MOODY'S
INVESTORS SERVICE

RATING METHODOLOGY
15 June 2021

TABLE OF CONTENTS

Scope 1
Rating approach 2
Apparel scorecard 3
Discussion of the scorecard factors 6
Other considerations 10
Using the scorecard to arrive at a scorecard-indicated outcome 13
Assigning issuer-level and instrument-level ratings 14
Key rating assumptions 15
Limitations 15
Moody's related publications 16

Analyst Contacts

Michael M. Zuccaro +1.212.553.4596
VP-Senior Analyst
michael.zuccaro@moodys.com

Guillaume Leglise +33.1.5330.5979
Vice President - Senior Analyst
guillaume.leglise@moodys.com

Shawn Xiong, CFA +852.3758.1653
AVP-Analyst
shawn.xiong@moodys.com

Raya Sokolyanska +1.212.553.7415
VP-Senior Analyst
raya.sokolyanska@moodys.com

Joe Tringali +1.212.553.1464
Analyst
joe.tringali@moodys.com

» Analyst Contacts continued on last page

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Rating Methodology

Apparel

This rating methodology replaces the *Apparel Methodology* published in October 2019. We have reordered and have made editorial updates to various sections of the methodology, and we have changed the presentation of the scorecard. These updates do not change our methodological approach.

Scope

This methodology applies to companies globally that are primarily* engaged in the sale of apparel, footwear and related accessories, such as handbags, wallets or jewelry, under brands they own or license. This methodology consolidates these product categories under the term apparel for ease of discussion.

Apparel companies covered under this methodology design, source or manufacture, and distribute products to third parties such as retailers, which sell directly to end customers through retail stores and online. Many apparel companies also operate their own direct-to-consumer channels, such as retail stores and online websites. Companies primarily engaged in sales through self-operated retail channels are covered under our retail methodology (a self-operated retail store is one that an apparel company operates, but the company may lease the real estate instead of owning it).

*The determination of a company's primary business is generally based on the preponderance of the company's business risks, which are usually proportionate to the company's revenues, earnings and cash flows.

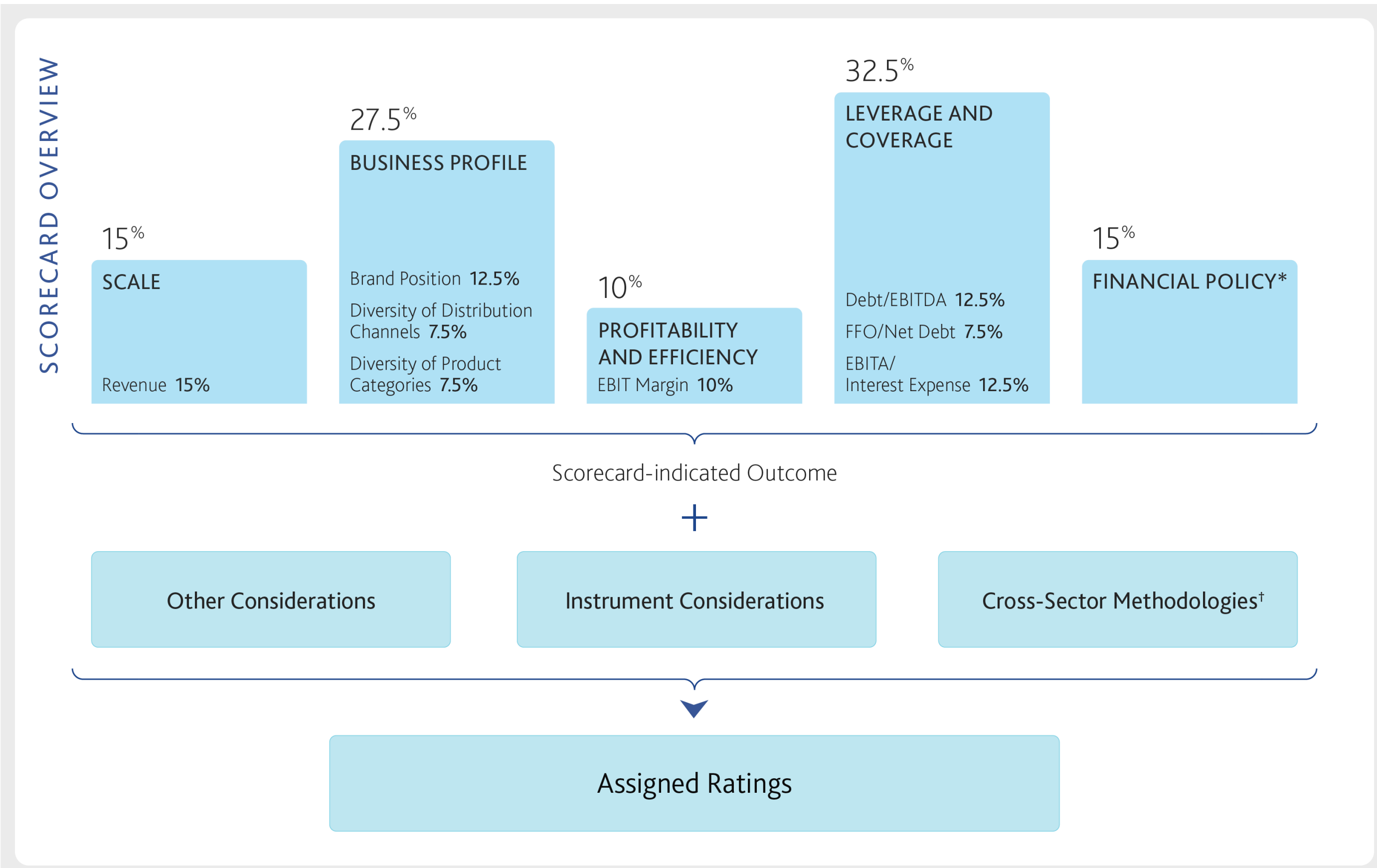
Rating approach

In this rating methodology, we explain our general approach to assessing credit risk of issuers in the apparel industry globally, including the qualitative and quantitative factors that are likely to affect rating outcomes in this sector. We seek to incorporate all material credit considerations in ratings and to take the most forward-looking perspective that visibility into these risks and mitigants permits.

The following schematic illustrates our general framework for the analysis of apparel companies, which includes the use of a scorecard.[1] The scorecard-indicated outcome is not expected to match the actual rating for each company. For more information, see the "Other considerations" and "Limitations" sections.

Exhibit 1

Illustration of the apparel methodology framework



* This factor has no sub-factors.

† Some of the methodological considerations described in one or more cross-sector rating methodologies may be relevant to ratings in this sector. A link to a list of our sector and cross-sector methodologies can be found in the "Moody's related publications" section.

Source: Moody's Investors Service

Apparel scorecard

For general information about how we use the scorecard and for a discussion of scorecard mechanics, please see the "Using the scorecard to arrive at a scorecard-indicated outcome" section. The scorecard does not include or address every factor that a rating committee may consider in assigning ratings in this sector. Please see the "Other considerations" and "Limitations" sections.

Exhibit 2

Apparel scorecard

	SCALE (15%)	BUSINESS PROFILE (27.5%)			PROFITABILITY and EFFICIENCY (10%)	LEVERAGE and COVERAGE (32.5%)			FINANCIAL POLICY (15%)
	Revenue (USD Billion)[1] (15%)	Brand Position (12.5%)	Diversity of Distribution Channels (7.5%)	Diversity of Product Categories (7.5%)	EBIT Margin[2] (EBIT / Revenue) (10%)	Debt / EBITDA[3] (12.5%)	FFO / Net Debt[4] (7.5%)	EBITA / Interest Expense[5] (12.5%)	Financial Policy (15%)
Aaa	≥ $50	Extremely strong global brands (at least 3) with leading market presence and enduring appeal; essentially all major brands are synonymous with the category; long term track record of organic growth and essentially no revenue volatility; and unwavering loyalty from customers, who would not consider alternatives.	Exceptionally diverse mix of wholesale, self-operated retail and online distribution channels; exceptional geographic diversification, with sales from all major regions (for example, at least four continents); and essentially no customer concentration.	Extremely diverse group of product categories (for example, 13 or more separate categories).	≥ 25%	≤ 0.5x	≥ 90%	≥ 20x	Expected to have extremely conservative financial policies (including risk and liquidity management); very stable metrics; essentially no event risk that would cause a rating transition; and public commitment to a very strong credit profile over the long term.
Aa	$30 - $50	Extremely strong global brands with leading market presence and enduring appeal; major brands are synonymous with the category; long-term track record of organic growth and minimal revenue volatility; very high loyalty from customers, who would consider few alternatives.	Excellent diversification across wholesale, self-operated retail and online distribution channels; excellent geographic diversification, with sales from more than one continent; and minimal customer concentration.	Highly diverse group of product categories (for example, 10 to 12 separate categories).	20% - 25%	0.5x - 1x	65% - 90%	12x - 20x	Expected to have very conservative financial policies (including risk and liquidity management); stable metrics; minimal event risk that would cause a rating transition; and public commitment to a strong credit profile over the long term.
A	$10 - $30	Extremely strong global brand with broad appeal across multiple product segments and a competitive position in these segments; long term track record of organic growth and very low revenue volatility; high brand loyalty; customer prefers and seeks brand in market.	Very good diversification across wholesale, self-operated retail and online distribution channels; very good geographic diversification; minimal customer concentration.	Well-diversified group of product categories (for example, 8 or 9 separate categories).	16% - 20%	1x - 2x	50% - 65%	7x - 12x	Expected to have predictable financial policies (including risk and liquidity management) that preserve creditor interests; although modest event risk exists, the effect on leverage is likely to be small and temporary; strong commitment to a solid credit profile.

	SCALE (15%)	BUSINESS PROFILE (27.5%)			PROFITABILITY and EFFICIENCY (10%)	LEVERAGE and COVERAGE (32.5%)			FINANCIAL POLICY (15%)
	Revenue (USD Billion)[1] (15%)	Brand Position (12.5%)	Diversity of Distribution Channels (7.5%)	Diversity of Product Categories (7.5%)	EBIT Margin[2] (EBIT / Revenue) (10%)	Debt / EBITDA[3] (12.5%)	FFO / Net Debt[4] (7.5%)	EBITA / Interest Expense[5] (12.5%)	Financial Policy (15%)
Baa	$5 - $10	Very strong global brand, or several well-recognized regional brands, with appeal across multiple product segments and a competitive position in these segments; long-term track record of revenue growth with low revenue volatility; customers have loyalty, but not exclusively to the brand.	Good mix of wholesale, self-operated retail and online distribution channels; good geographic diversification; low customer concentration.	Diverse group of product categories (for example, 6 or 7 separate categories).	12% - 16%	2x - 3x	35% - 50%	4x - 7x	Expected to have financial policies (including risk and liquidity management) that balance the interests of creditors and shareholders; some risk that debt-funded acquisitions or shareholder distributions could lead to a weaker credit profile.
Ba	$2 - $5	Strong global brand, or several well-recognized regional brands, with some product differentiation where price may be a driver; brand(s) may have distinctive and sustainable appeal but for a moderately sized product category; may have history of inconsistent revenue trends, indicating susceptibility to fashion misses.	Mix of at least two of wholesale, self-operated retail and online distribution channels, but may have moderate concentration in one channel or price range; moderate geographic diversification; moderate customer concentration.	Limited group of product categories (for example, 4 or 5 separate categories).	8% - 12%	3x - 4.5x	20% - 35%	2.25x - 4x	Expected to have financial policies (including risk and liquidity management) that tend to favor shareholders over creditors; above-average financial risk resulting from shareholder distributions, acquisitions or other significant capital structure changes.
B	$0.5 - $2	At least one strong brand in a niche category or in a commoditized category where price is the main driver; brand may have distinctive appeal but within a narrowly defined or small product category; may be in decline, evidenced by persistently negative revenue trends, or has highly volatile revenue, indicating the brand may have faddish characteristics.	Mix of at least two of wholesale, self-operated retail and online distribution channels, but concentration in one broad channel or price range; some geographic concentration; some customer concentration.	Few product categories or concentrated in one category (for example, 3 categories or more than half of sales from one category).	5% - 8%	4.5x - 6x	10% - 20%	1x - 2.25x	Expected to have financial policies (including risk and liquidity management) that favor shareholders over creditors; high financial risk resulting from shareholder distributions, acquisitions or other significant capital structure changes.

	SCALE (15%)	BUSINESS PROFILE (27.5%)			PROFITABILITY and EFFICIENCY (10%)	LEVERAGE and COVERAGE (32.5%)			FINANCIAL POLICY (15%)
	Revenue (USD Billion)[1] (15%)	Brand Position (12.5%)	Diversity of Distribution Channels (7.5%)	Diversity of Product Categories (7.5%)	EBIT Margin[2] (EBIT / Revenue) (10%)	Debt / EBITDA[3] (12.5%)	FFO / Net Debt[4] (7.5%)	EBITA / Interest Expense[5] (12.5%)	Financial Policy (15%)
Caa	$0.25 - $0.5	Brand with low market presence in a commoditized, narrowly defined category; may be in rapid decline with sizable decreases in revenues. Untested brand with a short track record.	Significant concentration in wholesale, self-operated retail or online distribution channels, including significant concentration in one broad channel or price range; high geographic concentration; or high customer concentration.	Very few product categories or very concentrated in one category (for example, at least three-quarters of sales from one category).	2% - 5%	6x - 7.5x	5% - 10%	0.5x - 1x	Expected to have financial policies (including risk and liquidity management) that create elevated risk of debt restructuring in varied economic environments.
Ca	< $0.25	Undifferentiated product in a commoditized category; may be startup with a limited track record.	Concentrated in one wholesale channel, or concentrated in one region on one continent; or very high concentration in or reliance on one customer.	Highly concentrated in a single product category.	< 2%	> 7.5x	< 5%	< 0.5x	Expected to have financial policies (including risk and liquidity management) that create elevated risk of debt restructuring even in healthy economic environments.

[1] For the linear scoring scale, the Aaa endpoint value is $100 billion. A value of $100 billion or better equates to a numeric score of 0.5. The Ca endpoint value is zero. A value of zero equates to a numeric score of 20.5
[2] For the linear scoring scale, the Aaa endpoint value is 40%. A value of 40% or better equates to a numeric score of 0.5. The Ca endpoint value is (2)%. A value of (2)% or worse equates to a numeric score of 20.5.
[3] For the linear scoring scale, the Aaa endpoint value is zero. A value of zero equates to a numeric score of 0.5. The Ca endpoint value is 15x. A value of 15x or worse equates to a numeric score of 20.5, as does a negative Debt/EBITDA value.
[4] For the linear scoring scale, when net debt is positive, the Aaa endpoint value is 150%. A value of 150% or better equates to a numeric score of 0.5. The Ca endpoint value is 0%. A value of 0% or worse equates to a numeric score of 20.5. When net debt is negative and FFO is positive, the numeric score is 0.5. When net debt is negative and FFO is negative or zero, the numeric score is 20.5.
[5] For the linear scoring scale, the Aaa endpoint value is 35x. A value of 35x or better equates to a numeric score of 0.5. The Ca endpoint value is (2)x. A value of (2)x or worse equates to a numeric score of 20.5.
Source: Moody's Investors Service

Discussion of the scorecard factors

In this section, we explain our general approach for scoring each scorecard factor or sub-factor, and we describe why they are meaningful as credit indicators.

Factor: Scale (15% weight)

Why it matters

Scale is an important indicator of the overall depth of a company's business and its success in attracting a variety of customers, as well as the cost advantages that typically come with a larger revenue base. Scale can also provide insight into the company's global brand strength and market position.

Larger scale allows apparel companies to reduce revenue volatility and leverage fixed costs, such as those associated with sourcing and distribution. Scale also allows companies to better manage operations under different demand and cost scenarios. In addition, apparel companies typically sell to large retailers, and greater scale provides greater capacity to offer these customers services and support.

How we assess it for the scorecard

REVENUE:

Scale is measured (or estimated in the case of forward-looking expectations) using total reported revenue in billions of US dollars.

Factor: Business Profile (27.5% weight)

Why it matters

The business profile of an apparel company is important because it greatly influences its ability to generate sustainable earnings and operating cash flow.

This factor comprises three qualitative sub-factors:

Brand Position

The ability to manage a brand, or portfolio of brands, is critical to success in the apparel industry, which typically experiences fluctuations in demand as economic conditions and fashion trends change. High reliance on a single brand increases a company's exposure to shifts in customer sentiment and brand missteps, whereas a company with multiple brands is less vulnerable to weakness in any one brand. A globally recognized brand provides a company with a potentially broader customer base than a regional brand and may limit its exposure to regional economic downturns. Companies whose major brands are synonymous with apparel categories or are competitive in multiple product segments typically have a stronger brand position than companies with a low market presence or those with commoditized brands.

Brands associated with apparel categories that are reliant on lower prices to drive sales are generally more exposed to competition. Price increases for such brands are more likely to result in reduced sales than they are for brands with loyal customers who are less willing to consider lower-priced alternatives. In commoditized categories where price is the primary driver of the decision to buy, companies generally have less ability to pass on rising input costs to customers without losing sales, which may lead to lower profitability if labor, material costs (e.g., cotton) or currency-related costs rise.

A company with strong brands also is generally more likely to successfully extend its brands into new product categories, expand the base of potential customers or sell directly to customers at higher price points; whereas one with weaker brands may rely more heavily on wholesale sellers. A company's track record of growth and revenue stability is an important indicator of its brands' staying power as customer tastes evolve. Companies with a history of inconsistent, declining or volatile revenue may have brands that are susceptible to missed fashion trends.

Apparel companies may distribute products under brands they own or for which they obtain a license to sell (as a licensee), typically paying a royalty fee (to a licensor) based on a percentage of sales. An apparel company may also act as a licensor, granting licenses to third parties to design, source or manufacture, or distribute products under its owned brand or brands, often for product categories where the licensor has less expertise, such as eyewear, cosmetics or fragrances, or for foreign markets where a local partner has more knowledge.

Diversity of Distribution Channels

Diversification across distribution channels is an important indicator of apparel companies' flexibility to accommodate shifting customer preferences. Core aspects of an apparel company's distribution channels are its diversification across wholesale, self-operated retail and online distribution channels; geographic diversification and customer concentration. For example, customers may shift to value-oriented channels during economic downturns, so a company that can distribute products to channels that offer a wide range of price points typically has more stable revenue through economic cycles.

An online presence allows an apparel company to offer a more convenient shopping experience, given that consumers can shop outside of typical brick-and-mortar store business hours, typically at a low cost and with minimal effort. Apparel companies with products in a diverse range of channels can also reach a wider range of customers across ages and income levels. Self-operated retail stores and websites typically give an apparel company greater control over the marketing, presentation and distribution of its brands, and better potential to enhance the customer's shopping experience.

Geographic diversification is important because economic and social trends may affect regions differently, so an apparel company with a presence in different countries and regions can typically withstand weakness in a region better than a company with a more limited geographic presence. A company with broader geographic distribution may also be better able to take advantage of its presence in regions where opportunities to expand business are strong.

Customer concentration is important because the more an apparel company relies on a single customer, the more vulnerable it is to that customer. An apparel company that is concentrated with one major customer generally has less negotiating power and can suffer repercussions if the customer's performance were to deteriorate (such as potential credit-related losses if a large retail customer files for bankruptcy), or if it takes actions that are not in the interest of its suppliers, such as inventory destocking or replacement of a brand.

Diversity of Product Categories

A diversity of product categories is important because it allows an apparel company to sell more products to a wider variety of customers and meet demand patterns that may vary by season and during economic cycles. For example, customers generally buy cold-weather gear such as heavy coats and gloves for winter, and most stores do not make these products available in large quantities year-round. At the end of a season, stores generally lower their prices to clear out inventory, which may lead to a reduction in profitability for an apparel company that predominantly sells cold-weather gear.

Limited product diversification also increases susceptibility to fashion risk and changing consumer preferences. For example, a jeans company would be more susceptible to lost sales from a consumer shift toward more comfortable pants, such as leggings. However, certain products, such as children's apparel, tend to have more stable demand because consumers tend to continue to spend on their children even during challenging times. An apparel company that sells a range of products that appeals to customers of different ages and genders also is less vulnerable to reduced demand within any one product category than a company that is focused on, for example, teenagers, who tend to change their preferences more often.

How we assess it for the scorecard

Scoring for this factor is based on three sub-factors: Brand Position; Diversity of Distribution Channels; and Diversity of Product Categories.

BRAND POSITION:

To assess the strength of an apparel company's brand, we consider customer awareness of the brand in the regions where it is primarily sold. We may review third-party data on brand awareness and market share. We also typically consider the price point of a company's products relative to comparable products. A brand sold at a price that is consistently below comparable products generally reflects a more commoditized, price-driven brand with less customer loyalty than one that is sold at a premium to other products. We consider the strength of the brand across categories, and the number of categories that are associated with the brand. We assess the company's revenue trends over time, including revenue by brand when data is available.

For companies that own multiple brands, our assessment typically considers the portfolio as a whole, not only its strongest or weakest brands. Some companies market multiple brands to different customers, product categories or distribution channels.

In cases where a company generates a material portion of earnings from licensing relationships, we assess these relationships, which often have case-specific characteristics. We may consider the remaining term of the licenses, the history and likelihood of license renewals, qualitative restrictions (e.g., the degree of control the licensee has over marketing expenses and channels of distribution), the breadth of the product category coverage in the licensing relationship and the importance of the relationship to both parties. A long-term license with few restrictions on the licensee and broad category coverage may indicate that the licensee has some degree of brand control, which may reduce the apparel company's (licensor's) ability to control its brand and may negatively impact its score for this sub-factor.

DIVERSITY OF DISTRIBUTION CHANNELS:

We consider the company's mix of sales through the wholesale channel (selling products to third-party retailers which then sell to consumers), self-operated retail stores and online distribution channels based on the percent of revenue from each channel, if available, as well as the location of stores. A company with high concentration in any one channel typically scores lower on this sub-factor than one with a greater mix of channels.

We typically assess a company's diversification across different types of wholesale channels, which include, for example, discount stores, moderately priced stores, high end stores, and specialty stores. These stores may sell products at different price points and target different customers. We also consider the number and location of a company's self-operated retail stores, if applicable. Companies may sell products online through their retailer partners' websites, an online-only partner or their own website, and we assess the materiality of these sales relative to the company's overall sales, based on available information. We also consider licensed product relationships to the extent these contribute materially to earnings (typically greater than 10%).

Given the importance of geographic diversity, we also consider sales outside of home markets. For example, an apparel company that has materially significant sales to the same type of channel in the US and Europe would generally score higher for this sub-factor than one with sales primarily in Europe.

In assessing customer concentration, we consider an apparel company's proportion of sales to an individual wholesale customer, given that a sizable concentration in one or more key customers increases risk related to that retailer's performance or strategies. An apparel company that has sales to one wholesale customer in excess of 10% of total sales may receive a lower score on this sub-factor than it would without this concentration.

DIVERSITY OF PRODUCT CATEGORIES:

We assess product diversification based on the number of material product categories an apparel company sells, and, for broad product categories, based on gender and age distinctions. We typically consider any product that generates close to 10% of a company's revenue to be a separate product category, although if a company has several clearly dominant categories and one much smaller one, we may not consider the smaller category if it generates less than 10% of total revenue.

Within broad categories such as apparel (e.g., tops, bottoms, suits and dresses), footwear, innerwear, (including intimates), and outerwear, we may consider the diversity of products a company sells based on customers' gender and age. Narrower product categories, such as handbags, home décor, bedding and towels, fragrances, fashion jewelry, watches, eyewear, occupational apparel and equipment such as camping gear or athletic equipment are considered distinct from the larger categories. However, we do not typically consider age or gender distinctions within these narrower product categories.

Factor: Profitability and Efficiency (10% weight)

Why it matters

Profits matter because they are needed to generate sustainable cash flow and maintain a competitive position. Profit margins are an important measure of an apparel company's overall brand strength, efficiency in marketing products through distribution channels, and ability to control costs. An apparel company with a strong competitive position and high relevance to consumers, based on its brands or the types of products it sells, typically has high consumer loyalty, leading to more recurring sales and stronger profit margins than a company with a weaker competitive position and less relevance to consumers.

How we assess it for the scorecard

EBIT MARGIN:

We use the ratio of earnings before interest and taxes to revenue (EBIT Margin).

Factor: Leverage and Coverage (32.5% weight)

Why it matters

Leverage and cash flow coverage measures provide important indications of an apparel company's financial flexibility and long-term viability.

This factor comprises three quantitative sub-factors:

Debt / EBITDA

The ratio of total debt to earnings before interest, taxes, depreciation and amortization (Debt/EBITDA) is an indicator of debt serviceability and financial leverage. The ratio is commonly used in this sector as a proxy for comparative financial strength.

FFO / Net Debt

The ratio of funds from operations to net debt (FFO/Net Debt) is an indicator of a company's financial flexibility and its ability to repay net debt (total debt minus cash and cash equivalents) before investments in working capital, dividends and capital expenditures.

EBITA / Interest Expense

The ratio of earnings before interest, taxes and amortization to interest expense (EBITA/Interest Expense) is an indicator of a company's ability to meet its interest obligations.

How we assess it for the scorecard

Scoring for this factor is based on three sub-factors: Debt/EBITDA; FFO/Net Debt; and EBITA/Interest Expense.

DEBT / EBITDA:

The numerator is total debt, and the denominator is EBITDA.

FFO / NET DEBT:

The numerator is FFO, and the denominator is net debt (total debt minus cash and cash equivalents).

EBITA / INTEREST EXPENSE:

The numerator is EBITA, and the denominator is interest expense.

Factor: Financial Policy (15% weight)

Why it matters

Financial policy encompasses management and board tolerance for financial risk and commitment to a strong credit profile. It is an important rating determinant, because it directly affects debt levels, credit quality, the future direction for the company and the risk of adverse changes in financing and capital structure.

Financial risk tolerance serves as a guidepost to investment and capital allocation. An expectation that management will be committed to sustaining an improved credit profile is often necessary to support an upgrade. For example, we may not upgrade the ratings of a company that has built flexibility within its rating category if we believe the company will use that flexibility to fund a strategic acquisition, cash distribution to shareholders, spin-off or other leveraging transaction. Conversely, a company's credit rating may be better able to withstand a moderate leveraging event if management places a high priority on returning credit metrics to pre-transaction levels and has consistently demonstrated the commitment to do so through prior actions. Liquidity management[2] is an important aspect of overall risk management and can provide insight into risk tolerance.

Many apparel companies have historically used acquisitions to spur revenue growth, expand business lines, consolidate market positions and advance cost synergies or seek access to new technology. We expect that M&A activity will remain a key growth driver for many companies.

How we assess it for the scorecard

We assess the issuer's desired capital structure or targeted credit profile, its history of prior actions, including its track record of risk and liquidity management, and its adherence to its commitments. Attention is paid to management's operating performance and use of cash flow through different phases of economic and industry cycles. Also of interest is the way in which management responds to key events, such as changes in the credit markets and liquidity environment, legal actions, competitive challenges or regulatory pressures. Considerations include a company's public commitments in this area, its track record for adhering to commitments and our views on the ability of the company to achieve its targets.

When considering event risks in the context of scoring financial policy, we assess the likelihood and potential negative impact of M&A or other types of balance-sheet-transforming events. Management's appetite for M&A activity is assessed, with a focus on the type of transactions (i.e., core competency or new business) and funding decisions. Frequency and materiality of acquisitions and previous financing choices are evaluated. A history of debt-financed or credit-transforming acquisitions will generally result in a lower score for this factor. We may also consider negative repercussions caused by shareholders' willingness to sell the company.

We also consider a company's and its owners' past record of balancing shareholder returns and debtholders' interests. A track record of favoring shareholder returns at the expense of debtholders is likely to be viewed negatively in scoring this factor.

Other considerations

Ratings may reflect consideration of additional factors that are not in the scorecard, usually because the factor's credit importance varies widely among the issuers in the sector or because the factor may be important only under certain circumstances or for a subset of issuers. Such factors include financial controls and the quality of financial reporting; corporate legal structure; the quality and experience of management; assessments of corporate governance as well as environmental and social considerations; exposure to uncertain licensing regimes; and possible government interference in some countries. Regulatory, litigation, liquidity, technology and reputational risk as well as changes to consumer and business spending patterns, competitor strategies and macroeconomic trends also affect ratings.

Following are some examples of additional considerations that may be reflected in our ratings and that may cause ratings to be different from scorecard-indicated outcomes.

Regulatory Considerations

Companies in the apparel sector are subject to varying degrees of regulatory oversight. Effects of these regulations may entail limitations on operations, higher costs, and higher potential for technology disruptions and demand substitution. Regional differences in regulation, implementation or enforcement may advantage or disadvantage particular issuers. As an industry with complex, global supply relationships, apparel is sensitive to trade barriers and tariffs.

Our view of future regulations plays an important role in our expectations of future financial metrics as well as our confidence level in the ability of an issuer to generate sufficient cash flows relative to its debt burden over the medium and longer term. In some circumstances, regulatory considerations may also be a rating factor outside the scorecard, for instance when regulatory change is swift.

Environmental, Social and Governance Considerations

Environmental, social and governance (ESG) considerations may affect the ratings of issuers in the apparel sector. For information about our approach to assessing ESG issues, please see our methodology that describes our general principles for assessing these risks.[3]

In the apparel sector, carbon taxes could increase transportation costs or costs to operate stores. Carbon taxes could also increase the costs of oil-based synthetic products used in apparel. Also, water shortages may lead to higher costs for cotton, a water-intensive crop, and certain steps within the manufacturing process, such as fabric dyeing or cutting, can create waste that pollutes the environment. Over time, companies could adapt by passing along higher costs to consumers, finding alternative manufacturers and suppliers or innovative production methods, and changing product offerings.

Social considerations that are relevant to the apparel sector may include customer relations as well as fair disclosure and labeling practices, and responsible marketing, distribution and production. Brand perceptions and customers' purchase decisions may be affected by headline risks from an apparel company's supply-chain practices, such as human rights controversies and violations, environmental impact, or political activism. Also, changing demographics, such as aging populations and generational shifts in values, and concerns over fair pricing and access to essential goods and services may affect customers' buying patterns.

Financial Controls

We rely on the accuracy of audited financial statements to assign and monitor ratings in this sector. The quality of financial statements may be influenced by internal controls, including the proper tone at the top, centralized operations, and consistency in accounting policies and procedures. Auditors' reports on the effectiveness of internal controls, auditors' comments in financial reports and unusual restatements of financial statements or delays in regulatory filings may indicate weaknesses in internal controls.

Management Strategy

The quality of management is an important factor supporting a company's credit strength. Assessing the execution of business plans over time can be helpful in assessing management's business strategies, policies and philosophies and in evaluating management performance relative to the performance of competitors and our projections. Management's track record of adhering to stated plans, commitments and guidelines provides insight into management's likely future performance, including in stressed situations.

Excess Cash Balances

Some companies in this sector may maintain cash balances (meaning liquid short-term investments as well as cash) that are far in excess of their operating needs. This excess cash can be an important credit consideration; however, the underlying policy and motivations of the issuer in holding high cash balances are often as or more important in our analysis than the level of cash held. We have observed significant variation in company behavior based on differences in financial philosophy, investment opportunities, availability of committed revolving credit facilities and shareholder pressures.

Most issuers need to retain some level of cash in their business for operational purposes. The level of cash required to run a business can vary based on the region(s) of operation and the specific sub-sectors in which the issuer operates. Some issuers have very predictable cash needs and others have much broader intra-period swings, for instance related to mark-to-market collateral requirements under hedging instruments. Some companies may hold large levels of cash at times because they operate without committed, long-term bank borrowing facilities. Some companies may hold cash on the balance sheet to meet long-term contractual liabilities, whereas other companies with the same types of liabilities have deposited cash into trust accounts that are off balance sheet. The level of cash that issuers are willing to hold can also vary over time based on the cost of borrowing and macroeconomic conditions. The same issuer may place a high value on cash holdings in a major recession or financial crisis but seek to pare cash when inflation is high. As a result, cash on the balance sheet is most often considered qualitatively, by assessing the issuer's track record and financial and liquidity policies rather than by measuring how a point-in-time cash balance would affect a specific metric.

Across all corporate sectors, an important shareholder-focused motivation for cash holdings, sometimes over very long periods, is cash for acquisitions. In these cases, we do not typically consider that netting cash against the issuer's current level of debt is analytically meaningful; however, the cash may be a material mitigant in our scenario analysis of potential acquisitions, share buybacks or special dividends. Tax minimization strategies have at times been another primary motivation for holding large cash balances. Given shareholder pressures to return excess cash holdings, when these motivations for holding excess cash are eliminated, we generally expect that a large portion of excess cash will be used for dividends and share repurchases.

By contrast, some companies maintain large cash holdings for long periods of time in excess of their operating and liquidity needs solely due to conservative financial policies, which provides a stronger indication of an enduring approach that will benefit creditors. For instance, some companies have a policy to routinely pre-fund upcoming required debt payments well in advance of the stated maturity. Such companies may also have clearly stated financial targets based on net debt metrics and a track record of maintaining their financial profile within those targets.

While the scorecard in this methodology uses certain leverage and coverage ratios with total (or gross) debt, we do consider excess cash holdings in our rating analysis, including in our assessment of the financial and liquidity policy. For issuers where we have clarity into the extent to which cash will remain on the balance sheet and/or be used for creditor-friendly purposes, excess cash may be considered in a more quantitative manner. While we consider excess cash in our credit assessment for ratings, we do not typically adjust the balance sheet debt for any specific amount because this implies greater precision than we think is appropriate for the uncertain future uses of cash. However, when cash holdings are unusually large relative to debt, we may refer to debt net of cash, or net of a portion of cash, in our credit analysis and press releases in order to provide additional insight into our qualitative assessment of the credit benefit. Alternatively, creditor-friendly use of cash may be factored into our forward view of metrics, for instance when the cash is expected to be used for debt-repayment. We may also cite rating threshold levels for certain issuers based on net debt ratios, particularly when these issuers have publicly stated financial targets based on net debt metrics. In cases where we believe that cash on the balance sheet does not confer meaningful credit support, we are more likely to cite gross debt ratios in our credit analysis, press releases and rating threshold levels.

Even when the eventual use for excess cash is likely to be for purposes that do not benefit debtholders, large holdings provide some beneficial cushion against credit deterioration, and cash balances are often considered in our analysis of near-term liquidity sources and uses. Such downside protection is usually more important for low rated companies than for highly rated companies due to differences in credit stability and the typically shorter distance from potential default for issuers at the lower end of the ratings spectrum.

Liquidity

Liquidity is an important rating consideration for all apparel companies, although it may not have a substantial impact in discriminating between two issuers with a similar credit profile. Liquidity can be particularly important for companies in highly seasonal operating environments where working capital needs must be considered, and ratings can be heavily affected by weak liquidity. We form an opinion on likely near-term liquidity requirements from the perspective of both sources and uses of cash. For more details on our approach, please see our liquidity cross-sector methodology.[4]

Additional Metrics

The metrics included in the scorecard are those that are generally most important in assigning ratings to companies in this industry; however, we may use additional metrics to inform our analysis of specific companies. These additional metrics may be important to our forward view of metrics that are in the scorecard or other rating factors.

For example, free cash flow is not always an important differentiator of credit profiles. Strong companies with excellent investment opportunities may demonstrate multiyear periods of negative free cash flow while retaining solid access to capital and credit, because these investments will yield stable cash flows in future years. Weaker companies with limited access to credit may have positive free cash flow for a period of time because they have curtailed the investments necessary to maintain their assets and future cash-generating prospects. However, in some cases, free cash flow can be an important driver of the future liquidity profile of an issuer, which, as noted above, can have a meaningful impact on ratings. Additionally, we may consider inventory days on hand and payable days. If inventory levels rise significantly above typical levels, that may indicate a potential need to liquidate inventory at discounted prices, which generally depresses EBIT margin. Shrinking payable days may indicate that suppliers are pressuring the apparel company for faster repayment, a negative for the apparel company's liquidity position.

Event Risk

We also recognize the possibility that an unexpected event could cause a sudden and sharp decline in an issuer's fundamental creditworthiness, which may cause actual ratings to be lower than the scorecard-indicated outcome. Event risks — which are varied and can range from leveraged recapitalizations to sudden regulatory changes or liabilities from an accident — can overwhelm even a stable, well-capitalized firm. Some other types of event risks include M&A, asset sales, spin-offs, litigation, pandemics, significant cyber-crime events and shareholder distributions.

Parental Support

Ownership can provide ratings lift for a particular company in the apparel sector if it is owned by a highly rated owner(s) and is viewed to be of strategic importance to those owners. In our analysis of parental support, we consider whether the parent has the financial capacity and strategic incentives to provide support to the issuer in times of stress or financial need (e.g., a major capital investment or advantaged operating agreement), or has already done so in the past. Conversely, if the parent puts a high dividend burden on the issuer, which in turn reduces its flexibility, the ratings would reflect this risk.

Government-related issuers may receive ratings uplift due to expected government support. However, for certain issuers, government ownership can have a negative impact on the underlying Baseline Credit Assessment.[5] For example, price controls, onerous taxation and high distributions can have a negative effect on an issuer's underlying credit profile.

Seasonality

Seasonality is an important driver of customer demand and can cause swings in cash balances and working capital positions for issuers. Higher volatility creates less room for errors in meeting customer demand or operational execution, particularly during peak seasons.

Cyclical Sectors

Scorecard-indicated outcomes in cyclical sectors such as apparel may be higher than the rating at the top of the economic cycle and lower than the rating at the bottom of the cycle. While using annual financials in the scorecard typically provides very useful insights into recent or near-term results, ratings may also reflect our expectations for the progression of yearly results over a longer period that may include a full economic cycle. However, cyclicality itself poses many different types of risks to companies, and cycles do not reverse themselves with predictable regularity. A cyclical sector may also be affected by a secular decline or expansion. These considerations may be incorporated qualitatively in ratings.

Using the scorecard to arrive at a scorecard-indicated outcome

1. Measurement or estimation of factors in the scorecard

In the "Discussion of the scorecard factors" section, we explain our analytical approach for scoring each scorecard factor or sub-factor,[6] and we describe why they are meaningful as credit indicators.

The information used in assessing the sub-factors is generally found in or calculated from information in the company's financial statements or regulatory filings, derived from other observations or estimated by Moody's analysts. We may also incorporate non-public information.

Our ratings are forward-looking and reflect our expectations for future financial and operating performance. However, historical results are helpful in understanding patterns and trends of a company's performance as well as for peer comparisons. Financial ratios,[7] unless otherwise indicated, are typically calculated based on an annual or 12-month period. However, the factors in the scorecard can be assessed using various time periods. For example, rating committees may find it analytically useful to examine both historical and expected future performance for periods of several years or more.

All of the quantitative credit metrics incorporate our standard adjustments[8] to income statement, cash flow statement and balance sheet amounts for items such as underfunded pension obligations and operating leases. We may also make other analytical adjustments that are specific to a particular company.

2. Mapping scorecard factors to a numeric score

After estimating or calculating each factor or sub-factor, each outcome is mapped to a broad Moody's rating category (Aaa, Aa, A, Baa, Ba, B, Caa or Ca, also called alpha categories) and to a numeric score.

Qualitative factors are scored based on the description by broad rating category in the scorecard. The numeric value of each alpha score is based on the scale below.

Exhibit 3

Aaa	Aa	A	Baa	Ba	B	Caa	Ca
1	3	6	9	12	15	18	20

Source: Moody's Investors Service

Quantitative factors are scored on a linear continuum. For each metric, the scorecard shows the range by alpha category. We use the scale below and linear interpolation to convert the metric, based on its placement within the scorecard range, to a numeric score, which may be a fraction. As a purely theoretical example, if there were a ratio of revenue to interest for which the Baa range was 50x to 100x, then the numeric score for an issuer with revenue/interest of 99x, relatively strong within this range, would score closer to 7.5, and an issuer with revenue/interest of 51x, relatively weak within this range, would score closer to 10.5. In the text or table footnotes, we define the endpoints of the line (i.e., the value of the metric that constitutes the lowest possible numeric score, and the value that constitutes the highest possible numeric score).

Exhibit 4

Aaa	Aa	A	Baa	Ba	B	Caa	Ca
0.5-1.5	1.5-4.5	4.5-7.5	7.5-10.5	10.5-13.5	13.5-16.5	16.5-19.5	19.5-20.5

Source: Moody's Investors Service

3. Determining the overall scorecard-indicated outcome

The numeric score for each sub-factor (or each factor, when the factor has no sub-factors) is multiplied by the weight for that sub-factor (or factor), with the results then summed to produce an aggregate numeric score. The aggregate numeric score is then mapped back to a scorecard-indicated outcome based on the ranges in the table below.

Exhibit 5

Scorecard-indicated outcome

Scorecard-indicated outcome	Aggregate numeric score
Aaa	$x \leq 1.5$
Aa1	$1.5 < x \leq 2.5$
Aa2	$2.5 < x \leq 3.5$
Aa3	$3.5 < x \leq 4.5$
A1	$4.5 < x \leq 5.5$
A2	$5.5 < x \leq 6.5$
A3	$6.5 < x \leq 7.5$
Baa1	$7.5 < x \leq 8.5$
Baa2	$8.5 < x \leq 9.5$
Baa3	$9.5 < x \leq 10.5$
Ba1	$10.5 < x \leq 11.5$
Ba2	$11.5 < x \leq 12.5$
Ba3	$12.5 < x \leq 13.5$
B1	$13.5 < x \leq 14.5$
B2	$14.5 < x \leq 15.5$
B3	$15.5 < x \leq 16.5$
Caa1	$16.5 < x \leq 17.5$
Caa2	$17.5 < x \leq 18.5$
Caa3	$18.5 < x \leq 19.5$
Ca	$19.5 < x \leq 20.5$
C	$x > 20.5$

Source: Moody's Investors Service

For example, an issuer with an aggregate numeric score of 11.7 would have a Ba2 scorecard-indicated outcome.

In general, the scorecard-indicated outcome is oriented to the corporate family rating (CFR) for speculative-grade issuers and to the senior unsecured rating for investment-grade issuers. For issuers that benefit from rating uplift from parental support, government ownership or other institutional support, we consider the underlying credit strength or Baseline Credit Assessment for comparison to the scorecard-indicated outcome. For an explanation of the Baseline Credit Assessment, please refer to *Rating Symbols and Definitions* and to our cross-sector methodology for government-related issuers.[9]

Assigning issuer-level and instrument-level ratings

After considering the scorecard-indicated outcome, other considerations and relevant cross-sector methodologies, we typically assign a CFR to speculative-grade issuers or a senior unsecured rating for investment-grade issuers. For issuers that benefit from rating uplift from government ownership, we may assign a Baseline Credit Assessment.[10]

Individual debt instrument ratings may be notched up or down from the CFR or the senior unsecured rating to reflect our assessment of differences in expected loss related to an instrument's seniority level and collateral. The documents that provide broad guidance for such notching decisions are the rating methodology on loss given default for speculative-grade non-financial companies, the methodology for notching corporate instrument ratings based on differences in security and priority of claim, and the methodology for assigning short-term ratings.[11]

Key rating assumptions

For information about key rating assumptions that apply to methodologies generally, please see *Rating Symbols and Definitions*.[12]

Limitations

In the preceding sections, we have discussed the scorecard factors and many of the other considerations that may be important in assigning ratings. In this section, we discuss limitations that pertain to the scorecard and to the overall rating methodology.

Limitations of the scorecard

There are various reasons why scorecard-indicated outcomes may not map closely to actual ratings.

The scorecard in this rating methodology is a relatively simple tool that can be used in most cases to approximate credit profiles of companies in this sector and to explain, in summary form, many of the factors that are generally most important in assigning ratings to these companies. Credit loss and recovery considerations, which are typically more important as an issuer gets closer to default, may not be fully captured in the scorecard. The scorecard is also limited by its upper and lower bounds, causing scorecard-indicated outcomes to be less likely to align with ratings for issuers at the upper and lower ends of the rating scale.

The weights for each factor and sub-factor in the scorecard represent an approximation of their importance for rating decisions across the sector, but the actual importance of a particular factor may vary substantially based on an individual company's circumstances.

Factors that are outside the scorecard, including those discussed above in the "Other considerations" section, may be important for ratings, and their relative importance may also vary from company to company. In addition, certain broad methodological considerations described in one or more cross-sector rating methodologies may be relevant to ratings in this sector.[13] Examples of such considerations include the following: how sovereign credit quality affects non-sovereign issuers, the assessment of credit support from other entities, the relative ranking of different classes of debt and hybrid securities, and the assignment of short-term ratings.

We may use the scorecard over various historical or forward-looking time periods. Furthermore, in our ratings we often incorporate directional views of risks and mitigants in a qualitative way.

General limitations of the methodology

This methodology document does not include an exhaustive description of all factors that we may consider in assigning ratings in this sector. Companies in the sector may face new risks or new combinations of risks, and they may develop new strategies to mitigate risk. We seek to incorporate all material credit considerations in ratings and to take the most forward-looking perspective that visibility into these risks and mitigants permits.

Ratings reflect our expectations for an issuer's future performance; however, as the forward horizon lengthens, uncertainty increases and the utility of precise estimates, as scorecard inputs or in other considerations, typically diminishes. Our forward-looking opinions are based on assumptions that may prove, in hindsight, to have been incorrect. Reasons for this could include unanticipated changes in any of the following: the macroeconomic environment, general financial market conditions, industry competition, disruptive technology, or regulatory and legal actions. In any case, predicting the future is subject to substantial uncertainty.

Moody's related publications

Credit ratings are primarily determined through the application of sector credit rating methodologies. Certain broad methodological considerations (described in one or more cross-sector rating methodologies) may also be relevant to the determination of credit ratings of issuers and instruments. A list of sector and cross-sector credit rating methodologies can be found here.

For data summarizing the historical robustness and predictive power of credit ratings, please click here.

For further information, please refer to *Rating Symbols and Definitions*, which is available here.

Moody's Basic Definitions for Credit Statistics (User's Guide) can be found here.

Authors:

Karen Berckmann

Michael Zuccaro

Endnotes

1 In our methodologies and research, the terms "scorecard" and "grid" are used interchangeably.

2 Liquidity management is distinct from the level of liquidity, which is discussed in the "Other considerations" section.

3 A link to a list of our sector and cross-sector methodologies can be found in the "Moody's related publications" section.

4 A link to a list of our cross-sector methodologies can be found in the "Moody's related publications" section.

5 For an explanation of the Baseline Credit Assessment, please refer to *Rating Symbols and Definitions* and to our cross-sector methodology for government-related issuers. A link to a list of our sector and cross-sector methodologies and a link to *Rating Symbols and Definitions* can be found in the "Moody's related publications" section.

6 When a factor comprises sub-factors, we score at the sub-factor level. Some factors do not have sub-factors, in which case we score at the factor level.

7 For definitions of our most common ratio terms, please see *Moody's Basic Definitions for Credit Statistics (User's Guide)*. A link can be found in the "Moody's related publications" section.

8 For an explanation of our standard adjustments, please see the cross-sector methodology that describes our financial statement adjustments in the analysis of non-financial corporations.

9 A link to a list of our sector and cross-sector methodologies and a link to *Rating Symbols and Definitions* can be found in the "Moody's related publications" section.

10 For an explanation of the Baseline Credit Assessment, please refer to *Rating Symbols and Definitions* and to our cross-sector methodology for government-related issuers. A link to a list of our sector and cross-sector methodologies and a link to *Rating Symbols and Definitions* can be found in the "Moody's related publications" section.

11 A link to a list of our sector and cross-sector rating methodologies can be found in the "Moody's related publications" section.

12 A link to *Rating Symbols and Definitions* can be found in the "Moody's related publications" section.

13 A link to a list of our sector and cross-sector methodologies can be found in the "Moody's related publications" section.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

REPORT NUMBER 1276303

Analyst Contacts

Jeanine Arnold +33.1.5330.1062
Associate Managing Director
jeanine.arnold@moodys.com

Janice Hofferber, CFA +1.212.553.4493
MD-Corporate Finance
janice.hofferber@moodys.com

Margaret Taylor +1.212.553.0424
Associate Managing Director
margaret.taylor@moodys.com

Clement Wong +852.3758.1561
Associate Managing Director
clement.wong@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S
INVESTORS SERVICE