Seeking Alpha

Transcripts | **Consumer**

Hanesbrands Inc. (HBI) CEO Gerald Evans on Q3 2019 Results - Earnings Call Transcript

Oct. 31, 2019 1:16 PM ET | 1 Like
by: SA Transcripts

Q3: 10-31-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $0.54 | Revenue of $1.87B (0.99% Y/Y) beats by $10.66M

Earning Call Audio

Subscribers Only

00:00 -41:49

Hanesbrands Inc. (NYSE:HBI) Q3 2019 Earnings Conference Call October 31, 2019 8:30 AM ET

Company Participants

T.C. Robillard - Chief Investor Relations Officer

Gerald Evans - Chief Executive Officer

Barry Hytinen - Chief Financial Officer

Conference Call Participants

Susan Anderson - B Riley FBR

Jay Sole - UBS

Westcott Rochette - Evercore ISI

Michael Binetti - Credit Suisse

Paul Lejuez - Citi Research

Tiffany Kanaga - Deutsche Bank

David Swartz - Morningstar

John Kernan - Cowen

Carla Casella - JP Morgan

Jim Duffy - Stifel

Operator

Ladies and gentlemen, thank you for standing by. And welcome to the Hanesbrands' Third Quarter 2019 Earnings Conference Call. At this time, all participant lines are in a listen-only mode. After the speaker’s presentation there will be a question-and-answer session. [Operator Instructions] Please be advised that today’s conference is being recorded. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Mr. T C Robillard, Chief Investor Relations Officer. Please go ahead, sir.

T.C. Robillard

Good day, everyone. And welcome to the Hanesbrands' quarterly investor conference call and webcast. We’re pleased to be here today to provide an update on our progress after the third quarter of 2019. Hopefully, everyone has had a chance to review the news release we issued earlier today. The news release, updated FAQ document and a replay of this call can be found in the Investors section of our hanes.com website.

On the call today, we may make forward-looking statements, either in our prepared remarks or in the associated question-and-answer session. These statements are based on current expectations or beliefs and are subject to certain risks and uncertainties that may cause actual results to differ materially. These risks are detailed in our various filings with the SEC and may be found on our website, as well as in our news releases.

The company does not undertake to update or revise any forward-looking statements, which speak only to the time at which they are made. Unless otherwise noted, today's references to our consolidated financial results, as well as our 2019 guidance, exclude all acquisition, integration, and other action-related charges and expenses.

Additional information, including a reconciliation of these and other non-GAAP performance measures to GAAP, can be found in today's press release. With me on the call today are Gerald Evans, our Chief Executive Officer; and Barry Hytinen, our Chief Financial Officer. For today' call, Gerald and Barry will provide some brief remarks, and then, we'll open it up to your questions.

I will now turn the call over to Gerald.

Gerald Evans

Thank you, TC. Hanesbrands delivered solid results in the third quarter right in line with our guidance. And as we’ve seen throughout the year, our diverse business model offers us many avenues to deliver consistent revenue, profit, and cash flow growth. In the quarter, constant currency revenue increased 2% over prior year. We grew operating profit and earnings per share, while simultaneously increasing investments to support future growth.

Operating cash flow increased 47% to more than $300 million and we reduced our net debt by nearly half a billion dollars over prior year. And we achieved these results in spite of apparel traffic trends that were softer than we expected in the United States. We continue to benefit from our multi-year diversification efforts with another quarter of strong performance from our key growth initiatives, including international, consumer directed, and Champion.

Within each of these initiatives, we generated double-digit constant currency revenue growth and expanded operating margins. Looking at our growth initiatives, international revenue was $20 million higher than our guidance, driven by stronger than expected performance in both our activewear and innerwear businesses. On a constant currency basis revenue increased 11% over last year.

We also continued to expand international's operating margin in the quarter. And over the past five years, we've increased this segment's margin by more than 600 basis points through supply chain optimization and volume driven leverage. International has quickly become our largest reporting segment.

Looking out over the next several years, we expect international to represent an even larger mix of total company revenue and profit through a combination of organic growth initiatives, cross regional opportunities, and complementary acquisitions. With respect to our consumer directed business. Our investments continue to generate strong returns.

In the quarter, revenues increased 13% in constant currency with double-digit growth both domestically and internationally. We have significant momentum and consumer directed with additional opportunities for growth across geographies. For example, the recent launch of our maidenform.com website is driving new users to the brand.

Our Bonds brand generated mid-to-high single digit retail comp growth in the quarter and our Bras N Things business also continued its strong performance with growth in Australia, New Zealand, and South Africa. We're redesigning our Champion website with a mobile first approach to significantly improve the consumer experience and increase engagement globally.

We've also increased brand in content investments on several social media platforms behind a number of our brands. And we're strategically investing in branded stores in Asia, Australia, Europe, and the United States. Consumer directed currently accounts for 23% of total company sales, and looking forward, we expect consumer directed growth to continue to outpace our category growth rates.

Turning to Champion, we continue to see solid double-digit growth. Excluding C9, global Champion sales increased 26% in constant currency during the quarter. This was ahead of our expectations for the third straight quarter this year. We're also expanding margins in our Champion business as our brand investments normalize and we leverage prior distribution investments.

Global Champion has generated over $1 billion of incremental sales in just three years, and as dollar growth continues to increase. Year-to-date, on a constant currency basis, global champion revenue has increased approximately $470 million. The growth through the first nine months of this year is already more than $100 million higher than the growth at all of 2018.

Looking ahead, we believe Champion is well-positioned to generate another billion dollars of growth over the next several years. Now, we have several factors supporting our view. We see strong secular trends within the activewear category. Champion's brand equity scores are growing, particularly with Gen Z and Millennials.

We’re expanding Champions product portfolio, including a broader assortment within our performance, kids and women's lines as well as in casual footwear and accessories. And we’re increasing distribution in large economies such as China and South Korea. All of which positions us for continued double-digit Champion growth in 2020 and beyond.

We believe we have strong momentum and long runways in each of our growth initiatives. This, along with contributions from allocating our strong cash generation should drive continued long-term revenue, profit, and cash flow growth for the total company. Touching on our U.S. innerwear business, we continue to execute our strategy to return this business to growth.

In the quarter, we delivered approximately $580 million of revenue. Sales were modestly below our expectations, driven by the impact of softer than expected retail traffic trends on our basics business. Despite the challenging environment, over the past year, our basic shares have remained stable, while our Comfort Flex Fit and X-Temp innovations continue to expand.

Our intimates business performed in-line with our expectations for the quarter. Shapewear delivered its fifth consecutive quarter of sales growth, and we saw early signs of success with our bra innovations, positioning our intimates business from improved revenue trends in the coming quarter.

Looking to the fourth quarter for total U.S. innerwear, we expect sequentially improving revenue trends and strong margin improvement as we benefit from our brand investments and innovation. We anniversary a large retailer bankruptcy and we benefit from our price increases as commodity pressures have peaked.

So, in closing, we delivered solid third quarter results. Our diversified business model continues to produce revenue, profit, and operating cash flow growth. With our strong cash generation year-to-date, we're approximately $100 million ahead of last year, and well-positioned to deliver our full-year cash flow goal, and our leverage is coming down positioning us for higher shareholder returns in 2020 as we will once again have acquisitions and share buybacks at our disposal.

And with that, I'll turn the call over to Barry.

Barry Hytinen

Thanks, Gerald. We delivered solid third quarter results with revenue and earnings per share coming in towards the high-end of our guidance. For the quarter, sales were $1.87 billion and adjusted operating profit was $280 million both increasing 1% over last year. Adjusted earnings per share increased 4%, and GAAP per share increased 9%. Cash flow from operations of $302 million increased 47%, and net debt declined $470 million from a year ago.

With that summary, let's turn to the details of the quarter's results. Sales increased $18 million or 1% over last year, despite a $23 million headwind from foreign exchange. On a constant currency basis, sales were up over 2% or $42 million. Adjusted gross margin of 38.7% declined 50 basis points over last year. The impact from foreign exchange rates drove 20 basis points of the decline with lower innerwear margins accounting for the remainder.

Higher Champion margins, partially offset these items. The price increases we implemented earlier in the year offset input cost inflation in the quarter. As we said before, Q3 was expected to be the peak for commodity cost. Now that we're past the peak, looking to the fourth quarter, we expect the net benefit from pricing to drive gross margin expansion over prior year.

Adjusted operating profit in the quarter was $280 million. This included $3 million of currency headwinds and $11 million of growth-related investments as compared to last year. Our adjusted operating margin of 15% was consistent with prior year. For the quarter, acquisition and other related charges were $10 million. Our tax rate of 14.1% was in line with our forecast, and adjusted and GAAP earnings per share were $0.54 and $0.51 respectively.

Now, let me take you through our segment performance. U.S. innerwear sales declined 3.5%, compared to last year, driven by headwinds from retail and bankruptcies, as well as softer apparel traffic trends. For the quarter, basics revenue declined 2%, while intimate was down in-line with our expectations.

Innerwear's operating margin of 21% was down 110 basis points, compared to prior year, due to volume, mix and increased investments to support our intimate’s business. And as previously discussed, higher commodity cost in the quarter were offset by pricing.

Turning to our U.S. Activewear segment, as we discussed before, we're focused on remixing parts of our activewear business to branded products, which drives improving margins. Therefore, for the quarter, revenue declined 1%, while operating profit increased 4% as compared to last year.

Champion activewear sales, excluding C9, increased more than 18% over last year. C9 revenue was consistent with prior year and ahead of our expectation, due to strong sell-through trends. And sales in the remainder of our activewear segment declined approximately $45 million as compared to last year. This was driven by the previously disclosed exit of commodity programs in the mass channel, which represented $30 million of sales last year, as well as softer trends in the printwear channel.

Activewear's operating margin increased 90 basis points to 17.8% even with higher levels of investments to support our growth initiatives. The strong margin performance was driven by improved Champion profitability, favorable contribution from our remixing activity and the benefit from pricing.

In our international segment, reported sales increased more than 7%, and constant currency sales increased 11% or $68 million driven by growth in both our activewear and innerwear businesses in the quarter. International's operating margin of 16.2% was up slightly over last year. This marks its fifth consecutive quarter above the company average and we see additional opportunities for margin expansion going forward.

Touching briefly on our Global Champion business, excluding C9, constant currency sales increased 26% over prior year well ahead of our expectations. This consisted of 29% growth in our domestic Champion business and 24% growth in Champion international.

Turning to cash flow and the balance sheet. In the quarter, we generated $302 million in cash flow from operations, an increase of $96 million, compared to last year. The growth was driven by improved working capital performance and higher GAAP net income. Year-to-date, cash flow from operations is up 73% as compared to last year.

Consistent with our cash generation and debt reduction strategy, our teams drove a five-day improvement in our cash cycle over last year. On a sequential basis, we reduced our inventory balance by $125 million in our net debt by approximately $250 million. And compared to last year, our net debt is down $470 million.

Our leverage at the end of the quarter was 3.3 times on a net debt to adjusted EBITDA basis. This is down half turn from last year's 3.8 times and down two-tenths from last quarter's 3.5x. We're on track to lower our leverage to 2.9 times by the end of the year. And now turning to guidance, I'll point you to our press release and FAQ document for more details, however I would like to share a few thoughts to frame our outlook.

For the full year, we narrowed our guidance range as for revenue, operating profit, and earnings per share. We raised the midpoint of our revenue range to reflect stronger than expected performances in our Champion and international businesses. We tightened the high-end of our operating profit range, and we raised the midpoint of our EPS range, driven by lower interest expense.

Today, we also issued fourth quarter guidance, which at the midpoint implies total sales of consistent year-on-year on a constant currency basis or down less than 1.5% on a reported basis. Our guidance reflects nearly $20 million of currency headwinds in the fourth quarter, as well as headwinds from the exited commodity programs in the winddown of C9.

With respect to our segments, the midpoint of our fourth quarter revenue guidance assumes a decline of approximately 2% in our U.S. innerwear segment. This outlook reflects improving sequential trends, including the anniversary of the Sears bankruptcy. In U.S. activewear, the midpoint of our guidance assumes a revenue decline of approximately 7% over last year. This is unchanged from our prior outlook although we now expect even stronger Champion growth in the quarter.

We increased our fourth quarter Champion activewear forecast by approximately $15 million to reflect a strong demand trends Gerald mentioned. We now expect Champion activewear, excluding C9 to increase at a high teens rate as compared to our prior outlook for a low double-digit growth. And reflecting my earlier comments, we’ve taken a more cautious outlook within the printwear channel.

In our international segment, the midpoint of our guidance assumes reported sales growth of approximately 4% in constant currency sales growth of approximately 7%. This is above our prior outlook as we've experienced stronger than expected performance all year from our international business.

Our fourth quarter operating profit range is $259 million to $284 million and reflects a $3 million headwind from exchange rates. At the midpoint, our guidance implies a $12 million increase as compared to prior year. We expect interest and other expense of approximately $51 million.

Our fourth quarter guidance assumes a tax rate of approximately 14%, diluted shares outstanding of slightly less than 366 million and approximately $11 million of acquisition integration and supply chain related charges. Therefore, at the midpoint, our fourth quarter adjusted net income guidance is approximately $190 million, and our guidance for adjusted and GAAP earnings per share range from $0.48 to $0.54 and $0.46 to $0.52 respectively.

So, in closing, we delivered another quarter of solid results once again underscoring the benefits of our diversified business model. Our key growth initiatives, including Champion and international continue to outperform our expectations. We're generating higher levels of operating cash flow and our leverage is coming down positioning us for higher shareholder returns in 2020 and beyond.

And with that, I'll turn the call back over to T.C.

T.C. Robillard

Thanks, Barry. That concludes our prepared remarks. We'll now begin taking your questions and will continue as time allows. I'll turn the call back over to the operator to begin the question-and-answer session. Operator?

Question-and-Answer Session

Operator

[Operator Instructions] Our first question comes from Susan Anderson with B Riley FBR. Your line is now open.

Susan Anderson

Hi. Good morning. Thanks for taking my question. I was wondering on the Basics pressure in the quarter, was this consumer not accepting price increases or was it mainly just lower traffic in the closed-doors? And then also maybe if you could talk a little bit about the pricing impact in the quarter, and then also the drivers that you see for fourth quarter for Basics and I guess the Innerwear category as a whole? Thanks.

Gerald Evans

Sure, Susan. Let me take the first half and I'll let Barry touch a little bit more on the pricing at the end. From the standpoint, let me just start with the quarter. We're very pleased with our quarter, once again coming in at the higher end of our expectations on sales and earnings. And from the standpoint of our diversified business, it is really continuing to show through and we love the way our growth initiatives continue to outperform.

Within the Innerwear segment, we also – as I noted, we delivered $580 million of sales in the quarter, and we viewed it as a solid quarter for Innerwear. Sales were modestly below our midpoint of our expectations and now it's about $8 million, $9 million, somewhere in there. And we really did see a little slower retail traffic than we expected early in the quarter and particular intended to pick up a bit as we work through, and more normalized as we work through, and actually seems early in October to be normalized as well.

So, we view this more as a short-term fluctuation in anything of significance to worry about underneath. We continue to see our Basics business. Our shares are performing very nicely as we look out over the last 12 months in spite of the challenging business environment and our innovations are gaining traction. For example, our Comfort Flex Fit POS continues to be up double digits even 18 months after its introduction, and we've now continued to roll that out into women's underwear and socks.

So, we feel like the things we've set out to accomplish in Innerwear are going fine on the Basics side on intimates, and intimates came in once again, and has all year right on where our expectations, where we've started to see in early on the shapewear performance. It was our fifth consecutive quarter of growth there. We're seeing our innovations in bras begin to get traction as well.

So, as we look to the fourth quarter, we do have an expectation of sequentially improving revenue results with particularly good results or movement in our intimates business, and that's really all behind our investments in our brands and our innovations, as well as we are overlapping a fairly significant retail bankruptcy in the quarter as well.

And then from a margin standpoint, our prices have been in place all year, and we're passing the peak of commodities and are beginning to see some supply chain efficiency that give us confidence on the margin – op margin side as well.

So, Barry do you want to touch a little bit on the pricing in particular?

Barry Hytinen

I think you hit the high points there, Gerald. Susan, hi, it's Barry. Good morning. Thanks for the question. We got all the pricing we expected. And as you recall from earlier in the year that was 4%, 5% on the vast majority of our Innerwear business. So, that is flowing through and has been for the last couple of quarters. And the element related to the fourth quarter is that input costs are meaningfully down as we move forward, and we've got a nice cost position.

So, from the standpoint of what you'll see is the net benefit of that pricing really starts to flow into our gross margin, as we've expected in the – for the fourth quarter for some time and that will help drive improved Innerwear operating margins as we move through the remainder of the year. Thanks for the question.

Operator

Our next question comes from Jay Sole with UBS. Your line is now open.

Jay Sole

Great. Thanks so much. So, asked about the Champion growth, 26% growth ex-FX outside of C9 for Champion. You're talking about double-digit growth next year. It sounds like you're raising that target from $2 billion to $3 billion in the long-term growth. You gave us some color on fiscal 2020, and maybe just talk about the shape of fiscal 2020? Do you think you can deliver positive growth for all the quarters of fiscal 2020? Because you know the compares are a little tougher in the first part of year than there will be in the next part of the year. So, maybe you could just help us there, and then talk about what the addition of distribution partners in South Korea and the second one in China, made the business? Will that be additive to sales right away and what kind of benefit might that adds to the Champion business?

Gerald Evans

No, we're very pleased. Thank you for the question on Champion. We're very pleased with how it performed once again. It once again outperformed our expectations, and you noted it was strong, up 26%, up 29% domestically, 24% globally up across our Innerwear, as well as our Activewear businesses, so I'm feeling really good about that. And we often get tangled up in the percentages, but when we look at the real growth, over $1 billion of growth in three years is just phenomenal and we're already ahead of pace by $100 million over the full growth last year.

So, we couldn't be happier with where it's going. We will surpass our $2 billion goal next year, two years early, and we do believe that, that that next billion can emerge over the next few years. So, we've got a lot of momentum behind it. You heard that we're seeing not only the secular trends in Activewear, but the equity scores growing, we're expanding our product lines and the new geographies to your question.

I think, I spoke last time about moving into China with a second partner which also puts us online. We've now added South Korea into that mix as well. So, tremendous opportunity there, and we do expect double-digit growth and beyond, and it will be an important driver as we look to next year from the standpoint of how the business performs in total and so we couldn't be happier with that.

Operator

Our next question comes from Omar Saad with Evercore ISI. Your line is now open.

Westcott Rochette

Hi, guys. This is Westcott on for Omar. I just have some more questions on Champion. You said you're going to be rolling out an updated online platform mobile-first, has an investment already kind of been absorbed, or is there an increased investment that need to go, that you need to make to expand that program? And thinking about the demand – balancing the demand, particularly domestically, I think a lot of people see the Champion product used as a promotion driver from a lot of your partners. Wondering how you balance like the demand aspect of keeping the demand high, but not getting people used to promo? Thanks a lot, guys.

Gerald Evans

Well, I think, let me just say, from the standpoint of the investment, we've been making that investment all year in the platform that we're going to roll. It comes active, the first of next year. So, that's already underway for Champion and it's an important part of the broader push we've got behind Champion in the digital push.

From the standpoint of the brands, nothing could be farther than the truth. It is prestigious of promotion brand. It actually continues to press its limits on price and premium position, and well segmented across the channels and we think there's a lot of legs to continue to push it even higher over time, as well as across the women's business, as kids and in performance. So, we feel good about the brand. As I noted in my comments, we think there's a lot of room to grow, and a lot of strength in this brand.

Barry Hytinen

And Westcott, it's Barry. I think I'll just add as a reminder, something we've made the point about throughout the year is our level of investments year-on-year to support brands and growth will be consistent in the fourth quarter of this year, whereas it's been a significant increase year-on-year through the first three quarters as you'll recall.

Last year, we elevated the level of investments and such that earlier in the year, we've said by the time we get to the fourth quarter, that will be kind of consistent year-on-year. So, that will no longer be a headwind to profitability, and will be part of the reason why the operating margin start to expand. So, we're looking forward to good trends here in the fourth quarter.

Operator

Our next question comes from Michael Binetti with Credit Suisse. Your line is now open.

Michael Binetti

Hi, guys, thanks for taking my questions here. Just a couple quickly. As you look at the expectation for pricing the flow through better in fourth quarter as the commodities come down. How should we think about the competition and what they may do with that expanding margin opportunity? Is there any risk we should think about, particularly some of the private label competitors out there that they try to reinvest some of that commodity benefit into lower – lowering the pricing spread? And then I also wanted to ask on, if you could help us unpack the gross margin in the quarter a little more between Champion and some of the Innerwear pressure that you saw? Obviously, I think you said you saw most of the pressure, excluding Champion. I think, you're expecting gross to just be about flattish. So, maybe just help us dimensionalize that and help us think forward on it a little bit? Thank you.

Gerald Evans

Yes, let me take the first half of that, and I'll let Barry take your second half. From the standpoint of pricing, our pricing has been in place since mid-February, and we've seen – as we've commented before, we've seen a number of competitors – and follow in different areas, as well as we've seen private label take pricing in certain areas. So, from the standpoint, these were – our prices were put in place to maintain our margins in the face of rising commodity and input costs, and we've seen others follow for the same reason to maintain their margins, I assume. So, we feel our pricing is in place and well-positioned.

Barry Hytinen

Yes, Michael. Hi, it's Barry. Good morning. You asked about the margin in the quarter. So, gross margin was down slightly below our forecast. I'd say there were three things that I would highlight as it relates to gross margin year-on-year. First thing is similar to earlier in the year, FX continues to be a big headwind and costs us about 20 basis points versus last year.

Second is, pricing Champion profitability improvement as you mentioned has continued and Activewear remixing all of those are quite favorable to growth and will continue to be in the fourth quarter. And then third, that was offset by higher commodity cost and Innerwear margins really related to mix and leverage. And as we look forward, we see that getting much better, actually, as we have a much better visibility on cost position getting better as we overlap these peak commodity costs as we've forecasted earlier in prior calls. And just as a reminder, year-to-date, gross margin is actually up 10 basis points on a constant currency basis and slightly down on a reported basis.

Operator

Our next question comes from Paul Lejuez with Citi Research. Your line is now open.

Paul Lejuez

Hi, thanks, guys. Can you just talk about pricing on the Champion side? I'm curious about AURs and your direct-to-consumer business for Champion, and how much is price a driver of Champion sales in the wholesale business as well? If price is a driver, curious how much is mix shift within the Champion brand versus higher prices on unlike items? And also, if you could – also on Champion, can you talk about the percentage of that brand sales coming from men's, women's, kid's and where you think those percentages might go couple of years down the line? Thanks.

Gerald Evans

Yes. Let me just take that. From the standpoint of price versus other means of growth, this business is growing at such a phenomenal level. It's a combination of all of that. It is a combination that continuing to push up to the more premium levels, but importantly it's continuing to build our distribution within our current customers across geographies and into new customers. So, it's just all the momentum that you would expect. I mean this is phenomenal growth here, so it's not one item that's driving this growth.

From the standpoint of the business mix today, it's more mixed into the men's side of things, but we certainly see the opportunity to continue to make that a bigger mix of women's, and then kids is an area of tremendous opportunity as well. And also, the performance across the genders, the performance of products across the genders is a small, but growing area that we also see as a growth potential for us. So, as you can tell, we are very optimistic and very bullish on this brand, because we see lots of ways to keep growing it.

Operator

Our next question comes from Tiffany Kanaga with Deutsche Bank. Your line is now open.

Tiffany Kanaga

Hi. Thanks for taking your questions. Given the very good growth in international, would you discuss where you believe we are in the maturity curve with respect to Champion outside the U.S. specifically? How the 24% international growth in the quarter might compare to growth next year? And how much of that you expect to be driven by adding distribution partners, as opposed to organic growth with existing ones?

Gerald Evans

Yes, let me just say, we're delighted with the International business and how well it's done, up 11% in constant currency, 7% in actual is phenomenal growth in that business and it's another quarter in a row that we've done that, and we've done it all year long. And this was a great indication of the power of the total business model. We saw growth in both our Innerwear and Activewear businesses.

We commented that Champion was up 24%, but the Innerwear business was up mid-single-digit. And if I dig down more on that Innerwear business in total, there’s growth across a number of geographies, the Hanesbrands delivered nice growth across Mexico, Japan, Canada, and Philippines. The Bonds brand and Bras N Things brand grew nicely in Australia, New Zealand and of course we saw Champion growth across the region.

So, from the standpoint of our growth, we've got a lot of room here to grow as well. And from the standpoint of new areas, we've obviously added a second distributor in China that we believe will quickly make China our second largest geography for Champion. As we look to next year and beyond, we just added a new distributor as we noted in our comments in Korea, that opens up that sizable economy to us as well. So, there’s tremendous opportunity to keep driving this business forward. It already is our business segment, and as I noted in my comments, I would expect it to get larger over time.

Operator

Our next question comes from Ike Boruchow with Wells Fargo. Your line is now open.

Unidentified Analyst

Yes. Hi, guys, this is [Matt] on for Ike. I appreciate the color on gross margin in 3Q, and getting to 4Q operating margins, should we continue to expect modest leverage on – deleverage on the SG&A side? And then as far as the updated guidance, can you just help us quantify the revised outlook for the U.S. retail market versus prior plan and kind of the longevity of those expectations going forward?

Barry Hytinen

Okay. Hi, Matt, this is Barry. I'll do the gross margin point, and then I'll let Gerald talk a little bit about retail. Yes, thanks for the question on the fourth quarter profit. At the midpoint, let me help you frame that. For the total company in the fourth quarter, our outlook assumes gross margin is up about 100 basis points and operating margin is up about 90 basis points, which equates to the $12 million more operating profit we have in the guidance year-on-year. I think the easiest way to explain that is to go right through the expectations that we have by segment.

So, on a year-over-year basis in U.S. Innerwear, we have both gross and operating margins up about 100 basis points, which when combined with our sales guidance is roughly $138 million of operating profit, which is an increase of $4 million year-on-year. I think a good way to explain how Innerwear expectation is developed is looking at it sequentially. As you'll see when comparing our fourth quarter guidance with the third quarter performance, the absolute sales level are basically the same and the pricing benefit is consistent.

So, if I explain Innerwear sequentially, our guidance would equate to about $16 million more profit in the fourth quarter versus the third quarter. And there are two drivers. First is, we have $10 million to $11 million of benefit due to improved supply chain efficiencies and lower input cost, and I'll note, we have very high visibility on those improvements. And then secondly, we'll have less promotional activity and better mix and lower expense, which is just seasonal, and those combined for about $5 million of sequential profit increase. And when you put that in your model, I think you'll see that it arrives at the guidance I referenced.

Now within U.S. Activewear, our guidance assumes operating profit dollars are consistent year-on-year based on our sales guidance, which puts operating margin up a little over 100 basis points versus the fourth quarter of last year for U.S. Activewear. Now, that's all explained through the remixing activity we've had underway in the segment to drive the improved profitability we've been seeing, which is really driven off the few factors.

First, Champion is going to grow nicely again and we're seeing strong margin improvement that will more than offset the decline we projected in C9. We have the benefit from the exited commodity programs, we call that was $20 million of sales last year with essentially no profit. And then, thirdly, as we noted in the commentary, we've got a sales decline in our printwear channel based on how that channel is developing and that's really a lower margin portion of the Activewear segment. So, that will get you to flat profit dollars in the quarter year-on-year.

And internationally, we're using incremental margin on the $25 million of reported sales increase that would get to about $6 million more profit, and you get about $1 million better from our other segment and corporate cost being consistent. And I think, at this point, I'll just remind everyone one more time that at a total level for the company, brand investment will be equivalent year-on-year in the fourth quarter. So, all in all, we have high visibility on the gross margin expansion, which with the good cost controls we've got underway will yield the increased operating profit that our guidance is calling for.

Gerald Evans

And I'll just jump on the retail side of things, just to finish the color on that side, and much of this was in my comments. Look, we feel good that sequentially we will see improvement in our Innerwear business based on the innovations that we have in place and the brand investment, as well as we do overlap a pretty significant bankruptcy in the third quarter of last year of this past year. So, from the U.S. Innerwear side, we feel that we've got good momentum there and we certainly have the prices in place to help propel that as well.

On the Activewear side, we're effectively booked. We can see our bookings at this point in time and Champion's driving the vast majority of that business. So, we feel that we've got a very thoughtful plan from the standpoint of U.S. Innerwear. We said all year, we were going to view the retail environment with caution, and we continue to do that in our guidance for the fourth quarter.

Operator

Our next question comes from David Swartz of Morningstar. Your line is now open.

David Swartz

Yes. Can you talk a little bit about the slowness in the printwear market and also your outlook and strategy in the long-term for printwear? Thanks.

Gerald Evans

Sure. Let me take that. From the standpoint of printwear, printwear is a fairly small part of our total Activewear business. It's a business that tends to be a bit more sensitive to economic fluctuations and so forth in the market. And so, it was a small fluctuation of what we expect in the third quarter about $15 million or so, and we projected a similar sort of level of impact in the fourth quarter out of caution. We'll see how that plays out, but it's a business that we manage tightly, and it's one you may recall, a number of years ago we restructured a bit the focus more on the branded elements of that, and that's how we still run the business today.

Operator

Our next question comes from John Kernan with Cowen. Your line is now open.

John Kernan

Hi. Good morning. Thanks for taking my question. Just wanted to go back to the International segment, the constant currency revenue growth here has been very consistent as has the margin profile all year. Can you just update us on the long-term thinking around this, the growth drivers, as well as the margin profile, both for not just long-term, but also for the fourth quarter as well?

Gerald Evans

Yes, let me take it from the growth drivers, and I'll let Barry jump in if he wants on – a little bit on the margin profile side of things, but clearly what we're seeing is early on was building this international presence through our acquisition strategy, which has proven to be very effective in broadening our business in a profitable manner. And we're now building upon that with organic growth and throughout we've seen the synergies come through from both the leverage of our scale, but also from our supply chain benefit.

And this business has gone from a high-single digit kind of business to a nice business outperforming the corporate average very quickly. And we think there's room to grow. And then this thing should become a bigger part of our business over time. And as it becomes a bigger part of the business, you would expect some additional scaling through the margin side. Barry, do you have anything to add?

Barry Hytinen

Hi, John, this is Barry. Good morning. I agree with your points. Thank you for them that the International business is continuing to develop exceptionally well. We beat our guidance in the quarter by $20 million on a reported basis, and even more on constant currency. I want to congratulate the team on the performance, because it's really been strong across all regions. And year-to-date, on a constant currency basis, the team has delivered growth in sales and profits in all of our regions. And we expect margin to be up in the fourth quarter and we have a modest amount of margin improvement in there that may just prove to be conservative.

In the third quarter, we increased some level of brand investment. We won't have that as a headwind in the fourth quarter year-on-year. And so, as we move into 2020 and beyond, we see the opportunity for our International margins to continue to expand, thanks to leverage mix, pricing and the underlying trends there are very good. So, we feel great about how the International business is developing. Thank you.

Operator

And our last question comes from Carla Casella with JP Morgan. Your line is now open.

Carla Casella

Hi. You may have answered this, but I may have missed it. Can you just give us an update on how you're viewing inventory both in the channel, as well as your own on the balance sheet, and your comfort level with both?

Gerald Evans

Yes, let me take the channel part of that, and I'll let Barry take our balance sheet part of that. From the standpoint of channel, we feel like we're well-positioned. The fluctuation that we saw in traffic a bit early in the quarter was – our business is replenishable in the Innerwear side, so when traffic fluctuates, the customers don't reorder quite as much, so the inventory stays in line. And certainly, we entered the fourth quarter with our inventory in line and we feel that we've done so in the Activewear side. And as we look across the global businesses, we have a good snapshot, as well as we're positioned around the world as we want to be going in the fourth quarter from the retail side of things. Barry, you want to take?

Barry Hytinen

Hi, Carla. Thank you for the question. Inventory was down $125 million from the second quarter, down versus last year as well. We improved days of inventory. I think the team is doing a great job with respect to it. As you'll recall, earlier in the year, we noted that we had invested some in front of some of the Champion growth to fund that, and that over the next couple of quarters, we'll be seeing inventory come down.

Obviously, we did that in the third quarter, and we expect to continue to see inventory coming down in the fourth. And over the next several years, I think the team is very focused on driving improved days of inventory and we would expect that to be a benefit to working capital in the future. So, appreciate the question. Thank you.

Operator

And we have a question from the line of Jim Duffy with Stifel. Your line is now open.

Jim Duffy

Thanks. Thanks for squeezing me in. Barry, with sidelines to be in – within the target leverage ratio into 2020, can you talk about how you think about use of cash flow thereafter? Do you consider share repurchases in the context of the share price or how do you prioritize that versus M&A opportunities to further diversify the business? Thanks.

Gerald Evans

Hi, Jim, this is Gerald. And yes, we are doing a great job on bringing down our leverage, and we will be back in our range as we've said, we will by the end of the year. And certainly, we are most comfortable operating in that debt range of two times to three times net debt-to-EBITDA. From the standpoint of what that allows us to do, it allows us to introduce both share repurchases and acquisitions back into our tool box, if you will, to drive shareholder returns.

And I think we've done a nice job over time of balancing the two and we will certainly continue to balance the two to drive the long and the best return for our shareholders at the given time. And I think you should expect that the acquisitions will be part of that mix over time. So, our goal has been to get back in that range, and we'll be solidly there next year to unleash the power of our – full power of our capital allocation model.

Operator

I'm showing no further questions in queue at this time, I'd like to turn the call back to T.C. Robillard for closing remarks.

T.C. Robillard

We would like to thank everyone for attending our call today and we look forward to speaking with you soon. Have a great day.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.