RATING REPORT

Naveena Exports Limited

REPORT DATE:
April 12, 2023

RATING ANALYSTS:
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RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A	A-1	A	A-1
Rating Outlook	Stable		Positive	
Rating Action	Maintained		Maintained	
Rating Date	*Apr 12, 2023*		*Feb 25, 2022*	

COMPANY INFORMATION	
Incorporated in 1989	**External Auditors:** Ibrahim, Shaikh & Co. Chartered Accountants
Public Limited Company – Unquoted	**Board Chairman:** Mr. Asif Riaz
Key Shareholders (with stake 5% or more):	**CEO:** Mr. Masood Riaz
Naveena Group (Private) Limited ~100%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Industrial 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).

Initially established as a private limited company, NEL was converted into unquoted public limited entity in 2006.

Profile of Chairman

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

RATING RATIONALE

Corporate Profile

Naveena Exports Limited (NEL), with a 34-year operating track record specializes in the production and sale of yarn and denim fabric. It has a global presence with office in Bangladesh and sales representatives in US, South America, Europe, and Turkey. The company is fully compliant with international social, environmental and quality standards, and employs over 2,000 workers.

Corporate Restructuring – Formation of Holding Company

In a recent restructuring process, the company underwent a transfer of ownership under the scheme of arrangement to Naveena Group (Private) Limited, which now serves as the holding company for NEL, Naveena Steel Mills, and Naveena Developers, Naveena Builders and Naveena Capital.

Environmental, Social, & Governance (ESG) Initiatives

NEL has an effluent treatment plant to treat industrial wastewater and an EPA-approved contractor to handle hazardous waste, minimizing ecological harm. As part of its commitment to environmental sustainability, the company has undertaken several proactive initiatives, such as upgrading looms, installing waste heat recovery boilers, utilizing energy-efficient lighting, neutralizing effluent pH through flue gases, implementing solar photovoltaic (PV) systems, and conducting afforestation projects. The company is also a member of WWF and supports their annual tree-planting efforts at various sites.

Operational Performance

Headquartered in Karachi, the company operates its spinning unit in Raiwand, Lahore while denim manufacturing units (I & II) are located in Korangi, Karachi and Raiwand, Lahore; both having equal capacity. Since last review, installed capacity for fabric division has risen by ~17% to 37.8m meters per year, while that of the yarn segment has remained largely unchanged. Production levels have increased considerably in FY22, resulting in higher utilization rates. However, the same have been impacted in the current fiscal year by global slowdown in demand and challenging macro-economic environment.

Table: Capacity & Production Data (Figures in millions)

	FY21	FY22	6M'FY23
Fabric Division			
Installed Capacity (meters)	35.5	37.8	18.9
Actual Production (meters)	27.4	35.9	10.2
Capacity Utilization	***77%***	***95%***	***54%***
Yarn Segment			
Installed Capacity (kgs)	22.4	22.6	10.7
Actual Production (kgs)	21.1	21.2	7.8
Capacity Utilization	***94%***	***94%***	***73%***

Management planned capacity expansion of the spinning segment, initially set to conclude by FY24, has been halted. However, land of worth Rs. 500m was acquired for the project during the year while financed through internally generated capital.

Key Rating Drivers

Business risk profile is constrained by current weak macroeconomic environment both globally and locally, demand slowdown, high interest rate situation, inflationary pressures and recent floods adversely affecting cotton crop while ongoing energy crisis in the country pose a challenge to 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 finally broke the threshold, coming in at USD 32.4b. Textile sector contributes nearly one-fourth to industrial value-added segment and 8.5% to the country's GDP, with an estimated market size of around Rs. 4.0tr. Barring seasonal and cyclical fluctuations, textiles sector has maintained an average share of about 60% in national exports.

Table: Pakistan Export Statistics (in USD millions)

	FY20	FY21	FY22		7M'FY22	7M'FY23
Pakistan Total Exports	22,536	25,639	32,450		17,285	16,882
Textile Exports	12,851	14,492	18,525		10,369	10,377
PKR/USD Average rate	158.0	160.0	177.5		170.0	224.7

Source: SBP

Export revenues from textile sector have noted sizeable growth over the years (FY22: $19.3b FY21: $15.4b; FY20: $12.5b; FY19: $13.6b). Knitwear, Readymade and Bed wear segments continue to contribute higher than other segments, with a cumulative contribution of more than 60% in textile exports. While the growth was primarily driven by volume (excluding knitwear and cotton yarn), higher prices also boosted exports.

Table: Textile Export Details (in USD millions)

	FY20	FY21	FY22		7M'FY22	7M'FY23
High Value-Added Segment	**9,669**	**12,427**	**15,605**		**8,853**	**8,326**
- Knitwear	2,794	3,815	5,121		2,888	2,803
- Readymade Garments	2,552	3,033	3,905		2,163	2,126
- Bed wear	2,151	2,772	3,293		1,924	1,639
- Towels	711	938	1,111		615	583
- Made-up Articles	591	756	849		491	435
- Art, Silk & Synthetic Textile	315	370	460		263	239
- Others	555	743	866		509	500
Low to medium Value-Added Segment	**2,858**	**2,972**	**3,717**		**2,080**	**1,714**
- Cotton Cloth	1,830	1,921	2,438		1,352	1,225
- Cotton Yarn	984	1,017	1,207		688	449
- Others	43	34	72		41	39
Total	**12,527**	**15,399**	**19,332**		**10,933**	**10,040**

Source: PBS

Cotton prices rose to a new 12-year high of ~Rs. 21,600/maund as of March'22, as a result of the shortage and higher input costs of fertilizer and energy. Cotton imports were also up 19.8%, in USD terms, for FY22 vis-à-vis preceding year.

Table: Cotton Prices Trend (In Rs.)

	FY19	FY20	FY21	FY22
Per Maund	8,770	8,860	13,000	17,380
YoY % Change	26%	1%	32%	34%

Floods in Sindh and Southern Punjab during recent monsoon season have caused significant damage to the cotton crop. According to industry estimates, ~45% of the crop has been washed, worth more than $2.5b, resulting in significant price increases. The government has announced facilitation for raw materials imports to compensate for domestic shortages. Nonetheless, in addition to affecting profit margins, higher raw material pricing is expected to increase the working capital requirements, which is likely to have a negative impact on the liquidity profile of textile operators, particularly spinners, weavers and dying companies.

Global and domestic challenges, such as slowdown in export demand (primarily from North America and the EU, which has begun to materialize in Pakistan's monthly export proceeds) due to recessionary trend, industrial gas load shedding expected in the country, and rising production costs due to inflation, will weigh on the business risk profile going forward. These factors may result in competitive market pricing for exporters.

Competitive edge from top global retail brands as major customers drives revenue growth through price, volume, and rupee devaluation impact. However, demand slowdown impacted sales growth in the current fiscal year.
While crossing the Rs. 21b mark, sales revenue posted a strong double-digit annual growth rate for two years in a row. The YoY growth of ~21% is primarily driven by an increase in prices in dollar terms, with comparable export volumes. In terms of indirect export and local sales, growth is driven by both volumetric and price uptick. Export sales, including direct and indirect exports, contribute to over 90% of entire revenues on a timeline, while the rest is derived from local sales. Fabrics continue to comprise entirety of export revenues, while yarn is sold exclusively in the local market.

Two-third of total exports are directed to Bangladesh and Egypt, with the remainder is spread across various regions such as Turkey, Srilanka, Mexico, Columbia, UAE and others. Client concentration is deemed satisfactory, with top ten clients contributing to ~20% of total sales, with the majority clients catering to well-known brands like Levi Strauss and Zara.

Despite declining volumes due to recent slowdown from global economic downturn, current fiscal year has seen sustained revenues of Rs. 13.7b in 8M'FY23, with consistent price increases in both export and local sales. Management projects full year sales to persist at previous year levels.

Record high bottom-line achieved by the company during FY22 due to strong revenue growth and jump in gross margins.
Gross margins have largely remained steady over time but slightly contracted in the current fiscal year due to higher raw material, salary, and power costs. Inventory is sufficient for the next three months of confirmed sale orders while average cost of cotton procured has more than doubled in the past 18 months, with imports making up ~60%; management aims to reduce this reliance to 50%.

On the cost front, higher outbound freight and traveling expenses have significantly increased distribution overheads, while administrative costs have risen with inflation and topline growth. Financial charges have surged due to higher benchmark rates. Nonetheless, the company achieved a record high bottom-line in FY22 on the back of strong revenue growth and significantly improved gross margin.

Debt coverage metrics remain healthy; working capital days have increased due to uptick in inventory holding.

Fund flow from operations (FFO) rose significantly in FY22, reaching Rs. 4.0b, up by ~21%, which aligns with record-high net profit. However, the contrasting cash flow trend during 6M'FY23, led to a weakening in debt coverage metrics as reflected from FFO to total debt and FFO to long-term debt of 0.30x (FY22: 0.44x; FY21: 0.31x) and 0.87x (FY22: 1.11x; FY21: 0.79x). Similarly, debt servicing coverage ratio has also trended down and stands at 2.17x (FY22: 3.14x; FY21: 7.02x).

Liquidity positon is satisfactory, with current ratio consistently reported above 1.2x, and sufficient coverage of short-term borrowings in relation to trade debts and inventory. Working capital days remained steady at 131 days in FY22, but increased to 165 days in the ongoing year due to higher inventory holdings days. Aging of trade debts remains strong as none is outstanding beyond due date.

Leverage ratios have increased slightly yet remains manageable and compare favorably to peers.

As part of restructuring process, the company's long term investment in Naveena Steel of worth Rs. 6.0b was transferred to the holding company, causing the equity base to decline by ~11 over the last 18 months, reaching Rs. 14.5b at end-6M'FY22. There is no documented dividend policy in place while no payout has been made in recent years. Debt profile is a mix of short-term and long-term debt with total interest bearing liabilities, amounting to Rs. 9.8b (FY22: Rs. 9.1b; FY21: Rs. 10.8b) at end-6M'FY23; ~65% constituted short-term debt while aggregated running finance lines stands at Rs. 10.9b (~39% being ERF facility). Leverage and gearing ratios have increased slightly since last review albeit remains favorable as compared to peers.

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 Exports Limited
Sector	Textile
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
Rating Type: Entity				
12-04-2022	A	A-1	Stable	Maintained
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. Omer Nabeel	CFO	March 27, 2023
Mr. Hasan Asif	Senior Treasury Manager	