Hanesbrands Inc.
Form 10-Q
October 28, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended October 2, 2010
or
o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number: 001-32891

Hanesbrands Inc.
(Exact name of registrant as specified in its charter)

Maryland	**20-3552316**
(State of incorporation)	*(I.R.S. employer identification no.)*
1000 East Hanes Mill Road **Winston-Salem, North Carolina**	**27105**
(Address of principal executive office)	*(Zip code)*

(336) 519-8080
(Registrant s telephone number including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company) Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

As of October 25, 2010, there were 95,778,117 shares of the registrant s common stock outstanding.

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Trademarks, Trade Names and Service Marks

We own or have rights to use the trademarks, service marks and trade names that we use in conjunction with the operation of our business. Some of the more important trademarks that we own or have rights to use that may appear in this Quarterly Report on Form 10-Q include the *Hanes, Champion, C9 by Champion, Playtex, Bali, L eggs, Just My Size, barely there*, *Wonderbra*, *Stedman, Outer Banks, Zorba, Rinbros* and *Duofold* marks, which may be registered in the United States and other jurisdictions. We do not own any trademark, trade name or service mark of any other company appearing in this Quarterly Report on Form 10-Q.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements include all statements that do not relate solely to historical or current facts, and can generally be identified by the use of words such as may, believe, will, expect, project, estimate, intend, anticipate, plan, continue or similar e particular, information appearing under Management s Discussion and Analysis of Financial Condition and Results of Operations includes forward-looking statements. Forward-looking statements inherently involve many risks and uncertainties that could cause actual results to differ materially from those projected in these statements.

Where, in any forward-looking statement, we express an expectation or belief as to future results or events, such expectation or belief is based on the current plans and expectations of our management and expressed in good faith and believed to have a reasonable basis, but there can be no assurance that the expectation or belief will result or be achieved or accomplished. More information on factors that could cause actual results or events to differ materially from those anticipated is included from time to time in our reports filed with the Securities and Exchange Commission (the SEC), including our Annual Report on Form 10-K for the year ended January 2, 2010, particularly under the caption Risk Factors.

All forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q and are expressly qualified in their entirety by the cautionary statements included in this Quarterly Report on Form 10-Q or our Annual Report on Form 10-K for the year ended January 2, 2010, particularly under the caption Risk Factors. We undertake no obligation to update or revise forward-looking statements that may be made to reflect events or circumstances that arise after the date made or to reflect the occurrence of unanticipated events, other than as required by law.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You can inspect, read and copy these reports, proxy statements and other information at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. You can obtain information regarding the operation of the SEC s Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website at www.sec.gov that makes available reports, proxy statements and other information regarding issuers that file electronically.

We make available free of charge at www.hanesbrands.com (in the Investors section) copies of materials we file with, or furnish to, the SEC. By referring to our website, www.hanesbrands.com, we do not incorporate our website or its contents into this Quarterly Report on Form 10-Q.

PART I

Item 1. ***Financial Statements***

HANESBRANDS INC.

Condensed Consolidated Statements of Income
(in thousands, except per share amounts)
(unaudited)

	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Net sales	$ 1,173,362	$ 1,058,673	$ 3,177,054	$ 2,902,536
Cost of sales	809,487	701,993	2,110,943	1,960,589
Gross profit	363,875	356,680	1,066,111	941,947
Selling, general and administrative expenses	249,815	248,267	743,534	702,204
Restructuring		15,104		46,319
Operating profit	114,060	93,309	322,577	193,424
Other expenses	1,094	2,423	5,128	6,537
Interest expense, net	36,326	42,941	110,394	124,548
Income before income tax expense	76,640	47,945	207,055	62,339
Income tax expense	15,328	6,807	23,818	9,974
Net income	$ 61,312	$ 41,138	$ 183,237	$ 52,365
Earnings per share:				
Basic	$ 0.64	$ 0.43	$ 1.90	$ 0.55
Diluted	$ 0.63	$ 0.43	$ 1.87	$ 0.55
Weighted average shares outstanding:				
Basic	96,496	95,247	96,417	94,880
Diluted	97,752	96,422	97,790	95,469

See accompanying notes to Condensed Consolidated Financial Statements.

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HANESBRANDS INC.

Condensed Consolidated Balance Sheets
(in thousands, except share and per share amounts)
(unaudited)

	October 2, 2010	January 2, 2010
Assets		
Cash and cash equivalents	$ 75,496	$ 38,943
Trade accounts receivable less allowances of $20,316 at October 2, 2010 and $25,776 at January 2, 2010	531,360	450,541
Inventories	1,377,286	1,049,204
Deferred tax assets and other current assets	270,870	283,869
Total current assets	2,255,012	1,822,557
Property, net	596,458	602,826
Trademarks and other identifiable intangibles, net	129,079	136,214
Goodwill	322,002	322,002
Deferred tax assets and other noncurrent assets	452,742	442,965
Total assets	$ 3,755,293	$ 3,326,564
Liabilities and Stockholders Equity		
Accounts payable	$ 461,879	$ 351,971
Accrued liabilities	303,130	295,635
Notes payable	42,651	66,681
Current portion of debt	150,000	164,688
Total current liabilities	957,660	878,975
Long-term debt	1,871,672	1,727,547
Other noncurrent liabilities	387,434	385,323
Total liabilities	3,216,766	2,991,845
Stockholders equity:		
Preferred stock (50,000,000 authorized shares; $.01 par value)		
Issued and outstanding None		
Common stock (500,000,000 authorized shares; $.01 par value)		
Issued and outstanding 95,776,484 at October 2, 2010 and 95,396,967 at January 2, 2010	958	954
Additional paid-in capital	298,930	287,955
Retained earnings	452,043	268,805
Accumulated other comprehensive loss	(213,404)	(222,995)

Total stockholders equity	538,527	334,719
Total liabilities and stockholders equity	$ 3,755,293	$ 3,326,564

See accompanying notes to Condensed Consolidated Financial Statements.

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HANESBRANDS INC.

Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Nine Months Ended October 2, 2010	Nine Months Ended October 3, 2009
Operating activities:		
Net income	$ 183,237	$ 52,365
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	54,232	57,476
Amortization of intangibles	9,046	9,293
Restructuring		6,978
Write-off on early extinguishment of debt	2,340	2,423
Charges incurred for amendments of credit facilities		4,114
Amortization of debt issuance costs	9,724	7,951
Amortization of loss on interest rate hedge	13,732	
Stock compensation expense	8,320	27,637
Deferred taxes and other	(10,224)	(8,422)
Changes in assets and liabilities:		
Accounts receivable	(77,782)	(128,636)
Inventories	(333,132)	159,432
Other assets	9,112	21,380
Accounts payable	109,964	(31,923)
Accrued liabilities and other	(15,643)	30,739
Net cash provided by (used in) operating activities	(37,074)	210,807
Investing activities:		
Purchases of property, plant and equipment	(78,570)	(99,709)
Proceeds from sales of assets	45,469	15,814
Other	(519)	10
Net cash used in investing activities	(33,620)	(83,885)
Financing activities:		
Borrowings on notes payable	991,061	1,169,301
Repayments on notes payable	(1,015,338)	(1,168,799)
Payments to amend credit facilities	(1,688)	(22,165)
Borrowings on revolving loan facility	1,597,500	1,353,525
Repayments on revolving loan facility	(1,459,000)	(1,353,525)
Repayment of debt under 2009 Senior Secured Credit Facility	(59,063)	
Repayment of debt under 2006 Senior Secured Credit Facility		(140,250)
Borrowings on Accounts Receivable Securitization Facility	191,424	176,616

Repayments on Accounts Receivable Securitization Facility	(141,424)	(170,190)
Proceeds from stock options exercised	3,437	376
Other	308	(824)
Net cash provided by (used in) financing activities	107,217	(155,935)
Effect of changes in foreign exchange rates on cash	30	288
Increase (decrease) in cash and cash equivalents	36,553	(28,725)
Cash and cash equivalents at beginning of year	38,943	67,342
Cash and cash equivalents at end of period	$ 75,496	$ 38,617

See accompanying notes to Condensed Consolidated Financial Statements.

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HANESBRANDS INC.

Notes to Condensed Consolidated Financial Statements
(dollars and shares in thousands, except per share data)
(unaudited)

(1) Basis of Presentation

These statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) and, in accordance with those rules and regulations, do not include all information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Management believes that the disclosures made are adequate for a fair statement of the results of operations, financial condition and cash flows of Hanesbrands Inc., a Maryland corporation, and its consolidated subsidiaries (the Company or Hanesbrands). In the opinion of management, the condensed consolidated interim financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the results of operations, financial condition and cash flows for the interim periods presented herein. The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make use of estimates and assumptions that affect the reported amounts and disclosures. Actual results may vary from these estimates.

These condensed consolidated interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s most recent Annual Report on Form 10-K. The results of operations for any interim period are not necessarily indicative of the results of operations to be expected for the full year.

To reflect a change previously made in the classification of freight expenses payable, a revision to the nine months ended October 3, 2009 Condensed Consolidated Statement of Cash Flows was made to reclassify changes in cash related to these payables from Accrued Liabilities and Other to Accounts Payable. This reclassification had no impact on the Company s previously reported total net cash flows from operating, investing or financing activities.

(2) Recent Accounting Pronouncements

Accounting for Transfers of Financial Assets

In June 2009, the Financial Accounting Standards Board (FASB) issued new accounting rules for transfers of financial assets. The new rules require greater transparency and additional disclosures for transfers of financial assets and the entity s continuing involvement with them and changes the requirements for derecognizing financial assets. The new accounting rules are effective for financial asset transfers occurring after the beginning of the Company s first fiscal year that begins after November 15, 2009. The adoption of these new rules did not have a material impact on the financial condition, results of operations or cash flows of the Company.

Consolidation Variable Interest Entities

In June 2009, the FASB issued new accounting rules related to the accounting and disclosure requirements for the consolidation of variable interest entities. The new accounting rules are effective for the Company s first fiscal year that begins after November 15, 2009. The adoption of these new rules did not have a material impact on the financial condition, results of operations or cash flows of the Company.

Fair Value Disclosures

In January 2010, the FASB issued new accounting rules related to the disclosure requirements for fair value measurements. The new accounting rules require new disclosures regarding significant transfers between Levels 1 and 2 of the fair value hierarchy and the activity within Level 3 of the fair value hierarchy. The new accounting rules also clarify existing disclosures regarding the level of disaggregation of assets or liabilities

HANESBRANDS INC.

Notes to Condensed Consolidated Financial Statements (Continued)
(dollars and shares in thousands, except per share data)
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and the valuation techniques and inputs used to measure fair value. The new accounting rules are effective for the Company s first interim fiscal period beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of the disclosures effective for the Company s first interim fiscal period beginning after December 15, 2009 did not have a material impact on the Company s financial condition, results of operations or cash flows but resulted in certain additional disclosures reflected in Note 8.

(3) Earnings Per Share

Basic earnings per share (EPS) was computed by dividing net income by the number of weighted average shares of common stock outstanding during the quarters and nine months ended October 2, 2010 and October 3, 2009. Diluted EPS was calculated to give effect to all potentially dilutive shares of common stock using the treasury stock method. The reconciliation of basic to diluted weighted average shares for the quarters and nine months ended October 2, 2010 and October 3, 2009 is as follows:

	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Basic weighted average shares	96,496	95,247	96,417	94,880
Effect of potentially dilutive securities:				
Stock options	664	205	781	
Restricted stock units	589	970	591	589
Employee stock purchase plan and other	3		1	
Diluted weighted average shares	97,752	96,422	97,790	95,469

For the quarters ended October 2, 2010 and October 3, 2009, options to purchase 606 and 4,612 shares of common stock, respectively, were excluded from the diluted earnings per share calculation because their effect would be anti-dilutive. For the nine months ended October 2, 2010 and October 3, 2009, 0 and 43 restricted stock units, respectively, and options to purchase 606 and 5,871 shares of common stock, respectively, were excluded from the diluted earnings per share calculation because their effect would be anti-dilutive.

(4) Inventories

Inventories consisted of the following:

	October 2, 2010	January 2, 2010

Raw materials	$ 130,573	$ 106,138
Work in process	126,674	100,686
Finished goods	1,120,039	842,380
	$ 1,377,286	$ 1,049,204

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HANESBRANDS INC.

Notes to Condensed Consolidated Financial Statements (Continued)
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(5) Trade Accounts Receivable

Allowances for Trade Accounts Receivable

The changes in the Company s allowance for doubtful accounts and allowance for chargebacks and other deductions for the quarter and nine months ended October 2, 2010 are as follows:

	Allowance for Doubtful Accounts	Allowance for Chargebacks and Other Deductions	Total
Balance at January 2, 2010	$ 15,502	$ 10,274	$ 25,776
Charged to expenses	(107)	6,026	5,919
Deductions and write-offs	(53)	(893)	(946)
Balance at April 3, 2010	15,342	15,407	30,749
Charged to expenses	(1,617)	(1,852)	(3,469)
Deductions and write-offs	(79)	(1,787)	(1,866)
Balance at July 3, 2010	13,646	11,768	25,414
Charged to expenses	914	(632)	282
Deductions and write-offs	(3,433)	(1,947)	(5,380)
Balance at October 2, 2010	$ 11,127	$ 9,189	$ 20,316

Charges to the allowance for doubtful accounts are reflected in the Selling, general and administrative expenses line and charges to the allowance for customer chargebacks and other customer deductions are primarily reflected as a reduction in the Net sales line of the Condensed Consolidated Statements of Income. Deductions and write-offs, which do not increase or decrease income, represent write-offs of previously reserved accounts receivable and allowed customer chargebacks and deductions against gross accounts receivable.

Sales of Accounts Receivable

In March 2010, the Company entered into an agreement to sell selected trade accounts receivable to a financial institution. After the sale, the Company does not retain any interests in the receivables and the financial institution services and collects these accounts receivable directly from the customer. Net proceeds of this accounts receivable sale program are recognized in the Condensed Consolidated Statement of Cash Flows as part of operating cash flows.

The funding fees charged for this program are recorded in the Other expenses line in the Condensed Consolidated Statement of Income.

During the quarter and nine months ended October 2, 2010, the Company recognized funding fees of $1,094 and $2,557, respectively, for sales of accounts receivable to financial institutions in the Other expenses line in the Condensed Consolidated Statements of Income.

HANESBRANDS INC.

Notes to Condensed Consolidated Financial Statements (Continued)
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(6) Debt

The Company had the following debt at October 2, 2010 and January 2, 2010:

	Interest Rate as of October 2, 2010	Principal Amount October 2, 2010	Principal Amount January 2, 2010	Maturity Date
2009 Senior Secured Credit Facility:				
Term Loan Facility	5.25%	$ 690,937	$ 750,000	December 2015
Revolving Loan Facility	4.76%	190,000	51,500	December 2013
8% Senior Notes	8.00%	500,000	500,000	December 2016
Floating Rate Senior Notes	4.12%	490,735	490,735	December 2014
Accounts Receivable Securitization Facility	2.82%	150,000	100,000	December 2010
		2,021,672	1,892,235	
Less current maturities		150,000	164,688	
		$ 1,871,672	$ 1,727,547	

As of October 2, 2010, the Company had $190,000 outstanding under the $600,000 revolving loan facility (the Revolving Loan Facility) under the senior secured credit facility that the Company entered into in 2006 (the 2006 Senior Secured Credit Facility) and amended and restated in December 2009 (as amended and restated, the 2009 Senior Secured Credit Facility), $17,046 of standby and trade letters of credit issued and outstanding under this facility and $392,954 of borrowing availability.

As previously disclosed in the Company s Annual Report on Form 10-K for the year ended January 2, 2010, the 2009 Senior Secured Credit Facility permits the Company, at its option, to add one or more term loan facilities or increase the commitments under the Revolving Loan Facility in an aggregate amount of up to $300,000 so long as certain conditions are satisfied, including, among others, that no default or event of default is in existence and that the Company is in pro forma compliance with the financial covenants in the 2009 Senior Secured Credit Facility. In order to support its working capital needs and fund an acquisition, on September 1, 2010, as permitted by the 2009 Senior Secured Credit Facility, the Company increased the commitments under the Revolving Loan Facility by an aggregate amount of $200,000, increasing the borrowing availability under the Revolving Loan Facility from $400,000 to $600,000. During the quarter and nine months ended October 2, 2010, the Company incurred $1,688 in capitalized debt issuance costs in connection with increasing the borrowing availability under the Revolving Loan Facility. Debt issuance costs are amortized to interest expense over the life of the debt instrument.

On January 29, 2010, in recognition of the lower trade accounts receivable balance resulting from the sale by the Company of certain trade accounts receivable to a financial institution outside the accounts receivable securitization facility that the Company entered into in November 2007 (the Accounts Receivable Securitization Facility), HBI Receivables LLC, the Company s wholly-owned bankruptcy-remote subsidiary that is a party to such facility, gave notice to the agent and the managing agents under the Accounts Receivable Securitization Facility that, as permitted by the terms of such facility, effective February 11, 2010, the amount of funding available under the Accounts Receivable Securitization Facility was being reduced from $250,000 to $150,000. During the quarter and nine months ended October 2, 2010, the Company recognized $0 and $686, respectively, of a write-off on early extinguishment of debt related to unamortized debt issuance costs on the Accounts Receivable Securitization Facility as a result of the reduction in borrowing capacity.

During the quarter and nine months ended October 2, 2010, the Company recognized $0 and $1,654, respectively, of a write-off on early extinguishment of debt related to unamortized debt issuance costs on the 2009 Senior Secured Credit Facility as a result of the prepayment of $57,188 of principal in April 2010. The Company also recognized $0 and $231 in additional charges related to the amendments of credit facilities in

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HANESBRANDS INC.

Notes to Condensed Consolidated Financial Statements (Continued)
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2009 during the quarter and nine months ended October 2, 2010, respectively. These charges are reflected in the Other expenses line of the Condensed Consolidated Statements of Income.

During the quarter and nine months ended October 3, 2009, the Company recognized $2,423 of a write-off on early extinguishment of debt related to unamortized debt issuance costs on the 2006 Senior Secured Credit Facility as a result of the prepayment of $140,250 of principal in September 2009. This loss is reflected in the Other expenses line of the Condensed Consolidated Statements of Income.

During the quarter and nine months ended October 3, 2009, the Company recognized charges of $0 and $4,114, respectively, in the Other expenses line of the Condensed Consolidated Statements of Income, which represent certain costs related to amendments of the 2006 Senior Secured Credit Facility and the Accounts Receivable Securitization Facility.

As of October 2, 2010, the Company was in compliance with all covenants under its credit facilities.

(7) Financial Instruments and Risk Management

The Company uses financial instruments to manage its exposures to movements in interest rates, foreign exchange rates and commodity prices. The use of these financial instruments modifies the Company s exposure to these risks with the goal of reducing the risk or cost to the Company. The Company does not use derivatives for trading purposes and is not a party to leveraged derivative contracts.

The Company recognizes all derivative instruments as either assets or liabilities at fair value in the Condensed Consolidated Balance Sheets. The fair value is based upon either market quotes for actively traded instruments or independent bids for nonexchange traded instruments. The Company formally documents its hedge relationships, including identifying the hedging instruments and the hedged items, as well as its risk management objectives and strategies for undertaking the hedge transaction. This process includes linking derivatives that are designated as hedges of specific assets, liabilities, firm commitments or forecasted transactions to the hedged risk. On the date the derivative is entered into, the Company designates the derivative as a fair value hedge, cash flow hedge, net investment hedge or a mark to market hedge, and accounts for the derivative in accordance with its designation. The Company also formally assesses, both at inception and at least quarterly thereafter, whether the derivatives are highly effective in offsetting changes in either the fair value or cash flows of the hedged item. If it is determined that a derivative ceases to be a highly effective hedge, or if the anticipated transaction is no longer likely to occur, the Company discontinues hedge accounting, and any deferred gains or losses are recorded in the respective measurement period. The Company currently does not have any fair value or net investment hedge instruments.

The Company may be exposed to credit losses in the event of nonperformance by individual counterparties or the entire group of counterparties to the Company s derivative contracts. Risk of nonperformance by counterparties is mitigated by dealing with highly rated counterparties and by diversifying across counterparties.

Mark to Market Hedges

A derivative used as a hedging instrument whose change in fair value is recognized to act as an economic hedge against changes in the values of the hedged item is designated a mark to market hedge.

Mark to Market Hedges   Intercompany Foreign Exchange Transactions

The Company uses foreign exchange derivative contracts to reduce the impact of foreign exchange fluctuations on anticipated intercompany purchase and lending transactions denominated in foreign currencies.

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Notes to Condensed Consolidated Financial Statements (Continued)
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Foreign exchange derivative contracts are recorded as mark to market hedges when the hedged item is a recorded asset or liability that is revalued in each accounting period. Mark to market hedge derivatives relating to intercompany foreign exchange contracts are reported in the Condensed Consolidated Statements of Cash Flows as cash flow from operating activities. As of October 2, 2010, the U.S. dollar equivalent of commitments to purchase and sell foreign currencies in the Company s foreign currency mark to market hedge derivative portfolio was is $12,550 and $38,501, respectively, using the exchange rate at the reporting date.

Cash Flow Hedges

A hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability is designated as a cash flow hedge. The effective portion of the change in the fair value of a derivative that is designated as a cash flow hedge is recorded in the Accumulated other comprehensive loss line of the Condensed Consolidated Balance Sheets. When the impact of the hedged item is recognized in the income statement, the gain or loss included in Accumulated other comprehensive loss is reported on the same line in the Condensed Consolidated Statements of Income as the hedged item.

Cash Flow Hedges Interest Rate Derivatives

From time to time, the Company uses interest rate cash flow hedges in the form of swaps and caps in order to mitigate the Company s exposure to variability in cash flows for the future interest payments on a designated portion of floating rate debt. The effective portion of interest rate hedge gains and losses deferred in Accumulated other comprehensive loss is reclassified into earnings as the underlying debt interest payments are recognized. Interest rate cash flow hedge derivatives are reported as a component of interest expense and therefore are reported as cash flow from operating activities similar to the manner in which cash interest payments are reported in the Condensed Consolidated Statements of Cash Flows.

The Company is required under the 2009 Senior Secured Credit Facility to hedge a portion of its floating rate debt to reduce interest rate risk caused by floating rate debt issuance. To comply with this requirement, in the quarter ended April 3, 2010, the Company entered into hedging arrangements whereby it capped the LIBOR interest rate component on an aggregate of $490,735 of the floating rate debt under the Company s $500,000 Floating Rate Senior Notes due 2014 (the Floating Rate Senior Notes) at 4.262%. The interest rate cap arrangements, with notional amounts of $240,735 and $250,000, expire in December 2011.

Cash Flow Hedges Foreign Currency Derivatives

The Company uses forward exchange and option contracts to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated transactions, foreign currency-denominated investments, and other known foreign currency exposures. Gains and losses on these contracts are intended to offset losses and gains on the hedged transaction in an effort to reduce the earnings volatility resulting from fluctuating foreign currency exchange rates. The effective portion of foreign exchange hedge gains and losses deferred in Accumulated other comprehensive loss is reclassified into earnings as the underlying inventory is sold, using historical inventory turnover rates. The settlement of foreign exchange hedge derivative contracts related to the purchase of inventory or other hedged items are reported in the Condensed Consolidated Statements of Cash Flows as cash flow from operating activities.

Historically, the principal currencies hedged by the Company include the Euro, Mexican peso, Canadian dollar and Japanese yen. Forward exchange contracts mature on the anticipated cash requirement date of the hedged transaction, generally within one year. As of October 2, 2010, the U.S. dollar equivalent of commitments to sell foreign currencies in the Company s foreign currency cash flow hedge derivative portfolio was $53,752, using the exchange rate at that date.

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HANESBRANDS INC.

Notes to Condensed Consolidated Financial Statements (Continued)
(dollars and shares in thousands, except per share data)
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Cash Flow Hedges Commodity Derivatives

Cotton is the primary raw material used to manufacture many of the Company s products and is purchased at market prices. From time to time, the Company uses commodity financial instruments to hedge the price of cotton, for which there is a high correlation between the hedged item and the hedge instrument. Gains and losses on these contracts are intended to offset losses and gains on the hedged transactions in an effort to reduce the earnings volatility resulting from fluctuating commodity prices. The effective portion of commodity hedge gains and losses deferred in Accumulated other comprehensive loss is reclassified into earnings as the underlying inventory is sold, using historical inventory turnover rates. The settlement of commodity hedge derivative contracts related to the purchase of inventory is reported in the Condensed Consolidated Statements of Cash Flows as cash flow from operating activities. There were no amounts outstanding under cotton futures or cotton option contracts at October 2, 2010 and January 2, 2010.

Fair Values of Derivative Instruments

The fair values of derivative financial instruments recognized in the Condensed Consolidated Balance Sheets of the Company were as follows:

	Balance Sheet Location	Fair Value October 2, 2010	Fair Value January 2, 2010
Derivative assets hedges			
Interest rate contracts	Other assets	$ 20	$
Foreign exchange contracts	Other current assets		407
Total derivative assets hedges		20	407
Derivative assets non-hedges			
Foreign exchange contracts	Other current assets	220	207
Total derivative assets		$ 240	$ 614
Derivative liabilities hedges			
Foreign exchange contracts	Accrued liabilities	(1,351)	(107)
Total derivative liabilities hedges		(1,351)	(107)
Derivative liabilities non-hedges			
Foreign exchange contracts	Accrued liabilities	(1,408)	(432)
Total derivative liabilities		$ (2,759)	$ (539)

Net derivative asset (liability)	$ (2,519)	$ 75

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Net Derivative Gain or Loss

The effect of cash flow hedge derivative instruments on the Condensed Consolidated Statements of Income and Accumulated Other Comprehensive Loss is as follows:

	Amount of Gain (Loss) Recognized in Accumulated Other Comprehensive Loss (Effective Portion) Quarter Ended		Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)	Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion) Quarter Ended	
	October 2, 2010	**October 3, 2009**		**October 2, 2010**	**October 3, 2009**
Interest rate contracts	$ (82)	$ (541)	Interest expense, net	$ (4,214)	$ 219
Foreign exchange contracts	(2,387)	(898)	Cost of sales	(514)	(127)
Total	$ (2,469)	$ (1,439)		$ (4,728)	$ 92

	Amount of Gain (Loss) Recognized in Accumulated Other Comprehensive Loss (Effective Portion) Nine Months Ended		Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)	Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion) Nine Months Ended	
	October 2, 2010	**October 3, 2009**		**October 2, 2010**	**October 3, 2009**
Interest rate contracts	$ (499)	$ 17,471	Interest expense, net	$ (13,836)	$ 348
Foreign exchange contracts	(2,096)	(1,768)	Cost of sales	(1,138)	(1,240)
Commodity contracts			Cost of sales		96
Total	$ (2,595)	$ 15,703		$ (14,974)	$ (796)

The Company expects to reclassify into earnings during the next 12 months a net loss from Accumulated Other Comprehensive Loss of approximately $11,287.

The changes in fair value of derivatives excluded from the Company s effectiveness assessments and the ineffective portion of the changes in the fair value of derivatives used as cash flow hedges are reported in the Selling, general and administrative expenses line in the Condensed Consolidated Statements of Income. The Company recognized gains (losses) for the quarter and nine months ended October 2, 2010 related to ineffectiveness of hedging relationships for foreign exchange contracts of $(1) and $6, respectively. The Company recognized gains related to ineffectiveness of hedging relationships for the quarter ended October 3, 2009 of $102, consisting of $75 for interest rate contracts and $27 for foreign exchange contracts. The Company recognized gains related to ineffectiveness of hedging relationships for the nine months ended October 3, 2009 of $246, consisting of $227 for interest rate contracts and $19 for foreign exchange contracts.

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The effect of mark to market hedge derivative instruments on the Condensed Consolidated Statements of Income is as follows:

	Location of Gain (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Income Quarter Ended October 2, 2010	Amount of Gain (Loss) Recognized in Income Quarter Ended October 3, 2009	Amount of Gain (Loss) Recognized in Income Nine Months Ended October 2, 2010	Amount of Gain (Loss) Recognized in Income Nine Months Ended October 3, 2009
Foreign exchange contracts	Selling, general and administrative expenses	$ (1,838)	$ 4,365	$ (1,309)	$ 3,189
Total		$ (1,838)	$ 4,365	$ (1,309)	$ 3,189

(8) Fair Value of Assets and Liabilities

Fair value is an exit price, representing the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company utilizes market data or assumptions that market participants would use in pricing the asset or liability. A three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value, is utilized for disclosing the fair value of the Company s assets and liabilities. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs about which little or no market data exists, therefore requiring an entity to develop its own assumptions.

As of October 2, 2010, the Company held certain financial assets and liabilities that are required to be measured at fair value on a recurring basis. These consisted of the Company s derivative instruments related to interest rates and foreign exchange rates. The Company s defined benefit pension plan investments are not required to be measured at fair value on a recurring basis. The fair values of interest rate derivatives are determined with pricing models using LIBOR interest rate curves, spreads, volatilities and other relevant information developed using market data and are categorized as Level 2. The fair values of foreign currency derivatives are determined using the cash flows of the foreign exchange contract, discount rates to account for the passage of time and current foreign exchange market data and are categorized as Level 2.

There were no changes during the quarter ended October 2, 2010 to the Company s valuation techniques used to measure asset and liability fair values on a recurring basis. There were no transfers between the three level categories and there were no Level 3 assets or liabilities measured on a quarterly basis during the quarter ended October 2, 2010. As of October 2, 2010, the Company did not have any non-financial assets or liabilities that are required to be measured at fair value on a recurring or non-recurring basis.

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The following tables set forth by level within the fair value hierarchy the Company s financial assets and liabilities accounted for at fair value on a recurring basis.

	Assets (Liabilities) at Fair Value as of October 2, 2010		
	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Foreign exchange derivative contracts	$	$ 220	$
Foreign exchange derivative contracts		(2,759)	
Interest rate derivative contracts		20	
Total	$	$ (2,519)	$

	Assets (Liabilities) at Fair Value as of January 2, 2010		
	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Foreign exchange derivative contracts	$	$ 614	$
Foreign exchange derivative contracts		(539)	
Total	$	$ 75	$

Fair Value of Financial Instruments

The carrying amounts of cash and cash equivalents, trade accounts receivable, notes receivable and accounts payable approximated fair value as of October 2, 2010 and January 2, 2010. The fair value of debt was $2,036,470 and $1,881,868 as of October 2, 2010 and January 2, 2010 and had a carrying value of $2,021,672 and $1,892,235, respectively. The fair values were estimated using quoted market prices as provided in secondary markets which consider the Company s credit risk and market related conditions. The carrying amounts of the Company s notes payable approximated fair value as of October 2, 2010 and January 2, 2010, primarily due to the short-term nature of these instruments.

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(9) Comprehensive Income

The Company s comprehensive income is as follows:

	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Net income	$ 61,312	$ 41,138	$ 183,237	$ 52,365
Translation adjustments	8,399	8,047	2,079	16,303
Amortization of loss on interest rate hedge, net of tax of $1,672, $0, $5,476 and $0, respectively	2,519		8,256	
Net derivative activity on qualifying cash flow hedges, net of tax of $(771), $(524), $(540) and $5,800, respectively	(1,162)	(823)	(814)	9,108
Recognition of loss from pension plan settlement, net of tax of $53, $1,227, $53 and $1,227, respectively	69	1,928	69	1,928
Amounts amortized into net periodic cost:				
Prior service cost, net of tax of $3, $3, $9 and $9, respectively	4	4	12	12
Actuarial loss, net of tax of $860, $888, $2,580 and $2,508, respectively	1,297	1,396	3,891	3,938
Comprehensive income	$ 72,438	$ 51,690	$ 196,730	$ 83,654

(10) Income Taxes

The Company s effective income tax rate was 20% and 12% for the quarter and nine months ended October 2, 2010, respectively, and 14% and 16% for the quarter and nine months ended October 3, 2009, respectively.

The higher effective income tax rate of 20% for the quarter ended October 2, 2010 compared to 14% for the quarter ended October 3, 2009 was primarily attributable to a lower proportion of the Company s earnings attributed to foreign subsidiaries in the quarter ended October 2, 2010 which are taxed at rates lower than the U.S. statutory rate. The lower effective income tax rate of 12% for the nine months ended October 2, 2010 compared to 16% for the nine months ended October 3, 2009 was primarily attributable to a discrete, non-recurring income tax benefit of approximately $20 million for the nine months ended October 2, 2010, partially offset by a lower proportion of the Company s earnings attributed to foreign subsidiaries in the quarter ended October 2, 2010 which are taxed at rates lower than the U.S. statutory rate. The income tax benefit resulted from a change in estimate associated with the remeasurement of unrecognized tax benefit accruals and the determination that certain tax positions had been effectively settled following the finalization of tax reviews and audits for amounts that were less than originally anticipated.

The Company and Sara Lee Corporation (Sara Lee) entered into a tax sharing agreement in connection with the spin off of the Company from Sara Lee on September 5, 2006. Under the tax sharing agreement, within 180 days after Sara

Lee filed its final consolidated tax return for the period that included September 5, 2006, Sara Lee was required to deliver to the Company a computation of the amount of deferred taxes attributable to the Company s United States and Canadian operations that would be included on the Company s opening balance sheet as of September 6, 2006 (as finally determined) which has been done. The Company has the right to participate in the computation of the amount of deferred taxes. Under the tax sharing agreement, if substituting the amount of deferred taxes as finally determined for the amount of estimated deferred taxes that were included on that balance sheet at the time of the spin off causes a decrease in the net

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book value reflected on that balance sheet, then Sara Lee will be required to pay the Company the amount of such decrease. If such substitution causes an increase in the net book value reflected on that balance sheet, then the Company will be required to pay Sara Lee the amount of such increase. For purposes of this computation, the Company s deferred taxes are the amount of deferred tax benefits (including deferred tax consequences attributable to deductible temporary differences and carryforwards) that would be recognized as assets on the Company s balance sheet computed in accordance with GAAP, but without regard to valuation allowances, less the amount of deferred tax liabilities (including deferred tax consequences attributable to taxable temporary differences) that would be recognized as liabilities on the Company s opening balance sheet computed in accordance with GAAP, but without regard to valuation allowances. Neither the Company nor Sara Lee will be required to make any other payments to the other with respect to deferred taxes.

Based on the Company s computation of the final amount of deferred taxes for the Company s opening balance sheet as of September 6, 2006, the amount that is expected to be collected from Sara Lee based on the Company s computation of $72,223, which reflects a preliminary cash installment received from Sara Lee of $18,000, is included as a receivable in Deferred tax assets and other current assets in the Condensed Consolidated Balance Sheets as of October 2, 2010 and January 2, 2010. The Company and Sara Lee have exchanged information in connection with this matter, but Sara Lee has disagreed with the Company s computation. In accordance with the dispute resolution provisions of the tax sharing agreement, in August 2009, the Company submitted the dispute to binding arbitration. The arbitration process is ongoing, and the Company will continue to prosecute its claim. The Company does not believe that the resolution of this dispute will have a material impact on the Company s financial position, results of operations or cash flows.

(11) Business Segment Information

The Company s operations are managed and reported in five operating segments, each of which is a reportable segment for financial reporting purposes: Innerwear, Outerwear, Hosiery, Direct to Consumer and International. These segments are organized principally by product category, geographic location and distribution channel. Each segment has its own management that is responsible for the operations of the segment s businesses but the segments share a common supply chain and media and marketing platforms. In October 2009, the Company completed the sale of its yarn operations and, as a result, the Company no longer has net sales in the Other segment, which was primarily comprised of sales of yarn to third parties.

The types of products and services from which each reportable segment derives its revenues are as follows:

Innerwear sells basic branded products that are replenishment in nature under the product categories of women s intimate apparel, men s underwear, kids underwear and socks.

Outerwear sells basic branded products that are primarily seasonal in nature under the product categories of casualwear and activewear.

Hosiery sells products in categories such as pantyhose, knee highs and tights.

Direct to Consumer includes the Company s value-based (outlet) stores and Internet operations which sell products from the Company s portfolio of leading brands. The Company s Internet operations are supported by its catalogs.

International primarily relates to the Latin America, Asia, Canada, Europe and South America geographic locations which sell products that span across the Innerwear, Outerwear and Hosiery reportable segments.

The Company evaluates the operating performance of its segments based upon segment operating profit, which is defined as operating profit before general corporate expenses, amortization of trademarks and other

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identifiable intangibles and restructuring and related accelerated depreciation charges and inventory write-offs. The accounting policies of the segments are consistent with those described in Note 2 to the Company s consolidated financial statements included in its Annual Report on Form 10-K for the year ended January 2, 2010.

	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Net sales:				
Innerwear	$ 512,486	$ 467,577	$ 1,522,553	$ 1,393,904
Outerwear	389,474	328,339	894,653	772,685
Hosiery	37,442	40,978	117,273	131,326
Direct to Consumer	100,327	100,204	278,680	275,058
International	133,633	117,830	363,895	317,541
Other		3,745		12,022
Total net sales	$ 1,173,362	$ 1,058,673	$ 3,177,054	$ 2,902,536

	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Segment operating profit (loss):				
Innerwear	$ 55,804	$ 54,678	$ 219,475	$ 185,346
Outerwear	34,308	38,706	56,631	31,869
Hosiery	11,333	12,781	38,672	42,358
Direct to Consumer	10,446	13,843	18,583	29,189
International	16,754	12,834	42,392	31,971
Other		(462)		(2,272)
Total segment operating profit	128,645	132,380	375,753	318,461
Items not included in segment operating profit (loss):				
General corporate expenses	(11,667)	(20,285)	(44,130)	(62,979)
Amortization of trademarks and other identifiable intangibles	(2,918)	(3,112)	(9,046)	(9,293)
Restructuring		(15,104)		(46,319)
Inventory write-offs included in cost of sales		(269)		(3,516)
Accelerated depreciation included in cost of sales		(118)		(2,392)
Accelerated depreciation included in selling, general and administrative expenses		(183)		(538)

Total operating profit	114,060	93,309	322,577	193,424
Other expenses	(1,094)	(2,423)	(5,128)	(6,537)
Interest expense, net	(36,326)	(42,941)	(110,394)	(124,548)
Income before income tax expense	$ 76,640	$ 47,945	$ 207,055	$ 62,339

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	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Depreciation and amortization expense:				
Innerwear	$ 8,631	$ 8,069	$ 25,847	$ 27,054
Outerwear	5,337	5,489	15,026	16,370
Hosiery	629	979	2,157	3,164
Direct to Consumer	1,589	1,810	4,359	4,172
International	418	561	1,573	1,589
Other		59		187
	16,604	16,967	48,962	52,536
Corporate	3,945	4,173	14,316	14,233
Total depreciation and amortization expense	$ 20,549	$ 21,140	$ 63,278	$ 66,769

	Quarter Ended		Nine Months Ended	
	October 2, 2010	October 3, 2009	October 2, 2010	October 3, 2009
Additions to long-lived assets:				
Innerwear	$ 10,186	$ 8,669	$ 37,326	$ 37,677
Outerwear	6,348	9,515	25,998	47,664
Hosiery	124	146	426	549
Direct to Consumer	2,388	1,498	9,741	7,734
International	504	368	1,763	857
Other				19
	19,550	20,196	75,254	94,500
Corporate	921	1,697	3,316	5,209
Total additions to long-lived assets	$ 20,471	$ 21,893	$ 78,570	$ 99,709

(12) Consolidating Financial Information

In accordance with the indenture governing the Floating Rate Senior Notes and the indenture governing the Company s $500,000 8.000% Senior Notes due 2016 (the 8% Senior Notes) (together, the Indentures), certain of the Company s subsidiaries have guaranteed the Company s obligations under the Floating Rate Senior Notes and the 8% Senior Notes, respectively. The following presents the condensed consolidated financial information separately for:

(i) Parent Company, the issuer of the guaranteed obligations. Parent Company includes Hanesbrands Inc. and its 100% owned operating divisions which are not legal entities, and excludes its subsidiaries which are legal entities;

(ii) Guarantor subsidiaries, on a combined basis, as specified in the Indentures;

(iii) Non-guarantor subsidiaries, on a combined basis;

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(iv) Consolidating entries and eliminations representing adjustments to (a) eliminate intercompany transactions between or among Parent Company, the guarantor subsidiaries and the non-guarantor subsidiaries, (b) eliminate intercompany profit in inventory, (c) eliminate the investments in our subsidiaries and (d) record consolidating entries; and

(v) Parent Company, on a consolidated basis.

The Floating Rate Senior Notes and the 8% Senior Notes are fully and unconditionally guaranteed on a joint and several basis by each guarantor subsidiary, each of which is wholly owned, directly or indirectly, by Hanesbrands Inc. Each entity in the consolidating financial information follows the same accounting policies as described in the Company s consolidated financial statements included in its Annual Report on Form 10-K for the year ended January 2, 2010, except for the use by the Parent Company and guarantor subsidiaries of the equity method of accounting to reflect ownership interests in subsidiaries which are eliminated upon consolidation.

Condensed Consolidating Statement of Income
Quarter Ended October 2, 2010

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Entries and Eliminations	Consolidated
Net sales	$ 1,104,713	$ 113,915	$ 830,265	$ (875,531)	$ 1,173,362
Cost of sales	875,963	43,270	748,701	(858,447)	809,487
Gross profit	228,750	70,645	81,564	(17,084)	363,875
Selling, general and administrative expenses	201,440	20,282	27,784	309	249,815
Operating profit (loss)	27,310	50,363	53,780	(17,393)	114,060
Equity in earnings (loss) of subsidiaries					