

Delta Galil Industries Ltd.

April 9, 2025

Rating Affirmation

'iIAA-' Rating Affirmed; Outlook Stable

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Overview

Key Strengths	Key Risks
<ul style="list-style-type: none"> • Wide geographical spread of operating markets and production sites. • Long-term relationships with leading apparel companies for brand development, design and production. • Low leverage. 	<ul style="list-style-type: none"> • Competitive environment. • Exposure to volatility in raw material prices and freight costs. • Exposure to exchange rate fluctuations.

Sales increased by approximately 10% for Delta Galil Industries Ltd. ("Delta" or "the Company") in 2024, reverting to its 2022 level. EBITDA and profitability also rose back to the levels posted in 2022. This follows the decline in performance that occurred in 2023 due to the global slowdown which led to an increase in discounts and promotions, along with the signing of new license agreements that temporarily weakened profitability. The Company's Brands segment posted sales growth due to both an increase in the quantity of products sold and an increase in their average price, but the segment's margins continued to decline, mainly due to higher freight expenditures and higher royalties in respect of sales under new license agreements. The Private Labels segment also posted sales growth, due to an increase in the quantity of products sold and stability in their average price, while improving margin both compared to 2023 and to 2022 following an increase in production volumes and the implementation of cost-cutting plan in subsidiary Bogart. In Delta Israel, sales growth was mainly due to higher sales of company-owned brands (higher same-store sales) as well as the launch of the Victoria's Secret and Bath & Body Works brands, alongside a change in the sales mix that contributed to higher margins, despite the war. In 2024, Delta posted an adjusted EBITDA margin of 13.3% compared with 12.3% in 2023. Its debt-to-EBITDA ratio improved to 2.1x from 2.6x in 2023. On the other hand, the Company posted lower operating cash flow, largely due to larger inventory levels following operation growth and new brand introduction, while in 2023 inventory levels decreased due to slower accumulation of new inventory and sale of previous seasons' inventory.

We estimate that 2025 will be challenging given global macroeconomic conditions, particularly in the U.S, and Germany, where low growth is expected, which may negatively impact consumer spending on consumer goods. As a result, we estimate that growth in the industry may come primarily from innovation. However, we understand that 60%-70% of the clothing products the Company produces are basic products that do not depend on changes in trends in the apparel industry or on macroeconomic conditions. As a result, the risk created due to the lower order volumes is mitigated by the Company's ability to reduce inventory over a longer period and without the need to offer significant

discounts on products. We believe the Company's main challenge this year will be improving profitability in the Brands segment through a successful introduction of new licenses and brands while balancing working capital needs, alongside dealing with the imposition of tariffs in the countries of production. In 2025 we expect the Company to post an adjusted debt-to-EBITDA ratio of about 2.0x-2.5x and adjusted EBITDA interest coverage of about 7x-8x, both commensurate with the current rating. We expect that even if profitability weakens due to high tariffs, the Company will post financial ratios commensurate with the rating.

Outlook

The stable outlook reflects our assessment that in the next 12 months, Delta will continue to post positive free cash flow alongside stable operating performance, adjusted debt to EBITDA of 2.0x-2.5x and EBITDA interest coverage significantly above 6x.

Downside Scenario

We may consider a negative rating action if the Company posts adjusted debt to EBITDA of 3.5x on a sustained basis. This scenario could materialize, for example, if the Company makes debt-financed acquisitions or distributes aggressive dividends. We may also consider a negative rating action if the Company's operating performance weakens, or if long-term low demand in the apparel industry is expressed, among other things, in higher-than-expected stock levels and in negative working capital. A deterioration in the Company's liquidity profile may also negatively pressure the rating.

Upside scenario

We may consider a positive rating action if the Company's business and financial profiles materially improve, which will be reflected in its competitive position and EBITDA base, while it maintains an adjusted debt-to-EBITDA ratio below 2x on a sustained basis.

Company Description

Delta Galil Industries Ltd. is a public company founded in 1975 and first offered to the public in 1982. The Company is engaged in the design, development, production, marketing and sale of underwear products, socks, children's clothing and activewear, as well as the development, production, design, marketing, distribution and sale of branded products in the jeans and outerwear categories and related products for women. The Company operates in four business segments: Brands, Private Labels, 7 For All Mankind and Delta Israel (public company, approximately 80% holding). Bare Necessities and Organic Basics activities are included under 'Other'. Most of the Company's shares are held directly and indirectly by Mr. Isaac Dabah (~49% of the Company's shares), Mr. Noam Lautman (~10%), institutional investors and the public (~41%).

Base Case Scenario

Key Assumptions

- An increase of 5%-6% in sales in 2025 and 1%-2% in 2026, mainly in the Brands segment and in Delta Israel.
- Adjusted EBITDA of \$280-\$290 million in 2025 and \$295-\$305 million in 2026.
- An adjusted EBITDA margin of approximately 13%-14% in 2025 and 2026. Similar to 2024.
- Investments of approximately \$140 million in 2025 for maintenance, investing in new factories and distribution centers, opening and renovating stores and investing in the SAP system.

Key metrics

Financial Ratio	2024A	2025E	2026E
Debt/EBITDA	2.1x	2.0x-2.5x	2.0x-2.5x
FFO/debt	33.8%	35%-40%	35%-40%
EBITDA/interest expense	7.5x	7x-8x	7x-8x

A - actual. E – Estimate. FFO – funds from operations.

Base Case Projections

Sales growth and slightly higher profitability

We expect the Company's sales to grow by 5%-6% in 2025, mainly due to growth in the Brands segment and in Delta Israel. We estimate that the Brands segment will post similar growth to 2024, due to new brands and licenses alongside the opening of new stores. We expect Delta Israel to continue to increase its sales following the opening of new stores, including Bath & Body Works (including in the European market) and Victoria's Secret stores, and investment in developing the leisurewear sector. However, challenging macroeconomic conditions in Europe and the U.S., including the imposition of new tariffs, may lead to lower growth than we assumed in our base scenario, and even to lower margins. We expect the Company to post coverage ratios commensurate with the rating even in this scenario.

Under our base case scenario, we expect an adjusted EBITDA margin of 13.5%-14.5% in 2025, a slight improvement compared to 2024, supported, among other things, by higher utilization rates at the Company's plants, and less discounts and promotions in light of the normalization of inventory levels compared to previous years.

Stability in adjusted debt

We believe that despite the Company's planned investments, such as the investment required to construct the U.S. distribution center, as well as investments required to open and renovate stores, the Company's adjusted debt will not grow materially. We note that leverage may increase in case of material acquisitions or investments in new licenses, but not to an extent that would jeopardize the rating.

Business Risk

Delta Galil's business risk profile is underpinned by extensive geographic distribution reflected in sales in approximately 90 countries, in worldwide development, production and distribution centers and in long-term relationships with leading customers such as Skims, Nike, Victoria's Secret, Calvin Klein and Walmart. Approximately 59% of the Company's sales in 2024 were attributed to the Company's brands (including Delta Israel, 7 For All Mankind and other licensed international brands) and the remainder to private labels and 'other'. The apparel market is characterized by many years of growth on the one hand and by many competitors and intense price competition on the other. The Company sells its products through brand store chains and retail chains as well as online. The Company's growth strategy includes, among other things, signing license agreements for the sale of brands such as Victoria's Secret and Bath & Body Works, for which it opened stores in Israel in 2024, alongside signing agreements with Polo Ralph Lauren and Florence by Mills overseas. The Company has also made acquisitions of companies and brands in its fields of activity, the most recent of which is the acquisition of the women's lingerie brand Passionata, which was completed in early 2024.

On the other hand, the Company's business risk profile is constrained due to the fact that, as is common in the industry, the Company does not have long-term contracts with its customers, but it should be noted that the relationships with them last for many years, some over 25 years. In addition, the Company operates in a competitive environment that pressures profitability.

Delta is exposed to volatility in the prices of raw materials such as cotton and various synthetic materials, to freight costs and to fuel prices. The Company is also exposed to exchange rates fluctuations as it operates in several currencies different from its operating currency (U.S.D), mainly the Shekel and the Euro, but it uses hedging to minimize this exposure. We assess the Company's fields of operation as competitive and therefore, when the prices of raw materials rise, its ability to raise prices for its customers is limited.

Financial Risk

Delta Galil's financial risk profile is underpinned by low leverage reflected in adjusted debt to EBITDA of 2.1x, FFO to debt of 33.8% and EBITDA interest coverage of 7.5x in 2024. We believe that the fact that some of the products sold by the Company are basic products somewhat mitigates the volatility of its cash flows, as these products are less subject to frequent changes in the apparel industry or in the macroeconomic situation, and therefore their stock accumulated in previous years can be sold at small or no discounts. On the other hand, we believe that macroeconomic conditions will remain challenging in 2025 against the backdrop of low growth in Europe and a possible recession in the U.S., and will limit growth in the apparel industry.

Table 1.

Delta Galil Industries Ltd. – Financial Summary (Mil. \$)

Industry Sector: Real Textile & Apparel

	2024	2023	2022	2021	2020
Revenue	2,045.7	1,857.7	2,031.5	1,951.0	1,446.2
EBITDA	271.4	228.9	275.1	291.1	116.7
Funds from operations (FFO)	193.8	185.1	231.2	242.5	81.8
Interest expense	36.0	34.5	32.7	35.2	32.6
Cash interest paid	31.2	31.2	26.9	33.1	33.0
Cash flow from operations	197.3	224.0	31.5	166.5	208.6
Capital expenditure	111.9	59.7	61.3	34.5	25.3
Free operating cash flow (FOCF)	85.5	164.3	(29.7)	132.0	183.3
Dividends paid	47.5	28.9	31.4	17.1	6.5
Discretionary cash flow (DCF)	38.0	135.5	(61.1)	114.9	176.8
Cash and short-term investments	120.5	174.5	190.9	230.1	230.8
Gross available cash	120.5	174.5	190.9	230.1	230.8
Debt	573.2	601.5	655.2	600.6	782.5
Equity	803.6	768.4	710.3	649.2	476.4
Adjusted ratios					
Annual revenue growth (%)	10.1	(8.6)	4.1	34.9	(14.4)
EBITDA margin (%)	13.3	12.3	13.5	14.9	8.1
Return on capital (%)	12.6	10.9	14.2	15.4	1.0
EBITDA interest coverage (x)	7.5	6.6	8.4	8.3	3.6
FFO cash interest coverage (x)	7.2	6.9	9.6	8.3	3.5
Debt/EBITDA (x)	2.1	2.6	2.4	2.1	6.7
FFO/debt (%)	33.8	30.8	35.3	40.4	10.5
Cash flow from operations/debt (%)	34.4	37.2	4.8	27.7	26.7
FOCF/debt (%)	14.9	27.3	(4.5)	22.0	23.4
DCF/debt (%)	6.6	22.5	(9.3)	19.1	22.6

Liquidity

We are examining the Company's liquidity on an expanded stand-alone basis – excluding Delta Israel, since Delta is unable to service debt from its public subsidiary's cash balances without a preliminary decision on dividend distribution. We assess the Company's liquidity as "adequate", based on our assessment that the ratio between the Company's sources and uses will exceed 1.2x in the next 12 months.

We estimate the Company's main sources and uses in the 12 months starting January 1, 2025, to be as follows:

Principal Liquidity Sources	Principal Liquidity Uses
<ul style="list-style-type: none"> Approximately \$88 million in cash and cash equivalents. Cash FFO of approximately \$115 - \$125 million. Dividends of approximately \$6.5 million received from Delta Israel in February 2025. 	<ul style="list-style-type: none"> Short-term bank loans and current maturities of long-term loans and bonds of about \$52 million. Maintenance capex of approximately \$20 - \$30 million. Working capital needs of approximately \$30 - \$40 million.

Debt Maturities					
Year	2025	2026	2027	2028	2029 and onwards
Maturities (Mil. \$)	52	52	37	35	63

Covenant Analysis

Compliance expectations

The Company has several covenants towards banks and bond holders. As of December 31, 2024, the Company had sufficient headroom on its financial covenants. We expect the Company to maintain sufficient headroom on all covenants in the near future.

Requirements

The Company's financial covenants include, inter alia, an equity requirement of at least \$150 million and a maximum debt to cap requirement of 60%.

Modifiers

Diversification/portfolio effect: Neutral (no impact)

Capital structure: Neutral (no impact)

Liquidity: Adequate (no impact)

Financial policy: Neutral (no impact)

Management and governance: Neutral (no impact)

Comparable ratings analysis: Positive (positive impact)

Environmental, Social, And Governance

ESG factors are an overall neutral consideration in our credit rating analysis of Delta-Galil Industries Ltd.

We consider the apparel industry to be increasingly subject to environmental and social concerns, including the environmental footprint and the labor conditions of the supply chain workforce, largely in lower-wage countries. This risk could lead to changing shopping habits and consumer preferences in the medium term, as well as increasing oversight from regulators, as considered in the U.S. and in Europe, which together represent about 80% of Delta's total revenue.

However, for now, the regulatory landscape is not yet so stringent that it would force the group to implement a full-scale circularity business model. This underpins our view that environmental issues do not have an impact on the rating analysis. The Company's environmental target plan includes, among other things, a 25% reduction in the products' average environmental footprint, 100% use of sustainable cotton and recycled polyester, zero hazardous chemicals and reduction in water consumption and wastewater recycling.

Recovery Analysis

Rationale

- We are affirming our 'iIAA-' rating, identical to the issuer rating, on unsecured bond series A and F. The recovery rating for these series is '3'.
- Our recovery prospect assessment is constrained to the 50%-70% range despite the simplified waterfall, due to our assessment that on the path to default the Company will exchange unsecured debt for secured or senior debt.

Simulated default assumptions

- Simulated year of default: 2030
- Heightened competition in the segments of operation or a sharp increase in raw material prices that Delta will not be able to pass on to its customers will negatively pressure the Company's cash flows and liquidity, such that it is unable to meet its debt service payments.
- The Company will continue to operate as a going concern, an assessment supported by its geographical spread and by the wide variety of products it develops, produces and markets.
- In the process of the Company's deterioration, it will use 85% of its committed credit facilities.

Simplified Waterfall

- EBITDA at emergence: approximately \$75 million
- Industry EBITDA multiple: 6.0x
- Gross enterprise value as going concern: approximately \$450 million
- Administrative costs: 5%
- Available value to cover secured debt: approximately \$428 million
- Secured debt claims: about \$287 million
- Net value available for unsecured debt: approximately \$141 million
- Unsecured debt claims: approximately \$58 million
- Recovery expectations for unsecured debt: 50%-70% (constrained as noted above)
- Recovery rating for secured debt (1 to 6): 3

All debt amounts include six months' prepetition interest.

Mapping Recovery Percentages To Recovery Ratings

Recovery expectations (%)	Description	Recovery rating	Notching above/below issuer rating
100%	Full recovery	1+	+3 notches
90%-100%	Very high recovery	1	+2 notches
70%-90%	Substantial recovery	2	+1 notch
50%-70%	Meaningful recovery	3	0 notches
30%-50%	Average recovery	4	0 notches
10%-30%	Modest recovery	5	-1 notch
0%-10%	Negligible recovery	6	-2 notches

Recovery ratings are capped in certain countries to adjust for reduced creditor recovery prospects in these jurisdictions. Recovery ratings on unsecured debt issues are generally also subject to caps (see Step 6, paragraphs 90-98 of Recovery Rating Criteria For Speculative-Grade Corporate Issuers, December 7, 2016, for further detail). ICR--Issuer credit rating.

Reconciliation to financial reporting

In order to create a basis for comparison with other rated companies, we adjust the data reported in the financial statements which we use to calculate financial ratios. The main adjustments we made to Delta Galil Industries Ltd's consolidated data for 2024 are as follows:

- Adjusting debt for pension obligations.
- Adjusting debt for bank guarantees due to rental agreements, royalty agreements and acquisitions of subcontractors and others.

Table 2.

Delta Galil Industries Ltd.--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. \$) for the Fiscal Year Ended Dec 31, 2024

	Debt	Shareholders' equity	EBITDA	S&P Global Ratings' adjusted EBITDA	Cash flow from operations	Capital expenditure
Reported Amounts	241.6	779.4	270.4	271.4	203.0	106.8
S&P Global Ratings adjustments						
Cash taxes paid	--	--	--	(46.4)	--	--
Cash interest paid	--	--	--	(31.2)	--	--
Trade receivables securitizations	12.5	--	--	--	(5.7)	--
Reported lease liabilities	279.5	--	--	--	--	--
Postretirement benefit obligations/deferred compensation	4.5	--	--	--	--	--
Share-based compensation expense	--	--	2.2	--	--	--
Income (expense) of unconsolidated companies	--	--	(0.3)	--	--	--
Nonoperating income (expense)	--	--	--	--	--	--
Noncontrolling interest/minority interest	--	24.2	--	--	--	--
Debt: Guarantees	29.6	--	--	--	--	--
Debt: Contingent considerations	5.5	--	--	--	--	--
EBITDA: Other (situational)	--	--	(0.8)	--	--	--
EBIT: Other (situational)	--	--	--	--	--	--
Capital expenditure: Other	--	--	--	--	--	5.1
Total adjustments	331.6	24.2	1.0	(77.6)	(5.7)	5.1
S&P Global Ratings adjusted amounts						
	Debt	Equity	EBITDA	Funds from operations	Cash flow from operations	Capital expenditure
Adjusted	573.2	803.6	271.4	193.8	197.3	111.9

Related Criteria And Research

- [Principles Of Credit Ratings](#), February 16, 2011
- [Methodology: Industry Risk](#), November 19, 2013
- [Country Risk Assessment Methodology And Assumptions](#), November 19, 2013
- [Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers](#), December 16, 2014
- [Recovery Rating Criteria For Speculative-Grade Corporate Issuers](#), December 7, 2016
- [Corporate Methodology: Ratios And Adjustments](#), April 1, 2019
- [Group Rating Methodology](#), July 1, 2019
- [Environmental, Social, And Governance Principles In Credit Ratings](#), October 10, 2021

- [Methodology For National And Regional Scale Credit Ratings](#), June 8, 2023
- [Corporate Methodology](#), January 7, 2024
- [Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers](#), January 7, 2024
- [Sector-Specific Corporate Methodology](#), April 4, 2024
- [S&P Global Ratings Definitions](#), December 2, 2024

Ratings List

Delta Galil Industries Ltd.	Rating	Date when the rating was first published	Date when the rating was last updated
Issuer rating(s) Long term	iIAA-/Stable	27/03/2022	10/04/2024
Issue rating(s) <u>Senior Unsecured Debt</u> Series A,F	iIAA-	27/03/2022	10/04/2024
Issuer Credit Rating history <u>Long term</u> March 27, 2022	iIAA-/Stable		

Additional details	
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