

- Cotton production in Pakistan, on the other hand, was at its lowest level in decades for FY21. Cotton prices rose to a new 11-year high of ~Rs. 13,000/maund as a result of the production shortage. Given favorable weather conditions in first half of FY22, cotton production in Pakistan posted strong growth, with cotton crop for Jul-Nov'21 (Rabi) season being 81% higher than SPLY. Nevertheless, the upward momentum in cotton pricing continued in H1'FY22, with prices as of December 2021 hovering at ~Rs. 17,800 per mound.

- The margins of textile operators have broadly depicted improvement partly on account of inventory gains on sizable increase in cotton pricing and partly due to favorable exchange rate movement. Nevertheless, higher raw material pricing has increased the working capital requirements for textile operators, which is likely to weigh on the liquidity of textile players.

Business Update - NEL

Sales & Operations

- NEL's capacity utilization remained strong throughout the period under review, particularly in the spinning segment, while finished fabric segment capacity utilization also stood at 100% in 1HFY'22 after being on the lower side in the past 2-year period due to pandemic.

- Subsequent to posting same performance in FY21 as compared to FY20, owing to the pandemic-induced slow down, NEL's revenue base grew by 13.7% in FY21. Revenue growth momentum has remained strong in the ongoing year, coming in at ~16% in H1'FY22 vis-à-vis SPLY. Revenue growth for FY22 is projected to remain in line with the interim period trend.

- The growth in FY21 was mainly a product of higher revenues from Yarn segment, which contributed ~88% of the topline increase for the period. Within the yarn segment, increasing revenues were equally a part of higher quantitative offtake and price increases. In the fabric segment, the revenues remained relatively flat, given 2.3% decline in quantitative offtake in combination with pricing increase, keeping revenue growth limited at 2%.

- The trend in H1'FY22 is considered positive, given increasing composition of denim fabric sales and significant price increases in the same composing 95% of overall sales.

- NEL's gross margins came under pressure in FY21, given the change in product mix. Nevertheless, these have rebounded in H1'FY22 owing to increasing denim fabric sales. In comparison to similar rated peers, the margin is considered superior. As per management, higher margins in comparison with the peers is mainly attributable to focused R&D efforts as a result of which the Company has acquired expertise in fulfilling certain market niches of denim fabric.

- Bottom-line of the Company stood 8% higher YoY for FY21. The stability in NEL's net margin is viewed positively from a ratings purview.

- The management projects revenue growth to come at ~10% during the rating horizon. In FY25, as the planned spinning plant becomes operational, the projections depict 80% increase.

Cash Flow Coverages

- Strong growth in revenues translates in similar growth in cash flows and hence a strong debt servicing capacity. As of Dec'21, the FFO to Debt implies full debt repayment with just a little under 3 year FFO. The Company' DSCR has decreased in the ongoing year, since a sizable principal payment on debt has become due in FY22.

- The cash conversion cycle has posted improvement in FY21 owing to reduction in inventory days. Stock in trade to sales has been reduced to 22.3% (FY20: 28.1%).

- Current ratio has remained consistently above 1x, supporting the short term rating assessment of NEL. Furthermore, coverage of short term debt by trade debts and inventory is considered adequately high.

Capitalization

- Equity base of the Company has improved on account of internal capital generation, growing at a CAGR of 20.7% during the last 5 years. (FY17-FY21). This is mainly a result of stable net margins, growing offtake and full profit retention.

- The Company's debt largely constitutes facilities extended under SBP's concessionary financing schemes, comprising 85% of the debt.

- Given adequate profit retention, the Company's gearing remained conservatively low during the period FY19-21. In H1'FY22, with Naveena Steel Mills (Private) Limited (NSMPL) being carved out of NEL and being absorbed by Naveena Group, the gearing has trended up, albeit remaining below 1x. Cognizant of the increase in the same, the shareholders plan to maintain policy of full profit retention in order to pull back gearing down to historical average of 0.7x.

<u>Key Rating Drivers</u>

Rating incorporates Sponsor Profile
NEL's rating incorporates NEL's sponsor profile. The Company is part of the Naveena Group, which is a diversified conglomerate, having operations in textile, steel, power, real estate and capital investment sectors.

Rating takes into account NEL's market positioning and long operational track record
Having been in the business for over three decades, NEL has established itself as a leading denim sector exporter. With revenue base diversified between exports and indirect exports, the same depicts diversification, while country-wise concentration is also considered manageable.

Rating incorporates Stability in Profitability and strong Cash Flow Coverages
Rating incorporates strong revenue growth, stable net margins and adequate cash flow coverage of debt. The gross margin depicted some contraction in FY21, given changes in product mix, albeit remain superior to peers. Going forward, margins are expected to remain strong during the rating horizon.

Rating incorporates Conservative Capitalization
Given stable net margin, growing offtake and full profit retention, equity base has grown at a CAGR of 20.7% during the last 5 years. (FY17-FY21). In H1'FY22, the

	equity base has contracted, given carving out of Naveena Steel. Nevertheless, gearing remains adequately low and is expected to recede back to historical levels, on the back of full profit retention.

Naveena Exports Limited Appendix I

FINANCIAL SUMMARY	*(amounts in PKR millions)*		
BALANCE SHEET	**FY19**	**FY20**	**FY21**
Paid Up Capital	850	850	850
Total Equity	11,316	13,698	16,273
INCOME STATEMENT			
Net Sales	15,612	15,506	17,627
Profit Before Tax	2,482	2,576	2,787
Profit After Tax	2,437	2,382	2,574
RATIO ANALYSIS			
FFO	3,083	2,964	3,320
Current Ratio (x)	1.55	1.35	1.27
Gearing (x)	0.71	0.74	0.66

ISSUE/ISSUER RATING SCALE & DEFINITION 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 Exports Limited
Sector	Textile Industry
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				
25/02/2022	A	A-1	Positive	Maintained
23/02/2021	A	A-1	Stable	Maintained
22/04/2020	A	A-1	Rating Watch-Developing	Maintained
31/01/2020	A	A-1	Stable	Upgrade
08/04/2019	A-	A-1	Positive	Upgrade
19/04/2018	A-	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.
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Due Diligence Meeting Conducted

Name	Designation	Date
Mr. Waqas Hanif	Chief Financial Officer	03-Feb-2022