Delta Apparel, Inc.

Fiscal Year 2018 Fourth Quarter and Year-End Results Earnings Conference Call

Operator:

Thank you, and good afternoon to everyone participating in Delta Apparel's Fiscal 2018 Fourth Quarter and Full Year Earnings Conference Call. Joining us from Management are Bob Humphreys, Chairman and Chief Executive Officer, and Deb Merrill, Chief Financial Officer and President, Delta Group.

Before we begin, I would like to remind everyone that during the course of this conference call, projections or forward-looking statements may be made by Delta Apparel's Executives. Such projections and statements suggest prediction and involve risks and uncertainty, and actual results may differ materially. Please refer to the periodic reports filed with the Securities and Exchange Commission, including the Company's most recent Form 10-K. This document identifies important factors that could cause actual results to differ materially from those contained in the projections or forward-looking statements.

Please note that any forward-looking statements are made only as of today and, except as required by law, the Company does not commit to update or revise any forward-looking statements, even if it becomes apparent that any projected results will not be realized.

I'll now turn the call over to Delta's Chairman and Chief Executive Officer, Bob Humphreys.

Robert Humphreys:

Good afternoon, and thank you for joining us on our fourth quarter and fiscal year 2018 earnings call. In a moment, I will briefly discuss our business results along with a few key highlights that showcase why we believe Delta Apparel is well positioned for profitable future growth. I will then turn the call over to our CFO, Deb Merrill, for a more detailed discussion of our financial results.

Before I dive into our results, I want to update you on a change in our business reporting. We recently made a strategic decision to realign our businesses into segments that better reflect our current operating model and allow us to further leverage our core expertise and more efficiently manage our cost structure as we plan growth across our business over the foreseeable future.

We are now defining our segments as the Delta Group and the Salt Life Group. The Delta Group comprises our DTG2Go digital print business, our Delta Activewear business, which includes our catalog and our private label FunTees divisions, along with our vertical manufacturing platform, and now includes our Soffe brand. As you can see from the financial information we provided in our press release, at $356 million in sales, the Delta Group represents approximately 90% of fiscal 2018 sales. The remaining 10% of our fiscal 2018, sales or approximately $40 million, was derived from our second reporting segment, the Salt Life Group, which now comprises our Salt Life and Coast lifestyle brands.

Now let me turn to our results. We were pleased with our solid finish to the year, most notably with nearly 60% year-over-year earnings per share growth, bringing earnings to $0.43 per diluted share from $0.27 per diluted share in the prior year fourth quarter. We delivered fourth quarter sales growth of roughly 2% despite having two of our major distribution centers closed for eight days due to hurricane Florence. We estimate that the shutdown of our DCs resulted in approximately $3 million of missed sales.

The topline growth for the quarter was driven from our Delta Group, which grew almost 4% and was partially offset by sales in our Salt Life Group segment. The impact on Salt Life from this year's hurricanes was much more significant in the quarter than it was last year, simply due to the fact that this year's hurricane impacted the distribution center. Not only were sales to independent retailers impacted, but we were also not able to ship major retailers orders on our e-commerce site right at the end of the quarter. We believe that our Salt Life branded sales volume would have had nearly 10% growth during the quarter had we not been impacted by the hurricane.

Our Delta Group performance for the quarter was led by our digital print and fulfillment business DTG2Go, which registered net sales growth of more than 120%. As a reminder, we acquired the DTG2Go business in March of this year, and we recently announced the acquisition of another digital print business, SSI Digital Print Services. These acquisitions solidify DTG2Go as the industry leader in digital print and fulfillment capabilities, and set the stage for meaningful expansion in this high growth space over the next several years.

We are very excited about the prospects for our digital print and fulfillment platform as a growth driver across our business for years to come. DTG2Go is the only digital print supplier in the world, offering customers a seamless fulfillment solution integrated with a vertical manufacturing platform by Delta’s Activewear offering of a reliable low cost supply of fashion and core basic garments, including fleece and shorts.

After its recent acquisition activity, DTG2Go now has a network of six digital print and fulfillment facilities and has the capacity to print over 70,000 unique prints per day and can deliver superior speed to market capabilities, reaching over 90% of the U.S. population with one to two-day shipping. DTG2Go has cutting edge technology and service offerings that are the forefront of revolutionizing the changing retail platform with virtual inventory, digital print and fulfillment capabilities.

Our DTG2Go business grew significantly in fiscal 2018, ending the year with sales of approximately $27 million. We see the DTG2Go business nearly quadrupling over the next four years, reaching approximately $100 million in sales and generating double-digit operating margins. Fourth quarter performance in our remaining Delta Group business was generally solid with some softness in our Soffe military business due to the usual program fluctuations in that channel.

The Soffe distribution center was also forced to close for eight days due to hurricane Florence delaying shipments of well over $1 million. Results at Delta Activewear were generally in line with the prior year quarter. For the full fiscal year, our Delta Activewear business saw sales growth in the high single digits with solid growth at both our Catalog and FunTees divisions. As a reminder, our Delta Catalog business serves its customers across the full market spectrum, including regional screen printers and customers in the promotional products and retail licensing channels.

The products offered in our Catalog business range from four basic tees to more fashion and performance tees, fleece and other garments. The vast majority of these garments are made in our own manufacturing facilities. Importantly, we are seeing growth generally across all sales channels in our Catalog business, as well as double-digit growth in our B2B e-commerce site. Our fashion basics line, including our Delta platinum line, which was introduced only two years ago, continues to exceed our expectations and sets the stage for deeper sales penetration with our existing customers, while also attracting new customers to the Delta Activewear family. Sales of our fashion basics products grew approximately 70% year-over-year and we expect to see that growth trend continue, as these products become a larger part of our overall sales mix.

We continue to focus heavily on the development of new fashion products and have moved away many of these products previously sourced from third parties onto our internal manufacturing platform to take advantage of shorter lead times and to better service our customers with faster replenishment. We achieved 10% sales growth in our Catalog business in fiscal 2018 and believe this business is well positioned for continued growth in fiscal 2019.

Our FunTees business, which as a reminder provides private label products to many recognizable global, national and regional brands, achieved record sales in fiscal 2018. We have been diversifying our customer base and increasing sales in newer channels, such as direct to retail. We continue to see favorable market dynamics in our private label business fueled by continued shift by brands towards Western hemisphere supply chain solutions, like those offered by FunTees to improve speed to market and customer service levels. We look forward to leveraging this momentum in our stronger more flexible business model in fiscal '19 and beyond.

Moving to our Salt Life business, which as I mentioned, was negatively impacted by the hurricane season during our fourth quarter, which dampened topline results. Despite the fourth quarter performance, we remain encouraged by the overall trends we're seeing in this business and in the expansion of the Salt Life brand. Sales in our Salt Life business grew approximately 2% year-over-year, and we are pleased to report that sales on our Salt Life.com e-commerce site delivered another record year of double-digit growth. We continue to see increases in e-commerce shopper conversion, as well as growth in our average order size, key indicators that the brand remains on a positive growth trajectory with both existing and new customers.

On the wholesale side, Salt Life continues to broaden its brand reach through key national retailer partnerships that are growing both within and outside of the brands' traditional strong regional market. Salt Life is also growing with new regional and independent accounts outside of its traditional market strongholds, and the enthusiastic response to the brand in international market has led additional go-to-market strategies and target foreign markets. We are pleased to see that we are starting-off the year with a healthy spring wholesale order backlog that is significantly higher than last year.

Salt Life also recently expanded its own branded retail footprint with a new store in Tampa Florida. We now operate six brick-and-mortar locations, including three in Florida, two in California and one in Georgia. Sales in this direct-to-consumer channel are growing nicely and we are targeting 12 additional store openings over the next three years with a focus on expansion within existing geographic regions.

Another key strategic growth pillar for our Salt Life brand is product extensions. As we highlighted on our third quarter call, Salt Life has expanded this offering into higher ticket performance and woven products and recently introduced a ladies' swimwear line through a license agreement with SWIM USA. Sales of Salt Life performance products continue to grow nicely with strong double-digit growth year-over-year, and we expect that positive market response to the new ladies' swim line to continue that these products become available in key national locations this spring.

Salt Life is also off to a good start with its recently expanded selection of bags within its accessories line and we're seeing some good traction with Salt Life sunglasses, which was previously sold to a licensee and is now marketed and sold on our in-house platform. Finally, on the product extension side, sales of Salt Life Lager, the brands' new craft beer continue to grow and its distribution continues to grow. This expansion adds additional visibility to the brand as it expands throughout Florida. We are accelerating our plans to expand Salt Life Lager's distribution into key Southeastern markets outside of Florida due to the positive market response we have seen to-date.

Fiscal year 2018 was another great year for our e-commerce site and we continue to invest heavily in this area. Sales on our B2B sites were collectively up over 20% for the year and sales on our B2C site were selectively up double-digits as well. To summarize, fiscal 2018 was a solid financial year for Delta Apparel. We delivered topline and bottom line growth, and we enter the new fiscal year well positioned to compete and grow in the current retail landscape.

I'll now turn the discussion over to Deb to review our financial results in more detail.

Deborah Merrill:

Thank you, Bob. As Bob mentioned we ended fiscal 2018 with solid overall performance, delivering moderate topline growth coupled with strong bottom line results. During the year, we made significant progress in a variety of areas and put ourselves in a position for future growth in both our more mature Delta Activewear business and our fast rising DTG2Go digital print business.

We also made significant strides in growing consumer awareness for our Salt Life group Brands and set the stage for more expansion there. In line with our new segment reporting channels that Bob shared with you, I'll now provide details on our fourth quarter performance followed by a review of our full year results.

For the fourth quarter, net sales were $92.9 million, up 2% from $91.3 million in the fourth quarter of fiscal 2017. This growth was driven by a 4% increase in sales from our Delta Group, which was led by significant growth in our DTG2Go business, as well as a slight increase in our Activewear business. These results were slightly offset by a $1.4 million sales decline in our Salt Life Group as it navigated the impact with two major hurricanes in key markets to close the quarter.

As Bob mentioned, our distribution centers in Fayetteville, North Carolina that service Salt Life and Soffe, as well as one of our DTG2Go digital print facilities, had to be closed for eight days and resulted in estimated lost revenue of approximately $3 million. Gross profit for the fourth quarter was up 15% to $19.2 million and gross margins improved 240 basis points to 20.6% compared to 18.2% in the prior year period. These results were driven by our Delta group, which was able to counter inflationary cost increases, primarily affecting the Activewear business.

SG&A expenses increased $2.4 million to $17.3 million compared to $14.9 million in the fourth quarter of fiscal 2017. The prior year fourth quarter included a benefit from the earlier than anticipated exit from certain lease liabilities in California. SG&A in the current year fourth quarter was also higher as we made investments in the expansion of our distribution facilities during the year to better service our growing product line.

Operating income was $3.5 million, up 50% from $2.3 million in the prior year fourth quarter, driven primarily by solid operating performance in our Delta Group. Net income was $3.1 million, an increase of $1 million from the $2.1 million in the prior year fourth quarter. Diluted earnings per share increased 59% to $0.43 compared to $0.27 last year, driven primarily from the strong performance in the Delta Group that I just reviewed with you and a lower tax rate, partially offset by higher interest expense.

Now turning to our full-year results, net sales increased 3% to $395.5 million for the year. Excluding the $15.6 million in sales in fiscal 2017 from the Junkfood Clothing business that we sold in March of 2017, which were in what we now refer to as our Salt Life Group segment, net sales increased 7% year-over-year. Underlying this overall performance was strong growth in our Delta Group with sales up 9% year-over-year.

Salt Life group net sales were $39.4 million compared to $58.5 million in the prior year with the declines due to the since divested Junkfood business and other strategic shifts in non-core business. Sales in our Salt Life brand were up 2.4% for the year, driven from the recent wins with national retailers and our direct-to-consumer business, partially offset by softness with independent retailers, which were hurt by the hurricanes a year ago and again this year.

Gross profit was $82 million, up 2% from $80.7 million in fiscal 2017. Gross margins improved in both the Delta Group and Salt Life Group, but declined 30 basis points overall from the stronger mix of Delta Group sales. SG&A expenses for the year declined $400,000 to $67 million compared to $67.4 million in fiscal 2017. SG&A as a percentage of sales leveraged favorably by 60 basis points to 16.9% compared to 17.5% in the prior year. Operating income was $17.5 million, up 8% from $16.2 million in fiscal 2017, primarily on the strength of a 12% year-over-year increase in the Delta Group segment. Salt Life Group operating income was generally flat year-over-year.

Net income was $1.3 million, compared to $10.5 million in fiscal 2017. Included in these results is tax expense of $10.7 million in fiscal 2018 related to the recent U.S. tax reform legislation and in 2017, there was a one-time pretax benefit of $1.3 million from the sale of our Junkfood business. Excluding both of those items, adjusted diluted earnings per share for fiscal 2018 was $1.62 compared to $1.22 in the prior year, a 33% improvement in per-share earnings.

Turning now to the balance sheet, cap ex, our total spending for the year was $13.3 million and in line with our prior guidance as we continue to invest in digital print and other machinery and equipment, as well as our direct-to-consumer initiative.

With regards to depreciation and amortization, including non-cash comp, we incurred approximately $12.6 million for the year. As a reminder, we paid $16.4 million for the Digital Print acquisition during fiscal 2018, of which $5 million was financed under our capital lease and the remainder financed through our U.S.-based revolving credit facility.

Regarding our share repurchase activity, during the fourth quarter, we repurchased 181,000 shares of our common stock at an average price of $18.42 per share for a total cost of approximately $3.3 million, bringing our year-to-date purchases to approximately 464,000 shares at an average price of $19.40 and a total cost of about $9 million. As of our fiscal year-end, we had approximately $12.3 million remaining approved for share purchases under our program.

Finally, we improved our operating cash flow by nearly $7 million to $20.9 million in fiscal 2018. Total inventory at the end of the fiscal year remained relatively flat with the year ago at $175 million with lower units on hand, partially being offset by higher per unit cost inventory, resulting from the inflationary cost increases. Total debt, including capital lease financing at the end of fiscal 2018 was $111.8 million compared to $96.2 million at the end of the prior year.

Looking ahead to fiscal 2019, we're excited to be in a position to capitalize on the opportunities that lay ahead due to the hard work of our team and the investments we made this year. Now here is Bob again for his final comments.

Robert Humphreys:

Thanks, Deb. We are pleased with the progress we made this fiscal year. We strengthened our leadership position in the digital print and fulfillment business, and we continue to develop exciting new products and gain new customers and markets share in our Activewear business. We also took a variety of important steps to increase the awareness of our Salt Life lifestyle brand, and believe we had it well positioned for strong growth in fiscal 2019.

We are already off to a fast start in our new fiscal year with the completion of the acquisition of SSI, which positions us as a leader in the digital print and fulfillment markets as we look to quadruple our DTG2Go business over the next several years. Our Salt Life business is also off to a solid start with a strong spring order book, which we'll begin shipping in January. We also have product extensions with higher price points that should help build on the brands' offerings for the upcoming year.

The expansion of Salt Life Lager distribution and the addition of lady swimwear should also bring additional consumers to the brand. In a few weeks, a new Salt Life restaurant overlooking the ocean in Fernandina Beach, Florida will be open, our restaurant licensee. These milestones, combined with additional expansion plans for the year, position us well for continued success in fiscal 2019 and beyond.

One other topic I'd like to address from a Delta Apparel standpoint is the increased tariffs on products out of China. We currently manufacture the vast majority of the products we sell from our locations in Central America, Mexico and the United States. We also manufacture a significant amount of apparel for other major brands from these same facilities. You've heard me say for many years now that we see more production move into this hemisphere to service consumers in this region. This has been a long-term trend that should help drive continued production growth in our manufacturing facilities.

We currently source small amounts of performance products and accessories from China for our various brands, which can be affected by increased tariffs. While not material to our overall results, we are currently taking steps to find alternative supply chains for these products. Before I close, I would like to add my thanks to all of our teams for their hard work and dedication to Delta Apparel this past year.

We look forward to another year of solid progress and now Deb and I'll be glad open up the call for any questions. Stephanie, you can open up the lines for questions now.

Operator:

Thank you. If you would like to ask a question, please signal by pressing star, one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star, one to ask a question. We'll pause for just a moment to allow everyone an opportunity to signal for questions.

We’ll move on to Dave King with ROTH Capital Partners. Please go ahead.

Male Speaker:

Hi, there. This is Andrew on for Dave. I guess first to start, if you could talk about the SSI acquisition a little bit more, and maybe get into how that complements DTG2Go. What capabilities did they add and then what made you excited about to acquire it? Should we be expecting any further acquisitions in the digital print space as you look to further grow that business? Thanks.

Robert Humphreys:

That was a business that we were certainly aware of, and it was of substantial size, similar to what we had in Art Gun and DTG2Go before we acquired that business. It was another meaningful player out there. It had manufacturing and fulfillment facilities in geographic locations that were places that we had planned to move to. It eliminated our need to start from production from scratch. Obviously further consolidate the growing business and leverage our ability to use our own garments in that production over time.

We saw it as putting, really, three of the significant players together with our technology, our cash flow and ableness to finance and keep equipment current, and our backroom operations and how we can manage incoming orders. We feel good about that. We have locations that service the marketplace geographically where we need them, by far of the broadest geographic footprint in the marketplace. We probably expect to grow more organically from here for the foreseeable future. Deb, do you have anything you want to add to that?

Deborah Merrill:

I think that covers it. It was really a strategic for the growth and leadership position of the business, and to continue to grow that overall market, which is currently in a fast growth pace. We are looking forward to that in fiscal '19 and in future years to come.

Operator:

We'll move to Jamie Wilen with Wilen Management.

James Wilen:

Hi, folks. Just a follow-up on DTG2Go. The acquisition in March, how much did that add to this year's sales and did it have an EPS impact as well? Then going beyond that, when you put these three together, what would you anticipate your sales levels to be in the coming fiscal year?

Deborah Merrill:

Yes, Jamie, I'll take that. It is a little hard and the reason we don't break it out is because we've integrated the businesses together. You can't necessarily combine—you can't necessarily break them out. But we would estimate that the acquisition of the DTG2Go combined with Art Gun this year, added about $7 million of additional revenue and everything else in that business was then the organic growth on top of the Art Gun business that we had. It was accretive to earnings this year.

Then as we look to the addition of the SSI business in fiscal '19, you'll have the remaining part of the DTG additional business for the first half of the year and then you'll have SSI for effectively the entire year. SSI is running at about $15 million pace on an annualized basis. We should be looking in fairly short order in that business to have $55 pushing $60 million business consolidated altogether.

James Wilen:

Okay, and as part of the game plan, we obviously do a good job with digital printing, but to sell Delta garments to the retailers or whoever taking advantage of our printing expertise?

Robert Humphreys:

Yes, absolutely, and we've seen that growing and obviously, when we do these acquisitions we can go to their customers and show the benefits of using our own garments. Then in several cases we have the print capacity in our own distribution centers, our garments are already there. We get to utilize inventory we already own and eliminate the cost of bringing in the shipping cost and handling cost of garments from other distribution centers. It's really a win-win on a vertical platform.

James Wilen:

What percent of your original business of Art Gun use your garments and what percentage of SSI was using your garments prior to the acquisition?

Robert Humphreys:

I would say on Art Gun by the time we started acquiring others, we were in the 20% to 25% use of our own garments and growing that pretty rapidly, particularly as we came out with our fashion basics line and platinum line and fleece and more people were adopting that. It’s obviously well below that, when we are acquiring these companies. Although, some of them were using our garments for various reasons, often times where customers were specifying them.

Anyway, that would be a great growth opportunity if and where we were with the old Art Gun business, but bringing on this additional volume as well.

Deborah Merrill:

Jamie, then we continue to be able to expand that as we add new product into our Delta Activewear every season. We're a getting a good response to that from the digital print customers as well. As that product line continues to expand, we see the capability of being able to increase the Delta products going to the digital print business.

James Wilen:

Okay, and from an accounting perspective, when you look at DTG2Go as $55 million to $60 million business, that does not include—I assume our own garment sales are separate and distinct from that?

Robert Humphreys:

No, that would be including the garment value going out.

James Wilen:

Okay. Moving over to Salt Life, just wanted to hear your thoughts about how we get to the next level, are there still regional differences in performance as far as where the growth is, to wins and losses with national retailers. Could you just talk about all those together?

Robert Humphreys:

Sure, we've consistently for the last couple of years, brought on one or two that we consider national or big regional retailers to the Salt Life business, and we haven't lost any of them. That's been a net new business and driven a good bit of the growth. I'd say for the last 18 months or so, the independent dealers have been more steady hurt in Florida significantly from the hurricanes but maybe not exclusively but growing nicely up, particularly the East Coast and up into Maryland and New Jersey and even New York. That's been nice to see.

I think for wholesale business, what we'd really like to see is where we've had success with some of these larger retailers, a better embrace by them of our brand, which would give us a better selling space and in store displays, and that sort of support of the brand. In our own retail stores and on our e-commerce sites, our performance products and accessories are about 50% of the business. We're only about 15% or 20% with these other customers. It is our job to educate that to them that they're missing a good business with that consumer and also higher-margin products for them.

James Wilen:

When you talk about significantly higher wholesale orders, how much of an indicator for you is that of the business moving forward?

Robert Humphreys:

Well, we think significantly and we've actually recently gone back and done the analytics on that for several years. Because obviously this business really kicks off in spring, which is January shipments to us, it gives us a big indicator for the last nine months of the wholesale channel, obviously, not in our retail stores or e-commerce. We're sitting here today with a significant increase in our wholesale pre-book business for spring.

The other thing that's kind of interesting on that I'd say that's primarily driven by our independent retailers. Our larger retailers like most retailers today, they are reluctant to give you pre-books for business a season or two out. They are asking us to kind of have product ready for them. We do that on a limited basis in Salt Life. We can do more if we operated the brand longer and have a better feel for what we can digest and not.

But anyway, it is a significant leading indicator and one we're encouraged about, but also realize you got weather and economy and travel patterns and all that also go into what's ultimately shipped.

James Wilen:

Lastly on Salt Life, wonder if you can talk about the metrics of your retail store model? When you first got into it, it was almost as kind of a brand awareness store, and we hoped we can make some money off of it. Now it appears, especially with the program you've outlined for how many stores you're going to open over the next several years, that it really could be a reasonable profit center. Can you talk about what kind of volumes and are these stores profitable?

Robert Humphreys:

They are not all profitable yet. What we have seen is significant continued growth by each store as we operate them, and for us right now, it's taken a couple of years generally to get those stores profitable on a full-year store basis. Thats too slow as a true retail model and we realize that. We have used them as branding opportunities, particularly on the West Coast and we think that's working. We continue to see good growth from those stores and good growth on our e-commerce shipments to California.

This year we've hired a retail consultant to help us pick sites and build our financial model more like a traditional retailer and what our expectations are in sales per square foot and that sort of thing. They have not selected or helped us select any sites as of yet. But that process is in place.

We do expect for all the locations to be profitable longer-term. We also will still take a slow movement into these waters to make sure we don't get the cart ahead of the horse on retail store operations.

James Wilen:

Got you. Lastly, on the tax rate, I'm always confused as to what it's going to be every quarter. Could you tell us what you put as your tax rate when you write this year's earnings numbers and what your expected tax rate would be in the coming fiscal year?

Deborah Merrill:

Well, I will try. Unfortunately, all the changes in the tax legislation, and even after it came out, interpretations of what it meant and changes on the implementation of it, has made it more of a challenge this year and it already was a challenge prior to that. If you exclude the tax reform items from this year we actually were in a tax benefit situation. That was driven just by the profits that we were able to put in foreign jurisdictions, most of which have a zero tax rate on them and others have lower than U.S. tax rate.

On a go-forward basis, and again, there is tax legislation that will come in and begin its implementation in this upcoming fiscal year. All that being said, we are looking at kind of a low double-digit tax rate maybe in that 13%, 14% for our upcoming fiscal year.

Robert Humphreys:

Then, Jamie, I would just add to that. As Deb was talking, it's obviously highly important of where we earn that money. As DTG2Go grows, that’s U.S. based profits, as Salt Life grows that’s U.S. based profits. While we would expect, as she said, kind of the mid-teens in the upcoming fiscal year. If our business plans work out the way we would expect, we would expect that tax rate to go up over the next several years as we make more profit in this country. But still be in that 20% or less as we know and understand the current tax laws.

James Wilen:

Okay, thanks Bob, thanks Deb.

Robert Humphreys:

Thank you, Jamie.

Operator:

Once again, as a reminder, it is star, one to ask a question. We’ll move on to Chris Reynolds from Neuberger Berman.

Chris Reynolds:

Yes, good afternoon.

Deborah Merrill:

Good afternoon, Chris.

Chris Reynolds:

I just had a general question about your inventory. You talked about nice orders and the quarter was terrific and outlook looks good. But just seems like the apparel categories are pretty choppy and big customers can pull back. You had disappointing numbers out of dealers today. How would you characterize your overall inventory levels today?

Robert Humphreys:

We think, good. We have less units in inventory than we did this time last year. Obviously, you got higher cotton costs and some other input costs in inventory. We’re actually tweaking up our manufacturing output in our own facilities based off inventory levels and anticipated business level. We would always like to operate our business more efficiently from an inventory standpoint and are focused on that but generally speaking, I think we're well matched or a little bit better off than we’ve been over the last year or two.

Chris Reynolds:

Okay, thank you.

Operator:

Moving onto Richard Mackee from First Associates.

Richard Mackee:

Good afternoon. Congratulations on another good quarter.

Robert Humphreys:

Thank you, sir.

Richard Mackee:

I was wondering, with interest rates rising, what your debt repayment schedules look like, and if you have any concerns about refinancing as we go forward?

Deborah Merrill:

The answer is no. We do not have concerns about that. We typically will use our cash flows from our business, our free cash flows from our business after the making the investments for growth that we have and every year we've continued our share repurchase programs. But outside of that, we do use that excess cash flow to pay down our debt. We do have a debt agreement that lasts through 2021 at this stage of the game, but has been with the Group for a very long time, and do not anticipate any concerns from that standpoint.

Of course, interest rates are rising and so the cost of debt is going up. But at this point in time, no concerns overall from our leverage standpoint, which continues to improve each year.

Richard Mackee:

Great, all right. Thank you very much.

Operator:

Up next is Dave King from ROTH Capital Partners.

Dave King:

Hi, there. Just wanted to squeeze one more in, if I could. Just on the Soffe business, if you possibly talk about the performance between military and consumer? Then I think on the last call you were targeting mid-single digit operating margins for that business. Just how close are you to that level and when do you expect you can get there? Thanks.

Robert Humphreys:

The military business is solid. But it's choppy with some of these programs and the military calls out a lot of product, and then they might not call out any, it's a little bit haphazard on the order flow. We are increasing our business; and having some good success in growing in some other channels of distribution with the military. We feel good about that.

The Soffe business, it's also growing at big box retail and sporting goods stores. We feel good about that; and are growing fairly nicely on our B2B e-commerce site. Those are all growth areas for Soffe. It was a military issue short that we enjoyed for a number of years that we ran through that process about the end of our third quarter of last fiscal year. A short that they brought in to their in-house kind a prison labor concept, and so we lost that business, which was several million dollars a year.

But have other areas growing that will take care of that this year. We would expect some slight topline growth out of Soffe this year. Our costs at Soffe are continuing to come down. We would expect in the next maybe a year or two to start get into to that mid-single digit operating profit at Soffe.

Operator:

Once again, it is star, one to ask a question. We'll take Jamie Wilen from Wilen Management.

James Wilen:

You are now half way through the first quarter. Any indications that you could talk about of how your sales levels are going relative to last year?

Robert Humphreys:

October started off good for us, and so we felt really good about shipments this in October, maybe got a little bit of tailwinds from some shipments that didn't go out with the hurricane that we've been discussing. But anyway, that's off to a good start. We've had good order inflows and we really have been busy in closing out the fiscal year. We're doing that of about 10 days earlier this year and expect to file our K Monday. We're excited to get that behind this. While we're obviously focused on getting sales and making product and shipping it, we'll get more into the analysis of that starting next week.

James Wilen:

As far as cotton pricing goes, seems like it is relatively stable now. Would you anticipate margins to be relatively stable?

Robert Humphreys:

Yes, I'd say steady as she goes on cotton pricing. We did make good progress over the last, really, 12 months of getting those cost increases into our pricing and accepted by the marketplace. Right now, we would expect that to continue and expect to have slightly better margins in fiscal '19 on a consolidated—

James Wilen:

Lastly, now that you are buying back stock below book and a nice multiple of earnings, could you tell us how many shares are currently outstanding?

Deborah Merrill:

Jamie, I believe it's about 6.8 million –

Robert Humphreys:

But higher on the fully diluted.

Deborah Merrill:

Correct, on the bit, yes, exactly.

Robert Humphreys:

About 7.3 million, I believe, on a fully diluted basis.

Deborah Merrill:

Yes, fully diluted for fiscal '18 ended with an average of 7.4 million, and there's probably, as Bob said, about 7.2 million, 7.3 million fully diluted right now.

James Wilen:

Perfect. Thanks, fellas, appreciate it.

Robert Humphreys:

Okay, thanks.

Operator:

There're no further questions in the queue. As a last reminder, it is star, one to ask a question. We will pause for just a few moments. There're no further questions in the queue. I'd like to hand the call back over to Bob Humphreys for closing comments.

Robert Humphreys:

Okay, well, thanks for joining us today. We're excited about our fiscal 2018 and are working hard on fiscal 2019 as we speak. We will look forward to updating you on our progress in our earnings call for our first quarter here in just a few months. Thank you very much.

Operator:

This concludes today's presentation. Thank you for your participation. You may now disconnect.