RATING REPORT

Naveena Exports Limited

REPORT DATE:
June 04, 2024

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		Stable	
Rating Action	Reaffirmed		Maintained	
Rating Date	*June 04, 2024*		*Apr 12, 2023*	

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 ***https://docs.vis.com.pk/docs/CorporateMethodology.pdf*** ***VIS Issue/ Issuer Rating Scale:*** ***https://docs.vis.com.pk/docs/VISRatingScales.pdf***

Naveena Exports Limited

OVERVIEW OF THE INSTITUTION

Naveena Exports Limited is a wholly owned subsidiary of Naveena Group which was incorporated in 1989.

NEL holds the status of being the flagship company within the Naveena Group.

NEL utilizes Oracle software for its tracking and monitoring, encompassing all functions related to Purchases, Finance, Sales, and Production within the software platform.

Profile of Chairman

Mr. Asif Riaz, with more than 30 years in the textile industry, presently serves as the Chairman of the Pakistan Denim Manufacturers and Exporters Association. He has been part of Naveena since its establishment.

RATING RATIONALE

Corporate Profile

Naveena Group was founded in 1989 and began its operations with manufacturing of textile. Currently, the group is operating in textiles, steel, energy, and development of real estate.

Naveena Exports Limited (NEL), established for 35 years, specializes in producing and selling yarn and denim fabric. The company operates globally, with an office in Bangladesh and sales representatives in the US, South America, Europe, and Turkey. NEL prioritizes adherence to international standards for social responsibility, environmental sustainability, and product quality, and it employs over 2,000 workers.

The Company's headquarters are situated in Karachi, with manufacturing facilities in Karachi and Lahore - Naveena Denim Karachi, Naveena Denim Lahore, and Naveena Spinning Unit in Lahore.

Environmental, Social, & Governance (ESG) Initiatives

The Company has implemented several Environmental, Social, and Governance (ESG) initiatives to minimize its environmental impact and contribute to sustainability. Notable environmental efforts include the operation of an efficient wastewater treatment plant. Moreover, the adoption of energy-efficient LED lighting and the installation of solar panels generating demonstrate a commitment to reducing greenhouse gas emissions. Additionally, the company is focused on water conservation through the implementation of water-saving technologies in its manufacturing processes. These initiatives reflect the company's dedication to environmental responsibility and sustainable practices. Moreover, the Company conducted training sessions and awareness programs for its employees.

Operational Performance

The Company's headquarters are situated in Bangalore Town, Karachi, with a denim manufacturing facility located in the Korangi Industrial Area, Karachi. Additionally, the Company operates a Denim Unit and a Spinning Unit situated on Raiwand Road, Lahore.

At present, each division (Karachi Denim, Lahore Denim, and Lahore Spinning) has a power requirement ranging from 4 to 5 MW, with a total demand exceeding 12 MW. About 70% of the power demand is fulfilled by gas generators, with the remaining portion sourced from external sources.

Primarily engaged in the sale of denim fabrics, the Company consumes approximately 90% of the yarn it produces in-house. Despite this operational model, the Company encountered challenges during the fiscal year 2023, attributed to a notable decrease in demand for denim fabric within the export market. Factors contributing to this downturn include a prevailing high-interest-rate environment, currency fluctuations, and elevated inflation rates, particularly within the United States, a key export destination for the Company.

Table: Capacity & Production Data (Figures in millions)

	FY21	FY22	FY23	HY'FY24
Fabric Division				
Installed Capacity (meters)	35.5	37.8	37.3	26.9

Actual Production (meters)	27.4	35.9	19.3	10.78
Capacity Utilization	***77%***	***95%***	***52%***	***40%***
Yarn Division				
Installed Capacity (kgs)	22.4	22.6	21.5	10.75
Actual Production (kgs)	21.1	21.2	16.5	9.98
Capacity Utilization	***94%***	***94%***	***77%***	***93%***

The capacity utilization levels of the Company's Fabric division witnessed a moderate decline, falling from 95% in FY22 to 52% in FY23. This decrease is primarily attributed to diminished demand from the Company's client base within the market. Similarly, the utilization rate of the Yarn division also experienced a slight decline, dropping from 94% to 77% in FY23. However, a positive trend is observed in the first half of FY24, with utilization levels rebounding to 93%.

Despite a further decrease in utilization levels within the Denim division during the first half of FY24, the Company anticipates a resurgence in utilization rates by the conclusion of FY24.

In the long run, the Company aims to expand vertically into the Garment segment by setting up two units, one in Karachi and the other in Lahore.

Sector Update

The business risk profile of the textile sector in Pakistan is characterized by a high level of exposure to economic cyclicality and intense competition. This sector's performance is significantly influenced by the broader economic conditions in the country, making it inherently vulnerable to fluctuations in demand driven by economic factors.

In FY23, the textile sector faced challenges due to various economic and environmental factors. These included damage to the cotton crop resulting from flooding in 1HFY23, escalating inflation, and import restrictions due to diminishing foreign exchange reserves.

During FY23, Pakistan's yarn production registered a substantial decline, primarily due to reduced availability of cotton, as a result of crop damage and import restrictions. The sector's profitability was constrained by factors such as higher production costs, increased raw material costs, and rising energy expenses, all of which constrained the sector's profit margin. The industry's performance is closely intertwined with the outlook of the cotton and textile industries, both of which were affected in FY23. Reduction in cotton supply, coupled with global economic slowdown and contractionary economic policies, led to a decrease in demand for textile products and, consequently, cotton yarn.

While the global outlook for cotton production is expected to rebound, local challenges persist. These challenges include high interest rates, increasing energy costs and inflationary pressures. Additionally, the sector's vulnerability to global market dynamics and the domestic economic landscape further contribute to its high business risk profile. However, there is optimism as an anticipated bigger cotton crop in FY24 is expected to alleviate some pressure on input costs and margins.

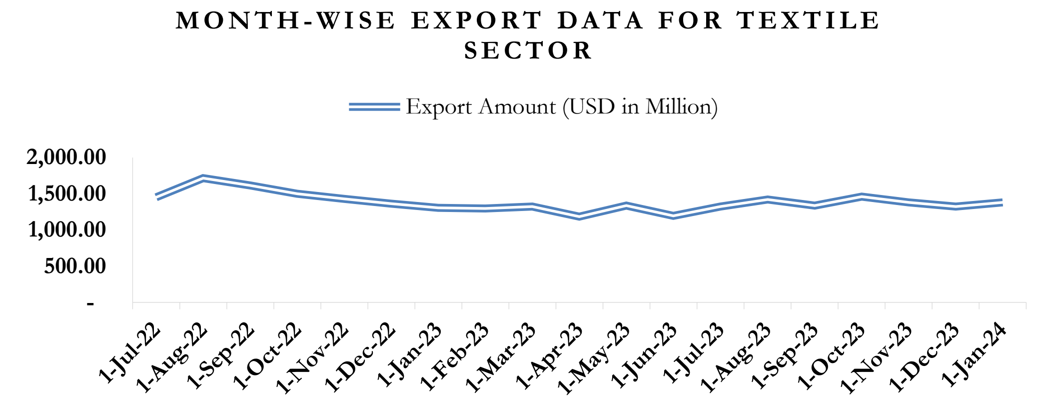

Figure 1: MoM Textile Exports (In USD' Millions)
Source: SBP

Key Rating Drivers

Topline has continued to increase during review period (FY23 & 1HFY24), while gross margins remained under pressure

NEL product portfolio mainly includes denim fabric and yarn. The Company's topline has registered a growth of 16% Y/Y during FY23. The same is attributed by a significant increase in yarn sales in FY23 compared to FY22. The Company has strategically increased its yarn sales amid lower demand of denim fabric during the year. The overall topline growth of the Company has outperformed its peer average in FY23. Export sales, including direct and indirect exports, contributed to around 96% (FY22: 98%) of the total sales in FY23, with the remaining generated from local sales. Due to changes in product mix, including higher yarn sales and lower denim fabric sales, combined with reduced closing inventory of finished goods, NEL's gross profit margin declined to 24.4% from 28.8% in FY22.

Administrative and selling expenses grew in line with inflationary pressures in the economy. However, finance cost surged significantly by 1.6x in FY23 compared to FY22. This is due to a higher interest rate scenario in the economy. Consequently, the net profit margin declined to 9.2% in FY23 (FY22: 14.8%).

In 1H'FY24, the Company's sales demonstrated a 23% Y/Y growth. The profitability margins continued to decline with gross and net margins reaching 20.8% and 4.8%, respectively.

Going forward, the Company foresees a sales rebound fueled by increased orders from its primary client. The cost pressures are expected to persist, therefore, NEL anticipates profitability margins to remain intact.

Lower profitability and high finance cost resulted in a debt service coverage to decline, but remained on adequate levels. Improvement in same is required in order to maintain given ratings.

In FY23, the Fund from Operations (FFO) experienced a slight decline, totaling Rs. 3.0 Bln (FY22: Rs. 3.9 Bln), attributed to a diminishing profitability profile. Consequently, both FFO to total debt and FFO to long-term debt ratios decreased to 0.34x and 0.95x, respectively, compared to FY22 figures of 0.4x and 1.1x. Despite a notable reduction in the Debt Service Coverage Ratio (DSCR) from 3.1x in FY22 to 1.9x in FY23, it remained healthy as of Jun'23.

Regarding liquidity, the Company observed a slight improvement in its current ratio, exceeding 1.5x compared to 1.4x in FY22, which is deemed adequate from a given ratings perspective.

In the first half of FY24, FFO amounted to Rs. 1 Bln, marking a 32% decrease from 1H'FY23 (Rs. 1.5 Bln) due to lower profitability margins. Consequently, both FFO to total debt and FFO to long-term debt coverage ratios further declined to 0.2x and 0.7x, respectively. Additionally, the DSCR decreased to 1.5x. It is imperative for the Company to uphold the DSCR to maintain its ratings.

Capitalization structure remained satisfactory
As of June 2023, the Company's equity stood at Rs. 15.7 Bln, reflecting a 17% year-on-year growth attributed to profit retention. The total debt saw a slight decrease from Rs. 9.0 Bln to Rs. 8.9 Bln, primarily due to timely repayments of long-term loans. Debt composition remained within the range of 30%:70% for long-term debt and short-term borrowings. Consequently, the gearing position of the Company strengthened from 0.68x in FY22 to 0.57x in June 2023. Additionally, the Company's Leverage position improved from 0.9x to 0.8x in June 2023.

By December 2023, a modest 4% growth was noted in total equity, reaching Rs. 16.3 Bln, driven by profit retention. A similar trend was observed for debt, with total debt amounting to Rs. 9.4 Bln, primarily attributed to higher short-term borrowings. Consequently, the gearing ratio of the Company slightly increased to 0.58x. The Leverage ratio of the Company stood at 0.83x. Capitalization indicators are expected to remain intact during the rating horizon.

REGULATORY DISCLOSURES — Appendix I

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				
04-06-2024	A	A-1	Stable	Reaffirmed
12-04-2023	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.
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Due Diligence Meeting Conducted

Name	Designation	Date
Mr. Omer Nabeel	CFO	May 03, 2024
Ms. Zareen Abbasi	Manager - Treasury	