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# EDITED TRANSCRIPT

Q2 2020 Herbalife Nutrition Ltd Earnings Call

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**John G. DeSimone** Herbalife Nutrition Ltd. - President

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## CONFERENCE CALL PARTICIPANTS

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**Wendy Caroline Nicholson** Citigroup Inc., Research Division - MD & Head of Global Consumer Staples Research

## PRESENTATION

### Operator

Good afternoon, and thank you for joining the second Quarter 2020 Earnings conference call for Herbalife Nutrition Ltd. On the call today is Dr. John Agwunobi, the company's Chairman and CEO; John DeSimone, the company's President; Alex Amezcuita, the company's Senior Vice President of Finance Strategy and the Investor Relations; and Eric Monroe, the company's Director, Investor Relations.

I would now like to turn the call over to Eric Monroe to read the company's safe harbor language.

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### **Eric Monroe Herbalife Nutrition Ltd. - Director of IR**

Before we begin, as a reminder, during this conference call, we may make forward-looking statements within the meaning of the federal securities laws. These statements involve assumptions and are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those discussed or anticipated. For a complete discussion of risks associated with these forward-looking statements in our business, we encourage you to refer to today's earnings release and our SEC filings, including our most recent annual report on Form 10-K and quarterly report on Form 10-Q. Our forward-looking statements are based upon information currently available to us. We do not undertake any obligation to update or release any revisions to any forward-looking statement or to report any future events or circumstances or to reflect the occurrence of unanticipated events.

In addition, during this call, certain financial performance measures may be discussed that differ from comparable measures contained in our financial statements prepared in accordance with U.S. Generally Accepted Accounting Principles referred to by the Securities and Exchange Commission as non-GAAP financial measures. We believe that these non-GAAP financial measures assist management and investors in evaluating our performance and preparing period-to-period results of operations in a more meaningful and consistent manner as discussed in greater detail in the supplemental schedules to our earnings release. A reconciliation of these non-GAAP measures to the most comparable GAAP financial measures is included in our earnings press release submitted to the SEC. These reconciliations, together with additional supplemental information, are available at the Investor Relations section of our website, [herbalife.com](http://herbalife.com).

Additionally, when management makes reference to volumes during this conference call, they are referring to volume points.

I will now turn the call over to our Chairman and CEO, John Agwunobi.

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### **John O. Agwunobi Herbalife Nutrition Ltd. - Chairman & CEO**

Good afternoon, everyone. I hope that you and your family are staying safe and healthy. With today's release, we announced record-breaking quarterly net sales results for the company. We reported net sales of \$1.3 billion, which grew 8.6%. Reported earnings per share grew 52%, and adjusted earnings per share grew 36% compared to the second quarter of 2019. As part of our pre-release a month ago, we announced that the second quarter of 2020 was also the largest quarter in our 40-year history in terms of volume points, with record results in both our North America and our EMEA regions.



Q2 also saw a record number of new members and preferred members joining the business. As a sign of the confidence that we have in our business and our long-term growth prospects, we announced last month that we made an offer to purchase \$750 million of our common shares. Alex will provide more details on this transaction later in the call.

As the numbers and facts demonstrate, Herbalife Nutrition is performing at an exceptional level, and we believe our distributors' entrepreneurial spirit, combined with our quality line of nutrition products, will lead to continued growth.

From a demand perspective, our business is backed by favorable consumer trends in an environment that has never been more responsive to what we bring to the table.

According to a recent study from [William & Hood], health is the new top global consumer priority. We believe that individuals around the world have a heightened focus on consuming healthy, nutrient-dense foods and supplements. Additionally, individuals who are seeking an economic opportunity are finding our business model to be attractive.

Our distributors are embracing technology to service their customers, which is helping them meet the increase in demand. We are assisting our distributors as they rapidly adopt digital tools, and the positive effects of this are evident in our results. The investments we've made in technology have allowed our distributors and their customers to stay connected when face-to-face interactions are unable to take place. Our ongoing technology strategy is focused on improving distributor scalability, increasing distributor-to-customer connectivity and enhancing the customer experience. We are encouraged to see increased usage of our digital tools, such as HN-connect, HN MyClub and Engage.

Let's dig a little deeper into our top 4 countries. Starting with the U.S., where year-over-year volume points were at an all-time high and grew 38% for the quarter. This growth is a testament to our entrepreneurial distributors, discovering innovative ways to run their businesses during the pandemic. The percentage of our U.S. business growing through distributors who operate a nutrition club model, which represents the majority of our volume in the country, remained relatively consistent with pre-pandemic levels. Although we've seen Nutrition Club operators continue to grow sales by individual prepared consumptions, we have seen them modify their businesses and shift a higher proportion of their sales to home delivery, when face-to-face interactions at clubs have been unable to take place.

Additionally, U.S. distributors have seen more unique customers. The monthly average number of unique customers in the U.S. increased year-over-year by more than 25% in the second quarter.

Moving on to China, where volume points grew 18% compared to the second quarter of 2019. During the quarter, we made further upgrades to our recently developed personal stores platform on WeChat, including new features, such as live streaming and optimization of our landing page. Volume coming from our China service providers and sales representatives personal stores accounted for approximately 23% of total sales in the country. Online meetings and trainings continue to be a focus in the region as the government continued to maintain strict controls over large, in-person social gatherings.

In the first half of the year, we've had over 2 million attend virtual trainings or seminars in China. China's first virtual Extravaganza took place in the second quarter with approximately 81,000 attendees.

India volume decreased by 15% during the quarter but materially improved as the quarter progressed, coming off the lows of a 30% year-over-year decline in April to slight growth in the month of June. Restrictions imposed in the market due to the lockdown resulted in the closures of many access points and disrupted national transportation, impacting product delivery. Towards the end of the quarter, the restrictions began to ease in non-containment zones. And by the end of June, the majority of our product access locations in the market were actually open.

In Mexico, volume points were down 4% in the quarter. And we're encouraged to see a return to growth in new members from Mexico this quarter, with the month of June, representing the largest number of new members in a single month since August of 2017.

I would also like to call out the EMEA region, which set a volume point record and grew 21% in the quarter. The growth came from countries such as Spain, which was up 20%; Turkey, which was up 27%; France, which grew 55%; South Africa, which increased 88%; and the U.K., which grew an astonishing 90%. Members in the region were able to adapt quickly to the new circumstances and transfer their businesses into a virtual environment. Given the continuing impact of COVID-19 on our business and the rapidly evolving landscape in response to these pandemic conditions, we are not providing guidance at this time. However, our year-over-year volume point growth rate improved each month during the second quarter, and we are encouraged that this trend continued in July. We remain confident in the long-term prospects of our business based both on the increasing demand for products we provide and on our focused growth strategy. This confidence is further supported by our strong financial foundation and the substantial investments we've made in our business. We have a proven track record of working through difficult situations, and I fully believe in our ability to overcome current and future challenges.

In closing, I want to thank everyone at Herbalife Nutrition for their hard work and diligence during these extraordinary times.

I'll now turn the call over to Alex to review the financials.

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Thank you, John. Second quarter net sales of \$1.3 billion represented an increase of 8.6% on a reported basis compared to the second quarter in 2019. This was a record for the company despite the 550 basis point currency headwind, driven by the significant strengthening of the U.S. dollar at the end of Q1. Adjusting for the change in foreign exchange rates, net sales for the quarter increased 14.1% year-over-year, excluding the impact from Venezuela.

We reported net income of approximately \$115.1 million or \$0.82 per diluted share. Adjusted earnings per diluted share were \$0.95, an increase of 36% compared to adjusted earnings per adjusted diluted share of \$0.70 for the second quarter last year. The impact of currency fluctuations represented a year-over-year headwind of approximately \$0.08 on results for the second quarter.

Note that our reported and adjusted results this quarter include expenses related to the China Growth program of approximately \$2.3 million or \$0.01 per share.

Reported gross margin for the second quarter of 79.7% decreased by approximately 65 basis points compared to the prior year period. The decrease was primarily driven by increased freight costs related to orders being shifted to home delivery versus member pickup as a result of COVID-19.

Second quarter 2020 reported SG&A as a percentage of net sales was 35.7%, and adjusted SG&A as a percentage of net sales was 35.4%. Adjusted SG&A, excluding China member payments, was 26.3%, approximately 200 basis points lower than the second quarter in 2019. The reduction in expense was largely driven by a decrease in member promotion and event costs as a result of delays, cancellations and reformatting of promotional events due to the COVID-19 pandemic. However, we expect a significant portion of these reduced expenses to be spent in the third and fourth quarter.

Our second quarter reported effective tax rate was approximately 28.5%, and our adjusted effective tax rate was 21.5%, which was lower than the prior year, primarily due to a favorable change in the company's geographic mix of income and a reduction in the income tax rate of certain foreign jurisdictions.

During the first half of the year, we generated \$385 million in cash flow from operations. This is a significant increase over 2019 as many of the timing accounts that negatively impacted cash flow in the first half of 2019 have now reversed. We currently have \$1.7 billion of cash on hand, and our previously announced modified Dutch auction self tender offer to purchase up to 750 million of shares is scheduled to expire on August 11 unless the offer is extended. We continue to believe the repurchase of common shares is consistent with the company's long-term goal of maximizing shareholder value, and this tender offer provides a mechanism to return capital to shareholders who seek liquidity under current market conditions and to allow shareholders who do not participate in the tender offer to share in a larger portion of the company's future potential. If fully subscribed, this offer will reduce our outstanding equity by approximately 10% to 12%.

This concludes our prepared remarks. Operator, please open up the line

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Our first question will come from Wendy Nicholson with Citi.

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### Wendy Caroline Nicholson *Citigroup Inc., Research Division - MD & Head of Global Consumer Staples Research*

Just 2 questions, if I can. First, just on the tender offer. Given that the stock is above the offer range, what's your plan? Is there an expectation that you will bump up that tender range? Or if you'd comment on that, that'd be first.

And then just secondly, thinking about the business, I mean the momentum is fantastic, and I think you've done a great job explaining how important things like the Tencent partnership have been for you. But I guess my question is, we've sort of seen now a couple of other direct sellers also report strong numbers, and it does feel like at least in the U.S. market, there has been this momentum in the industry and maybe because people are at home and feeling entrepreneurial and looking for extra income. So I guess, just my question is, do you think there's something to that from sort of a high-level industry perspective? Or do you really think this is all very much Herbalife specifics and a result of the initiatives that you've undertaken to grow your business? Sorry for the long question, but that's what I'm interested in.

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### Alexander R. Amezcua *Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR*

Thank you. Wendy. And thanks for the good questions. I'll start -- this is Alex. I'll start with the tender offer first. So obviously, the tender offer does not expire until next week, August 11, and so we don't have a crystal ball in terms of what that stock price might be at the end of this tender. So at this point, there's really not much more I can comment on what we might do and so we see where we are. The offer that is out there is the offer that is out there, and we'll see how the coming days play out.

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### John G. DeSimone *Herbalife Nutrition Ltd. - President*

Yes. This is John. I'll take the second question. So I can speak specifically to Herbalife. I mean, I've read the releases of other companies. But at Herbalife, and I'll start with numbers, we announced at the beginning of May that April was down 1% in volume, and we finished the quarter up over 12%, which means incredibly strong May and June. And as Alex said in his remarks, Dr. A said in his remarks, sequentially, May was better than April, but June was even better than May, and that continued into July. So there is a lot of momentum. And I think when you kind of run the numbers, it might even be stronger than what we're seeing in the industry. So I think there is some truth that globally, mainly the industry is doing well for whatever reasons you want to ascribe to it, it's really hard to know, right? But I think we're actually exceeding those industry statistics. And we're doing it pretty much globally. I know there were 3 of 6 regions did not increase in the quarter. But that really was mostly a weak beginning of the quarter. At the end of the quarter, we saw a lot of strength. And a matter of fact, every region in the month of June, new members are up double digits. And Mexico was 30% in June for new members. So that really is, I think, sets us up, at least for the near term, sets us up well. I mean, obviously, long term, the cycle of growth we're seeing now is got to flatten a little bit, but I think it does give us a new foundation.

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### John O. Agwunobi *Herbalife Nutrition Ltd. - Chairman & CEO*

This is John Aguilo. And I would just add to that answer. Or rather, I would just urge everyone to kind of look back at our Q4 2019 and our Q1 2020 results. And you'll see, I believe, that ours is a company that the strategy is working in. It's been working since even before the more recent kind of external issues that have hit the entire marketplace. We're confident in our strategy, and we think that it underlies all of the numbers that you're seeing in Q2 and beyond.

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### Wendy Caroline Nicholson *Citigroup Inc., Research Division - MD & Head of Global Consumer Staples Research*

And just if I can follow-up on that. I think maybe this is a point of clarification. The \$2.3 million that you called out, I think, as incremental investment in China. Is that sort of an update and a sort of constant, whatever, fine-tuning of your investment spending in that market? And I guess the question is to keep the momentum going, how much more spending do you think you're going to need to do to continue to bolster those digital tools and keep them offering something new and compelling to the distributors?



**John O. Agwunobi Herbalife Nutrition Ltd. - Chairman & CEO**

Right. So Wendy, just as a reminder, that \$2.3 million that you've highlighted is investment that comes out of our China Growth and Impact Investment Program. That is monies that we receive from the Chinese government effectively that we commit to reinvest back into China in some way, shape or form. Last year, we spent a lot of that money into our branding. Some of it went into our technology. So it's just some form of investment that we make into China. I want to call that out. I would say that, that's sort of a separate pot of investment that we make when we think about technology and overall infrastructure, so like the Tencent investment, that's part of what I would call a more part of our run rate investments that we're making into China. So kind of 2 separate. We have sort of run rate investments. Those are things like our Tencent partnership. And then there are investments, we have \$105 million remaining in the China Growth fund for other sorts of onetime investments that we make as we receive monies for the China government, we will then invest those monies back into China.

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**Operator**

Our next question will come from Hale Holden with Barclays.

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**Hale Holden Barclays Bank PLC, Research Division - MD**

I guess some of the volume numbers that you posted were just extraordinary. I was wondering if you could just give us some context on and maybe just some specific regions in the Americas and in the U.K. number you gave, what you think is adding to that benefit? And then Dr. A, I heard your comment that it's going to flatten out of a new baseline, but assuming that the current environment stays, how sustainable do you think it is?

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. Look, so -- and by the way, when we're talking about flattening out, what we're seeing is some of these growth rates, I mean, by like, indirect selling in general, growth can be spiky, okay? And you kind of see it step its way up, and this is a stair, we think. And so we don't know when it will come to a more normalized growth rate. But it inevitably will, and I think that was the point. As far as what's driving the growth, it's definitely distributor activity. That activity is being driven by engagement. It's hard to quantify specifically if that's because people are home more or if just people are looking for good nutrition, which is something that's really important these days, there's really lots, there's not one thing and it's just building on itself. And so that's what we're seeing. I can't even be honest with you be more specific than that because it's not one thing.

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**Hale Holden Barclays Bank PLC, Research Division - MD**

I would just ask another way to --

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

I am sorry, I would just add that there are 2 Johns in the room there's John A and there's John D. And I think your comment -- the comments related to flattening in the future came from John D.

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**Hale Holden Barclays Bank PLC, Research Division - MD**

Yes, sorry. I guess maybe if I put it another way, presumably, the higher volume points mean that your distributors are doing better financially, and they're more engaged on a go-forward basis. So how do you guys ensure that this momentum continues when we move to a more normalized state of affairs?

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**John O. Agwunobi Herbalife Nutrition Ltd. - Chairman & CEO**

Yes. So this is John A. I would note that a couple of things. First of all, I do think that on the consumer side, that people's behaviors have changed acutely in response to the pandemic. But I would wager to -- that these -- many of those behavior changes will have some persistence to them, right? There are going to be consumers out there that commit themselves to living healthier and more healthy, active balanced lifestyles in the future, right? So that's number one. On the distributor behavior side, yes, I think our distributors have worked extraordinarily hard over the course of this quarter. And yes, as a result, I think they're seeing -- they'll see that in their rewards. Ours is a business that is built on momentum and what we call the marketing plan, the ability to achieve -- to set goals and to achieve those goals and to be -- they're incremental, those goals build on themselves, as they hit a certain level in the marketing plan they then kind of subscribe and aspire to hitting the next level. So we do expect that the momentum, the energy that is being generated within our

distributor base will continue on into the future. To my colleague, John D's comment, this is a business that kind of has stair steps as it grows. At least traditionally, as we've looked to the past, that's kind of the pattern that we've seen. There's accelerated spurts in growth followed by more moderated growth followed by an acceleration again then in the future. So that's kind of the way it works or at least it has around the world in the past. And I think we should expect to see the same as we go forward.

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**Operator**

Our next question will come from Steph Wissink with Jefferies.

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**Stephanie Marie Schiller Wissink Jefferies LLC, Research Division - Equity Analyst and MD**

I just have a couple of housekeeping questions, and then I'd like to unpack your category performance. But the first question, Alex, is for you. You mentioned some of the savings that you would respense those in the back half of the year. I'm wondering if you can just help us think through the SG&A rate in the back half as you recover some of those savings? And then secondly, I think John DeSimone, you had mentioned that the July month was another month-over-month momentum. Should we anticipate it is better than June? Or it has maintained June's run rate exit?

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Steph, thanks for the questions. I'll actually take -- I'll take both of those questions. So the first on the expense. So in my remarks, I mentioned that our adjusted SG&A, excluding member payments, improved by about 200 basis points over last quarter 2019 or Q2 2019. The expenses that we anticipate being delayed to the back half of the year, if those expenses occurred this quarter that would be about 100 basis points of that 200 basis points. So hopefully, that gives you some idea of magnitude. Related to the second question with respect to July, yes, in fact, that is what we're saying. We're saying the growth rate that we saw in July is in excess of the growth rate that we had in June.

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**Stephanie Marie Schiller Wissink Jefferies LLC, Research Division - Equity Analyst and MD**

Excellent. And then I want to unpack your category performance. It looks like your sports fitness business and even your Targeted Nutrition business were both extremely strong, both up in the mid-teens. Can you talk a little bit about what you're seeing within those businesses? Are you gaining new customers? Are customers entering the brand in those 2 areas and then traveling across the category portfolio? Maybe give us some perspective on what you're seeing kind of within your category performance.

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. I mean, obviously, sports nutrition and Targeted Nutrition are on a relative basis to our weight management part of the portfolio, a smaller piece of the portfolio. So when you see overall, our company growing at the growth rates that you are seeing when you have that amount of growth on the smaller base, it's just -- I think if you look at our sports nutrition category, generally, quarter-over-quarter, you're seeing that double-digit growth even when we are experiencing more moderate levels of growth. So I just think this is an attractive categories. Obviously, sports nutrition is a big opportunity. We talk about sports nutrition and targeted nutrition as being the big opportunities for us to penetrate with us having market-leading position in the weight management side. And so this is just very much on trend with the strategy, the second pillar of our strategy, technology being the other.

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**Operator**

Our next question will come from Doug Lane with Lane Research.

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**Douglas Matthai Lane Lane Research - Principal & Director of Research**

Just to start, Alex, when you call out the \$6.1 million of COVID expenses, what exactly are those kind of expenses?

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. So those are expenses that we have to do -- that we have to perform today above and beyond what normal operations are. So for example, sanitation, for example, compensation for employees going above and beyond what they would have to do in a non-pandemic situation. Expenses like you might have just seen in our recent press release where we had to cancel the LA Triathlon, the Herbalife Nutrition LA Triathlon, and we had some costs that were sunk into that, that now there's no return on that investment. So we had to -- so those are just sunk expenses. So it's those types of things that we're experiencing as it directly relates to COVID-19 impact.





**Douglas Matthai Lane Lane Research - Principal & Director of Research**

Okay. Got it. And then just a follow-up on the product question. I think in the last call, you were talking about some of your immunity products being particularly strong, immunity essentials, things like that. Is that still the case? Or is the strong volume really broad-based at this point?

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. I would say the strong volume is broad-based. Again, it's a little bit of the answer that I just gave to Steph. Clearly, Targeted Nutrition is growing at a double-digit rate. And so part of that portfolio does include our immunity products. So we're encouraged to see that growth in those areas, those new market areas for us. But the growth, if you look across the portfolio, I would say, is broad-based.

**Douglas Matthai Lane Lane Research - Principal & Director of Research**

Okay. Fair enough. And then lastly, Dr. A, I appreciate your comments on the momentum of the business, which seems to be pretty common across direct selling where you see momentum build and then it eases a little bit in particular regions, and that I totally get. So the question I have is with your Asia Pacific region, which has been growing double digits for the last 2 years plus, and all of a sudden it went negative this quarter. And I know you talked about India being down 15%, but there's got to be something more than just India there.

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

India is -- by the way, just to be very clear, when you look at our global business and the impact that the pandemic has had on it, by any accounts, APAC has been under that umbrella, longer than any other region in our business. It started there. And places like Korea, India, Indonesia and a few other locations have been particularly impacted by their government's responses to the pandemic. India, especially, I think. So let me hand this off to John D. and he'll jump in with a little more detail. But I would just kind of point to the fact that it is principally COVID-related and -- with India in the forefront.

**John G. DeSimone Herbalife Nutrition Ltd. - President**

Yes. And just kind of to profile it out a little bit. As we said in the May call that Asia was hit specifically hard because of some of the infrastructure challenges in many of those countries, it's not just India. But Indonesia, Korea. And so in June, the end of the month, Asia actually had growth again. And so it was really much of a -- much more of a -- you can see that in April when we released volume was down almost 14% in Asia, and it finished only down 5% in Q2. So it definitely had some momentum that built during the quarter or momentum might be the wrong word. It's probably more -- it was a solution-oriented set of programs that we put together in Asia to overcome some of the challenges. And so I think that was very successful and India itself was actually flattish in exiting the quarter.

**Operator**

Our next question will come from Ivan Feinseth with Tigress Financial.

**Ivan Philip Feinseth Tigress Financial Partners LLC, Research Division - Director of Research**

And congratulations on another great quarter. All right. So were there any specific standout products in the quarter? And also any products that surprised you as far as the demand or lack of demand? And were there any products that you ran low on or ran out of and had shortages that if you had more, you would have done better?

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Well, so look, there was no major surprises. We had some product launches. They did pretty much as expected. But I will say there were some product shortages because demand was higher-than-expected from the lead time that we need to build product, especially for some of the products that are not made by us, and some of those manufacturers have their own issues because of closures and things like that. So towards the end of the quarter, we definitely had some out of stocks. I think we recovered it pretty quickly. Whether that ended up being lost sales or not, I'd rather not say, I think, whether that was redirected to other products temporarily or it was caught up later in the quarter, I'm not sure. But there was definitely some out of stock issues, which is not unexpected when you have such a dramatic shift in trends.



**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

Any products that you thought were going to sell well, but didn't?

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**Alexander R. Amezcua *Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR***

No, no. No surprises. No surprises. Not that I'm aware of.

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**John O. Agwunobi *Herbalife Nutrition Ltd. - Chairman & CEO***

And to your point, the other question about whether or not there's one that did more better than expected. Across the board, we've seen across all categories. If that's a surprise, that's the fact that across all our categories have seen really good growth.

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

And then as far as, let's say, tools that your agents are using since more, almost everybody has had to go to more online rather than in-person meetings. What kind of process have you learned from that and thoughts of putting new platforms in place to support sellers going forward?

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

Yes. This is John D. Let me hit what I think is one of the more important takeaways from the movement toward more technology. That was really forced upon everybody. Certainly, it's a virtual world and our distributors have embraced that. But I think the bigger takeaway is that out of the need for more technology, there was a -- I think there was more demand for segmentation. As you know, we segment our business in a small number of markets. And now we have plans that by the end of next year, volume or 80% of the volume, maybe even up to 90% of our volume will come from markets that have segmented. And so that's a big advantage that's coming out of what I think is just the increased use of technology. There's lots of different kinds of technology. As market segment, they'll have access to the different technologies that are out there.

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

When you say more segmented markets, you mean as far as product lines that sell well? Or...

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

No, it's a preferment. I'm sorry. So there's a little history here. Some terms that are -- maybe it's outdated, but there was a point in time where everybody who signed up was a distributor. And then we segment that to have just customers to be able to sign up with just customers and not do the business. And that was...

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

No, no, I'm familiar with that...

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

So yes. So that -- having the option to sign up as just a customer is something that will be in markets that represent 80% to 90% of our volume by the end of next year. There's a lot of technology that goes into programming and getting it executed. That's why it takes till the end of next year. But that's a big step forward.

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

And as far as increases in new distributors, what areas have you seen driving that? And what products did new distributors tend to lead off with or focus on?

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

Yes. I think the most important part of the new distributor equation that we're seeing is our distributors getting younger. We're getting a lot more millennials and Gen Zers than we've had in the past. And we already saw that movement starting, but it's even bigger now. Even in Mexico, now the majority of new members joining are millennials or younger, and that was a market that was not quite there 1 year ago. So that's a big advantage. And so that's the demographics we see coming in. I'm not familiar with -- off the top of my head, whether their product portfolio purchases is different than the average. Certainly nothing stands out in my mind, but I'm just not that familiar with

it, I'll track it that way. But that's really the single biggest advantage of what I would say is the demographics coming into the business right now.

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

And what do you think is driving that?

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

Well, I mean, again, it kind of I think goes back to the question that was asked earlier, which is what's driving the business. And there is no one thing. I think there's a lot of momentum. I think the awareness of the importance of good nutrition has never been better. And so I think our product line more than anything is probably what's driving it, or at least what's helping distributors get confident and drive the business is people -- we have solutions to real issues around obesity and around out healthy, active lifestyle and basic nutrition. So I think that's probably the most important thing.

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

Do you think the younger people are coming on as distributors or younger people are coming on as customers and the younger people if they're coming on as distributors are coming because they're more entrepreneurial and looking for the business opportunity?

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

Well, I think across the board, we're getting younger, both on the customer side and the distributor side. I don't want to compute what that -- what their goal is. I mean, a lot of them come in as customers first and then move over to the distributor side. I do think the business opportunity is attractive. I think there's a lot of momentum and excitement. And so that's part of it, but there's a whole host of reasons that people join. But again, products, the service might be the engine of the company but the products are the fuel.

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**Operator**

Our next question will come from Karru Martinson with Jefferies.

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**Karru Martinson *Jefferies LLC, Research Division - Analyst***

Just in terms of the unique customer increase that you had in North America, the 25%. We've touched on the technology, but could you talk to us how are the distributors reaching that connectivity so that they can actually retain these customers who perhaps have tried your products here in the pandemic for the first time. How do you keep that customer in-house going forward?

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**John G. DeSimone *Herbalife Nutrition Ltd. - President***

Look, our technology segment -- I mean, I'll give you a multilayer answer. So first is segmentation, which allows customers to sign up, which gives informational access to the distributors to be able to stay in contact with them. Then as the tools built around segmentation to help automate some of the opportunities to keep engagement high. And then, of course, there is the receding tools that are made available, certainly in the U.S., but they're outside the U.S. now, and they're going to be in a lot more markets, where there's a lot more transaction, field level transactions that are captured in a database that can be used to keep that interaction more frequent. It's more about community and connectivity, and it will be a little bit more -- the information will be more available with these tools.

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**Karru Martinson *Jefferies LLC, Research Division - Analyst***

Okay. And when you talked about the SG&A rate in the second half, we have the 100 basis point shift being higher. Is that kind of a return to some of your in-person sessions? Or how do we think about what the pandemic lockdown is going to do on that side of the equation? Or is that something that we should look at for next year?

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**Alexander R. Amezcua *Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR***

Yes. It's not necessarily return to in person. I think primarily, that is just a shift from what was going to be in person in Q1, Q2, moving to virtual events or virtual different types of promotions that are just largely hitting in Q3 and Q4. What needs to happen effectively is there needs to be an absorption by the distributor base in a particular market of, okay, if we can't go with plan A, we want to go with plan B and C. And so it just takes some time to develop what those new promotions and what those new events might be. And so what was going to happen in the second quarter is now just happening later in the year as those plans are being developed.

**Karru Martinson Jefferies LLC, Research Division - Analyst**

Okay. And just lastly, the higher freight costs you referenced as you shift to more residences. Is that something that, over time, you kind of negotiate those costs down? Or is that just a new part of the business that we just have to absorb?

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

It's not necessarily a new part in of itself. I mean, what we're seeing, and this is a little bit in John A's comments. So for example, in the U.S., where you had Nutrition Club distributors or distributors that own a Nutrition Club, they effectively represented about the same amount of volume in the quarter, but they shifted the way that they received product and got product to their customers from in person or from -- to more of a direct ship to home. So you're using home delivery in that vehicle to get products from effectively our warehouse to the customers. So what is -- what we don't know yet is as things evolve as these conditions evolve, how are we going to offset? How are we going to think about? Is this the new way? Is this the new shift in our -- in shipping? Or do we return back to effectively how our supply chain was designed to be optimal. So we're going to have to just -- this is something that we're going to have to see how that develops and react accordingly.

**Operator**

Ladies and gentlemen, thank you for participating in today's question-and-answer session. I would now like to turn the call back over to Dr. John Agwunobi for any closing remarks.

**John O. Agwunobi Herbalife Nutrition Ltd. - Chairman & CEO**

Thank you. I'll keep this short. First, thank you all for the work that you do following us and for your questions today. I'll just kind of point out the obvious here for a quick moment. And that is ours is a company that's been -- this had a strategy that's been in place for quite a few years now, at least over the last 24 months, I would ask you to take a look at the trajectory of our business. You'll begin to note that the business and the strategy we're working even before the pandemic. It's true, and I think appropriate to state that during the pandemic, that strategy's impact would appear to have accelerated. That strategy continues to work. We continue to drive it. And even after the pandemic, we feel really confident that our strategy is going to deliver on our goals.

With that, I would just point out one last thing, which is there are a number of -- I think it's worth noting that our distributors around the world have worked extraordinarily hard over the last quarter, over the last 2 quarters, actually over the last 4 quarters. And their work is directly related to the results that we're talking about today. So with that, I'll just say thank you. Stay safe, and see you soon.

**Operator**

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

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