Olaplex Holdings, Inc.
Third Quarter 2024 Earnings Results Conference
November 7, 2024

<u>Presenters</u>
Patrick Flaherty, Vice President of Investor Relations
Amanda Baldwin, CEO & Director
Catherine Dunleavy, COO & CFO

<u>Q&A Participants</u>
Jungwon Kim - TD Cowen
Ashley Helgans - Jefferies
Alec Legg - Canaccord Genuity Corp.
Korinne Wolfmeyer - Piper Sandler & Co.
Shovana Chowdhury - JPMorgan Chase & Co
Lauren Lieberman - Barclays Bank
Olivia Tong Cheang - Raymond James & Associates, Inc.
Robert Ottenstein - Evercore ISI Institutional Equities

Operator
Greetings, and welcome to the Olaplex Holdings, Incorporated Third Quarter 2024 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press Star zero on your telephone keypad. As a reminder, this conference is being recorded.

It is now my pleasure to introduce Patrick Flaherty, Vice President of Investor Relations. Thank you. You may begin.

Patrick Flaherty
Thank you, and good morning. Joining me today are Amanda Baldwin, Chief Executive Officer, and Catherine Dunleavy, Chief Operating Officer and Chief Financial Officer.

Before we start, I would like to remind you that management will make certain statements today, which are forward-looking, including statements about the outlook of Olaplex's business and other matters referenced in the company's earnings release issued today. Each forward-looking statement is subject to risks and uncertainties that could cause actual results to differ materially from those projected in or implied by such statements. Additional information regarding these factors appears under the heading Cautionary Note Regarding Forward-Looking Statements in the company's earnings release and in the filings the company makes with the Securities and Exchange Commission that are available at www.sec.gov, and on the Investor

Relations section of the company's website at ir.olaplex.com. The forward-looking statements on this call speak only as of the original date of this call, and we undertake no obligation to update or revise any of these statements.

Also, during this call, management will discuss certain non-GAAP financial measures, which management believes can be useful in evaluating the company's performance. The presentation of non-GAAP financial measures should not be considered in isolation or as a substitute for results prepared in accordance with GAAP. You will find additional information regarding these non-GAAP financial measures and a reconciliation of these non-GAAP financial measures to the most directly comparable GAAP measures in the company's earnings release.

A live broadcast of this call is also available on the Investor Relations section of the company's website at ir.olaplex.com. Additionally, during this call, management will refer to certain data points, estimates and forecasts that are based on industry publications or other publicly available information as well as our internal sources. The company has not independently verified the accuracy or completeness of the data contained in these industry publications and other publicly available information. Furthermore, this information involves assumptions and limitations, and you are cautioned not to give undue weight to these estimates.

With that, I will now turn the call over to Amanda.

Amanda Baldwin
Thank you, Patrick. Good morning, everyone, and thank you for joining us.

This morning, we reported third quarter net sales of $119.1 million, which declined 3.6% compared to a year ago. While this represented sequential improvement from Q2, we did underperform our expectations, primarily due to weaker-than-expected results in our international business as we continue in our efforts to build the right foundation for the future. Adjusted EBITDA was $44.6 million for an adjusted EBITDA margin of 37.5%.

Coupling our third quarter results with our updated learnings, we are revising our guidance for fiscal year 2024 and now expect net sales in the range of $405 million to $415 million and an adjusted EBITDA margin in the range of 29.9% to 30.6%. As we have shared on past earnings calls, we planned for 2024 as a year to begin our transformation, taking a long-term view and prioritizing the strategies and initiatives aimed at building a healthier business. While we now believe it will take longer than originally expected to achieve our goal, we are making great progress and taking the steps we believe are necessary for the long-term health of the business.

Much of this work has been happening behind the scenes, while at the same time this quarter, we announced three new innovative products: our No. 5 Leave-In Conditioner, Bond Shaper Curl Rebuilding Salon Treatment and No. 10 Bond Shaper Curl Defining Gel. Although we are disappointed with this revised outlook for the remainder of the year, I remain confident that we have the right strategy and are implementing the right actions to achieve a solid foundation for long-term growth.

Olaplex at its core is an innovative, science-enabled and pro-inspired beauty company with demonstrated global appeal. As a top brand in the prestige hair care category, Olaplex had four of the five best-selling prestige hair care products year-to-date 2024 per Circana's retail tracking data of the U.S. hair market. Our research indicates that the Olaplex brand remains strong with positive associations to build upon, including innovative, reparative, healthy and effective. And we possess a healthy balance sheet and strong cash generation, which provide flexibility and enable us to invest in future growth. Overall, I continue to believe that the best years lie ahead for this company.

Let me walk you through three key assumptions that drove the revision to our full year outlook. First, we anticipate weaker performance from our international business as we reset for the future. We conducted a market-by-market review to better understand our business, evaluate our current structure and partnerships and develop the go-forward road map for our global reach. I personally spent time meeting with many of our key partners and traveling the globe to see the brand in this current presentation on the ground and better understand the end consumer and unique markets.

From this assessment, while the enthusiasm and passion for this brand remain incredibly high, we now believe that the issues within our international business are more complex than we originally anticipated. This requires simplifying our international model with fewer distributor partners, as well as developing localized direct distribution approaches and brand support that are designed to be appropriate for the unique dynamics across the world. This work will take time, but we believe it will ultimately better position our business for long-term success.

We have referenced throughout the year that we are consistently executing an international distributor rationalization program. This effort has primarily impacted our international pro business, where we have closed certain accounts that we believe were the source of diverted product as well as our international DTC channel, where we have deprioritized certain international e-commerce customers that we believe do not build equity in our brand. As the year has progressed, we now believe it is appropriate to further realign our distributor network to fewer, stronger partners with clear accountabilities for market and brand development. While this activity will reduce net sales in the near term, we believe we're selecting the right partners who are excited with where we are taking the brand and will prioritize Olaplex, better support our transformation and be more integrated into our own internal processes.

Additionally, while we are redefining our international go-to-market strategy, we have felt it prudent to wait to align our new marketing efforts to coincide with deeper partnerships and our new brand vision in order to position ourselves to maximize the return on the investment. As such, we believe the slower investment in international sales and marketing in the near term has contributed to a moderation in demand.

Second, from a sales and marketing perspective, we now believe it will take longer to experience a lift in the overall demand from our brand investments. Earlier this year, we kicked off the beginning of our marketing evolution, building a stronger go-to-market engine, which includes elevated content creation and a creator-led approach, focused investments on launches and our core products, deeper coordination with our stylists and retail partners and more efficient ROI-driven media spend.

We recently started to deploy this new strategy in the U.S. We have observed positive early indicators that our new marketing activations are resonating with pros and consumers with improvements in brand engagement and momentum in earned media value metrics. In this region, we continue to observe sell-through trends at our key accounts that are largely consistent on an absolute dollar basis with what we have seen throughout the year, demonstrating continued progress towards stabilization. However, coming into the year, we did anticipate that these investments would begin to yield growth across the entire business, but we have not yet experienced the overall lift in demand that we were expecting.

We are encouraged by the sell-through trends of our new products launched during the third quarter, supporting our belief that powerful innovation, clear messaging and stronger execution can drive better results. We plan to apply these learnings next year across our entire portfolio. But as mentioned, we now believe it will take longer for this new strategy to yield improved top line performance across the assortment.

Third, the beauty market remains healthy, but also highly competitive. We previously believed that we would be able to pull back on promotional levels during the quarter, but now expect that the overall promotional environment will intensify during the holiday period and that we will need to participate effectively to win over the consumer. We continue to prioritize strategic promotions that maintain brand health and new customer acquisition, but we anticipate our promotional activity across geographies during Q4 will be higher than originally expected.

At this stage in our transformation, we continue to believe marketing investment is essential for the long term as we engage with our community and broaden the knowledge of our competitive strength, making a clear statement that Olaplex delivers results and stands apart from other brands. Therefore, we will continue to make such investments in the fourth quarter in an effort to maximize our performance during the important holiday season and build for the future.

I am proud of the progress we have made so far on our transformation journey as we continue to execute against our three key strategic initiatives for 2024. As a reminder, these include maximizing the impact of our sales, marketing and education investments to generate demand, strengthening our capabilities and culture to support our future and developing the long-term road map and future vision for Olaplex.

As it relates to our first initiative to maximizing the impact of our sales, marketing and education investments to drive demand. One of the most important priorities of our new sales and marketing strategy has been to return to our stylist roots and nurture our connection to the pro community. By showing up in salons and listening to stylists' feedback, elevating our presence at industry shows and investing in additional educational tools, we aim to increase our visibility, demonstrate our commitment and deepen our engagement with this key audience. As an industry leader, we also recognize the significant role we play in delivering innovation and new services that can help stylists make their business even more successful.

To that end, among our new launches launched during the third quarter, were two products for curly hair consumers, which were developed with the pro in mind. First, our Bond Shaper Curl Rebuilding Treatment, which is a three-step professional curl treatment to repair, redefine and lock in the shape of natural waves, curls and coils, created with new patented technology. And second, our No. 10 Bond Shaper Curl Defining Gel, which is an at-home reparative curl styling gel that revives natural curl pattern.

To support these launches, our education team in partnership with our pro ambassadors and members of the Olaplex Pro Collective influencer team educated at more than 50 national and regional trade events and hosted virtual training sessions to educate stylists and our distributor partners about our new technology. We are pleased with the early performance as early adopter salons across the globe are offering the Bond Shaper Curl Rebuilding Treatment to their clients and our No. 10 Bond Shaper Curl Defining gel ranked in the Top Three within Ulta Beauty's Curl subcategory.

Another important initiative for our marketing team during the third quarter was generating excitement and buzz of our consumer-focused new product launch, No. 5 Leave-In Conditioner. Supported by a holistic marketing plan with social media and experiential pop-up during New York Fashion Week and trade activations, powered with support from our influencers and pro ambassadors, the campaign generated strong response with more than 2 million social media impressions, people testing the product and touting its efficacy. Exceeding initial forecast, No. 5 Leave-In Conditioner became a Top Two SKU on olaplex.com and a Top Five SKU in Sephora's U.S. leave-in conditioner subcategory.

As I mentioned earlier, we believe these successful launches are signs of a stronger innovation engine and improved marketing strategy, delivering enhanced creative partnerships and improved content creation. On our last earnings call, we highlighted a new marketing campaign launched during the second quarter, featuring the transformative benefits of a complete routine of Olaplex No. 4 Bond Maintenance Shampoo and No. 5 Bond Maintenance Conditioner. The campaign drove positive lifts and brand favorability above our peer benchmarks, and Olaplex's brand engagement levels have risen year-to-date across our competitive set.

Also, we believe our strategic participation in our customers' tentpole marketing events indicate strong consumer interest in our brand. For example, our performance during a key customer's promotion in July was very successful, with nearly 70% of customers during that period identifying as new Olaplex users and five of our SKUs featured in the event were the #1 ranked items in their respective categories.

And lastly, according to data tracked by CreatorIQ, we regained our position as the #1 U.S. hair care brand in earned media value in the third quarter with momentum building throughout as we earned the #1 spot in both August and September.

Moving to our second priority to strengthen our capabilities and culture to support our future, we recently strengthened our leadership team with several highly talented appointments who we believe will position Olaplex for future success. Over the last several months, we've added a new Chief Operating Officer and Chief Financial Officer, Catherine Dunleavy, who is here with me today, as well as the Chief Marketing Officer and a Senior Vice President of International, both of whom will be important leaders of our go-to-market strategies across the globe.

With these new senior leaders in place, we are transforming how we work across the organization to strengthen our foundation. We have implemented and continue to deploy enhancements to new, integrated business planning approach that will give us a better global view of the business. Also, we launched a new strategic planning process, bringing leadership teams across the organization together more frequently, working in even greater detail to craft the strategic plans for the future.

As it relates to our marketing processes, we are streamlining and integrating how the entire marketing organization engages with our agency partners, developing a more disciplined approach that we believe will yield better planning and a higher quality creative content engine. We also expect this to strengthen each new product introduction as our new approach allows us to present marketing messages that are better aligned with how consumers interact with brands. We have more to do, but we're deep in this work.

Overall, we believe we are creating a corporate culture that is more collaborative and makes informed decisions based on data and business processes that can be applied across the globe. It's rewarding and exciting to see our teams come together to work towards achieving a common goal. Our business leaders and team members are energized, committed and working hard to move our business forward in a positive way.

Our third priority is developing the long-term road map and future vision for Olaplex. Supported by an in-depth brand perception study rooted in pro and consumer insights, we've developed a new and clear brand vision for Olaplex that will start to be visible to the pro and consumer in the coming year. At various stages of this work, we have been in active dialogue with our partners. The feedback from these conversations have been overwhelmingly positive, but there is strong support and excitement for this new phase of Olaplex.

We also completely redesigned our new product pipeline, development and go-to-market processes following the creation of our new innovation team to align with our new brand vision. We rolled out new commercialization strategies for our product launches with additional enhancements planned for the next year. Additionally, as we work to inflect to growth, we're continuing to finalize our strategic plan and expect to provide details in early 2025.

In conclusion, this is a truly transformational period for Olaplex that requires thinking and acting for the long term. I remain confident in the brand's strong foundation that we can build upon to return to sustainable growth, truly differentiated science that will deliver superior results, a powerful R&D platform, a passionate community of stylists and consumers who love our products and a unique global footprint and a talented team that is dedicated to position this brand for success.

With that, I will now pass it over to Catherine, who has been a tremendous partner already, and the company and myself are incredibly fortunate to have her with us on this journey. Catherine?

Catherine Dunleavy
Thank you, Amanda, and good morning, everyone. I am pleased to speak with you today on my first earnings call as the Chief Operating Officer and Chief Financial Officer of Olaplex. Since I've not met or spoken with many of you since I joined the company, I thought it would be helpful to provide you with a short summary of my background and what I've been focused on during the first 12 weeks of my time at Olaplex.

For the past two decades, I have held senior leadership roles at leading global consumer and media companies, including Away, Nike, Comcast, NBCUniversal and GE. During this time, I led and executed strategic operational and financial initiatives that helped drive profitable growth. The decision to join Olaplex was an easy one. As an everyday user, I am a loyal fan of Olaplex and have admired how the company disrupted the hair care category with its patented technology. I also thrive in fast-paced environments and see significant opportunity to take part in driving the strategy and elevating the company's financial foundation to provide the framework to maximize the power of our brand.

Olaplex is an innovative company and one of my strengths is managing core functions with discipline, execution and rigor while also leaving room for flexibility to enable creativity. Having been in the role for almost 90 days, I am very enthusiastic about the potential ahead. Olaplex possesses a strong community of people, partners, stylists and consumers, and I am proud to be in a position to help shape our future.

I recognize there are many opportunities to bring operational best practices to life at Olaplex, and I look forward to helping the company to continue to build out an infrastructure that will support future growth for this business.

Now, let me share more details about our third quarter results and our updated outlook. Net sales for the third quarter declined 3.6% year-over-year to $119.1 million. Although our Q3 net sales performance improved sequentially from the second quarter, this result was below our expectation with the underperformance largely driven by our international business. For the quarter, we continue to observe sell-through trends at our key accounts in the U.S. that are largely consistent with what have been seen throughout the year on an absolute dollar basis. Outside the U.S., sell-in was negatively impacted by our ongoing efforts to realign our business, as well as a moderation in demand trends due to slower investment in international sales and marketing, as Amanda discussed earlier. We continue to believe that the months on hand of core inventory positions at our major U.S. accounts remain in healthy position.

In regards to performance by channel, specialty retail sales were little changed, down 1.3% year-over-year to $42.6 million, with our performance reflective of increased competitive intensity on our core SKUs, partially offset by the addition of product launches. Professional channel net sales decreased 12.6% year-over-year to $42.2 million, driven by our international business, which decreased due to weaker demand and a focus on prioritizing international distributors and partners that build brand equity, which more than offset the slight growth in our North American professional business.

Direct-to-consumer sales were up 6.8% year-over-year compared to the third quarter of 2023 to $34.3 million due to strong sell-in ahead of a successful major customer promotion in July and growth from olaplex.com, which increased double digits year-over-year. This growth was partially offset by a decline in international DTC.

Moving on, adjusted gross profit margin was 70.8%, up 110 basis points from 69.7% in the third quarter of 2023. This expansion was primarily driven by favorability due to lapping higher levels of inventory obsolescence reserves from last year. This increase was partially offset by contraction primarily due to an unfavorable product mix driven by the sell-in of holiday kits, which are highly profitable, but lower margin relative to the rest of our assortment, as well as slight deleverage on warehouse and distribution costs.

Adjusted SG&A increased to $40.4 million compared to $33.7 million in the third quarter of 2023, driven primarily by an increase in sales and marketing expense. During the third quarter of 2024, we spent approximately $16 million in non-payroll-related advertising and marketing expenses compared to approximately the same amount in the second quarter of 2024, bringing the year-to-date total to approximately $43 million.

Adjusted EBITDA declined 13.4% to $44.6 million versus $51.5 million in the third quarter of 2023. Adjusted EBITDA margin was 37.5% compared to 41.7% a year ago. Adjusted net income decreased to $28.7 million or $0.04 per diluted share in the third quarter of 2024 from $33.4 million or $0.05 per diluted share in the third quarter of 2023.

Let me now turn to our balance sheet. Inventory at the end of the third quarter of 2024 was $85.9 million, a decrease of $14.3 million from $100.2 million at the end of the second quarter of 2024. The sequential decrease was primarily the result of the sell-in of our holiday kits and new products during the third quarter.

Moving to cash flow. During the first nine months of 2024, we generated $93.4 million of cash from operations. We anticipate that 2024 will be another year of healthy cash flow generation as we continue to drive an asset-light model and high profitability. We ended the third quarter with $538.8 million in cash and cash equivalents, an increase of $30.9 million from the end of the second quarter of 2024. This cash is generating interest income at an annual rate of about 5%. Long-term debt, net of current position of deferred fees was $645 million.

Now, turning to our financial outlook. As disclosed in the press release issued this morning, we are revising our guidance for fiscal year 2024. Starting with the top line, for fiscal year 2024, we now expect net sales in the range of $405 million to $415 million, down from the previous range of $435 million to $463 million.

As Amanda mentioned earlier in the call, the revision can be broken down into three primary buckets. First, we anticipate weaker performance from our international business. As Amanda discussed earlier, we have performed a deeper assessment of our international operations and discovered that the issues are more complex than we originally thought. We are now redefining our international go-to-market strategy.

Second, while we believe we continue to observe sell-through trends in our U.S. key accounts that are largely consistent on an absolute dollar basis with what we have seen throughout the year and our key accounts remain in healthy core inventory positions, we are not yet experiencing the anticipated lift in demand from the deployment of new sales and marketing investments.

And third, we anticipate increased promotional activity during the holiday period across geographies relative to our previous assumptions.

In the fourth quarter, from the perspective of year-over-year net sales growth rates in order of magnitude, we expect our professional channel to be the most pressured followed by our direct-to-consumer and specialty retail. We now anticipate adjusted gross margin in the range of 70.9% to 71.6% compared to our initial assumption in the range of 72.5% to 73.1%. We expect that the primary driver of this decrease will be additional promotional activity during the fourth quarter and greater deleverage from lower sales volumes on our fixed warehousing costs.

Furthermore, we now expect full year 2024 adjusted SG&A expenses in the range of $167 million to $170 million compared to our previous expectation of $172 million to $179 million. Specifically, we expect full year non-payroll-related advertising and marketing expenses in the range of $62 million to $65 million compared to our previous assumption of $66 million to $70 million as we continue to invest through our transformation.

Given the lower net sales forecast against our expectations for continued investment in operating expenses, we now expect more adjusted EBITDA deleverage than our prior assumption. For 2024, we expect adjusted EBITDA in the range of $121 million to $127 million or a margin of 29.9% to 30.6%. This compares to our previous range of $143 million to $159 million or a margin of 32.8% to 34.3%. We expect net interest expense to be $34 million, and an adjusted effective tax rate of approximately 19.5% for the year.

In conclusion, Olaplex has significant competitive strengths that we believe we can build upon to deliver consistent and sustained rates of growth. We believe that we have identified key issues that have contributed to recent challenges as well as the appropriate actions to correct them. Fundamentally, we are working to build a better Olaplex, strengthening operating discipline, improving our business and financial processes and maintaining strong cash generation. I look forward to sharing our progress along the way.

I will now pass it over to Amanda for some closing remarks.

Amanda Baldwin
Thank you, Catherine. Olaplex remains an incredibly powerful brand, a leader in the attractive high-growth prestige hair care category and an important strategic partner for our customers who are supportive of and excited about the direction we are taking the business. The trajectory of our transformation may have shifted, we are progressing and making the tough decisions that we believe are necessary to create a healthy business set up for long-term success. Ultimately, we believe we are still in the early stages of the history of this company and that Olaplex can perform at a higher level. I remain optimistic as ever about the future.

This concludes our prepared remarks. We will now turn the call back over to the operator for questions. Operator?

Operator
Thank you. We will now conduct a question-and-answer session. If you would like to ask a question, please press Star 1 on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press Star 2 if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the Star key. Once again, that's Star 1 at this time. One moment while we poll for our first question.

Our first question comes from Jungwon Kim with TD Cowen. Please proceed.

Jungwon Kim

Thank you for taking my question. Just curious on the overall consumer health, what you're seeing at the salon and as well as your DTC and on the retail side overall? You've mentioned higher promotions. Do you think it's more because the consumers are cautious? I would love any color there. And I would love to dig a little bit deeper into what you saw in terms of your international business. What are your, you know, key assessment there? And how you're thinking about the opportunity going forward and what it could be as a percentage of the mix over time? Thank you so much.

Amanda Baldwin
Thank you for the question, and thank you, everyone, for being here today. You know, first, I'll take the first half of that, which is with respect to kind of what we're seeing around the consumer, and I believe you're asking about both within the salon channel as well as, you know, retail and the consumer more broadly. You know, within the salon channel, I think we've been talking about, you know, earlier on throughout the year about overall trends within the salon category where there certainly over time has been less frequent visits into the salon. That hasn't changed in either direction in particular. I think it is sort of the way that people are thinking about their salon. And certainly, part of our focus and our strategy in supporting the stylist and rooted behind the launch of something like Bond Shaper Curl Rebonding Treatment is really supporting the stylists and making sure there's more reasons to come back to the salon. So, we're excited to really support our stylists in that way.

With respect to the consumer overall, yes, we did make a very conscious decision as we were thinking about going into this quarter and watching what we're seeing out in the marketplace and expecting overall a more promotional environment, making sure we're doing that, both, you know, some typical promotions, which we do use from a strategic point of view around key tentpole moments, but also in trade marketing and overall support for our retailer partners, both on the pro side as well as to the consumer. So, that is something that we're watching carefully. And I think, you know, we'll see a lot of the things that many others have been talking about as we go into this key holiday season.

With respect to international, I have spent a lot of time very recently on this topic. The first thing I would say is that the enthusiasm for this brand is incredibly strong. One of the things and one of the reasons why I joined this brand nearly a year ago was because I think it's very rare to find brands that have such global resonance. And that I have now seen on the ground, having been with consumers, having been with our retailer partners, distributor partners, sitting in salons around the world, this product really resonates and really translates.

I think what we've really learned and what we were talking about today was that in order to ensure that we really maximize that opportunity, we need to be much closer. We can't have arms relationships. We need to be much more involved with our distributor partners. We need to be better with translating our marketing efforts, all the things that we've started working on here in the United States that we are seeing early signs of opportunity around our marketing efforts. We need to be translating those internationally. And so, in order to do that, that does require making sure that we have fewer, bigger partnerships that we are -- you know, that was part of the rationale of bringing on someone to lead that part of our business, so that we're just better partners, and we can support this brand globally.

Jungwon Kim
Thank you.

Operator
The next question comes from Ashley Helgans with Jefferies. Please proceed.

Ashley Helgans
Hi, thanks so much for taking our question. So, I know you kind of talked about not yet seeing the marketing efforts provide any sort of lift. Just any more color on when you expect to start to see a lift? And any changes you think you need to make to the strategy? Thanks so much.

Amanda Baldwin
Yes. Thanks for the question. I want to make sure that we really pull apart what we are seeing within our new launches and what we want to see across the entire portfolio and to draw a distinction between those two. So, if we recall, you know, in marketing and sales education, you know, I really believe that brand is the thing that will -- you know, along with innovation, will drive this business going forward. We've spent a lot of time, as we talked about, getting the brand, you know, vision right, getting the future product pipeline right. And what we had this fall was the opportunity to have two new launches and to start the process of really building a marketing muscle in this organization.

We've seen a lot of really good things happen out of that. One of the things that we highlighted in the call was our No. 5 Leave-In Conditioner. I think that's really the first time that this brand has had, what I'll call, a full 360 approach, a tight partnership with Sephora, the ability to launch an exclusive SKU with them to really put the right experiential marketing, the right influencer marketing, the right kind of assets, the right kind of language. I mean we've been talking about this really since the beginning about, it's not just the money we spend, but it's how we spend it. And that launch is outperforming our expectations. So, that's really exciting to see.

What we need to see going forward and the thing that is sort of driving our guidance today is we need to make sure that we have that across the entire portfolio. And that's really going to be Phase Two of this. And as we think about going forward and how, you know, we have a brand new CMO, Katie Gohman, who joined us in July, and she's fantastic and I think really helping us take this to the next level. So, these things are a work in progress, but I do feel like we're on the right track that we have, you know, again, a brand vision that I alluded to, and I look forward to sharing more about that, as that becomes, you know, out in the world, and we have a great product pipeline. And so, we're going to get better and better at this.

Ashley Helgans

Thanks so much.

Operator
The next question comes from Susan Anderson with Canaccord. Please proceed.

Alec Legg
Hi, good morning. Alec Legg on for Susan. On the fourth quarter sales really does take a big step down with the updated guide. How much of that is from the international realignment and expectations for how the U.S. will perform? Thank you.

Catherine Dunleavy
Hi. Thanks for the question. Yes, international is the primary driver of what is driving our fourth quarter guidance down. While all three are very important, it really is mainly the international and the impacts of other two on international.

Alec Legg
Thanks. And then just a follow-up. I guess, with international being reset and realigned, what is the expectation for sales to start stabilizing? How long do you think it will take to kind of recreate the brand that you're trying to work in -- with the distributors over in Europe? Thank you.

Catherine Dunleavy
Well, we're still working through our plans for 2025 and beyond, and we're not really providing guidance today. But I can tell you a couple of things. One, as Amanda and I mentioned earlier, in our home market, on a week in and week out basis, our selling -- are relatively consistent. So, we started in the U.S. and put in place our actions, and that is starting to work. So, then we just have to take that playbook and put it in international. And as Amanda described, she spent a lot of time market by market, creating a very detailed strategic plan for how we're going to go to market. So, this is a transformation. It will take some time, but we're confident we've identified the right actions to drive future success. And I'll just add that we are very fortunate to have a strong balance sheet and healthy cash flow that allows us to make the tough decisions and continue to invest for long-term future profitability.

Operator
The next question comes from Korinne Wolfmeyer with Piper Sandler. Please proceed.

Korinne Wolfmeyer
Hey, good morning. Thanks for taking the question. I'd like to touch a little bit on the cost structure and how we should be thinking about that for Q4 and heading into 2025. I believe the SG&A guidance implies still a meaningful step-up in Q4, even though you're pulling back on some of the marketing and ad spend. So, can you touch on, you know, what's driving that number? And then as we head into 2025, how should we be thinking about your marketing and advertising budget relative to the rest of the SG&A expense? Thanks.

Amanda Baldwin
So, thanks for the question. I think that, you know, as Catherine alluded to, we think it's important to continue to invest behind this brand in the fourth quarter. And so, you know, we'll continue to make sure that we're building for the future. We aren't providing guidance for 2025 at this time, but, you know, we certainly are learning a lot as we, you know, as I talked about before. We're learning a lot from our marketing efforts that will help drive our planning for next year. We're spending a lot of time on this international business, so we really understand what it's going to take to set that up for success as well as really, you know, spending a lot of time on the road now with the future brand vision and really working with our partners to plan for next year.

Operator
The next question comes from Andrea Teixeira with J.P. Morgan. Please proceed.

Shovana Chowdhury
This is Shovana Chowdhury on for Andrea. Can you give us a little bit more insight on the international competitive landscape and your confidence level in bringing about fruitful results by realigning distribution network and updating the marketing strategy outside the U.S.? And additionally, if I can tack another one, understand that the guidance was lower mainly due to the international space. But in quarter 3, the U.S. market top line also declined by 3.3%. So, if you could just tell us a little bit more like what is causing -- understand that it has to do with not seeing the lift in demand, but your new launches were doing pretty well as per the commentary. Thank you.

Amanda Baldwin
So, yes. I can take that -- that first one as we think about the international competitive landscape. I think what you see is similar to a lot of different brands and different categories in beauty. You'll see some global players who will be very similar across the globe. And then you obviously see some more local players. And that's, you know, when I was speaking earlier about kind of really getting on the ground, understanding the dynamics, understanding the different channels, being in salons, being in the stores, watching what's happening online, really understanding what the consumer is seeing and what they're -- as well as the stylists and what they're looking for in their respective markets.

What I would say is it's more similar than it is different. There are certainly, like anything else, some global nuances to this to be mindful of. And we do have a business that has incredible reach. And I think, again, I think there's a lot of appeal for this brand and the fundamental nature of hair health, of hair repair is something that is very consistent. But how you might approach the market. And that's actually a big advantage to having a distributor network, is that they are on the ground, that they do really understand the nuances of their individual markets.

So, we -- again, this is about a closer partnership about having much more involvement in how we're going to market in these places and making sure that we're kind of taking advantage of both of our sets of expertise, ours of our own brand and what it can do, that we're translating our marketing, our sales and our education across the globe and that we're leveraging those partnerships to be closer to the consumer, to be closer to the stylists and really have, you know, our hands -- you know, arms, legs, ears, eyes on the ground for us. So, that's really how we're thinking about that part of the business.

Catherine Dunleavy
And then I'll try to address your Q3 question. In Q3, our professional sales were down 12.6% and our retail sales were, you know, only down about 1.3% and our DTC was up. And then I think your question was specifically in the retail channel, what were we seeing there? And, you know, it was down 1.3%. We did see some timing with some of our major customers with the sell-in of holiday kits. And so, that might be some of the variance that you're seeing.

Shovana Chowdhury
Thank you for the color. I'll pass it on.

Operator
The next question comes from Lauren Lieberman with Barclays. Please proceed.

Lauren Lieberman
Hi, thanks. Good morning. Amanda, I missed the beginning of the call, so apologies if you've kind of directly answered this already. But, you know, I know you talked about it's taking longer to see the lift on new product launches and the new campaigns, but also spoke about the success of the Leave-In Conditioner. So, I just wanted to see if you could talk a little bit about almost like a postmortem on the -- what's not worked so far and why, you know, as contrasted to what has gone well with that Leave-In Conditioner product? And I know you talked about the 360 on the Leave-In, so maybe it's more about the what wasn't working on the earlier pieces? Thanks.

Amanda Baldwin
Yes. I mean, I think the places were -- and as you can imagine, we certainly have done a lot of our own internal reflections. And we have, like I said, a brand-new CMO who joins us with an extraordinary background. She's really dug in on this with her team, and it is something that we really think is very important as we go forward to make sure we understand what works and what doesn't and kind of continue to improve over time. That's certainly something I believe strongly in. Again, I think what we really are seeing is that the brand resonates, right? I think that's a very important thing to talk about that as we improve our marketing muscle, that the pro responds, that the client response, right, like that was really what we needed to understand this year, so that we have that information as we go into, you know, a future brand vision as we bring on this team as we build the muscle.

I think we feel, again, that there's some very important signs of success. One of the things that, you know, we talked about very early on when I joined was this concept of creator-led marketing. The concept -- and that is something that is, you know, certainly at the helm of a lot of how beauty industry operates and it is something that we really believe that we can do very successfully. It was also the first time with the Leave-In Conditioner that we had an experiential event, so a physical pop-up that we did for Fashion Week here in New York. And certainly, I had the fun of getting to go to that and, you know, lines around the block. But I think that what was so interesting and exciting about that was that people really -- again, they wanted to see the brand, they wanted to experience the brand, but they were also really curious about our science.

And that is something that we're seeing across the board is that people really do see the power of this product. They are interested in how it works. They're interested in how to use it. They want to know about that, and we are getting better and better at explaining that. I think that was also something that I called out very early on is that we have this unbelievable technical foundation. We need to get much better at explaining it and explaining it, whether it's to a stylist, to a consumer and social media and influencers, leveraging the power of that technology and translating it into language that really makes sense for the broader universe is something that I think, you know, I look at it as a really exciting proof point for what we're seeing today. But, you know, I'll always be of the mindset we can do better. We can -- and that's certainly something that Catie and I share, and we'll continue to evolve our processes and the marketing that we put up.

Lauren Lieberman
All right. Great. Thank you so much.

Operator
The next question comes from Olivia Tong with Raymond James. Please proceed.

Olivia Tong Cheang
Great, thanks. With respect to international, do you have a sense on how much has to come out of it and how long it will take? And what the business looks like after you have rightsized it? And more importantly, why do you think now is the right time to make the international changes you're planning? Obviously, you've got quite a bit on your to-do list already. So, where is the incremental manpower coming from to drive more of a cleanup in international markets right now? Thanks.

Amanda Baldwin
I think, yes, we have the good fortune of being able to make the hard choices, right, and to make sure that we're building for the future. And so, you know, I really believe -- and we've talked about that the power of marketing, sales, education and innovation, those are the things that are going to drive this business forward. We believe that we need to realign that international business in order to take advantage of that. So, I do think it's important. Like I

said, however, there is a lot of enthusiasm for this brand, so we're going to do this in the right way. So, at this point, I'm not going to be able to give a timeline. But, you know, we'll do the same thing that we've done with everything else in this business is that we're going to operate with a sense of urgency that's important in a transformation, but we're also going to take the time to make sure we do the right analysis that we pick the right partners, that we do this in the right way. And those will obviously be in balance, and we'll certainly keep people posted as we work through this.

Olivia Tong Cheang
Got it. Thank you.

Operator
Thank you. The last question will be from Rob Ottenstein with Evercore. Please proceed.

Robert Ottenstein
Hi, thank you. You kind of touched on this a couple of times, but I just maybe want to give it another shot and drill down a little bit. You know, I think all of us, you know, who have been involved were incredibly impressed with the product, the technology, the efficacy, right? And then something happened and there were social media issues. And I think you're largely behind that. Correct me if I'm wrong. But I think what may have also happened is, you know, increased competition that may have confused the consumer, you know, with various different kind of bonding products or trying to, you know, play off your claims, but in different ways. And so, I guess the question is, is, you know, is consumer confusion part of the problem? And then to the extent that is, and I know you talked about better communication, but can you be maybe even more specific about how to deal with that confusion and how you can actually get across, you know, that you're unique in terms of the science and the efficacy? And again, I know you touched on it, but it's so important. I was just wondering if you can kind of address it a little bit more? Thank you.

Amanda Baldwin
Yes, absolutely. And I think it's a great question. I think when, you know, what I was saying before a little bit about the importance of our ability to explain our science, that is the crux of it, right? How do you take something that is truly world-class patented technology, it's complicated stuff, right? And how do you take that and how do you translate that to the consumer? This is the place that we're really focused. And again, I think we're seeing some early signs of success. We've made some very material changes in how we're approaching social media, how we're creating content.

You know, certainly, if you were to go on our Instagram page and you looked at it 12 months ago and you look at it now, it's going to look different. That, I think, is a good indicator of how we're approaching science in a different way and how are we thinking how we communicate because I think you are right that we need to make sure that people are clear on what sets us apart. Just because we know that we are, doesn't mean that the consumer knows that and that the stylist knows that. And those are related, but not 100% the same thing, right? There's overlap in how they consume information, but there's also unique channels about it. So, that's something that we're thinking a lot about as we continue to build our marketing muscle.

And then I think it's also the importance of innovation and the importance of introducing new SKUs that allow us to continue to push the boundaries of innovation. And I would say that I really believe that this brand is certainly harnessing the power of bond building technology, but this is way more than a bond brand. This is a prestige hair care brand. I really believe that, that's the category that we compete in, that it's very important to establish the brand in that way and to communicate that way because that will, I really believe, increase our ability to really be a part of people's daily hair care routines.

Robert Ottenstein
Thank you.

Operator
Thank you. At this time, I would like to turn the floor back to Amanda Baldwin for closing remarks.

Amanda Baldwin
Well, you know, I'll just say thank you for everyone who joined this morning, and please do reach out with any further questions.

Operator
Thank you. This does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a great day.