RATING REPORT

Interloop Limited

REPORT DATE:
July 18, 2024

RATING ANALYSTS:
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RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AA-	A-1	A+	A-1
Rating Outlook	Stable		Stable	
Rating Action	Upgrade		Reaffirmed	
Rating Date	*July 18, 2024*		*May 10, 2023*	

COMPANY INFORMATION	
Incorporated in 1992 (PSX Symbol: ILP)	**External Auditors:** Kreston Hyder Bhimji & Co. Chartered Accountants
Public Limited Company	**Board Chairman:** Mr. Musadaq Zulqarnain
Key Shareholders (with stake 5% or more):	**CEO:** Mr. Navid Fazil
Mr. Musadaq Zulqarnain ~32.88%	
Mr. Navid Fazil ~34.22%	
Mrs. Shereen Aftab ~6.36%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Corporates:
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

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

Interloop Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Interloop Limited (ILP) was established in April 1992 as a privately held entity. It transitioned to a public unlisted company in July 2008 before being listed on the Pakistan Stock Exchange (PSX) in April 2019. The company's registered office is located at P-157, Al Sadiq Plaza, Railway Road, Faisalabad.

ILP has conducted a series of comprehensive training programs over the past year, specifically tailored to enhance both functional expertise and leadership capabilities.

Corporate Profile

Interloop Limited ("ILP" or "the Company") stands as the foremost textile entity listed on the Pakistan Stock Exchange, holding the position of the largest market capitalization. It operates as a vertically integrated multi-category corporation, specializing in the manufacturing of Hosiery, Denim, Knitted Apparel, and Seamless Activewear for globally recognized brands and retailers. Additionally, ILP engages in yarn production catering to a diverse clientele within the textile sector. The Company boasts a strong presence across key markets, notably in Netherlands, China, Japan, USA, and Sri Lanka, with a workforce exceeding 35,000 individuals.

Furthermore, with orders reaching full capacity in Pakistan for its clients, ILP has strategically diversified its operations. This includes 64% stake acquisition of Top Circle Hosiery Mills Co, Inc. ("Top Circle") in the United States, aimed at expanding its global presence. Top Circle, known for its established brand recognition and subsidiary entities, aligns with ILP's objective to penetrate the Chinese market and mitigate regional risks. This strategic move not only enhances ILP's global footprint but also strengthens its ability to meet the increasing demands of its clientele across diverse regions.

Average energy demand of 28 MW is met through an optimal mix of national-gridline and gas generators, with contingency access to diesel and HFO generators, 12.6 MW solar plant, and a biomass steam boiler.

ILP has achieved the milestone of ranking as Pakistan's largest exporter in FY24.

Environmental, Social & Governance (ESG) Initiatives

Interloop Limited is committed to the triple bottom line approach, comprising planet, people, and prosperity, to lead towards sustainable growth. The Company's commitment to environment and sustainable practices is exemplified by several key initiatives, from wastewater treatment and recycling utilizing Nano-Bubble Technology to partnering with WWF for AWS certification, the company showcases a commitment to water conservation and community impact. Energy-saving measures are evident through LEED certifications, waste heat recovery systems, and significant investments in renewable energy sources such as solar and biomass. Effluent and hazardous waste treatment are managed through third-party agreements and adherence to ZDHC chemical standards. Further, solidifying its commitment to environment, Interloop commissioned 55 ton-per-hour biomass boilers, achieving a substantial annual reduction of 50,000 tons of CO_2 emissions.

Additionally, Interloop's waste management practices, including recycling initiatives and Cradle to Cradle certification, underscore its dedication to circularity and reducing environmental footprint. The company also actively engages in tree plantation drives and commits to addressing climate-related risks through Science Based Targets, UN charter commitments, and participation in initiatives like the Jeans Redesign. Interloop achieved consecutive recognition for exemplifying the Global Compact Principles and advancing the UN Sustainable Development Goals (SDGs), receiving the first prize in the Large National Enterprise category at the Global Compact Business Sustainability Awards 2022, hosted by UN Global Compact Network Pakistan.

"Interloop Regen Kapas" program was launched, involving 1,000 partner farmers, promoting sustainable cotton farming practices, improving soil health, reducing environmental impact, and enhancing livelihoods. These initiatives demonstrate Interloop's dedication to operating sustainably throughout its value chain. Moreover, Interloop prioritizes health and safety with well-defined policies and systems, ensuring a preventive approach across all operations and facilities.

Operating Performance and Business Segments

Hosiery – Interloop specializes in the production of variety of socks including tights and leggings. ILP continues to position itself as a key supplier of socks for international brands and retailers such as Nike, Adidas, H&M, Target and many others. The expansion plan for the 5th Hosiery Plant has been successfully concluded, and it is operational at full capacity. As of FY23, the annual production capacity within the Hosiery segment totaled to 66.3 million (mln) dozen pairs. The board has approved funding for the construction of the sixth plant in the Hosiery division, expected to be operational by the last quarter of FY25.

Apparels – The Apparel segment of ILP has garnered attention from brands and retailers in various markets, including the EU, UK, and North America. The Company's product range encompasses T-shirts, Polo shirts, sweatshirts, and Fleece Hoodies, which are exported to renowned brands such as Tom Tailor, Adidas, and Target. ILP is undertaking a capacity expansion initiative exceeding Rs. 28 billion to establish a new, high-tech, and fully vertically integrated facility for its Apparel segment.

Denim – The denim plant operated by ILP boasts an annual production capacity of 6 million pieces. The Company's product line encompasses bottoms, shorts, jackets, and work wear gear, catering to all ages, genders, and sizes. Notable customers of ILP's Denim Wear include Guess, Hugo Boss, Mustang Diesel, among others.

Active wear – ILP is a key supplier of high quality active wear to leading brands such as Adidas, Reebok, Zara and H&M. It has an annual production capacity of 4 million garments.

Range of Yarns – Interloop possesses an annual capacity to produce 32 million pounds of yarn (Converted into 20/s), catering to a diverse array of textile customers. The raw materials utilized for spinning encompass a range of inputs, including but not limited to virgin fibers and various recycled fibers. This manufacturing process results in the production of multiple yarn varieties, including plain, multi-count, slub, and Lycra yarns.

With an annual dyeing capacity of 5.5 million kilograms, Interloop offers various types of yarns, including polyester, nylon, acrylic, Coolmax, modal, Tencel, viscose, wool, bamboo, blended fibers, microfibers, and recycled yarns.

Table: Capacity & Production Data (Units in millions)

Division (Figures in millions)	Unit	FY21	FY22	FY23	HY'FY24
HOSIERY					
Installed Capacity - knitting	DZN	60.73	66.30	66.34	36.20
Actual Production - knitting	DZN	51.66	55.70	50.07	29.88
Capacity Utilization		**85.1%**	**84.0%**	**75.5%**	**82.5%**
SPINNING					

Installed Capacity after conversion into 20/s count	LBS	29.95	29.95	31.64	15.82
Actual Production after conversion into 20/s count	LBS	25.18	26.21	25.76	14.25
Capacity Utilization		***84.1%***	***87.5%***	***81.4%***	***90.1%***
YARN DYEING					
Installed Capacity	KGs	4.87	5.07	6.34	3.07
Actual Production	KGs	4.05	4.47	4.48	2.55
Capacity Utilization		***83.2%***	***88.1%***	***70.7%***	***83.1%***
DENIM					
Installed Capacity	PCs	6.00	6.00	6.00	3.24
Actual Production	PCs	3.93	4.62	4.23	2.61
Capacity Utilization		***65.5%***	***77.0%***	***70.6%***	***80.8%***

As a result of reduced global demand, the capacity utilization levels in the respective departments have decreased, reflecting the alignment of actual production with demand and current orders. However, a recovery in demand has been observed, leading to a restoration of utilization levels to their standard benchmarks during the first half of fiscal year 2024.

<u>Sector Update</u>

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.

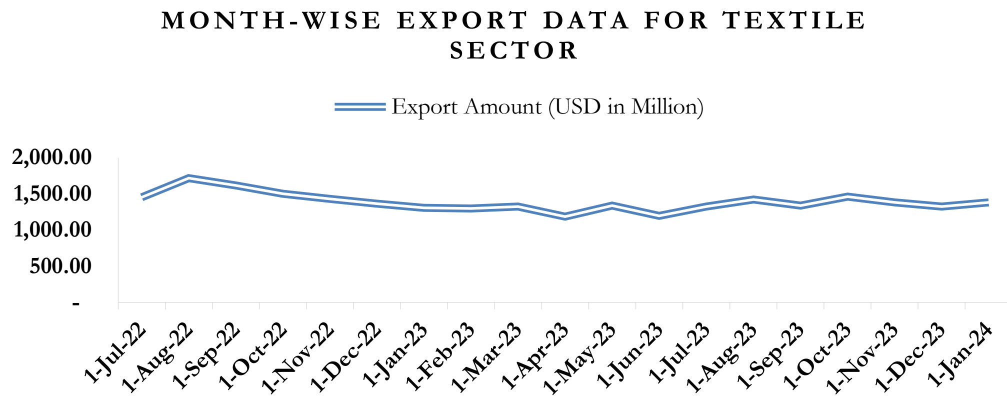

Figure 1: MoM Textile Exports (In USD' millions)
Source: SBP

Key Rating Drivers

Topline surpasses Rs. 100 billion mark while gross margins continued to remain sound
ILP achieved a remarkable 5-year CAGR of 26% from 2019 to 2023, the highest among textile industry peers, surpassing Rs. 100 billion in net sales to reach Rs. 119.2 billion in FY23. This signifies a 31% year-on-year growth, primarily attributed to rupee depreciation. Approximately 94% of the net sales originate from exports, with remaining 6% of sales occurring domestically.

In the fiscal year 2023 (FY23), there were notable shifts in the Cost of Sales wherein Fuel and Power component saw a substantial increase, growing by 51% year-on year. Despite the cost escalations, the gross profit margin demonstrated a rise from 28.7% to 33.4% mainly owed by rupee depreciation. In absolute terms, gross profit of ILP clocked in at Rs. 39.9b (FY22: 26.1b) in FY23, supported by both topline growth and improved margins.

Distribution and Administrative Expenses aligned closely with inflationary trends within the economy. Conversely, the Finance cost experienced a significant surge, more than doubling from Rs. 2.5 billion in FY22 to Rs. 5.5 billion in FY23. This escalation is attributed to heightened debt levels within the Company's financial portfolio and the prevailing high-interest-rate environment in the country.

However, the Company's net profit exhibited substantial growth, escalating from Rs. 12.4 billion to Rs. 20.2 billion in FY23, resulting in a net profit margin of 16.9%, compared to 13.6% in the preceding year.

In FY23, approximately 87.4% of total sales were generated from the top-10 countries. The United States led with 44%, followed by Germany at 12%, and the Netherlands at 7%. Client concentration remained moderate, with over 65% of total sales coming from the top-10 clients. Nike led with over 22% of sales, followed by Target Corporation at 15%. Comfort is derived from a premium customer base of the Company, including Nike, Adidas, Puma, H&M, Target, Hugo Boss and Guess.

In the first nine months of fiscal year 2024 (9M'FY24), the Company achieved sales totaling Rs. 112.8 billion, marking a significant growth of 34.1% compared to the same period in fiscal year 2023 (9M'FY23). Although, the gross profit increased in absolute terms, amounting to Rs. 33.8 billion compared to Rs. 28.2 billion in 9M'FY23, but the gross margin decreased to

30% from 34% in the 9M'FY23 period, primarily due to higher costs associated with fuel and power. Additionally, the net profit margin of the Company declined to 11.7% in 9M'FY24, compared to 16.8% in 9M'FY23, largely attributed to the elevated finance cost component.

ILP's export sales surged to USD 529 million in FY24, marking a 25.7% growth from USD 421 million in FY23, firmly establishing it as Pakistan's top exporter for the year.

ILP has historically shown a diversified product portfolio, starting with a foundation in hosiery and expanding into the denim segment in 2020 to enhance its revenue streams. The Company continues to implement its diversification strategy through planned investments in Hosiery, Knitted Apparels and Denim segment which are poised to propel sales growth in the medium term. While Hosiery will remain a major segment for ILP, significant growth is anticipated in Apparels sales, with projections indicating that it will represent 18% of 2025 export sales.

Adequate liquidity profile along with robust debt service coverage

ILP witnessed a significant 48.3% surge in Funds from Operations (FFO), totaling Rs. 27.1 billion in FY23, credited to improved profitability margins. Correspondingly, the FFO coverage in relation to total debt increased from 0.36x to 0.45x, and FFO to long-term debt rose from 1.1x to 1.5x during the same period. The Debt Service Coverage Ratio (DSCR) also showed a slight uptick from 4.5x in FY22 to 4.9x in FY23, in line with enhanced profitability. The Company maintained a stable working capital cycle, persisting at around 145 days (FY23: 146 days | FY22: 143 days), while its current ratio remained above 1x consistently. Despite a satisfactory current ratio of 1.1x in FY23, there was a decline compared to 1.3x in FY22, attributable to reduced inventory holdings and increased short-term borrowings.

During the 9M'FY24 period, the overall all cash flow coverages has marginally declined amid lower profitability wherein Funds from Operations (FFO) came in at Rs. 17.1 billion. Resultantly, FFO to total debt and FFO to long-term debt experienced a slight reduction to 0.35x and 1.2x, respectively, compared to FY23. The Debt Service Coverage Ratio (DSCR) also decreased to 3.2x, although the same is considered healthy from a ratings perspective. The current ratio of the Company remained satisfactory at 1.1x. It is pertinent to highlight that maintaining a healthy current ratio will be crucial from a ratings perspective. Going forward, the debt coverage and liquidity indicators are projected to remain intact.

Equity continued to post strong growth amid internal cash generation. Overall capitalization profile registered marginal improvement during review period

ILP's Equity has demonstrated a 5-year CAGR of 19.6%, with its equity clocking in at Rs. 43.8 billion as of Jun'23. This growth can be attributed to Company's strong profitability and profit retention. Total Debt of the Company amounted to Rs. 59.6 billion, compared to Rs. 51.4 billion in June 2022. The debt profile of the Company comprise of 70.7% short-term debt and 29.3% long-term debt. This led to an improvement in the Company's gearing ratio from 1.72x to 1.36x in June 2023, primarily due to a higher increase in equity compared to debt levels. Moreover, the Company disbursed a final cash dividend of Rs. 2 per share for the fiscal year ending June 2023.

As of March 2024, the Company issued shares under the Employee Stock Option Scheme (ESOS) worth Rs. 16.8 million, resulting in a slight increase in paid-up capital. Consequently, the total equity amounted to Rs. 51.4 billion as of March 2024 primarily attributed to profit retention. Furthermore, The Company increased its total debt to Rs. 65.7 billion attributed to higher short-term borrowings and long-term debt. As a result, the gearing of the Company improved further to 1.28x due to higher increase in equity compared to debt. Furthermore, the Company distributed an interim cash dividend of Rs. 2 per share in FY24.

The board has approved investments totaling USD 92.1 million across various segments, with funding to be allocated as 65% debt and 35% equity. Whereas, as per the management, the debt has been secured by ILP at Kibor minus rates. Moving forward, the Company anticipates a gradual reduction in its capitalization indicators, primarily attributed to the higher growth in equity compared to the increase in total debt.

Furthermore, ILP has maintained its growth trajectory while consistently rewarding shareholders with dividends since its listing on the PSX in 2019. The Company's dividend per share has grown from Rs. 2.00 per share in 2020 to Rs. 5.00 per share in 2023.

Corporate Governance and Operational Framework

ILP has set up a clear organizational structure with separate departments for different functions, each with its own management team. The Board of Directors comprise of nine members, including four independent directors. Out of these nine members, four members are female. Five board-level committees oversee various aspects of governance. An independent internal audit function reports directly to the Audit Committee.

For operations, ILP uses tailored ERP software and Oracle E-Business Suite. Oracle is used for Hosiery segment of the business, whereas, Datatex software is used for Apparels and Denim division of the business. The software track the production and all other divisions comprehensively. These systems are managed from the production data center, with disaster recovery measures in place. Both on-site and off-site data backups are maintained, and automated processes ensure data preservation at scheduled intervals every day.

Interloop Limited Appendix I

BALANCE SHEET	FY21	FY22	FY23	9M'FY24
Property, plant and equipment	26,193.0	34,730.4	58,650.9	66,684.2
Long term Investments	-	-	-	1,727.8
Stock-in-Trade	11,276.3	23,142.0	19,728.8	27,842.1
Trade Debts	15,052.9	28,604.0	34,138.7	32,948.1
Cash & Bank Balances	374.4	117.1	1,544.5	119.0
Total Assets	60,694.8	96,315.5	125,244.7	142,508.3
Trade and Other Payables	5,551.6	9,084.8	12,003.9	14,247.2
Long Term Debt	10,917.8	16,434.1	17,452.2	18,888.1
Short Term Debt	19,636.1	35,007.9	42,148.9	46,872.7
Total Debt	30,553.8	51,442.0	59,601.1	65,760.7
Total Liabilities	40,180.2	66,375.3	81,438.3	91,132.6
Paid Up Capital	8,722.0	8,983.6	14,014.5	14,017.1
Total Equity	20,514.6	29,940.3	43,806.4	51,375.7
INCOME STATEMENT	FY21	FY22	FY23	9M'FY24
Net Sales	54,962.3	90,894.0	119,200.3	112,856.1
Gross Profit	14,212.3	26,066.2	39,872.4	33,840.1
Operating Profit	7,857.0	15,859.3	26,953.2	21,723.6
Profit Before Tax	6,872.9	13,423.5	21,583.9	14,722.1
Profit After Tax	6,291.6	12,359.5	20,171.8	13,155.3
RATIO ANALYSIS	FY21	FY22	FY23	9M'FY24
Gross Margin (%)	25.9%	28.7%	33.4%	30.0%
Net Margin (%)	11.4%	13.6%	16.9%	11.7%
Net Working Capital	6,089.8	14,254.6	7,936.5	7,725.8
Trade debts/Sales	27.4%	31.5%	28.6%	29.2%
FFO	9,614.6	18,276.5	27,107.8	17,109.8
FFO to Total Debt (%)	31%	36%	45%	35%
FFO to Long Term Debt (%)	88%	111%	155%	121%
Current Ratio (x)	1.22	1.30	1.14	1.12
Debt Servicing Coverage Ratio (x)	7.13	4.47	4.99	3.24
Gearing (x)	1.49	1.72	1.36	1.28
Leverage (x)	1.96	2.22	1.86	1.77
(Stock in Trade+Trade Debts)/STD	134%	148%	128%	130%
ROAA (%)	11.9%	15.7%	18.2%	13.1%*
ROAE (%)	33.3%	49.0%	54.7%	36.9%*

**Annualized*

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	Interloop 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				
18-07-2024	AA-	A-1	Stable	Upgrade
10-05-2023	A+	A-1	Stable	Reaffirmed
03-06-2022	A+	A-1	Stable	Reaffirmed
20-04-2021	A+	A-1	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. Hamza Gillani	Sr. GM Finance	May 17, 2024
Mr. M Omer Masood	Sr. Manager Finance	