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Genuine Parts Company (GPC) CEO Paul Donahue on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-17-19 Earnings Summary

Press Release *10-Q*

EPS of $1.5 beats by $0.03 | Revenue of $5.02B (6.18% Y/Y) misses by $-14.69M

Earning Call Audio

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Genuine Parts Company (NYSE:GPC) Q3 2019 Earnings Conference Call October 17, 2019 11:00 AM ET

Company Participants

Sid Jones - SVP, IR

Paul Donahue - Chairman & CEO

Carol Yancey - EVP & CFO

Conference Call Participants

Christopher Horvers - JP Morgan

Gustavo Gonzalez - RBC Capital Markets

Matt McClintock - Raymond James

Daniel Imbro - Stephens

Kate McShane - Goldman Sachs

Greg Melich - Evercore ISI

Seth Basham - Wedbush Securities

Jacob Moser - Wolfe Research

Bret Jordan - Jefferies

Operator

Greetings, and welcome to the Genuine Parts Company Third Quarter 2019 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Mr. Sid Jones, Senior Vice President, Investor Relations for Genuine Parts Company. Thank you. You may begin.

Sid Jones

Good morning, and thank you for joining us today for the Genuine Parts Company third quarter 2019 conference call to discuss our earnings results and outlook for 2019. I'm here with Paul Donahue, our Chairman and Chief Executive Officer; and Carol Yancey, our Executive Vice President and Chief Financial Officer.

Before we begin this morning, please be advised that this call may include certain non-GAAP financial measures, which may be referred to during today's discussion of our results as reported under generally accepted accounting principles. A reconciliation of these measures is provided in the earnings press release issued this morning, which is also posted in the Investors section of our website.

Today's call may also involve forward-looking statements regarding the company and its businesses. The company's actual results could differ materially from any forward-looking statements due to several important factors described in the company's latest SEC filings, including this morning's press release. The company assumes no obligation to update any forward-looking statements made during this call.

Now I will turn the call over to Paul for his remarks.

Paul Donahue

Thank you, Sid. And let me add my welcome to our third quarter 2019 conference call. We appreciate you taking the time to be with us this morning. Earlier today, we released our third quarter 2019 results. I'll make a few remarks on our overall performance, and then cover the highlights across our businesses. Carol Yancey will provide an update on our financial results and our current outlook for the full year. After that, we will open the call to your questions.

So to recap, our third quarter performance across our global platform. We are pleased to set a quarterly sales record achieving the $5 billion quarterly sales mark for the first time in our company's history. This represents a 6.2% sales increase from Q3 of 2018 and follows a 2.3% total sales increase last quarter with the improvement driven by a 1.2% comp sales increase and a 6.7% benefit from strategic acquisitions. These items were partially offset by a 1.7% headwind from foreign currency translation and the decline in sales related to the Auto Todo divestment earlier in the year.

Net income in the third quarter was $227 million and earnings per share were $1.56, excluding the impact of transaction and other cost and income related to acquisitions and divestments, adjusted net income was $219 million or $1.50 per share. This compares to $1.48 reported in the third quarter of last year. Our teams were active this quarter executing our strategy to further optimize our portfolio. This included actions to complete the Inenco industrial acquisition and Australasia, the sale of EIS and the investment in Sparesbox Australia's leading online automotive and accessories business. We made significant progress in several areas, this quarter and we are excited for the growth opportunities we see ahead.

We will cover each of these areas as we review our business segments. Our global automotive sales, which represented 56% of our total revenues were up 5.3% from last year and improved from 1.4% in Q2, comparable sales were up 1.8%, which was improved from the 1.3% in Q2 and acquisitions added another 6.5% of sales. This growth was partially offset by an approximately 2% unfavorable foreign currency translation and a 1% impact from the sale of the Auto total business in Mexico.

In our North American operations, U.S. automotive sales were up 2.5% on a comp basis and our Canadian Automotive business posted 3.8% sales comps. We remain confident in the ongoing strength of the North American automotive aftermarket and expect these markets to gain positive momentum over the balance of the year and well into 2020. For the second consecutive quarter, we had positive sales growth with both our commercial and retail customers with sales to the DIFM segment performing very well and outpacing our DIY sales.

Among our DIFM customer segments, sales to our NAPA AutoCare Center customers continue to outperform our overall commercial sales growth. This customer group represents approximately 18,000 independent repair shops in the U.S. and another 2,000 in Canada. So obviously a very key segment to us. We were also pleased to see stronger growth with our major account customers with sales increases in each of our categories including our fleet and government customers, national tire centers, regional accounts and OE dealers.

Now turning to our retail segment, while our team generated a positive revenue increase in the quarter, we have experienced a few headwinds in this segment of our business.

We believe this reflects a combination of lapping strong comps associated with our impact store rollout in 2018, a continued slowing of our transaction count, which we have seen across the industry and finally, timing related to major promotional events.

Our team has launched a series of initiatives, which we expect to improve this trend in the quarters ahead, while Carol will provide more financial details later, it's worth adding that both our U.S. and Canadian businesses delivered improved profitability and strong margins in the quarter. So a solid quarter for our North American automotive operations and we expect to continue to build on this positive momentum. In Europe, we continue to operate in a challenging sales environment although we are pleased to report an improvement in our core sales performance relative to the second quarter.

Overall, our sales comps were down mid-single digits, an improvement from the high single-digit decline in Q2. Across our geographical regions, we saw a significant improvement in our largest market, France, which posted a slight increase in the quarter.

Germany was down slightly while the UK was our most challenged region as it continues to feel the effect of Brexit along with tough comps fueled by a series of one-time events in 2018.

The UK labor market remains strong despite a decline in employment in Q3 while domestic growth is showing signs of slowing and overall business sentiment is lumping. That said, the news coming out of the UK this past week is somewhat encouraging and we remain hopeful the UK, and European Union can reach an agreement sooner or rather than later. The AAG team has made progress in executing on their sales and cost savings plans and we believe we are beginning to see the impact on our business, both on the revenue and cost side of the ledger.

Specifically related to sales one key initiative to highlight would be the Q3, Q4 rollout of the NAPA brand across several product categories. We believe the introduction of a quality private label offering will further distinguish our European business from the competition and provide incremental growth opportunities for us. As it relates to cost savings, our efforts thus far are having a positive impact on our European operating profits and we expect to generate additional expense reductions in the periods ahead.

In addition, we also made progress with our European M&A strategy during the quarter. We continue to integrate the PartsPoint acquisition, which closed on June 1st with our overall European business and this group performed according to plan. Likewise, we closed on the Todd acquisition in France on October 1st. This strategic acquisition positions us as the market leader in the heavy-duty segment across the French market. As a reminder PartsPoint and Todd are expected to add $330 million and $85 million in annual revenues. So despite current market conditions, we see many good things taking shape in our European business, and we remain committed to our growth and integration plans for this important segment of our Automotive operations.

Now turning to Australia and New Zealand, our team continues to outperform the market with solid comp sales growth of 4.2% for the quarter. This represents our strongest core sales growth in 2019 despite more challenging economic conditions across the region. We were also pleased to complete our full -- our first full quarter with our 87% investment in Sparesbox which closed on July 1. As a reminder Sparesbox is Australia's leading online automotive parts and accessories business and while not material to our financial results, this partnership serves to enhance our understanding of the digital marketplace and grow our digital sales capabilities in Australasia, and potentially across all of our global operations. So that's a review of our global automotive business and now we will turn to our industrial business.

Our Global Industrial Parts Group continues to push further with our portfolio optimization initiatives with the closing of the Inenco acquisition on July 1 and the sale of EIS on September 30. We will address both transaction shortly, but overall this group had a solid quarter with sales of $1.7 billion, up 9.9%, including an approximately 1% comp sales increase and a 9% benefit from acquisitions. This group also improve their operating margin by 30 basis points for the second consecutive quarter and 50 basis points if we exclude EIS. So we are pleased with the continued progress in our Industrial business. The softness we have seen in our top line growth is not unexpected given the overall slowdown we have seen in the industrial economy.

This has translated to mixed results across our product and industry sector sales with eight of our 14 product categories and seven of 12 industries positive in the third quarter. With the slowing U.S. manufacturing trends the Motion team continues to look for strategic tuck-in acquisitions as part of its overall growth strategy and effective October 1 acquired the fluid power house headquartered in Ontario, Canada.

FPA which is a full service fluid power distributor with four locations and projected annual sales of $20 million. Our Industrial business in Canada has been growing at a high single-digit pace or better for 11 consecutive quarters and we are excited to bolster their position in the Fluid Power segment. We have also further diversified our industrial footprint with the entry into Australasia. We were pleased to close on the Inenco acquisition and Australasia on July 1 and they have hit the ground running. Inenco is a leading industrial distributor in this region with operations in Australia, New Zealand and Indonesia, and this business performed very well in the quarter, providing accretive sales and profitability. We continue to believe that Inenco was an excellent strategic fit with Motion in North America and presents tremendous opportunities for global industrial growth.

Finally, during the third quarter, we announced a definitive agreement to sell the Electrical Specialties Group of Motion Industries and this transaction ultimately closed on September 30, 2019. As background, we had determined that this was in the best interest of the company given its lower growth and lower margin profile relative to our core industrial operations. We were very pleased to complete the sale of this business and take another step forward in our strategy to optimize our portfolio and best position GPC for sustainable long-term growth. So now let's discuss S.P. Richards, our Business Products Group.

For the third quarter, comp sales for this business were down approximately 1%. This sales decreased primarily reflects the slower sales in our core office supplies and technology categories as well as slower sales with our National Accounts Group. In contrast, our facilities and safety supplies business delivered another quarter of solid results and we expect continued growth from this category in the quarters ahead.

Despite the softness in the top line, the BPG team has stabilized its operations with improved profitability and a 40 basis point year-over-year improvement in operating margin for the quarter. This is significant progress and especially impressive given a devastating fire that occurred at our Atlanta DC at head office in mid-July.

First, we want to say how pleased we are to report then no one was injured during this unfortunate event. Second, our team was well prepared with an effective business continuity plan enabling them to get back up and operational in a matter of days. We are proud of our team for their attention to safety and servicing our customers under very difficult circumstances. So that's a recap of our consolidated and business segment results in the third quarter of 2019.

But before I turning it over to Carol for her remarks. We wanted to update you on our action plans and progress in accelerating our ongoing cost savings plans and developing aggressive expense reduction initiatives. These efforts are designed to more effectively address our cost structure, drive meaningful savings and deliver incremental value. So today, we are pleased to announce that we have plans in place to generate annualized savings of $100 million by the end of 2020. And as Carol will discuss later these are meaningful cost reductions that will help drive operating margin expansion in the years to come. Our team is committed to this mission and excited to work together to achieve these savings.

So with that, I'll hand it over to Carol.

Carol Yancey

Thank you, Paul. We will begin with a review of our key financial information and then provide you with our updated outlook for 2019. With our third quarter total sales of $5 billion representing a 6.2% increase, our gross margin for the quarter was 32.4% compared to 31.4% in 2018 with the improvement in margin relating to several factors. These include more flexible and sophisticated pricing strategies, favorable product mix and the benefit of higher supplier incentives.

In addition, the PartsPoint and Inenco businesses have higher gross margin profiles. These factors drove improved gross margins in all three of our business segments and we continue to expect our 2019 gross margin rate to remain relatively in line with our current run rate. The pricing environment across all three of our segments has been relatively in place scenario thus far in 2019. In automotive, the price increase is primarily related to the impact of tariffs, while Industrial and Business Products has seen increases associated with general inflation in areas such as raw material pricing, commodities and supplier freight.

Thus far we have been successful in passing on the price increases to our customers to protect our gross margins. So we continue to believe that the current levels of inflation have been a net positive to our results and we expect this to continue through the balance of 2019. Specific to tariffs their impact in the third quarter primarily reflects the 25% tariff on List 1, 2, 3 items, although business products was also impacted by the 15% tariff on the List 4A items which was effective September 1. With this in mind, the impact of tariffs on our Q3 sales was approximately 2% for U.S. automotive immaterial for industrial and approximately 1% for business products. We would add that the tariffs have had no impact on our gross margins.

Turning to our SG&A. These expenses were $1.3 billion in the third quarter, up 13.5% from last year and 25.3% of sales. Our SG&A expenses continue to be impacted by the effect of rising costs in areas such as payroll freight and delivery, IT, and cyber security, as well as ongoing investments to improve our efficiencies and productivity. The PartsPoint and Inenco businesses also have a higher SG&A profile, and this was a factor in the increase. In addition, we are seeing the deleveraging of expenses due to slower comparable sales growth in certain operations. As Paul mentioned earlier, we've been enhancing our initiatives and intensifying our efforts to reduce our costs and more effectively leverage our expenses.

While these efforts are still in the early stages of implementation. We've made significant progress and we expect to generate meaningful savings as we move forward. By the end of 2020, we expect to generate annualized savings of $100 million and we will continue to evaluate opportunities for additional cost reduction in the years beyond. As part of our commitment to drive efficiencies and eliminate redundant costs, we're focused on a variety of cost saving initiatives. We intend to reorganize and streamline several functional areas across our operations including numerous back office responsibilities. In addition, we expect to consolidate and ultimately reduce our total number of distribution facilities and to enhance the automation utilized and distribution and back office functions.

These actions will require organizational changes and we're currently working on a number of workforce initiatives to successfully drive this process, while also maintaining excellent customer service. We look forward to providing more details on these plans and initiatives as they are finalized and launched and executed in the coming quarters.

So now let's discuss the results by segment. Our Automotive revenue for the third quarter was $2.8 billion, up 5% from the prior year and our operating profit of $222 million was down 2% with an operating margin of 8.0% compared to 8.6% margin in the third quarter of 2018. This quarter, the 60 basis point decline in margin directly relates to the challenges we are facing in Europe. And as mentioned, we expect to see improvement in Europe as well as all of our Automotive operations through the saving plans that we will be implementing through the next 12 months.

Our industrial sales were $1.7 billion in the quarter, a strong 10% increase from Q3 of 2018. Our operating profit of $138 million was up 15.4% and their operating margin improved to 7.9% from 7.6% last year with a 30 basis point increase due to gross margin expansion and the leveraging of expenses. The industrial business continues to operate well with a 11 consecutive quarters of solid sales and operating results.

Our business products revenues were $492 million, down 1% from the prior year. Their operating profit of $21.6 million is up 9%, and their operating margin improved to 4.4% from 4.0% last year. So it's nice to see the margin expansion and continued steady results for this business. Our total company operating profit in the third quarter was $381 million, up 4% on a 6% sales increase and our operating profit margin was 7.6% compared to 7.7% last year. We had net interest expense of $25 million in the third quarter, which is up slightly from the second quarter and up from the $22 million in the third quarter last year.

Looking ahead, we are currently expecting net interest to be in the $92 million to $93 million range for the full year, which is down from our previous estimate of $97 million to $98 million. This improvement reflects our lower projected interest rates and debt levels for the balance of the year. Our total amortization expense was $26 million for the third quarter and we continue to expect full-year amortization to be approximately $100 million.

Our depreciation expense was $42 million in the third quarter and we are narrowing the range for our full-year depreciation expense to $170 million to $175 million for the year. On a combined basis we expect depreciation and amortization to be in the range of $270 million to $275 million for 2019. Continuing with the segment information presented in our press release, the other line which primarily represents our corporate expense was $26 million in the third quarter including an approximate $12 million benefit associated with the transaction costs and other income related primarily to the Inenco acquisition and the sale of EIS.

The acquisition of the final 65% interest in Inenco resulted in a $39 million gain on the revaluation of our original 35% investment. This was partially offset by transaction costs, and the $6 million net loss related to the sale of EIS, excluding these items, our corporate expense was $38 million or a $6 million increase from last year and primarily relates to payroll pressures increased legal and professional fees, ongoing investments in IT, Cyber security, Digital and overall omnichannel initiatives. For 2019, we are narrowing our expected range for corporate expense to $130 million to $135 million. Our tax rate for the third quarter was 25.3%, an increase from the 24.5% rate in the prior year, primarily due to transaction and other associated costs. For the full year, we continue to expect our 2019 tax rate to be approximately 25%.

Now let's turn to our balance sheet, which remains strong and an excellent condition. Accounts receivable of $2.7 billion is up 3% from the prior year. This compares to our 6% total sales increase and represents a 2.5% increase excluding acquisitions, foreign currency and the impact of EIS. So we did a good job of managing this account and we remain pleased with the quality of our receivables. Our inventory at September 30 was $3.7 billion, up 5% from September of last year, excluding acquisitions, foreign currency and EIS our inventory was up less than 1% and we're very pleased with the progress our teams are making in maintaining this key investment at the appropriate levels.

Our accounts payable of $4.2 billion is up 4% due mainly to the increase in purchasing volume and to a lesser degree the benefit of improved payment terms with key global partners. At September 30, our AP to inventory ratio was 113%. Our total debt of $3.4 billion at September 30 is down from the $3.9 billion at June 30th due primarily to the repayment of debt as a result of our strong cash from operations in the third quarter. At September 30, our average interest rate on our total outstanding debt stands at 2.23% which is improved from the 2.63% at September 30 last year. We remain comfortable with our current debt structure and we have a strong balance sheet and the financial capacity to support our future growth initiatives and our ongoing priorities for effective capital allocations.

As mentioned, we had strong cash flows in the third quarter and we've generated $745 million in cash from operations thus far in 2019. For the full year, we continue to expect approximately $1 billion in cash from operations and free cash flow, which excludes capital expenditures and the dividend to be in the $300 million to $350 million range. So we expect our cash flows to continue to support our ongoing priorities for the use of cash which we believe serves to maximize shareholder value.

Our key priorities for cash remain the reinvestment in our businesses, strategic acquisitions, the dividend and share repurchases. We have invested a $183 million in capital expenditures thus far in 2019 up $91 million from 2018. This reflects our growing global platform and the planned increase in our investments in areas such as technology and productivity in our facilities.

For the year, we're updating our capital expenditures to the range of $250 million to $300 million. Regarding the dividend 2019 represents our 63rd consecutive year of increased dividends paid to our shareholders. Our 2019 annual dividend of $3.05 represents a 6% increase from 2018 and it's approximately 54% of our 2018 adjusted earnings, which is in line with our targeted payout ratio. Turning to our share repurchase program we have purchased approximately 800,000 shares of our common stock thus far in 2019 and today we have $15.6 million shares authorized for repurchase. We expect to be active in the program over the long term and continue to believe that our stock is an attractive investment and combined with the dividend provides the best return to our shareholders.

So now let's discuss our current outlook for 2019. We are updating our full year 2019 sales and earnings guidance in consideration of several factors. These factors include our results through the nine months of the year, our current growth plans and initiatives, the market conditions we see for the foreseeable future across all of our operations, the September 30 sale of EIS and the ongoing impact of a strong U.S. dollar. With these items in mind, we expect our full year sales to increase approximately 3.5%. This updated sales outlook represents a change from our previous guidance for a plus 4.5% to plus 5.5% sales increase and it accounts for the sale of EIS as well as the incremental impact of foreign currency translation relative to our previous guidance.

As this is customary, this guidance excludes the benefit of any future acquisitions, by business we are guiding sales to be up 3.5% to 4% for the Automotive segment, which has changed from our previous guidance of plus 4% to plus 5% and primarily due to the impact of foreign currency and a challenging sales environment, which we continue to face in Europe, plus 4% to plus 4.5% for the industrial segment, which is down from the plus 7% to plus 8% previously primarily related to the sale of EIS, and down approximately 1% for the business products segment.

On the earnings side, we expect diluted earnings per share to be in the range of $5.44 to $5.52, which accounts for the transaction and other costs and income incurred through the nine months in 2019. And we are updating our outlook for adjusted earnings per share to $5.60 to $5.68 from the previous $5.65 to $5.75, this represents a $0.05 to $0.07 change in earnings primarily due to the sale of EIS. As a reminder, adjusted diluted earnings per share excludes any nine month and future transaction and other costs, that completes our financial update and our outlook for 2019 and I will now turn it back over to Paul.

Paul Donahue

Thank you, Carol. We were pleased to perform in line with our expectations for the third quarter, and would highlight several accomplishments. We had record quarterly sales, surpassing $5 billion in sales for the first time in our company's history. We achieved another quarter of positive comp sales growth in our U.S., Canadian and Australasian automotive businesses as well as our Industrial business. We further improved our gross margin with a 105 basis point year-over-year gain.

Our Industrial business continue to perform well, generating a 30 basis point margin improvement. The Business Products Group further stabilized posting a 40 basis point margin improvement. We improved our working capital position and generated strong cash flows and finally, we expanded our global footprint via several diversified acquisitions, both by segment and geography, including a Inenco and Sparesbox on July 1, and the fluid powerhouse and Todd on October 1.

In addition to these accomplishments, we have made strong progress on our ongoing business transformation. We continue to take steps to optimize our portfolio of businesses as demonstrated by the sale of EIS on September 30. Finally, we strengthened our focused on sustainable, value-creating initiatives to drive meaningful enduring efficiency including the cost reduction actions we discuss today. We will also continue to execute on our aggressive initiatives to improve top line performance. We plan to achieve this by incrementally growing revenue through new business generation, executing our digital strategy and finally securing strategic bolt-on acquisitions. We are focused on creating significant long-term value for our shareholders and we will continue to update the investment community as we make progress towards this important objective.

We thank you for listening, and with that, we'll turn it back to the operator and Carol and I will take your questions.

Question-and-Answer Session

Operator

Thank you. At this time, we'll be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Christopher Horvers with J.P. Morgan. Please proceed with your question.

Christopher Horvers

Thanks, good morning everybody. So first, a cleanup question, did both NAPA and Motion have one less Sunday in the quarter and what was the approximate comp benefit to that?

Carol Yancey

Yes. So we really, while we did have arguably an extra day in the third quarter and we were sort of day in Q1, it varies depending on the business and the geography in the segment. So we would say it was more of a minimal impact.

Christopher Horvers

Minimal. And so I guess -- maybe historically said 50 basis points or something less than that.

Carol Yancey

Something less than that. That's correct.

Christopher Horvers

In Motion, did have one less?

Carol Yancey

They did, yes.

Christopher Horvers

Okay, got it. And then could you maybe first on the Motion side, can you talk about those core Motion comps ex that extra day noise. Did it turn negative in September. And how are you thinking about the outlook over the coming quarters given the fact that the PMI has been I think negative in back-to-back months.

Paul Donahue

Yes. So Chris, thanks for the question. The look our Motion business, despite the decline two months in a row in PMI. And if you go back further Chris, PMI has been declined for six consecutive months and 10 out of 13. So not a new phenomenon by any stretch. Our Motion business we're pleased with the way the guys delivered in the quarter. Much like our overall business their strongest month of the quarter was August. They had a good month in August. July and September were both slightly weaker than August. But again, we're very pleased with the way the team delivered, and what is clearly a slowing industrial environment, but as we have seen in this cyclical business in the past, Chris they've done the right things in terms of cost take out and fortunately we're deliver -- we're able to deliver nice operating margin improvement in the quarter.

Christopher Horvers

Got it. And then just having to be able to run through the numbers, but I guess you think about what's the sort of implied Motion comp for the fourth quarter.

Carol Yancey

Chris, that would be similar to what it was in Q3, so around a 1% comp. And one other just item to note we're really pleased to have our expansion in a different geography in the industrial business going into Q4 and beyond with Inenco and Australasia. They're not quite as susceptible to some of the things that we're seeing in North America. So as we look ahead, still strong reported total sales, but a similar comp for Q4.

Christopher Horvers

Got it. And then just lastly the -- similar discussion around the U.S. NAPA business. How did you see the monthly trends ex that -- the extra day noise? And then how -- what the implied in U.S. NAPA comp here for the fourth quarter?

Paul Donahue

So I'll take the first part of the question, Chris the cadence of the quarter again, very similar to what I described in Industrial. Good August, very good August for the team here in the U.S. September not a surprise. We are up against our strongest comp of the year in September. And then July, what I'd say about July, we got off to a better start in July, and I think I might have even a commented on it during the last call, we saw that slow in the second half of the month of July. But all-in-all, very similar to the cadence that we outlined for industrial. And as far as guidance looking forward I'll let Carol tackle that one.

Carol Yancey

Yes, sure, Chris. As we look as we just ended the nine months with U.S. automotive coming around 3%, we would expect to be similar in Q4 was around 2.5% to 3% comp.

Christopher Horvers

Perfect, thanks so much. Best of luck.

Paul Donahue

Thanks, Chris.

Operator

Thank you. Our next question comes from the line of Scot Ciccarelli with RBC Capital Markets. Please proceed with your question.

Gustavo Gonzalez

Hi, good morning. This is actually Gustavo Gonzalez on for Scot today. Thank you for taking our questions. Just on sort of the strategic M&A and in particular automotive and sort of industrial and acknowledging, there are a lot of sort of puts and takes market-by-market. Can you sort of update us on how the M&A environment or opportunity set out there, it looks like right now versus, say, two or three years ago and maybe even sort of directionally touch on what kind of multiples you're seeing in the market today versus prior years?

Paul Donahue

Sure, I'll touch on that, the -- from our vantage point, from an M&A standpoint we will embark upon our plastic strategy at GPC to always be on the lookout for strategic bolt-on acquisitions across our different business segments and geographies. A classic coupled for us this past quarter were the Todd acquisition in France, which bolsters are heavy duty footprint and positions us at number one in that market, the fluid power house acquisition for our motion business, which strengthens our fluid power business in Canada. So those are our classic approach to M&A and certainly we will continue to look at bolt-on acquisitions that our strategy is generally to look for 1% to 2% per year in bolt-on acquisitions.

In terms of the larger, more strategic acquisitions like AAG we're going to be more focused on integrating those more strategic acquisitions in 2020 and beyond. And then in terms of valuations the valuations that we look at in our bolt-on acquisitions that really has not changed in previous years those -- most of those type acquisitions, we know the players, they know us, we're not getting into a bidding more, and it's a very sane environment, if you would.

Gustavo Gonzalez

Got it, thank you.

Paul Donahue

You're welcome.

Operator

Thank you. Our next question comes from the line of Matt McClintock with Raymond James. Please proceed with your question.

Matt McClintock

Hi. Yes, good morning everyone. I wanted to -- I wanted to know if you could focus on European automotive for a few minutes. I believe that you said that the French business returned to positive or slightly positive growth this quarter and I wanted to dig into that a little bit, what did you actually see in that business during the quarter that, that brought around that improvement that be the first question.

Paul Donahue

And thanks for the question, Matt. Look, what I would say, first and foremost is we were very pleased to see our European business rebound in Q3. As you know, Q2 was a challenge. So the team rebounded nicely, the French team, which is our single largest market in Europe had a solid quarter and delivering a positive sales increase after a significant decline in Q2. I think that the initiatives that they put into place will continue to drive here going forward. But the French team did a good job, where -- where we saw softness in the quarter was in the UK and again, we believe those issues that we face in the UK are largely transitory we were pleased to see that perhaps there may be a resolution to the Brexit issues and that will certainly help our business going forward if they are able to reach resolution.

Matt McClintock

And that has actually my follow up is the Brexit deal that apparently was reached today if that actually does go into place. Is that something that would remove an overhang immediately in your business? Or is that something that you would think would have to play out over a period of quarters before the overhang is removed. Thanks.

Paul Donahue

Yes, that's a good question, Matt, and I wish I could give you a specific answer. It's hard to say, but I will tell you that there has been is a bit of malaise in the marketplace, folks aren't sure with all the uncertainty around Brexit in the past number of quarters, I think it just weighed on business in general. So if they are to reach resolution if it makes its way through Parliament and they do reach resolution. I don't know that we'll see an immediate bounce back, but I do expect there to be a bounce back for sure. And I would also add Matt, that the initiatives that we're taking whether it happens or not. We're getting aggressive in introducing our NAPA brand into the UK, we launched a couple of product categories in Q3, and intend to accelerate that in Q4 going forward. So whether they reach resolution or not? Our team stands ready to improve that business.

Matt McClintock

I appreciate the color. Best of luck.

Paul Donahue

You're welcome. Thank you.

Operator

Thank you. Our next question comes from the line of Daniel Imbro with Stephens Inc. Please proceed with your question.

Daniel Imbro

Yes, good morning and thanks for taking our questions. What is there on North America, automotive organic growth, saw a nice acceleration in the two-year stack basis. Can you just talk about how much you think your programs, like the store remodels, loyalty or NAPA AutoCare are driving that growth versus just an industry acceleration we've seen as weather improves.

Paul Donahue

Yes, Daniel. Thanks for the question, what I would tell you about our NAPA business in Q3, and it was a very similar trend as we saw in Q2 is our DIFM category, which is our largest segment by a large percentage, it performed very well in the quarter. I would point out our NAPA AutoCare business as a very bright spot in the quarter. Our team, the NAPA AutoCare team continues to do a terrific job, and we also saw a better lift in our major account business. So both did quite well. We've got opportunities on the retail side, we saw our retail business soften in Q2 that carried into Q3, we've anniversaried some of the new retail initiatives that we have been driving in the last few years, but we're confident our team will get that business back on track but DIFM is the real highlight for us in Q3 as it was in Q2.

Daniel Imbro

Thanks a lot, that's helpful. And then maybe, following up on the last question, I think you mentioned you're rolling up the NAPA brand across some product categories in Europe. Can you help us think about how much of your business in Europe today is private label. I mean, how does that compare to existing players, and then how has the consumer responded so far to the new brand?

Paul Donahue

Yes, it's probably a bit early Daniel to give you an update on how they've responded to the NAPA brand. I will tell you that our team was excited, we launched it at a major show in Q3, a lot of excitement, a lot of buzz. They know the NAPA brand in the U.K. What I would say overall about private brands in Europe, it varies by market. So, very little private label in Germany, a bit more in France and the U.K. would be the strongest market for private label, which is why we chose the UK to launch first, but make no mistake our intent will be to move into France, Germany and the Netherlands with the NAPA private brand.

Daniel Imbro

Got it, thanks so much. Best of luck.

Paul Donahue

You're welcome. Thank you.

Operator

Thank you. Our next question comes from the line of Kate McShane with Goldman Sachs. Please proceed with your question.

Kate McShane

Hi, good morning. Thanks for taking my questions. I just wanted to go back and ask about the savings. Just in terms of timing, is there aren't going to be any impact to 2019, and then of the $100 million, you've identified, are you able to identify, how much could flow through versus how much needs to be reinvested given the rework changes you mentioned?

Carol Yancey

Yes, so I appreciate the question, and as we kind of look ahead at the $100 million and your comment specifically about 2019, what we're planning for is that we would have annualized $100 million by the end of 2020 and that would be a net number that would flow in, but it would be over a number of several quarters as it comes in and in doing the things that we're talking about and we're obviously still working on our plans and still looking at a number of initiatives in areas, we could have some costs in Q4 that come out of either head count related or facility related as we look ahead, those would be one-time type non-recurring that we could have in Q4, but again we're going into 2020 with the expectation that it's $100 million annualized by the end of the year. And then we obviously would be continuing to look for other opportunities as we move ahead, we're certainly not going to stop with just this initial look at the first $100 million.

Kate McShane

Okay, thank you. And then if we could just go back to the automotive industry and what you've seen now that tariffs, have been in place. Can you talk us through the impact on sales from inflation versus units and just what you think the impact was in the third quarter from tariffs specifically?

Carol Yancey

Yes. So as we, and again we commented that primarily we're talking about for Automotive and is the list one through three of the 25% tariff that went up on July 1, that was in Q3 about 1.9% on our sales for U.S. automotive. It was about 1% first half, so we would expect a similar amount for Q4. So we have kind of a blended 1.5% full-year basis for U.S. automotive. For the industrial business, it's really immaterial and for business products it was about 1% in Q3 and we would have a similar amount for Q4 they do have List 4b that comes in, as of now 12/15, but there could be around 1% for them also in Q4.

And again, I guess I would just leave you with, our teams have done a tremendous job navigating through all the puts and takes as it relates to tariffs. And we have successfully become much more agile and nimble in moving prices and being able to pass those through and have seen no impact on our gross margins.

Kate McShane

Okay, thank you. And then my final question on automotive. You mentioned the timing of promotional events. Were certain promotional events brought forward or were they pushed into Q4?

Paul Donahue

They were pulled forward Kate and honestly, we think that we'll balance those out as we roll into Q4, we'd begin to hit some colder weather. And we think we're going to be fine going forward, I would also just comment Kate, you ask about the U.S. automotive business. So I think one thing that we would absolutely stress is the health of the overall aftermarket, when you look at miles driven, which we saw a nice jump in July, gas price is down considerably, year-over-year the average age, all the fundamentals continue to be really solid for automotive aftermarket and when I look at our performance in the quarter, it plays to our strength, which is DIFM and I think that plays very well for us going into Q4 in 2020.

Kate McShane

Okay, thank you.

Paul Donahue

You're welcome. Thank you.

Operator

Thank you. Our next question comes from the line of Greg Melich with Evercore ISI. Please proceed with your question.

Greg Melich

Hi, thanks. I want to follow up a little bit on the tariffs and inflation. Carol in the past you guys have talked about general inflation in your COGS. Could you give us those numbers? Or highlight how much of the inflation that's occurring is related to tariffs as opposed to just some other inflation that might be out there.

Carol Yancey

Yes, happy to do that, Greg. What we saw the tariffs and inflation for U.S. automotive are virtually the same. So the inflation that they've had, be it on the COGS side or passing through on the sales side, more like a 1.5% to 2% is generally been inflation. Our industrial business is running around 2% for inflation and there is more indirect to tariffs you would talk about raw materials and supplier freight and things like that, and that's a normal level for them and then business products, they would probably running about 3% in total for inflation with about 1% tariff related.

Greg Melich

Got it. And then maybe as a follow-up to that, why is this quarter through the peak benefit to sales in terms of pass through? Is that just the timing of when the tariffs hit and when you flow it through. Is there something else we should be watching is to look at ebb and flow that -- is that number going forward.

Carol Yancey

No, I guess, if you recall, the original 10% tariff that we were under, that's how we operated through the first half of the year, so the pass-through on pricing was about 1% and again we didn't take that full 10% tariff, but what we did take about half of that we passed through and that led to about a 1% impact first half the tariffs went up July 1% to 25% and again we didn't take that full amount but we knew our second half would be more pronounced. So that's why we've said all along, second half would be around 2% first half was 1%.

Greg Melich

Got it. And then this is maybe a bigger picture question. The do-it-for-me was stronger, and you guys clearly went in there early and leaned into that, but DIY a little softer. Do you think there is -- is there any evidence that the consumer is having trouble with any of this inflation or may be deferring any decisions?

Paul Donahue

It's a great question, Greg and one that certainly we've contemplated as well because we have seen a bit of softening on the retail front. I think it's -- may be a bit early yet to make a call there. But what I will tell you is we are watching it very, very closely. One of the key stats that we obviously always monitor closely are the number of tickets flowing through our stores and then obviously the average basket size.

Basket size, both retail and wholesale was very healthy this quarter. Our retail ticket were down more so than our wholesale ticket. But, so I would tell you we're monitoring it closely. We're monitoring our competitive stand in the marketplace, and we'll react if and when necessary. But I think it's maybe just a bit early yet to make that call.

Greg Melich

That's super helpful, thanks a lot. Good luck.

Paul Donahue

Thank you, Greg.

Operator

Thank you. Our next question comes from the line of Seth Basham with Wedbush Securities. Please proceed with your question.

Seth Basham

Thanks a lot, and good morning.

Paul Donahue

Good morning, Seth.

Carol Yancey

Good morning.

Seth Basham

Good to hear that you have some plans for further cost savings. As we think about the outlook for 2020 from those savings, would it be appropriate to think that you'll be able to drive SG&A leverage, assuming a normalized sales environment in line with your long-term guidance?

Carol Yancey

Yes. Look the $100 million is about a 50 basis point in operating margin improvement and we would expect to drive -- again, as you mentioned normal comparable sales growth, we would expect to drive SG&A improvement operating margin improvement.

Seth Basham

Great. And then, as it relates to gross margin in the quarter, you talked about supplier incentives providing some benefit. Can you give a little bit more color as to what segment that was in and the sustainability of those types of incentives.

Carol Yancey

Yes, so actually in all three of our segments we had gross margin improvement. The larger share of the gross margin improvement is coming from what I call, just the core gross margin and that is from favorable product mix to all the initiatives we've done in the area of pricing, so significant buy side and sell side initiatives that we're doing in all of our businesses has improved our gross margin. We have had -- because we have better growth, we have had positive supplier incentives and those are primarily been an automotive and office products. And then as we mentioned, we do have a little bit of an uplift in gross margin from PPG, PartsPoint and Inenco that carry a higher gross margin, but really the core is what's driving this which is just us delivering on our buy side and sell side initiatives and again doing it with a good bit of tariff impact and inflation.

Seth Basham

Got it. Can you just provide a little more color on the gross margin benefit and SG&A headwind associated with the PPG and Inenco?

Carol Yancey

Yes, happy to. So when you look at our gross margin as Paul mentioned, it was up 105 basis points if you exclude the purchase accounting adjustments we had, about a third of that was related to the two new acquisitions, so two-thirds of that was from our core business being up. And then on the SG&A side, when you look at our SG&A and if you take out again the one-time costs our SG&A was up around 120 basis points. We would tell you, it's similar 30 to 40 basis point impact for PPG and Inenco. So, our core business again should be improving a bit when you take out some of these things and it's important to kind of look at the operating margin side as well.

Seth Basham

Understood. Thank you very much.

Paul Donahue

Thank you, Seth.

Operator

Thank you. Our next question comes from the line of Chris Bottiglieri with Wolfe Research. Please proceed with your question.

Jacob Moser

Hey guys, this is actually Jacob Moser on for Chris. Thanks for taking the question.

Paul Donahue

Okay.

Jacob Moser

So I'm just wondering of the $100 million of cost reductions. I think you guys said you still had some remaining from the $25 million synergy target from the AAG acquisition. So is this all incremental to that $25 million?

Carol Yancey

Yes, it is that $25 million, as it relates to AAG, which we are on track and that was all related to gross margin and global procurement, those $100 million is in the area of SG&A. So it is more payroll and facility and freight-related.

Jacob Moser

Okay, got you. And is it possible to quantify how much of that $25 million of synergies has come through at this point?

Carol Yancey

No, we have -- we said we would achieve that by the end of three years and we are on track to receive that. So -- I mean look, it's -- we would argue that we're on track, it's in our gross margin number, but it's the bulk of our improvement is coming from all the other stuff that we're doing.

Jacob Moser

Got you, okay. And then just, you said you paid down some debt in the quarter. So I think, now you're around three times debt-to-EBITDA versus maybe 1.5 historically like, have you changed how you're thinking about leverage and where do you see that shaking out?

Carol Yancey

Yes. So what we had in the quarter is we had some really nice improvement in our working capital and we were able to take that improvement in our working capital and use that to pay down some of our debt. The proceeds from the sale of EIS had in effect been redeployed on the two other acquisitions that we made earlier in the quarter. So when we look at where our debt was and it had ticked up a bit at the end of Q2 and obviously we're pleased with where it is now and expected to come down maybe just a little bit more by the end of the year. We're comfortable with where it was before and we're comfortable with where it is now, what we really look at is having flexibility and looking at what the right opportunities are. So again we're still comfortable with the amount of leverage we have today and we will certainly take it up for the right opportunity.

Jacob Moser

All right, great. Thanks for taking the questions.

Paul Donahue

Thank you.

Carol Yancey

Thank you.

Operator

Thank you. Ladies and gentlemen, our final question this morning comes from the line of Bret Jordan with Jefferies. Please proceed with your question.

Bret Jordan

Good morning guys. Carol, I -- if we think about the forecast on inflation, is it fair to think the '20 might have first half inflation similar to second half of '19 and the negligible in the second half, just as we lap those second list of tariffs?

Carol Yancey

I mean like again assuming tariffs kind of stay where they are and I think the year-over-year what you've laid out makes sense. We don't really see any other -- other inflationary things that would come in, but I would think that would be reasonable first half versus second half 2020.

Bret Jordan

Okay. And then a question on private label in Europe, when you think about the margin profile of private label, what is the delta over there. And I guess to sell private label you need to price it more aggressively against the market that's used to branded. I mean how do you think you can pick up margin over there with a bigger private label program.

Paul Donahue

Well, maybe I would start, Bret, by just mentioning again the initial launches in the U.K., we've launched private label batteries, as well as some suspension products, they will be priced a bit more aggressively then where our core product categories are today, what we've seen in the U.K., Bret, and you've probably seen, I know you follow it pretty closely over there, is a little bit of a flight to value, given the challenges, they are having in their economy and that's why, certainly we think we've got a big opportunity with the NAPA private brand.

Bret Jordan

Okay, great. And then one cleanup. Regional performance in the U.S. NAPA, any particular strengths or weakness?

Paul Donahue

Yes. Very similar Bret to Q2, which was our northern tier division. So that would include our Group in the Northeast which led the way again for us in Q3, the central part of the U.S., the Mountain Midwest all really performed well, Southwest did just fine. Where we saw a bit of softness was out west, which we also saw in Q2, and a little bit in the Atlantic. We think the Atlantic may have benefited a year ago from some one-time sales via the hurricanes coming through, so we are up against some bigger comps. So I wouldn't read too much into that. But the Northern part of the U.S. really, really performed well for us.

Bret Jordan

Okay, great. Thank you.

Paul Donahue

You're welcome. Thank you, Brett.

Operator

Thank you. Ladies and gentlemen, that concludes our question-and-answer session. I'll turn the floor back to management for any final comments.

Carol Yancey

We'd like to thank you for participating in our call today and we look forward to reporting out our year-end numbers. So thank you for your support of Genuine Parts Company.

Operator

Thank you. This concludes today's teleconference, you may disconnect your lines at this time. Thank you for your participation.