

FINAL TRANSCRIPT

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HLF - Q3 2008 Herbalife Ltd. Earnings Conference Call

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PRESENTATION

Operator

Good morning and thank you for joining the third-quarter 2008 earnings conference call for Herbalife. On the call today is Michael Johnson, the Company's Chairman and CEO; Des Walsh, Executive Vice President; Rich Goudis, the Company's CFO; and Brett Chapman, the Company's General Counsel.

I would now like to turn the call over to Brett Chapman to read the Company's Safe Harbor language. You may read, sir.

Brett Chapman - Herbalife Ltd. - General Counsel

Good morning. Before we begin and as a reminder, during this conference call, comments may be made that include some forward-looking statements. These statements involve risk and uncertainty and as you know, actual results may differ materially from those discussed or anticipated. We encourage you to refer to yesterday's earnings release and our SEC filings for a complete discussion of risks associated with these forward-looking statements and our business.

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 US 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 and comparing period-to-period results of operations in a more meaningful and consistent manner. Please refer to the Investor Relations section of our website, herbalife.com to find our third-quarter press release containing a reconciliation of these measures. And now I will turn it over to Michael.

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Michael Johnson - Herbalife Ltd. - Chairman & CEO

Thanks, Brett. Good morning, everyone, on Election Day in the United States and to our friends worldwide, welcome to our third-quarter 2008 earnings call. These are interesting times. Our credit markets are in turmoil. Our financial failures are abounding and the US unemployment is projected at the highest level since the 1980s. As we consider the big picture and the economic challenges here and around the world, it has been and will likely continue to be, for some time, a punishing operating environment for many companies in many industries. Herbalife will not be immune, but let me address why we believe our business offers compelling advantages in this environment.

At Herbalife, we offer product solutions, which address the global obesity epidemic and we provide a business opportunity that enables people the opportunity to earn part-time and full-time income in one of the most uncertain economic times in history. We offer a healthy meal for around \$2.00, a much healthier and lower-cost alternative than most fast food options.

In addition, our business is globally diversified, operating in 69 markets. We have significant revenue and growth opportunities throughout Asia, Latin America, Eastern Europe and here in the US as our distributors dive deeper into penetration into their markets. And they focus on business methods that create daily consumption of our products.

During the quarter, our top 10 markets grew 21% year-over-year and four of our top 10 markets grew at an accelerated pace. We believe the reasons we are successful in these chaotic times is the focus on daily consumption methods that provide a sticky customer, resulting in higher retail and retention figures.

We continue to see markets that are evolving to a better balance of recruiting, retailing and retention by focusing on daily consumption models. Markets such as the USA, Brazil, Taiwan and now Korea have all benefited from this ongoing conversion to daily consumption.

Moreover, our products' low price point on a per-serving basis helps our distributors attract new customers who are looking for weight management and good nutrition at an attractive price. And in this weak economic climate, many consumers are looking for ways they can trade down on their purchases.

We had revenue of \$602 million, which reflects our 19th consecutive quarter of double-digit revenue growth and one which we generated almost \$80 million in cash flow from operations, an increase of 19% year-over-year. We did not repurchase shares during the quarter considering the market volatility and a desire to pay down debt remained conservatively capitalized during this period of uncertainty in the credit markets. We have an undervalued balance sheet, underleveraged balance sheet, excuse me, little or no reliance on the capital markets and we are self-funded from strong free cash flow generation.

In a normalized market, we would be buyers at these levels during the quarter. We look to make opportunistic purchases of our stock when market volatility wanes and we believe the valuation is dislocated from the fundamentals.

Net income for the quarter was \$58 million, an increase of 20% compared to a year ago. We reported diluted earnings per share of \$0.89, reflecting an earnings growth of 33%. While earnings per share was ahead of expectations in the third quarter, we were increasingly impacted by the unprecedented fluctuations in foreign exchange rates, as well as a slowdown in volume point growth in a few of our top markets.

Foreign currency headwinds are a consequence of the global economic crisis. However, our volume slowdown reflects issues that are unique to Herbalife. Going forward, to assist investors, we will provide volume point growth guidance, as well as foreign exchange assumptions for the key currencies, which could affect our financial results.

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Despite solid positioning throughout many of our markets, we are actively refining our growth and profitability plans to address the global market changes. We anticipate, at current spot rates, currency headwinds are going to have a negative impact on revenue and earnings per share in the fourth quarter of 2008 and potentially throughout 2009.

Additionally, we may experience inconsistent volume growth in certain markets, primarily reflecting the transition within these markets to the daily consumption model. In the face of these unprecedented times in the economy, the opportunity for ongoing top-line success speaks volumes to the dedication of our distributors. Many of our distributors started or increased their business in tough economic times and we believe their unwavering commitment will allow them to continue to grow their business.

During these times of unprecedented foreign exchange volatility and slower volume in a few key markets, we considered not providing guidance at this time, but we thought that given the stability of our business model and positive trends in several of our top markets, coupled with the development of our profit improvement plan, we wanted to provide a floor for the 2009 earnings. Therefore, our initial earnings per share guidance for 2009 is \$3.00 to \$3.20, reflecting our current volume point trends along with current spot foreign exchange rates. While we are not sure where this foreign exchange volatility will settle out, it is our goal to be more profitable and generate higher cash flow from operations in 2009 compared with 2008.

We are currently developing a profit improvement action plan, which will include appropriate reduction of expenses, organization changes and savings within our supply chain to help us achieve this goal and mitigate further foreign exchange erosion.

Our cost structure is highly variable, which we believe will help us weather slower top-line growth periods and still allow us to produce significant levels of cash flow. Additionally, our focus on continuous improvement allows us to reduce discretionary spending while refocusing and prioritizing investment behind distributor initiatives. We anticipate concluding these plans in early December and reviewing them with the Board and sharing them with our investors at our Investor Day December 16 in New York.

Herbalife is a fantastic business. For the past 28 years, our distributor leaders have successfully weathered economic downturns. We believe our business is well-positioned to take advantage of this uncertainty by providing a healthy meal at an attractive price, as well as a means of addressing the obesity epidemic, which plagues the world.

But success will not come from sitting back and waiting. It will come from taking positive and proactive steps. We will continue to work closely with our distribution team to help them even be more successful in 2009. Now let me turn it over to Des who will discuss volume and provide in-depth update in key markets.

Des Walsh - Herbalife Ltd. - EVP

Thank you, Michael. Before I begin my prepared remarks, I would like to take the opportunity to thank our distributors and employees for their dedication and hard work during the third quarter. Without their positive attitude and resilience in the face of these turbulent economic times, we would have been unable to lay the foundation for success in coming quarters and they will play an integral role in the continued transformation of our business to one that provides greater consumer access to daily consumption of our products and a healthy meal at an attractive price point.

Let me now share some insights on key business trends in key business markets, including the US, Mexico, China, South America, Taiwan and Korea. Our results in the US market were above expectations in the quarter and bucked the negative consumer market cycle, validating how well our business can perform in challenging economic times. The US market remains our largest market and net sales increased 23% year-over-year, reflecting an acceleration of 3% sequentially from the second-quarter growth rate.

During the third quarter, 66% of the US volume came from our Latino distributors, which grew 27% year-over-year, reflecting the ongoing momentum we have experienced by Latino distributor leadership since the introduction and evolution of Nutrition

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Clubs in late 2004. Our general market business comprised 34% of the US business in the quarter and grew 3% year-over-year, which also experienced a slight increase sequentially from the second quarter of 2008.

We are also seeing the emergence of Nutrition Clubs in the general market, indicating the commitment of both our general market and Latino distributors to provide improved consumer access to a healthy meal at attractive price in communities throughout the US.

Volume points for the top 25 metro areas in the US were up 23% year-over-year, growing at a faster rate than the total US market that grew at 18%. The top 25 metro markets for the Latino market experienced volume point growth of 27% versus a year ago while the general market's top 25 metro markets experienced a year-over-year volume point growth of 11%.

While each segment grew at a faster rate than the overall Latino and general markets, we have seen three consecutive quarters of our non-top 25 metro markets showing sequential volume growth. We believe this trend is due to initiatives we have put in place, such as our relationship with the AYSO, which helps us more deeply penetrate the US market. We expect this trend to continue into 2009.

Now onto Mexico. Mexico, our number two market, reported third-quarter net sales growth of 3%. Excluding the favorable impact from currency, sales declined 3%. We believe the decline in local currency sales in Mexico is primarily attributable to a 15% VAT that had been newly levied by the Mexican government on the import and resale of certain products. This newly leveled VAT impacts approximately 60% of our volume in the Mexican market and follows a 2.5% price increase in May, which, together, had a meaningful impact on demand since the Company began passing on the VAT in August.

For the four months prior to implementing the VAT, volume in Mexico increased 1% over the prior year. However, August and September were 8% and 17% below the prior year respectively. We believe that most of our products should not be subject to VAT and we, along with other industry participants, are in the process of challenging the Mexican government's VAT change.

However, given the effective price increase created by the VAT, we don't anticipate volume point growth in Mexico until the back half of 2009, unless the VAT issue gets resolved sooner than we anticipate. We continue to work closely with our Mexican distributor leadership to help support our combined initiative to more deeply penetrate this market.

Now onto China, our number four market in terms of net sales. During the quarter, China reported third-quarter net sales growth of 87%, up 6% sequentially. In local currency growth, net sales were up 70%. During the quarter, results were negatively impacted by the Olympics as the Chinese government did not allow us to host meetings at our retail stores during the period leading up to and during the event.

During the quarter, we received five additional direct selling licenses from the Chinese government. While it is difficult to quantify the impact of these licenses in the near term, we believe these expanded licenses provide enhanced sales employee confidence, increases our competitiveness in the market and provides credibility with both consumers and with Chinese government relations.

Additional provincial licenses, coupled with increases in our store base and improved store productivity, along with the potential introduction of the Nutrition Club concept and our preferred retail program, should act as continued catalysts for growth as we head into 2009. However, we continue to pursue a better balance of recruiting, retailing and retention. During this transition period, we therefore anticipate continued sequential net sales growth rates to slow.

South America is comprised of seven markets and as a whole, this region's sales growth slowed, primarily reflecting a slowdown in Venezuela and Argentina, offset by accelerated growth in Brazil. First, the positive story. In Brazil, we are pleased to deliver on our expectation of positive local currency sales growth that increased 28% year-over-year for the quarter. Including the benefit from currency, Brazil reported third-quarter net sales growth of 47%. Brazil is a good example of a successful market shift from a recruiting-based model to a consumption-based model.

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Among those distributors who have been using the Nutrition Club DMO for more than a year, volume points were up 46% during the quarter and 32% year-to-date. In addition, we remain encouraged with the growth of and refinement to the Nutrition Club DMO. Our traditional business within Brazil also remained strong, so the Nutrition Club growth is now incremental growth for Brazil.

In Venezuela, we face the unique situation arising from the country's currency restrictions and high inflationary rates. To address this issue, we raised prices approximately 50% during the year in order to keep up with rising costs. Additionally, the volatility of the parallel exchange rate, as compared to the official rate, coupled with our inability to get cash out of Venezuela on a timely basis, has created a difficult business environment for the distributors residing outside Venezuela, but having sales within the country. These factors have resulted in a 35% decline in volume points. We continue to work with local distributor leadership to identify investments and sales initiatives, which will help increase recruiting.

Argentina had negative local currency net sales, volume point declines and decreases in new supervisors during the quarter. This country has seen socioeconomic disruptions and we believe is transitioning to a better balance of recruiting, retailing and retention, much like Brazil did in late 2006. We believe this transition will take some time, but in the long run, will produce a more stable market.

Now I want to close with a few comments on Taiwan and Korea. In previous calls, we alluded to the growth in Taiwan being driven by the addition of Nutrition Clubs. In the quarter, our distributors opened the 1000th Nutrition Club in Taiwan and the clubs have contributed greatly to the growth and stability in the market.

While this market has one of the highest volume points per capita ratios for the Company at just over six versus an average of 1.14 for the entire company, Taiwan produced 6% year-over-year volume point growth in the quarter. The question for many of you has been whether distributors in other Asian countries could be successful in acculturating these clubs to their own countries.

We are delighted to report that in Korea in just the last year, over 500 Nutrition Clubs have opened. We believe that these clubs are a significant factor in Korea's 44% year-over-year volume point growth in the quarter. Based on these successes, other distributors throughout Asia are now embracing the Nutrition Club model that we believe will help accelerate the adoption of this daily consumption business method companywide. Now I will turn over to Rich for an update on the financials.

Rich Goudis - Herbalife Ltd. - CFO

Thanks, Des. Let me briefly walk you through the third-quarter financial results, provide you with financial guidance for the fourth quarter and full year 2008, along with our initial guidance for the full year 2009 and explain key assumptions underlying the guidance. Then we will open it up, the call, for your questions.

Net sales of \$602.2 million in the third quarter were up 13.7% versus the third quarter of '07. FX had a 487 basis point favorable impact during the quarter, reflecting the fact that 80% of our sales are derived outside the US. Last quarter, we started providing investors with a listing of our top 10 markets in terms of net sales by quarter for the past three years. This quarter, we have expanded our disclosure to include local currency net sales as well. You can find this information on our website at www.herbalife.com under the Investor Relations tab.

On a reported basis, gross profit in the third quarter was \$485.6 million or 80.6% of net sales. This is an increase of 63 basis points compared to the third quarter of 2007. The improved margin was the result of country mix, approximately 13 basis points, and foreign currency fluctuations, approximately 50 basis points.

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Royalty expense in the third quarter was \$200.3 million, or 33.3% of sales, reflecting an improvement of 195 basis points compared to last year. Normalizing for the China sales employee expense, which, as you know, is recorded in SG&A, the royalty rate would have improved 59 basis points, primarily reflecting the timing of certain distributor promotions.

SG&A was \$196.8 million, or 32.6% of sales. Again, normalizing for the China sales expense, SG&A expense was \$176 million or 29.2% of sales, an increase of 90 basis points versus last year. The increase primarily reflects higher salary expense, primarily due to merit increases and compensation associated with full-time employees in China. Additionally, higher advertising and promotion expenses, higher sales event expenses, primarily reflecting the timing of events, higher net foreign exchange costs and higher depreciation and amortization, which relates mostly to the development of our technology infrastructure and the expansion and relocation to new facilities all contributed to the increase in year-over-year SG&A.

Third-quarter operating income was \$88.5 million, or 14.7% of net sales, reflecting a decrease of nine basis points compared to last year. Third-quarter interest expense was \$3.4 million versus \$2.7 million in the third quarter of last year. The increase primarily reflects a higher average net debt balance as we used our excess cash and our revolver to repurchase stock over the past year and was partially offset by lower interest rates. The weighted average interest rate on our debt was 5.08% in the quarter versus 6.54% in the third quarter of 2007.

I want to remind investors that we do not need our credit facilities to finance our day-to-day business and that our facility doesn't expire until 2012.

Our third-quarter effective tax rate decreased to 31.7% compared to 36% a year ago, primarily due to the decrease in the operating effective tax rate reflecting country mix, the tax holiday in China, the lack of stock option exercises and the favorable impact of our global entity structuring and planning.

Net income was \$58.1 million in the quarter, an increase of 20.2% compared to the year ago. Third-quarter diluted earnings per share was \$0.89 compared to \$0.67 in the third quarter, reflecting an increase of 33%.

Now let's turn to the balance sheet. We ended the third quarter with \$149.4 million in cash and \$326.2 million in outstanding debt. Our inventory increased \$7.9 million from December 2007, primarily to support sales growth. And in terms of efficiency, our inventory days on hand increased two days year-over-year, while inventory turnover decreased to 2.94 times versus 2.97 times a year ago.

In the quarter, we invested \$32.6 million in capital, primarily in technology investments such as Oracle and BizWorks to support improvements in distributor services. Over the past four months, we successfully upgraded our existing Oracle applications and went live with Oracle in Mexico, Central America and South America and just this past weekend, we went live in Brazil. We now have nearly 60% of our revenue transaction entirely on the Oracle platform. We anticipate going live with Oracle in Asia-Pacific, excluding China, in January 2009 and we will finish with EMEA in April of 2009.

Now let's move on to guidance, which we expanded a bit to give you better insight into the potential impact from foreign currency volatility and volume trends. For the fourth quarter, we expect diluted earnings per share to be between \$0.65 and \$0.70 on volume points flat to down 3% and net sales declines of 6% to 8% compared to the same period in '07 respectively, reflecting late October FX rates and an effective tax rate of 28% to 28.5%.

Based on our fourth-quarter guidance, we are lowering our full-year 2008 diluted earnings per share guidance to the range of \$3.50 to \$3.55 on volume point growth of 4% to 5% and revenue growth of 10% to 11%, coupled with an effective tax rate of 28% to 28.5%. Our fourth-quarter 2008 and full-year 2008 tax rate excludes a potential \$6.5 million non-cash charge for the write-off of certain deferred tax assets in connection with the Company's ongoing legal entity capital structuring.

For the full year 2008, capital expenditures are expected to be in the range of \$100 million to \$105 million, again primarily reflecting investments in Oracle.

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The Company's initial diluted earnings per share guidance for 2009, as Michael said, is a floor of \$3.00 to \$3.20 on volume point growth of 4% to 5% and net sales flat to up 1% compared to 2008 respectively, reflecting late October FX rates, coupled with an effective tax rate of 27.5% to 28.5%. Additionally, full-year 2009 capital expenditures are expected to be in the range of \$55 million to \$60 million, reflecting the conclusion of our initial rollout of Oracle.

During the past several months, we have been asked repeatedly how the recent strengthening of the US dollar impacts our bottom line. So I want to give some additional information, which factors into our guidance. While we have operations in 69 different countries, our FX exposure, as it relates to profitability, is weighted towards two currencies -- the Mexican peso, approximately 32% and the euro, about 27%.

Since the quarter ended, we have seen significant US dollar strengthening, up 19% and 12% respectively. As we look at our 2009 guidance, there are two components we want to provide additional guidance -- FX and volume. When we first rolled out our 2009 budget, our earnings-per-share expectations were north of \$4.00 per share using early July FX rates. Our initial 2009 guidance reflects current volume point trends, coupled with late October spot FX rates. Specifically, it assumes a spot euro price of \$1.33 and a spot Mexican price of 12.83.

Additionally, we have performed sensitivity analyses in the event currency exchange differ from these spot rates. If all rates in our basket of countries were to move plus or minus 10%, our current earnings-per-share range would increase 21% and decrease 21% respectively. In addition, our guidance does not include any accretion resulting from any future share repurchases.

As Michael stated earlier, it is our goal to be more profitable and generate increased cash flow from operations in 2009 compared to 2008. Our initial guidance does not reflect this goal. Rather, it represents what we believe is a floor in earnings given the positive volume trend in several of our top markets, which Des reviewed with you, and the stability of our business model to generate free cash flow and earnings.

We are in the process of evaluating how we can remove excess costs from our infrastructure, reduce discretionary spending while investing appropriately against numerous sales growth initiatives. We need another four to six weeks to complete this plan and we will update you at our Investors Day in December in New York. This concludes our prepared remarks and now we will open up the call for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Simeon Gutman, Goldman Sachs.

Simeon Gutman - Goldman Sachs - Analyst

Hey, Michael. The first question -- you opened up with some commentary on the economy and the turmoil, but when Des diagnosed some of the issues in some of the big markets, it didn't really place the blame on the macro. So as you look back at the quarter and then as you look forward, is there more macro sensitivity, less or the same as you expected?

Michael Johnson - Herbalife Ltd. - Chairman & CEO

Well, a lot of questions there, Simeon. The one thing that I am going to keep focusing on is that I would say plus 90% of the issues are ours to focus on. We have our own unique set of issues. I don't think they are economy-driven. I think the one place that we might have some economic issues and they are rather small is in some of the outlying smaller villages in Mexico where

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money has flowed from the US from day workers here back into those villages that may be supporting consumption at those village levels in Nutrition Clubs.

We heard -- a couple of our top distributors told us that instead of two or three family members showing up at a Nutrition Club, it is one or two. So there has been some impact there. But I would hesitate to say that's a huge impact on us in Mexico. I think that when we look at our economic issues, they are our own. I think it always goes back to our leadership. You are familiar enough with this company to understand how important our distributor leadership is. I think that the less money flowing in probably has an impact. We can't probably quantify that as carefully as I would like to be able to, but you have got to remember, we put a VAT increase into Mexico at the same time that this economic crisis hit.

What we have is an opportunity there that is still -- I am very high on. I look at Mexico over a long range of time and I know I am just addressing Mexico, but that is probably where our biggest economic impact on the marketplace. We still have a huge penetration opportunity in that country and we are going to get there. It is just going to take us a little longer than we thought.

Simeon Gutman - *Goldman Sachs - Analyst*

And on the Company-owned problems, I don't know if you would prioritize and I will throw a couple of things out there -- I don't know if it is one issue more than the other or maybe an issue that I don't even mention, but this transition to the daily consumption, possibly maybe distributor engagement and/or is it a management oversight in that country? And then I have a follow-up related to that.

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Well, Simeon, I think, if you look at us, we are really isolated to three marketplaces where we have some issues -- Mexico, Venezuela and China -- and those happen to be three big ones, which is unfortunate. Usually we have in our portfolio of countries markets up, markets down. In those three instances, they are all extraordinarily unique to those marketplaces. I don't want to give Mexico one banner issue, but if you did it, you would say the VAT, 15% in the marketplace. If you looked at Venezuela, you would say we have to adjust to the real currency market there. You have got a strange management of that country in terms of governmental, not in terms of Herbalife, and the curve rate against the official rate keeps moving on us.

And in China, we are probably at the core as much as the market. We want to make sure China is a real retail marketplace and we are focusing on the three Rs there. And so in some effect, we may have slowed China down on our own just to say, you know something, let's make sure it is not just a recruiting market, that we have got a real retail presence in daily consumption and the drive to get to a -- and I'm going to call it a Nutrition Club model. I am going to be careful of calling it strict Nutrition Clubs in China, but it is a consumption model. What happens in China is typically the North slows down in the winter a little bit. We are heading into the winter. It is going to tend to slow just a little bit there. It tends to be part and parcel of doing business there. I have always been a bit conservative about China and I will continue to be, but it really boils down into three markets.

And then you turn on the other side, and I'm going to use the opportunity of your question to talk like a politician and say -- talk about the good things. Brazil, the United States, Taiwan, South Korea, incredible growth in all three of those markets. I don't know too many people who are saying that in our marketplace about the United States right now. We are making that statement and we continue to grow here and we are not only seeing it in the Latin market, we are seeing it in the English-speaking market too and the lessons that came out of the Los Angeles Extravaganza were go deep, go deep in your marketplace and we are going to be doing all sorts of things in the next month.

You are going to see a viral marketing campaign coming out of us, which you heard when you were on hold at the beginning of this call. There is a video that we patterned after some of the Get Out to Vote videos. We thought it was done very well. We're going to ask every distributor we will be releasing this by the end of the week. We're going to ask every distributor to send it

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to 15, 20, 25 people and attach their name to it. And we will be able to blanket the marketplace. So going deeper is as important as anything that we do in this company right now.

Simeon Gutman - *Goldman Sachs - Analyst*

And as the focus gets back on improving those markets or just extending the success you have had in others, in the context of the profit improvement plan, how are you going to be prudent to make sure that the expenses are allocated where they need to be versus taken from I guess where they are not needed.

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Well, one thing we are going to do, Simeon, is make sure we are arm in arm with our distributors on every marketing tactic that we put into the marketplace. I think we have led a few times incorrectly. I think we have led a few times correctly. I think that the Galaxy promotion for us was a huge winner because it established us as a global brand almost immediately and we used -- we drafted off the popularity of Beckham and some of the players on that team and that team's global presence, the third largest selling jersey in the world. That really helped us.

I think in a couple other instances, we got out ahead of distribution. I don't mean ahead in terms of a race ahead. We just didn't fully engage in the manner that we should have engaged with our distributors to make sure that everything we are doing is a success. That runs against my grain of making sure that we are competently communicating and putting plans out there.

I think this is one of Des' great strengths in this Company is his ability to work with our distributors very closely through our strategy and planning teams, through our 20K, meaning the 20,000 teams, distributors who are getting \$20,000 in royalties every month, to make sure we are implementing ideas that not just sound good, but work good. And we are going to see expenditures aligned with those.

Simeon Gutman - *Goldman Sachs - Analyst*

And the last question maybe for Rich, the volume growth that is anticipated in the fourth quarter, and I realize it still may be conservative, but as that builds to the full run rate that you have put in the guidance for the following year, what are the big changes in that? Is it a sequential build? Do you plan to end the year at a much higher rate and the average for next year is going to be in that 4% to 5% range? It just seems like a pretty big move going from the current quarter where we were, I think, at about 9%, down to about 0% to negative 3% and then back up to 4% to 5% for the year.

Rich Goudis - *Herbalife Ltd. - CFO*

Yes, I think it is definitely sequential build, primarily because of what we described with Mexico. We implemented the VAT in August, so I wouldn't expect -- looking this far out, I wouldn't expect next year to comp positive until we cross that period unless we are able to successfully get the VAT repealed.

But I think other markets that are going through this conversion that we have seen in other markets, it takes some time. We are very fortunate that large markets like the US continue to grow and actually accelerate this quarter. That gives us overall contribution to volume, but it also continues to send the signal to distributors that this daily consumption model, whether it is clubs or weight loss challenge, really do work in this business, especially during these tough economic times.

So I would say that our conservative outlook and with typically conservative early looking into the next year is a sequential build throughout the year. We will apply for additional Chinese licenses as we exit this year. Hopefully, we get those at midyear next year and that provides, again, additional confidence and catalysts in that large market.

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We look to Eastern Europe to try to stimulate growth there. Russia and Poland are both growing very strong double digits right now. We want to expand that strength. At the same time, we want to continue to nurture the great success that we've had in the Mediterranean markets like France, like Italy and hopefully as we get past May of this year, we will start comping positive in Spain. The Spain numbers have been down, but they have stabilized and we think that, as we get towards the summer next year, those also should start to comp positive.

So you start to look at our top 10 markets, which compromise 70% of our sales, and you look to this back half of '09 conservatively and you see those all potentially being all green and that is a positive indication for us, not only to have confidence that will sequentially grow, but also leading into 2010 that we could have very strong success again.

Simeon Gutman - *Goldman Sachs - Analyst*

Thanks.

Operator

Chris Ferrara, Merrill Lynch.

Chris Ferrara - *Merrill Lynch - Analyst*

Hey, guys. Just wondering if you can talk a little bit about what you're seeing on the ground in China. Can you give some real world examples of why that business has slowed sequentially? Like what you are doing to push to make sure that it is more of a retail model just so we can better understand that, just a little more color.

Des Walsh - *Herbalife Ltd. - EVP*

Yes, hi, Chris. This is Des. So China, obviously, we have always been conservative about the Chinese market, Chris and obviously, this is a market that has been very much based upon growing of our sales employees in China. That has been a key focus for us. That together with the expansion of our store operations and obviously, what we are now doing is that we are building a strong foundation for the future and so we are focused more and more now on different retailing methods, stressing this whole issue of daily consumption.

We recently had a fabulous [world] team school in Macau, which was attended by several thousand of our sales employees from China and the key focus of that entire meeting was all centered around the issue of increased retail, increased product consumption and training on our products, rather than what has primarily been a key focus before of that, but also a key emphasis on adding new sales employees.

The other issue that we are doing as we are going forward now is that based on the very successful adoption and acculturation of the Nutrition Clubs initially in Taiwan and now spreading across into Korea and Japan, we are actually also looking extensively at how we can incorporate that business model into China, along with a new program called an Authorized Retailer program.

So this is the transition that we are going through. We believe that it is, based on everything we are seeing elsewhere around the world, that it is the right move for us strategically because, at the end of the day, what we want is we want strong, stable growth in China built on a very strong and firm base for the future.

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Chris Ferrara - Merrill Lynch - Analyst

Got it. Is that sort of a trend change? What are you seeing in the local market that is causing you to sort of not deemphasize, but move a little bit further away from recruiting? Because, obviously, people have been recruiting pretty aggressively, not just for you guys, but for others and I guess what sort of change? Like why will we see a pullback on that now versus six months ago or three months ago?

Des Walsh - Herbalife Ltd. - EVP

So Chris, we have always been conservative about China and that has been a message that you have actually seen us emphasize from the very, very beginning. So what our commitment is is that we want to build a strong base in China. It is our number four market today. We believe that, obviously, the potential there is absolutely huge. We have got very entrepreneurial people there. We have got a growing epidemic of obesity in China.

So for us, all the catalysts are there, but what matters is that we do that built on a solid foundation and that is why we are really focused on where we are today. The ramp-up was in Phase I getting us to where we are today. Now Phase II, it is really about emphasizing the three Rs and obviously, that is really the transition that we are talking about.

Chris Ferrara - Merrill Lynch - Analyst

And can you talk a little bit about (inaudible) in Eastern Europe? Obviously, you guys have been talking about focusing on the tremendous opportunity in developing versus developed Europe. Can you just give an update on where you are with that and given your desire to cut costs out of the system and be more efficient, how much more of a focus is Central and Eastern Europe going to be in '09 versus what it was in '08?

Des Walsh - Herbalife Ltd. - EVP

Sure. So well, certainly what we are doing is this, Chris. We are, obviously, focusing on those parts of the world where we believe we have the most potential and when we look around the world, what we see happening in Russia and the former CIS countries, in Poland and Eastern Europe, we actually see a number of different factors coming together.

First of all, we see a large group of people who are vitally interested in a business opportunity. The second thing that we see is we see a growing discretionary income in there and also a transition to more Western diet that is impacting obesity. So any time you've got a combination of growing obesity rates, you've got growing discretionary income and that you have got people -- and you have people in [terms] of economic opportunity, that for us is the perfect storm.

Also a little -- I guess almost two years ago, we actually brought in some key personnel to head up that whole area for us and I think that has been one of our factors for growth and the other thing is that we have a very active, engaged distributor leadership in all of those markets that is becoming more so. So for us, all of the factors are there that indicate to us that this is going to see growth in the future and we are reallocating resources accordingly.

Chris Ferrara - Merrill Lynch - Analyst

And just finally, I guess, Michael, you sort of referenced a buyback and given the volatility in the market, you guys pulled back on your buyback in the third quarter. And I can also understand given what you guys are seeing coming on the FX front, but as we go forward, how are you thinking about that? I think you said you view the shares as undervalued, but do you view the shares as dramatically undervalued and how aggressive can you get?

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Michael Johnson - Herbalife Ltd. - Chairman & CEO

Well, let's put it this way, I am staring at the same monitors you are staring at right now. So dramatically undervalued. I want to be careful what I say here, but we are going to be opportunistic here. Now that the foreign exchange, the credit and the stock are settling, we are going to take advantage of this opportunity.

Chris Ferrara - Merrill Lynch - Analyst

Thanks a lot, guys.

Operator

Karen Howland, Barclays Capital.

Karen Howland - Barclays Capital - Analyst

Good morning. I was wondering if you could talk a little bit about -- I noticed in the 10-Q that it looks like the Mexico City Extravaganza actually had fewer attendances than a similar Extravaganza the year before and that was before the VAT change took place. I was wondering if there were any indications prior to the VAT change that that business was slowing.

Des Walsh - Herbalife Ltd. - EVP

So the issue primarily in Mexico, clearly, was exacerbated by a VAT situation. So the VAT introduction, obviously, happened literally just a couple of weeks before the Extravaganza and essentially, we passed on what was a 15% increase. And the thing about the situation in Mexico is that anytime you have got an increase of that magnitude in a country where you have got a significant amount of our business in Nutrition Clubs, which by definition, to a certain extent, are focused on the lower economic segment, when you have that increase passed on in the clubs, what we saw is that we have people still coming to the clubs, but maybe coming a little less regularly. So people who might have come to the clubs four times a week, the price has gone up and so they may be coming three times a week. What we are hearing from our distributor leadership, of course, is that this hasn't impacted the customers who are coming. It is an issue primarily relating to the frequency.

As far as the Extravaganza is concerned, the numbers were slightly less, but I think primarily this is a function of space and other issues, not so much reflecting a slowdown in the business. The other issue is that, this year, we actually had one venue compared with two in 2007 and that was a factor as well.

Karen Howland - Barclays Capital - Analyst

Okay. So it wasn't -- it was more of a function of how you planned for it rather than necessarily that there wasn't the demand for people to come?

Des Walsh - Herbalife Ltd. - EVP

Yes, that's exactly right. It was a question of space and availability rather than attendance per se.

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Karen Howland - *Barclays Capital - Analyst*

Okay. And looking at the -- I know new supervisor growth is typically a leading indicator of sorts for sales and earnings growth. New supervisor growth is down. Has this model changed given the push towards daily consumption model or do you -- would we expect that to be -- is that a concern, that the new supervisor growth is, in fact, down?

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Karen, I will start. As a global indicator, we have always said that new supervisor is a good near-term lead indicator of volume and I think the fact that we were down 0.7%, or just nearly 1% this last quarter in new Sales Leaders is why we are very cautious to guide volume of flat to down 3% in the fourth quarter.

Each market has their own specific reasons why, and the correlation might be slightly different market-by-market whether it is going through a series of retrenchment, etc., but overall globally, I think you can use that as a key lead indicator for the next, let's say, 60, 90, 180 days.

Karen Howland - *Barclays Capital - Analyst*

But there was a pretty serious deceleration being from up 10% the last three quarters to being down. Mind you, just minorly, but down this quarter.

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Sure. And I think if you look at the markets that really contributed to that, and we have alluded to it, but number one was Mexico. When we implemented the VAT and since then, we have seen nearly a 20% reduction in the run rate of our business and I think that has a meaningful impact.

Number two is Venezuela. Volume was down 35% in the quarter and the issues that we illustrated earlier in the prepared remarks I think is giving rise to that slower recruitment and people into the business. Additionally, markets that are turning around like Argentina, like Portugal, like Turkey and others that are following the path of Brazil over a year and half ago are all giving rise to a significant slowdown in the number of new people. Now let me be clear, we are still bringing in new people; it is just not at the same rate as a year ago.

Des Walsh - *Herbalife Ltd. - EVP*

And if I can add to that, that is exactly the issue. So first of all, if you actually look specifically at those markets, those are the markets where we are actually seeing that impact. So on a worldwide basis, the trend is the opposite.

The other issue is that if you look to our situation in Brazil, this is just a very good example of a country where we went through that transition where recruiting did slow during that transition to a consumption market, but where once the market adopted that daily consumption, then you see recruiting increase. So in the long run, we see this as being a healthy transition for our business as we switch in many markets from a very much recruiting market to a market where we are going to see a better balance of the three Rs.

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Karen Howland - *Barclays Capital - Analyst*

In looking at Mexico and Venezuela as being two of the most significant impacts though, that will continue to cycle throughout the course of this year though. It is not as if that is going to -- Mexico I know you said you don't expect to change until the second half of next year. Venezuela presumably is the same.

Rich Goudis - *Herbalife Ltd. - CFO*

Possibly Venezuela a little bit earlier because I think their issues are a little bit different and more unique to the actions that we have taken versus the VAT, which is uncontrollable to us and as Michael mentioned, the flow of dollars to some of these outlying regions. So hopefully Venezuela, we see a recovery sooner than Mexico.

Karen Howland - *Barclays Capital - Analyst*

Okay, thank you. And foreign exchange -- I'm sorry?

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

We didn't say anything, Karen.

Karen Howland - *Barclays Capital - Analyst*

Oh, sorry. Foreign exchange, obviously, has been a significant impact. Have you -- can you give an indication of what it was to earnings the past couple of quarters and what you have factored in for next quarter as a negative?

Rich Goudis - *Herbalife Ltd. - CFO*

I will just let Andy follow up with you on that call, but let me just say about FX, a lot of people asked us last night and this morning, why weren't we better hedged in '09 and the answer is if we were hedged in '09, you would have still seen the same guidance for '09. We would basically just have accelerated the P&L income or pickup from those hedges in the third quarter because we do not have hedge accounting treatment here at Herbalife. So it is very much a mark-to-market type of hedge treatment that we have and we are pretty conservative.

I think what most people missed was the fact that, while we definitely have the translation issue with net sales, that outside of Europe and outside of China, so effectively 70% of the rest of our business is all produced in US dollars. So in markets specifically like Mexico and Brazil and others that are large, we got a double hit, not only in sales, but also in cost of sales.

Karen Howland - *Barclays Capital - Analyst*

And that double benefit that you presumably have gotten over the course of the last couple of quarters has been a tailwind for you. I know you haven't previously quantified it, but was just wondering, given that we have got everyone on the public call right now, if it makes sense to actually give those numbers.

Rich Goudis - *Herbalife Ltd. - CFO*

Again, I will let Andy follow-up with you, but, again, remember the benefit that we had gotten we were calling out in gross profit for the last couple of quarters, basically saying that people had not seen the impact of higher commodity costs because

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we were getting benefit of FX and also our hedges were going the other way. So while we were getting a pickup converting through gross profit, we were actually getting at the SG&A expense of those hedges sort of mitigating or muting some of that because it typically is our goal to hedge about 50% of our operating profit expectations.

Karen Howland - *Barclays Capital - Analyst*

And the hedge impact to SG&A this quarter?

Rich Goudis - *Herbalife Ltd. - CFO*

This quarter being what? Third quarter or fourth quarter?

Karen Howland - *Barclays Capital - Analyst*

Third quarter.

Rich Goudis - *Herbalife Ltd. - CFO*

Let me just put my finger on it. \$2.9 million.

Karen Howland - *Barclays Capital - Analyst*

And that is comparable to the \$14 million from last quarter?

Rich Goudis - *Herbalife Ltd. - CFO*

Let me just put my finger on the number. Yes.

Karen Howland - *Barclays Capital - Analyst*

I'm sorry.

Rich Goudis - *Herbalife Ltd. - CFO*

Yes.

Karen Howland - *Barclays Capital - Analyst*

Okay. Why would it be so much less?

Rich Goudis - *Herbalife Ltd. - CFO*

I think it is a reflection -- excuse me -- it is a reflection of our -- the gains and the losses as it relates to the actual hedges that are in place.

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Karen Howland - *Barclays Capital - Analyst*

Okay, thanks very much.

Operator

Doug Lane, Jefferies & Co.

Doug Lane - *Jefferies & Co. - Analyst*

Good morning, everybody. Michael, we saw, as we just talked about, momentum slow pretty sharply in June and into September and you have got a lot of market-by-market explanations. Can you talk about the three kind of exogenous --?

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Exogenous?

Doug Lane - *Jefferies & Co. - Analyst*

Exogenous events, the battle with the FDI earlier in the year, the Spanish Health Ministry alert and I guess not so exogenous, but the departure of the Chief Operating Officer. Let's just call them unusual events and how they may have impacted the management of the business.

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Well, I don't -- when you use the word exogenous, you threw me there. Doug, you are being very literal today. I think we're well beyond those events. I don't see us as having any residue. The COO's departure was quickly filled and competently filled by Des and without any hesitation. We, in fact, have hired an incredible new head of supply chain operations here under Rich's watch there and someone who is totally experienced and in fact, more experienced than anyone we have had in the past in that position. So I think the fill-in there was very quick.

I think that the Spanish Ministry of Health issue is fast fading. When you think about it, we have been cleared by the SEC during this period of time. We had an agitator after us who has been gone. Our Spanish Ministry of Health, we look at that issue as being more political than product-oriented and I believe those issues are fast fading into the scenery.

I think that any issues that we have and again, I am going to point to -- I think they can be pointed market-to-market. When you have got 69 marketplaces like we do, a portfolio of businesses, you are going to have unique characteristics and our goal really is, and again, I don't want to be political here and sound like I am moving to a different direction, our goal really is to get daily consumption models built in this business. And I think we have come through some incredible challenges this year with incredible strength.

I wrote everybody an e-mail this morning when I saw the stock price and took out a little explorer friend of mine, not a friend, but an explorer that found his way through Africa and got into terrible condition and I said bash on, guys. We have an incredible company here. We have an incredible business model. And our problems that are plaguing us right now are some environmental, but they are mostly internal to three specific marketplaces.

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I look at the marketplaces that are growing and I look at this Company and again, you want to look back -- let's take it back a little further. In 2003, this Company was a \$1.1 billion company. We will be a \$2.3 billion to \$2.4 billion company today. We have doubled in size. We are going to continue to grow this Company. We have got distributors who have a business opportunity in front of them and a health opportunity in front of them that is unique in these times.

So last year, we said that our stock was going to be somewhere between \$3.17 to \$3.23 and that equated to a \$40 -- our EPS would be \$3.17 to \$3.23 and equate to a \$40 stock. Today, we are seeing between \$3.00 and \$3.20 and we have got an under \$20 stock. So go figure. That is just hard for us to understand in the market now. We understand the environment that is going on. We are not ignorant to the marketplace and the issues that are happening out there, but I look at these events and I keep saying, well, let's see, the USA is up higher than it has ever been, got more momentum in that marketplace than we have ever had.

When we took this company public, people said you will never get the USA back. We have got a couple of issues in Mexico. We have got one in Venezuela and we are -- seven out of our 10 markets, we are up right now, of our top 10 markets. So I am not panicking. I am not hitting the panic button. People who are selling our stock are hitting the panic button. That is their issue, not mine.

We're going to continue to grow this company, make this company prosper. We will be stronger for every experience we have been through and this is, I would say, a pretty tuned management team who has been through an incredible, incredible year and is coming out with their heads high and we will be more profitable in '09 than we are in '08 and I don't know too many companies that are saying that right now.

Doug Lane - *Jefferies & Co. - Analyst*

No, I know, but you have had such good momentum, and it clearly slowed over the summer, and you have had an unusual year for the reasons I mentioned, and even in the third quarter, Spain and Germany were down 27% and Portugal was down by half, which has got to be a byproduct of the Health Ministry alert. In retrospect, how productive was it for you to be fully briefed on the lead content of Formula 1 when you have got a big local company to run here? So I just wonder -- I am trying to get the lay of the land for when you think the business can reaccelerate. Is this all behind us and it should be sooner rather than later or do you think these issues will take the better part of a year or two to work out like Mexico and Brazil took?

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Well, I think it takes time for these business models to adjust. You pointed out a couple of marketplaces. Spain and Germany are done. Netherlands is up 6% year-on-year right now and that is a marketplace that has been trending down for three years. Brazil is in a complete change for us right now. South Korea is a phenomenal story.

So my goal is to get those stories, and this is what Des and I share in common, is to get those stories in front of our distributors who are articulate at following the money. They are very, very shrewd and very smart when it comes to adapting new business methods and new business models. Where we have had some problems, you bet. In Europe, we have had some problems with this article that was in the Journal of Hepatology, an article that we continue today to refute. And you have got to remember, not one single product, not one single ingredient has ever been removed from the marketplace with all this storm and all this drum banging.

So when you say have I been disfocused by understanding lead content, no, I am not disfocused at all. In fact, I am deeper in our product pipeline than Steve Henig sitting here and he will tell you I am spending more time there. And I don't think that is a lack of focus. I think that is a smart focus for a CEO of a company to know everything about every ingredient in his product to understand it more deeply and penetrate the understanding of that deeper into our leaders and it will build continuous improvement in our Company in terms of product, in terms of how we release new products, how we come to decisions.

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This is yesterday and you have asked some penetrating questions, so I will hit you back some penetrating answers. Yesterday, I had a group of seven people sitting in a room discussing what I think is a breakthrough product for this Company. Now one issue on that product was it is just way too expensive and so we looked at a way to make this an add-on product to something that we have that will be very unique and people with distributor input sitting around talking about a very incredible method to bring a new product to the marketplace. Those are the kinds of things that excite me in this Company. It is the go-forward, not the go-back. Yes, you learn everyday from experiences. You didn't walk when you were born and then you learned to run and you don't go back to the days when you couldn't walk and say, gee, I was just a crawler. You are not disfocused by that, you are moving forward and that is what we are doing in this company. That is what businesses are. They are a continuing set of issues, they are a continuing set of imperfect situations that you continue to fight your way through and leaders are more Churchillian than they are not Churchillian. You have got to keep the focus up and you've got to keep moving forward.

Our distributors are incredibly confident right now and so in these tough economic times, we have got a great business opportunity and a great model for success. So I am going to -- without sounding like I am not answering your question, I am going to go forward. Did some of that stuff disfocus us? Maybe. Maybe not. Maybe that was -- that is just the way life is.

Doug Lane - Jefferies & Co. - Analyst

Okay, fair enough. Just one last question on strategy, Michael. It looks like -- call it Nutrition Club, call it daily consumption, but you are really running with that concept more broadly than maybe I had realized. Is that something that is really going to be the feature global model for the Company or some subset of it? Just where are you going with the daily consumption model?

Michael Johnson - Herbalife Ltd. - Chairman & CEO

Well, I think daily consumption is about a sticky customer. I was -- you have got to have a sticky customer in a business to make it real and last long. Whether you are Herbalife or a daily retailer of coffees for ice creams or whatever you have got, if you have got a customer coming in and seeing you daily and this is what is exciting is the retention rate among those customers in Nutrition Clubs and you go down to the oldest set of Nutrition Clubs that we have on the face of the earth, which are in Mexico, you meet people who have not ever left the Nutrition Clubs. They've been coming three, four and five years. That is exciting to me. And so when we talk about daily consumption, you bet I am placing bets there because that is a winner all across the board for our distributors, for our Company, for our consumers.

Doug Lane - Jefferies & Co. - Analyst

Okay, thank you.

Operator

Scott Van Winkle, Canaccord Adams.

Scott Van Winkle - Canaccord Adams - Analyst

Hi, thanks. Most of my questions have been answered. An easy one for Rich. Rich, what percentage of your SG&A is denominated in currencies other than the US dollar?

Rich Goudis - Herbalife Ltd. - CFO

About 44%.

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Scott Van Winkle - *Canaccord Adams - Analyst*

Okay. And then a quick question on Mexico -- sorry -- on China, but related to Mexico. When you went through the Nutrition Club issue, what, two years ago in Mexico, you really leaned on your senior leadership in the distributor ranks to kind of help bring the message along. In China, do you have that same type of organization? Because it is such a different model, do you have a group of senior distributors that you kind of lean on with assistance and spreading the word?

Des Walsh - *Herbalife Ltd. - EVP*

Yes, so what we are doing is we are actually taking -- in fact, actually it is happening next week. So we have got a group of our Chinese team actually who are actually visiting both Taiwan and Korea next week because they will spend some time visiting the clubs because ultimately they are the best people who are familiar with the business in China, who can best see how that business model can be acculturated there. So that is what our game plan is as far as the introduction and acculturation of the clubs for the Chinese market.

Scott Van Winkle - *Canaccord Adams - Analyst*

Thank you much.

Operator

(Operator Instructions).

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

Kevin, why don't we just take one more call then.

Operator

That was actually the last question.

Michael Johnson - *Herbalife Ltd. - Chairman & CEO*

I want to thank everyone for being on the call. I know this is an interesting day. You have got your eyes glued to the TV on election results and we have got them glued to the monitors on what is going on in everything in our business. We just actually put in a new dashboard that gives us more information on the markets on a daily basis in which we can react to manage this Company.

The credit markets are going to sort out their current mess, but while they do that, our team at Herbalife, both employees and distributors, and I just said this and I don't want to get off this soapbox, we are committed to growing our Company top and bottom line. Our Company has never been more profitable. Our business practices have never been more balanced and our geographic reach has never been as broad. We are going to continue to focus on the strengths of this Company.

Our future is bright. Why? Because it is the extraordinary work of our distributors that have paved the way for success with the development of daily consumption business models and you will keep hearing us come back to that. Our management team, alongside our independent distributors, will continuously look for various ways in which we can implement initiatives to improve daily consumption growth, expand our product breadth and availability and expand our presence globally.

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And I think you guys know this already, but our distributors are our business partners and they are positioned unbelievably well in this current environment to benefit from both the attractive business opportunity and our compelling product results and pricing.

And finally, we are excited by the accelerating pace with which our distributors are attending training sessions to learn more about daily consumption business practices. Recent successes in several of our top 10 markets, including the US, Brazil and Korea, will help us build a stronger business base and remember, our distributors, they follow success and they breed on success. This is which will build a more stable, resilient base in soft economic times.

We look forward to seeing you guys at our Investor Day on December 16. We will update you on our goal to be more profitable in 2009 versus 2008 and I want to thank all of you for your continued support. Go out and have a great day and vote.

Operator

Ladies and gentlemen, that's concludes today's presentation. You may now disconnect.

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