Kontoor Brands Inc.
1Q 2024 Earnings Conference Call
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Presenters

Michael Karapetian, Vice President, Corporate Development, Strategy and Investor Relations
Scott Baxter, President, CEO and Chair of the Board
Joe Alkire, EVP and CFO

Q&A Participants

James Duffy - Stifel Financial Corp.
Robert Drbul - Guggenheim Securities
Brooke Roach - Goldman Sachs
Mauricio Serna - USB Group AG
Laurent Vasilescu - BNP Paribas
Will Gaertner - Wells Fargo & Company
Paul Kearney - Barclays Capital

Operator

Greetings, and welcome to the Kontoor Brands First Quarter 2024 Earnings 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 0 on your telephone keypad. As a reminder, this conference is being recorded.

It is now my pleasure to introduce Michael Karapetian, Vice President, Corporate Development, Strategy and Investor Relations. Thank you, Michael. You may begin.

Michael Karapetian

Thank you, operator, and welcome to Kontoor Brands' First Quarter 2024 earnings conference call. Participants on today's call will make forward-looking statements. These statements are based on current expectations and are subject to uncertainties that could cause actual results to materially differ. These uncertainties are detailed in documents filed with the SEC. We urge you to read our risk factors, cautionary language and other disclosures contained in those reports. Amounts referred to on today's call will often be on an adjusted dollar basis, which we clearly defined in the news release that was issued earlier this morning. Our outlook is presented on an adjusted dollar basis.

Reconciliations of GAAP measures to adjusted amounts can be found in the supplemental financial tables included in today's news release, which is available on our website at kontoorbrands.com. These tables identify and quantify excluded items and provide management's view of why this information is useful to investors.

Unless otherwise noted, amounts referred to on this call will be in constant currency, which exclude the translation impact of changes in foreign currency exchange rates.

Joining me on today's call are Kontoor Brands' President, Chief Executive Officer and Chair Scott Baxter and Chief Financial Officer Joe Alkire. Following our prepared remarks, we will open the call for questions. We anticipate this call will last about one hour. Scott?

Scott Baxter

Thanks, Mike, and thank you to everybody joining us on today's call. We are pleased with our better-than-expected start to the year. Compared to our outlook provided in February, we saw a broad-based upside from revenue, gross margin and earnings. Joe will unpack the details, but our relative strength in the quarter, combined with improving visibility gives us confidence to raise our full year guidance.

I will step through the highlights in a bit, but first, let me start with the organizational announcements we made in March. As we discussed last quarter, we have commenced Project Jeanius to transform our organization. This multiyear project is focused on driving three things: first, create a global best-in-class multi-brand platform; second, simplify the organization to increase speed and efficiency; and third, free up investment capacity to accelerate growth and increase profitability.

As part of these actions, Tom Waldron has been appointed COO. You've had a chance to hear from Tom during our year-end calls. He is an incredibly talented leader who has led the return to growth and strong profitability for Wrangler. From 2019 to 2023, Wrangler has grown revenue at a mid-single-digit CAGR and expanded reported profit margins by over 300 basis points. In his new role, Tom will amplify our strategic playbook across both brands to drive improvements throughout the organization, from our commercial and go-to-market teams to global operations.

We have also elevated Jenni Broyles to EVP and Global Brands President of Wrangler and Lee, and Ezio Garciamendez to EVP and Chief Supply Chain Officer. Congratulations to both Jenni and Ezio, who have joined our executive leadership team. The team we have in place has a proven track record of success at every position, and I am confident will drive the next leg of our value creation journey.

Now let me touch on highlights from the quarter. Wrangler's momentum continues with product and demand creation platforms that are elevating the brand like never before. While wholesale pressures are impacting the near term, as expected, the strength of our DTC business and point-of-sale outperformance are real proof points, Wrangler is winning with the consumer.

During the quarter, Wrangler's global DTC business grew 8%, and we gained 60 basis points of market share in denim longs according to Circana. This marks the eighth consecutive quarter of market share gains for the brand. To support this momentum, Wrangler continues to diversify beyond denim. In fact, approximately half the business is now outside of denim bottoms, reflecting the success we have had expanding into new categories.

Outdoor is a great example, which is now an approximately $200 million business. The investments we are making in the team and our product development capabilities are helping to drive further penetration in this large and growing category, leading to successes like the outdoor performance cargo, which is one of the fastest-growing pants in Kontoor's history. And Wrangler ATG is elevating the brand into newer channels of distribution such as specialty sporting goods supported by new launches like the ATG Chino and Cliffside Utility this fall, as we are on track for another year of double-digit growth in outdoor.

We are also advancing our consumer insights and research capabilities, as part of our evolution to a more data-driven organization, allowing us to better align with changing consumer buying habits and behaviors. This behind-the-scenes work is a great example of how we are becoming a more efficient organization with targeted investments that generate higher returns.

And finally, we have a strong pipeline of demand creation platforms and collaborations. Lainey Wilson's first collection launches later this year, and based on early reads is on track to become the largest global collaboration to date. We are also continuing our very successful collaboration with STAUD in the second quarter, which is helping to bring the right balance of newness, while reaching a younger female consumer. And we are amplifying the brand with events at the ACM Awards and Stagecoach, where we are the official denim sponsor. These are great examples of how we are building momentum throughout the year with demand creation investments that fit together and deepen the connection with our consumers.

Turning to Lee. Similar to Wrangler, Lee experienced softness at wholesale, as retailers tightly managed inventory levels. As we discussed last quarter, the business was also impacted by conservatism on seasonals. That said, we are seeing green shoots from our innovation platforms and with our younger female consumer.

On the men's side, we continue to advance our innovations focused on comfort. These platforms now account for two-thirds of our U.S. men's business and our genuine distinction in the market. And within female, our heritage collection and iconic rider platform is expanding the brand's reach, while being supported by new equity campaigns. This is translating to share gains and growth at point-of-sale. During the quarter, POS in the U.S. increased 2%, and market share in denim longs gained 40 basis points, as measured by Circana.

Looking ahead, we have several initiatives that give us confidence. First, our improving product development capabilities are enabling category expansion. Our tops business has been a great success story and is on track to deliver strong double-digit growth for the year and Lee Golf

launches in the second quarter with innovative fabrications that are appealing to a broad range of male consumers. We are excited about the potential in this growing category, as part of Lee's office to outdoor evolution.

Second, our innovation pipeline is getting the most significant addition in years. Lee x will launch later this year and combines elite comfort with world-class aesthetic. This will be a true platform that crosses denim and non-denim tops and bottoms at a price point that simply does not exist for this level of performance.

And last but not least, we are getting sharper with our brand positioning in the marketplace. This foundational level work is a significant focus for the second half of the year and is part of the new multi-brand platform we are developing. We are conducting an end-to-end assessment to ensure alignment with our refreshed consumer segmentation, brand investments and product development. We are confident this will pay significant dividends in the years ahead.

Before I turn it over to Joe, let me close with a perspective on the balance of the year. Since we spoke in February, point-of-sale has improved for both brands. We have continued to gain share. The wholesale channel has found better balance and gross margin expansion exceeded our expectations. We also made further progress working down our inventory position, ending the quarter 24% below prior year levels.

Combined with our better-than-expected profitability, we now expect to generate more than $335 million in cash from operations this year. As a result, our capital allocation optionality continues to improve, allowing us to return $48 million to shareholders during the quarter, including $20 million in share repurchases under our new $300 million authorization.

Longer term, Project Jeanius planning is well underway with impacts expected to start in the fourth quarter. We have a line of sight to the higher end of the $50 million to $100 million of annualized run rate savings, none of which are included in our guidance. That will structurally raise our profitability ceiling, while significantly increasing our investment capacity to drive more profitable growth over time.

While the near-term environment remains dynamic, we are operating from an offensive position. We are off to a better-than-expected start and have improving visibility to the balance of the year. I am confident we are on a path to drive strong value creation for all stakeholders. Joe?

Joseph Alkire
Thanks, Scott, and thank you all for joining us today. Let me start by providing perspective on our first quarter results relative to the outlook we provided in late February. Our results were stronger than expected, driven by higher revenue, gross margin, earnings and cash flow. Our brands continue to drive market share gains in our largest points of distribution and POS and inventory levels at retail improved modestly late in the quarter.

Gross margin expansion was stronger than expected, driven mainly by lower product costs and favorable mix. And when combined with further inventory reductions supported robust cash generation and capital allocation optionality, as evidenced by the $48 million of cash returned to shareholders through share repurchases and dividends in the quarter. Overall, we're pleased with our start to the year.

Let's unpack the quarter in more detail. First, POS strengthened as we progressed through the quarter, and we saw a better balance between sell-in and sell-through as inventory levels at retail modestly improved and replenishment order patterns normalized. If you recall, we did not assume an improvement in either POS or inventory levels in our outlook, as we continue to plan the business conservatively. So, these results were above our expectations and drove the majority of the revenue upside in the quarter.

Second, gross margin expansion exceeded our expectations driven by lower product costs and the structural benefits from mix. Relative to our assumptions, we also realized a smaller-than-expected impact from pricing, the majority of which is timing related and will begin to impact our gross margin more meaningfully in the second quarter. Our gross margin visibility has improved relative to 60 days ago, and we now expect our full year adjusted gross margin to match our previous high of 44.6% reached in 2021.

Lastly, we continued to drive strong cash generation through improved profitability and reductions in net working capital, including a 24% decline in inventory. We are opportunistically working through our excess inventory and driving improvements in supply chain execution through higher fill rates and more efficient demand supply matching. We continue to take a conservative approach to planning the year but based on our better-than-expected first quarter results and improved visibility, we are raising our full year gross margin, earnings and cash flow outlook.

I'll dive deeper into our updated outlook in a moment, but first, let's review the additional details of our first quarter results. Starting with Wrangler. Global revenue decreased 4%. The decline was primarily driven by U.S. wholesale, offset by growth in DTC, including 7% growth in digital and 10% growth in brick-and-mortar. Retailer inventory management actions continue to impact the business near term. However, underlying brand momentum remains strong, as evidenced by improving POS, ongoing market share gains and DTC strength. Nowhere is the brand's momentum more evident than in the success in diversifying into new categories.

Wrangler's Outdoor business, led by ATG, continues to scale, as we advance our product development capabilities and reach new consumers. During the first quarter, Wrangler Outdoor grew 5%. Nearly 50% of the global Wrangler business is now in categories outside of denim bottoms. And we expect the non-denim business, including outdoor, tops and non-denim bottoms to grow at a mid-single digit rate this year. Wrangler International revenue decreased 13%. European wholesale remains under pressure due to challenging macro conditions.

However, this was partially offset by double-digit DTC growth, supported by investments in owned stores and our digital platform.

Turning to Lee, global revenue decreased 9%. As expected, reduced shipments in U.S. wholesale and a decline in the seasonal business negatively impacted the quarter. That said, revenue for the Lee brand was above our expectations.

Similar to Wrangler, Lee is having success expanding beyond denim, particularly in tops. During the quarter, tops grew 20% and now comprise over 10% of the total business. We expect strong growth in these categories to continue for the balance of the year.

Lee international revenue decreased 5%. In Europe, revenue declined 9%, driven by ongoing macro pressure. In APAC, revenue declined 2%, as the market recovery remains uneven, and we work to further improve the quality and health of our retail network. We continue to anticipate growth in APAC for the full year.

Turning to gross margin. Adjusted gross margin expanded 270 basis points to 45.7% driven by the benefits of channel mix and lower product costs. This was partially offset by targeted pricing actions, which went into effect late in the first quarter.

Relative to our expectations, we saw greater-than-expected favorability from mix and lower input costs in addition to a smaller-than-expected impact from pricing, resulting in adjusted gross margin exceeding our expectations by approximately 160 basis points.

Adjusted SG&A expense was $195 million. Investments in demand creation, technology and DTC were partially offset by disciplined management of expenses and lower distribution in freight. And adjusted earnings per share was $1.16, consistent with the prior year.

Now turning to the balance sheet. Inventory decreased 24% to $501 million compared to our initial expectations of a 20% decline. We remain intensely focused on improving net working capital to supplement our strong operating earnings growth and drive enhanced cash generation in support of our capital allocation framework.

We finished the quarter with net debt or long-term debt less cash of $564 million and $215 million of cash on hand. Our net leverage ratio, our net debt divided by trailing 12-month adjusted EBITDA was 1.6x within our targeted range.

During the quarter, we repurchased $20 million of stock under our current authorization, and as previously announced, our Board declared a regular quarterly cash dividend of $0.50 per share. Finally, on a trailing 12-month basis, our adjusted return on invested capital was 25%.

Now turning to our outlook. Revenue is still expected to be in the range of $2.57 billion to $2.63 billion, reflecting a decrease of 1% to an increase of 1%. We are encouraged by our better-than-

expected start to the year and the improvement we saw in both POS and inventory levels at retail across the first quarter.

So how are we thinking about the remainder of the year? First, we continue to plan the business conservatively with the majority of the year still ahead of us. Retailers remain in a conservative posture, and we are cautious on the environment, as the consumer, while resilient, remains under pressure around the globe. We continue to assume no meaningful improvement in overall POS or retail inventory positions for the balance of the year.

Second, we have good visibility to category expansion and distribution gains, including expansion of our tops and outdoor businesses, as well as new innovation platforms in the second half of the year. And we expect ongoing growth in our DTC business, reflecting investments in our digital platform, improved product segmentation and a more robust demand creation pipeline. Taken together, we continue to anticipate first half revenue to decline at a mid-single-digit rate, followed by mid-single-digit growth in the second half of the year. Beyond the first quarter, we expect revenue growth of approximately 2% for the year-to-go period.

Moving to gross margin. Based on our stronger first quarter results and improved visibility, we are raising our outlook to approximately 44.6% from our prior range of 44.2% to 44.4%. Our updated outlook represents an increase of 210 basis points compared to adjusted gross margin of 42.5% in 2023, excluding the out-of-period duty charge. In the first half of the year, we now anticipate more than 300 basis points of gross margin expansion compared with our previous outlook of more than 250 basis points.

Our gross margin outlook includes the following assumptions. First, we will continue to benefit from the structural drivers of mix. This is expected to contribute approximately 30 basis points to 40 basis points to the full year. Longer term, we expect the benefits of mix to continue, as we scale DTC and international.

Second, we have good visibility on input costs with costs locked into the third quarter on manufacturing and into the fourth quarter on sourced product. Our visibility for the balance of the year has improved. And when combined with the proactive actions to optimize our supply chain footprint, we anticipate over 200 basis points of benefit for the year from lower product costs.

And finally, we assume a modest headwind from lower pricing promotions and the disruption from the Red Sea. Collectively, these inputs are expected to negatively impact our margin by less than 1 point. I have high confidence in our ability to drive gross margin expansion beyond our previous expectations over time, supported by Project Jeanius, but we'll share additional details on that in the coming quarters.

SG&A is still expected to increase at a low to mid-single-digit rate. We will continue to make investments in demand creation, DTC and technology, as well as product development capabilities to support our growing innovation platforms and category expansion plans.

Operating income is now expected to be in the range of $377 million to $387 million, reflecting growth of 8% to 11% compared to the prior year, excluding the duty charge. This compares to our previous outlook of $372 million to $382 million.

EPS is now expected in the range of $4.70 to $4.80, representing growth of approximately 6% to 8% compared to adjusted EPS in the prior year, excluding the out-of-period duty charge. This compares to our prior outlook range of $4.65 to $4.75. Full year EPS growth will be negatively impacted by about five percentage points from a higher tax rate.

First half EPS is now expected to increase at a mid-single-digit rate compared to our prior outlook for EPS to be consistent with prior year levels. In the second quarter, we expect EPS of approximately $0.85, representing 10% growth.

Finally, we now expect cash from operations to exceed $335 million, primarily as a result of stronger earnings growth. This compares to our previous outlook of cash from operations to exceed $325 million.

Before opening it up for questions, I'd like to reiterate the confidence we have in our ability to deliver our 2024 objectives. We are off to a better-than-expected start to the year. The fundamental profile of the business is accelerating, and our brands are winning in the marketplace and continue to drive market share gains.

We are on track to generate significant cash from operations this year, which combined with our strong balance sheet, provides us with considerable capital allocation optionality. We are operating from a position of strength, and I am confident in our commitment to deliver superior returns for all stakeholders.

This concludes our prepared remarks, and I will now turn the call back to our operator.

Operator
Thank you. We will now be conducting 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 would 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. We ask that you please limit yourself to one question and one follow-up question. One moment please while we poll for your questions.

Our first questions come from the line of Jim Duffy with Stifel.

Jim Duffy
Good morning. I wanted to start, pardon my voice, fighting a cold here. I wanted to start by asking for more perspective on how the quarter and your thoughts on the year have evolved since late February, there are some moving parts. It sounds like you saw a further improvement in POS and retailer inventories in March, revenue and gross margin came in better for the quarter, but the full year doesn't pass through the revenue upside and the earnings increase was just a fraction of the Q1 earnings upside. So, I'm curious, is there something you're seeing or hearing from channel partners that's making you more cautious on Q2 and the back half of the year?

Joseph Alkire
Hey, Jim, good morning. It's Joe. I'll start, and then Scott may want to provide some thoughts on the environment. So yes, we beat Q1. We beat the outlook by approximately $25 million, largely driven by improved POS and inventory levels at retail in March. This was largely driven by our major customers in the U.S. So, this drove the majority of the upside in the quarter.

From a gross margin standpoint, also above our expectations by about 160 basis points. That was mainly due to lower product costs and a small delay in the pricing actions that we're implementing, which is a bigger Q2 impact versus our original plan.

Look, as we said in February, we're planning the business conservatively in light of the environment. We've got the toughest quarter behind us now, and the business fundamentals are positioned to accelerate across the balance of the year from here, which we're highly confident.

And I'd say from a full year outlook, we raised the first half, we raised the full year largely, as a result of stronger-than-expected Q1. We increased our gross margin assumption modestly for the balance of the year based on our increased visibility. From an overall revenue standpoint, we've got good visibility into the improvements for the balance of the year, again, largely driven by new programs and distribution gains. But from my perspective, nothing that we're seeing in the environment just being cautious on the outlook for the year.

Scott Baxter
And Jim, I would just add that the environment, it got modestly a little bit better than we thought in Q4. Really nice balance from our big customers from an inventory standpoint, thought that worked itself well through pretty good. We remain optimistic for the rest of the year. We do have some programs that Joe mentioned, both channel and category that we're excited about that we've talked a little bit about. So, a little bit conservative, but I want to make sure that we go ahead and hit our commitments going forward.

Jim Duffy
Great, thanks. A couple of related questions on the guide. Joe, the inventory progress in Q1 was meaningful. Can you speak about this in the context of the full year cash flow from operations

guide? Really good reduction in the inventories. You increased the cash flow from ops by about $10 million. Does that assume some reinvestment in inventory later in the year?

And then, I'm also curious if you could just give us an update on the seasonals business. Is the headwind from seasonals business -- have those categories normalized? Are those headwinds behind you?

Joseph Alkire
Yes, I'll start with the inventory, Jim, and Scott can take seasonal. So yes, from an inventory standpoint, really good progress. The first quarter will be our largest year-over-year decline. We expect declines pretty much for the balance of the year, somewhere in that low double-digit range. This is contributing to the cash flow. But yes, as the grows -- the growth inflects in the second half, we will lean back into some inventory. But for the year, as a whole, inventory will be a contributor to our cash.

Overall, Jim, we still have about 130 days of inventory on the balance sheet. I would say steady state for us continues to be somewhere in that plus or minus 100-day range. So, there's still a considerable amount of cash on the balance sheet that we'll release at some point. But in terms of composition of our inventory, we still feel pretty good somewhere in that 75% to 80% range is core. So, the inventory is in good shape.

Scott Baxter
Then Jim, just a couple of comments on seasonals. After 20-plus years of riding the seasonal wave up and down and weather and all kinds of patterns and geographies, it's very typical. We've seen this play before. It's a little cool right now. But all of a sudden, here where we are and part of this area and this geography got really hot yesterday, supposed to get really hot this weekend, and we really like our position. We like our product this year. We like our distribution. We think we're in a really good spot. And just because it was a little bit cool at the beginning of the season doesn't really bother us. We've been through that before, so no issues.

Jim Duffy
Thank you, guys.

Operator
Thank you. Our next questions come from the line of Bob Drbul with Guggenheim Partners. Please proceed with your questions.

Robert Drbul
Hey, guys, good morning. And Scott, 85 in New York today. So, it's happening finally.

Scott Baxter
There it is. There it is.

Robert Drbul
So, I have just a couple of things I'd like to focus on and talk about. Can you expand a bit more just on the organizational structural changes that you're making and sort of really how we should think about that? And then there's just a lot of -- you guys talked a lot about the new category growth and expansion. Can you just talk about like when you size them up, which one should we really be focused on? Which ones are needle movers that you have the most optimism around. That would be helpful. Thanks.

Scott Baxter
Sure. Thanks, Bob, for the questions. We always had a plan to go down to one COO and it was part of what we did, but everyone remembers we spun off and we did it in 10 quick months, and it was a clone and growth structure, and we probably would have gotten to this position sooner if it weren't for the pandemic, kind of slowed things down and what have you.

But when we decided and finished our ERP and decided that we needed to go ahead have the exact model that we need to be successful as a company versus when you do spin-off and after being together so many years, you do a lot of things the same and then you have to work through, where you want to be. And we're at that place, but we know exactly where we want to be. So, we rolled out Project Jeanius, finished our ERP, and it was the perfect time to put in place the organizational structure we needed to be successful.

So, this streamlines our decision-making, putting Tom in the COO role and success breeds success. And Tom has had a tremendous amount of success in what he's done with the team in Wrangler. So, we're really excited to put Tom in that elevated position. And then about two years ago, Tom took the operational piece, too, our supply chain piece and has done an exceptional job there. So, combining those, I think, has been instrumental in our success.

So, our decision-making now is much more streamlined. It's moving faster. It's part of what we're doing from a Jeanius standpoint. It moves us to the organization we want to be. I think the one thing that I want to make sure that everybody does realize, though, is that the fact that we do have two separate go-to-market teams, right?

They funnel up to Tom at some point, but we have a Lee team from a go-to-market standpoint, we have a Wrangler team that are separate from a go-to-market standpoint. But what happens, though, is they collectively come together on the back end, and that also funnels up to Tom. But we combine that back-end piece from a synergy standpoint and a cost savings standpoint, and it's really, really helpful. So that's kind of the background and the thinking about it, but how we're going to go to market and who we want to be in all part of our project Jeanius work.

And then from a category standpoint, yes, we've been talking a lot about the categories that we entered in over the last few years. When we spun, we entered outdoor, we entered tees. We entered work in a more significant way, although we were there in outdoor and work to a degree. But you think about like outdoor, in the last four years we've gone from $100 million to

$200 million, and you talked about which ones are still accelerators, outdoor is definitely an accelerator for us.

We're just getting better at it and smarter at it, and we've hired some talent, and our product looks better. And with time, you learn some things and you learn about your consumer, and we really like the new product that's coming out here. So, I feel really good about that. And our tee business has been accelerating really, really nicely. So, we think about those two.

Right now, work is a little bumpy for us. So, we'll continue to work through that and get that in a place that it needs to be, but we still love that channel. It's a big channel for us, as a company already. And we think that it is just a business that we're going to be in for the long term, and it's got real structural tailwinds for us. So, we're excited about that, too. But that's kind of where I would focus and emphasis from those newer categories that we enter.

Operator
Thank you. Our next questions come from the line of Brooke Roach with Goldman Sachs. Please proceed with your questions.

Brooke Roach
Good morning and thank you for taking our question. Scott, you've talked a lot about the optimism that you have on new categories and the growth of the business in non-denim today, but I was hoping you could give us your view on the health and the outlook for growth of the U.S. denim market. Have you seen any benefit from some of the recent Western cultural moments? And are you seeing accelerating April POS, as a result of the recent pricing changes that have been put in place at some of your key customers?

Scott Baxter
Yes, good morning, Brooke. Thanks for the question. No question. We have a significant business obviously, and it's critically important to us, and we call it our core business. And we see that denim is in fashion, has been in fashion and the casualization of the world. One of the things that was really interesting was that we went through this casualization when we went through the pandemic. And then when we came out, people said that we'll probably return to normal, and people dress like they used to. It just never happened. People stayed casual or continuing to be casual. And we fit right into that in a really perfect way around the globe. So, we feel really good about that.

And then we do have some new distribution coming even in our core denim categories here for the second half of the year, which is pretty exciting with a big retailer that we've talked about. So, you couple those two things.

And then when you go to Western, the one thing I always think about and try to remind people is that we've been on a Western trend since 1947 when we brought out the first really great cowboy jean, our MWZ13's. And we've been working that and loving that for a long time, and

we are Western. If you think about Western, you think about the cowboy, you think about the mountains, you think about that lifestyle, the first thing you think about is Wrangler jeans and Wrangler tops. So, we are a huge part of that business, and it just continues to grow, and it's been really nice.

And I think it's really spiritual for some people to be part of that, the West, and what it stands for and what it stood for, for us as a country. And it's interesting, too, now that for the first time in a long time, we did have this many, many, many years ago, but the Western piece is starting to hit Europe a little bit now, so -- which is really interesting for us. So, we're enthusiastic about and we'll see what happens there. But we are seeing some green shoots in that respect over in the European area.

But we continue to bring new products to market in our Western business, and I don't know if everybody saw or has heard the new Miranda Lambert song that came out about Wrangler jeans that's debuting here today, I think. And Miranda is the all-time winningest ACM Award winner ever. So, it's pretty interesting that things like that happen, and they're completely organic for us, as a company. And it just goes to show you when people think about that Western business, they think about Wrangler first.

Joseph Alkire
Now, Brooke, just on April specifically, we actually saw April POS soften a little bit versus Q1. Nothing dramatic, nothing that concerns us. It did improve sequentially over the course of the month. That's continued into the first couple of days of May here, and that's all reflected in our outlook. But it was a little softer than Q1.

Brooke Roach
Great. And if I could just follow up on international. It appears that Europe wholesale continues to be a little weaker than we would have expected. I was wondering if you could discuss relative to your outlook for Europe and Asia provided in February. What are you forecasting for growth in both wholesale and DTC in those markets for the remainder of the year?

Scott Baxter
Yes. Brooke, I'll go ahead and start and then kick it over to Joe. But yes, you're right. Europe is still a little bit lumpy. The business there is kind of up and down, and we've been riding that like a lot of other folks. We're certainly hopeful that, that economy starts to pick up here over time. We are seeing some things that are beneficial.

Our product is still resonating in a pretty significant way, and we've got a really good team on the ground there. And our new Project Jeanius work should help that from a global standpoint, as we go ahead and accelerate our global product development under one person. So, I do have some optimism, but we do need to see the economy improve, and we're hopeful that, that happens and strengthens throughout the rest of the year. But truly, we think it's going to pick up a little bit more steam in 2025 than in 2024.

Joseph Alkire
Yes. Just in terms of this year, Brooke, we actually came through Q1 a little better than our plan, both Europe and Asia. Again, just to the point I made earlier, we planned the business pretty conservatively. So, no real change in terms of how we're thinking about the business. Europe will be tougher than Asia. Asia, we still expect growth more in that mid to high single-digit range on a full year basis, much stronger in the second half. Within that, we expect stronger growth from DTC, which you've seen from both regions pretty consistently.

Brooke Roach
Thanks so much, I'll pass it on.

Operator
Thank you. Our next questions come from the line of Mauricio Serna with UBS. Please proceed with your question.

Mauricio Serna
Hi, good morning. Thanks for taking my questions. Yes. I just wanted to confirm first on the sales guidance that Q1, like the sales beat, there wasn't really any shift in shipments from Q1 -- from Q2 to Q1? And if that's the case, just to understand, again, like why is that not being flown through to the full year sales guidance?

Second, on that, thinking about the full year sales guidance, maybe if you could like provide some type of bridge or kind of explanation similar to what you mentioned in the gross margin outlook in terms of like how much you're getting from roughly contribution from the new distribution gains or channel expansion and particularly interested on the launch in the second half of Wrangler denim, like how much do you think that could contribute to your sales growth? Thank you.

Joseph Alkire
Hey, Mauricio, it's Joe. I'll start. So, on the first half guidance specifically, we kept it the same. So, no real change. We raised the outlook at least from a revenue standpoint, no change for first half or full year. I'd say we're just being a little bit cautious just given the environment, but no real change. We continue to not assume any real improvement or any improvement in either POS trends or inventory levels at retail.

We held the year as well, down -- 1% to up 1% -- on the top line and the growth we assume in the back half is really all non-comp distribution gains, category expansion, DTC in China. So, from a top line standpoint, there's really no change to our outlook for the year. There's been some movement between the quarters, but nothing significant in the context of the full year.

Mauricio Serna

Got it. And then just a quick follow-up. Could you talk a little bit more about what you saw in China? Usually, you mention that on the release, but I didn't see any comments this quarter. And maybe also like how should we think about with the meaningful cash flow generation that you have for this year, how should we think about the optionality in terms of return to shareholders, in terms of dividends and share repurchases. Thank you.

Scott Baxter
Hey, Mauricio, it's Scott. I'll go ahead and start. From a China standpoint, we took 2023 to really spend some time to work with our partners and clean up our inventory, which our team -- and I want to be very thankful to them for this, but they did an outstanding job there. So really appreciate that get inventory levels really clean. Because if you remember, and I think everybody does, China came out of the pandemic a little bit slower than everybody else. So, as we go through these kind of inventory issues, they're kind of a tailwind of it. So really nice work there.

Now we're going about and we're refreshing about 70% of our fleet over there, which is fairly significant over the next two years, but it's really good work and work that needed to be done. Teams heavily engaged in that. We did a lot of resource work in there and done a lot of insight work in there. So, we're in a really good place, as we start that process going forward.

Some of the things that we're thinking about over there, we're leaning into the newer live streaming platforms, which have become really, really interesting and really powerful from a speech and speaking to the consumer standpoint. So that's kind of where that consumer has migrated a bit. So those are some of the things that we're doing.

But really like where we are right now, as we come through a very difficult time there way back in 2022 and 2023. And a little bit of it, Mauricio, I would say, is a little bit of blocking and tackling that we're doing there and then just building some great product and doing what we do. So, look forward to the future there.

And then I'll go ahead and start cap allocation and kick it over to Joe. It is a fabulous position to be in. We're creating a lot of cash. The business is doing well. We've got options in front of us. You saw that we went ahead and bought back $20 million of stock this quarter under our new $300 million program that we have in addition of our dividend, our very significant dividend that we pay, and we're investing back in the businesses.

If we want to do M&A, we're in a really good position to do M&A. Maybe I can make a few comments on that. From an M&A standpoint, I've said it before, I said it for years, we're not going to surprise you. Anything that we do you would immediately get. And anything we do, we would look to do something accretive, we would look for a very, very fast paydown and payback. So, count on that too, we're very prudent.

Listen, we're really serious about making sure that we continue to do what's best for our shareholders and stakeholders. And right now, we're in a really good position. There's difficulty in the environment, there's difficulty in the sector, but we're not in that position. We're in a position of strength. So, we can look at things from a position of strength, which is also really important. So, we feel really good about where we are and the cash that we're generating, as a company. And we've done a really prudent job, as far as how we've gone ahead and given it back to the shareholders.

Joe, anything to add?

Joseph Alkire
Yes, Mauricio, I would say from a priority standpoint, the priorities are unchanged. We want to prioritize reinvesting in the business first. We're committed to growing the dividend over time, and then you've got share repo and M&A. Our cash flow is accelerating. It's stronger. We raised the outlook. The balance sheet is strong. We repurchased $20 million of stock in the first quarter. We repurchased $30 million in the fourth quarter. So, we're putting more capital to work.

The M&A environment is active, as you know. We do think it's an opportunity for us, but we're going to stay disciplined. We like our strategic plan. And so, I'd say the bar is high relative to where we can invest in Kontoor today. So again, a lot of optionality given the position we're in and Project Jeanius just further supports our flexibility going forward.

Mauricio Serna
Understood, thank you very much.

Operator
Thank you. Our next questions come from the line of Laurent Vasilescu with BNP Paribas. Please proceed with your questions.

Laurent Vasilescu
Good morning, thank you very much for taking my questions. I wanted to follow up on Mauricio's question on China. Last quarter, the transcript called out that China grew 25% in the fourth quarter and that Lee China would accelerate. Curious to know how China actually performed for this quarter year-over-year? That would be great. And are you still expecting for China to accelerate throughout the year?

Joseph Alkire
Yes. Hey, Laurent, it's Joe. Yes. So, China was down a little bit in the first quarter. It was a little ahead of our plan. We still expect growth for the full year. Digital increased at a double-digit rate. Brick-and-mortar was a little tougher. As you know, Lee has a larger presence from a brick-and-mortar retail standpoint and traffic trends were difficult in the quarter. Inventory levels just in the market are much improved versus a year ago. I'd say we're pretty much back at more

normalized levels of inventory, and we continue to work on improving the health and quality of our retail partners. So, no real change. It remains a pretty significant opportunity for us long term.

Laurent Vasilescu
Very helpful, Joe. And then I wanted to ask about the 1Q adjustments. The footnotes call out, streamlining and transferring selection production within your internal manufacturing network. Maybe could you provide a little bit more color to the audience what this means? And should we assume roughly $0.10 of adjustments per quarter over the next three quarters, so we can get to the model GAAP net income?

Joseph Alkire
Yes. Hey, Laurent, yes, so in the first quarter, what you saw on the gross margin line was a little bit of a spillover from the fourth quarter restructuring charge we took on the supply chain. That was really exiting our manufacturing in Nicaragua and consolidating into Mexico. I'd say the majority of the onetime costs in the first quarter were more Jeanius related.

As we highlighted last quarter or disclosed last quarter, we'll have some onetime costs related to that program, as we activate it over the next couple of quarters. But I'd say going forward, outside of Project Jeanius and the impact of which we'll disclose appropriately, I'd expect our onetime cost to be pretty minimal, if any. So, you should start to see a much cleaner picture for the business going forward.

Laurent Vasilescu
Very helpful. Thank you so much for all the color.

Operator
Thank you. Our next questions come from the line of Will Gaertner with Wells Fargo. Please proceed with your question.

Will Gaertner
Hey, guys. Thanks for taking my question. Joe, I just want to talk about the lower product costs, how sustainable is that past this year? I think you parsed out the impact this year. Just maybe talk a little bit about what's going to happen once you lap those product costs, those lower product costs?

Joseph Alkire
Yes. Hi, Will. So, we said about 200 basis points benefit for the year from lower product costs. That's more front half loaded than back half. As we get to the fourth quarter, we'll start to lap those. But for the second half as a whole, our outlook implies over 100 basis points of gross margin expansion. So that's 2024.

I'd say just as you think about the gross margin algorithm going forward, we basically have our structural mix, which we think is somewhere in that 30 basis points to 40 basis points range. I'd say for everything else, FX cost, pricing, over time, that tends to neutralize for us. That's been our model historically. And I'd say there's no structural reason why that would change for us going forward. But we do have Project Jeanius, just as we think about evolving our supply chain. That will layer on some additional opportunity on the gross margin side, but more to come on that over the next few quarters.

Will Gaertner
Great. And just maybe talk a little bit about the share gains, what -- I mean, what's driving that? Are you selling into new doors at existing retailers? Or is it new retailers? Are you getting shelf space with core product? Or is this driven more by category expansion?

Scott Baxter
Yes. Hi, Will, this is Scott. You know, Will, I'll tell you exactly what to do in a great product. Our team is designing and building fantastic products that our consumers want. And you combine that great product with things like a new Lainey Wilson collection, our new STAUD collaboration that we've continued, and just those things that we're doing, it's just driving the consumer to our brand. It's a really exciting time. Lots of -- lots of just excitement and enthusiasm about both brands, and that's just adding to what's going on here at our company. So again, I go back to it, it's a fairly simple formula. You build really great product. You market it really well. You treat your consumers really well. We sell our product at a very fair price, a lot of value and people love our brands. It's a great combination for us.

Will Gaertner
Got it. So, is it -- are you expanding into new sellers? Or is it more existing doors? Can you just kind of give a little bit more color there?

Scott Baxter
Yes. Sure. We've expanded into some new retailers for sure. And then in the second half of this year, we do have some new business that we've talked a little bit about, which is part of the reason that we're going to have a little acceleration in our revenue, and that is happening both at existing customers and also at new customers. And some of our new areas that we talked about earlier, like outdoor and tees are really working and they're picking up new distribution, too. So, it is a combination of all of those.

Will Gaertner
Got it, thank you.

Operator
Thank you. Our next questions come from the line of Paul Kearney with Barclays. Please proceed with your questions.

Paul Kearney
Hey, everyone. Thanks for taking my question. Most of them have been answered, but maybe can you talk about the investments you're making for the back half innovation and channel launches? Where are you allocating marketing? And how should we think about that spend longer term on the SG&A line? Thanks.

Scott Baxter
We have done a really nice job -- good morning, Paul. We've done a really nice job of accelerating our marketing spend since the spin, and we continue to do that. But I think the most important thing is we've actually been very intelligent on how we've done that going forward. I think one of the things that's been really important for us here is our new consumer insights focus. When we built our new ERP system, it gave us an opportunity to go ahead and build out our consumer insights group for both Wrangler and Lee, which really wasn't very robust before. And let me give you a really great example of how that's worked.

We found out here recently, not that long ago through our new consumer insights groups that our Lee male consumer is playing and also watching more golf than the average consumer. So, we went ahead and went to the market with a new Lee golf pant short, and that just kicked off in the marketplace, and it's actually kicked off in a really nice way. We've been really pleased with the performance of it already. But that's a great example of how we're looking at these different opportunities and utilizing our new ERP system and investing in consumer insights going forward.

Paul Kearney
Perfect, thank you.

Operator
Thank you. There are no further questions at this time. I'd now like to turn the floor back over to Scott Baxter for any closing remarks.

Scott Baxter
Folks, I just wanted to thank you for all your questions and thank you for your interest in our company and certainly appreciate that and have a wonderful beginning of the summer. And we'll look forward to touch in base with you in July about mid-summer and getting you up to date on our progress and everything we talked about today. But again, thank you for your participation today, and we'll talk to you soon.

Operator
Thank you. This does conclude today's teleconference. We appreciate your participation. You may disconnect at this time. Enjoy the rest of your day.