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NHTC.OQ - Q2 2020 Natural Health Trends Corp Earnings Call

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CORPORATE PARTICIPANTS

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Timothy Scott Davidson *Natural Health Trends Corp. - Senior VP, CFO, Chief Compliance Officer & Secretary*

CONFERENCE CALL PARTICIPANTS

Kimberly Orlando *ADDO Investor Relations - SVP*

PRESENTATION

Operator

Greetings, and welcome to the Natural Health Trends Corp. Second Quarter 2020 Conference Call. (Operator Instructions) As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Kim Orlando.

Kimberly Orlando - *ADDO Investor Relations - SVP*

Thank you, and welcome to Natural Health Trends' Second Quarter 2020 Earnings Conference Call.

During today's call, there may be statements made relating to the future results of the company that are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Actual results, performance or achievements could differ materially from those anticipated in such forward-looking statements as a result of certain factors including those set forth in the company's filings with the Securities and Exchange Commission.

It should also be noted that today's call will be webcast live and can be found on the Investors section of the company's website at naturalhealthtrends.com. Instructions can be found for accessing the archived version of the conference call in today's financial results press release, which was issued at approximately 9 a.m. Eastern Time.

At this time, I'd like to turn the call over to Chris Sharng, President of Natural Health Trends.

Chris T. Sharng - *Natural Health Trends Corp. - President, CEO & Director*

Thank you, Kim. And thanks to everyone for joining us this morning to discuss our second quarter 2020 financial results. With me today is Scott Davidson, our Senior Vice President and Chief Financial Officer.

The second quarter marked a continuation of the challenging macroeconomic climate we experienced during the first quarter of 2020 as the COVID-19 pandemic persisted into the summer months. That said, we were very pleased with the stability and resilience of our field leadership, which helped us generate a 10% increase in total revenue over the prior quarter to \$16.4 million. I'd like to sincerely thank our leaders, members and prefer customers for their support of NHT Global through this unprecedented time.

COVID-19 has shown us that the world is truly interconnected. Despite the immense challenges this pandemic has presented on a global scale, we have enjoyed positively contributing our wealth of knowledge on health and wellness-related products with our loyal consumer base.

In addition, our aggressive cost reduction measures enabled us to return to profitability during the second quarter, with positive operating income of \$183,000 compared to an operating loss of \$1.4 million in the first quarter of 2020.



As previously announced, we put a program in place in the second half of 2019 to position us for increased operating efficiencies in several areas, including reduced headcount and promotional spending. Through this program, we made significant progress in reducing our SG&A expenses during the second quarter through reductions of nearly 20% versus the first quarter of 2020 and more than 1/3 versus the prior year period.

Since we last spoke in May, our main markets have begun to slowly resume economic activity, though various forms of government-mandated travel restrictions have remained in place. While there has been some relaxation in personal mobility, company-sponsored in-person activities still remain highly limited, though we are cautiously optimistic the operating environment will continue to improve as we move forward.

We are well aware of the challenges our leaders continue to face without being fully able to support their groups in person. By nature of our business model, we operate as an e-commerce platform, which does not require much physical contact. This has served us well through the pandemic. But our leaders, who are crucial to our success and effectively operate as our sales force and marketing team in the field, have been limited in their ability to support their geographically diverse groups.

Fortunately, since we made the decision to suspend member activities in early 2019, we have successfully transitioned our business to function as a digital operation, which has allowed us to continue sharing information about our high-quality product across various different markets and channels. We do this through informative product webinars and virtual events, with online trainings being held regularly to help promote improve immunity, healthy diet, lifestyle and beauty care tips.

Through mostly online activities, we were able to slightly improve order volume over the first quarter of 2020. Further, given our efforts earlier this year to mitigate any potential supply chain disruptions, we have been able to fulfill orders by working closely with our vendors and planning for ample product availability. In addition, given international travel restrictions, we have also extended qualification periods and certain incentive trips from the first half of 2020 into the second half of 2020 and next year.

You may recall we had to cancel our major first half event in the first quarter due to COVID-19. We will continue to make modifications as necessary, though we remain hopeful we'll be able to conduct more in-person events in the coming months.

Now turning to our geographical expansion priorities. While we remain focused on further diversifying our operations into new emerging markets, COVID-19 has delayed our progress in this regard as a result of government-mandated shelter-in-place orders. However, we did make some positive strides during the quarter.

In China, we launched additional products to be sold on our e-commerce site including our new water purifier, which became available on the platform in June, along with Mycelia, cleansing water and Alura Lux, which launched in mid-July. We prefaced the introduction of our water purifier product with our first product road show in 18 months, which was very well received.

In Peru, our operations continue to be adversely impacted by COVID-19. However, since we have been able to resume shipping into the larger Peruvian cities in late Q1, we successfully introduced some new products including OcuFocus. We also unveiled new products in India including Triotein, Enhanced Essential Probiotics and Glucosamine.

Lastly, we were very pleased to obtain our direct selling license in Thailand and are gearing up to commence activity beginning with product registrations.

In summary, I am very pleased with our ability to manage elements within our control throughout this global crisis, which led us to achieving positive growth in total revenue, gross profit, operating income and net income for the second quarter compared to the first quarter of 2020. I'd like to once again thank all of our leaders who have proven themselves time and time again in navigating difficult and complex operating environments such as this one. We remain cautiously optimistic the macroeconomic situation will continue to improve in the second half of 2020.

I would like to conclude by reiterating that the health and safety of our members, employees and customers served as the foundation of our success. We thank them for their dedication and commitment to NHT Global and wish good health to all.

With that, I'd like to turn the call over to our CFO, Scott Davidson, to discuss our second quarter 2020 financials in detail. Scott?

Timothy Scott Davidson - *Natural Health Trends Corp. - Senior VP, CFO, Chief Compliance Officer & Secretary*

Thank you, Chris.

Total revenue for the second quarter was \$16.4 million, a decrease of 30% compared to \$23.4 million in the second quarter of 2019. The year-over-year decline was primarily due to the challenging and uncertain operating environment arising from the COVID-19 pandemic and the resulting effects on our members' abilities to hold meetings and events, which negatively impacted our performance.

While we anticipate the effects from COVID-19 will continue to adversely impact our results in the near term, we are encouraged by recent trends in many cities in our key markets. Greater China has started the process of opening back up, including lessening restrictions on travel and small gatherings.

Our active member base decreased 4% to 54,400 at June 30 from 56,500 at March 31 and was down 31% from 78,300 at June 30 last year.

Turning to our second quarter costs and operating expenses. Gross profit margin of 70.6% declined from 76.9% in the second quarter last year due primarily to additional logistics costs and product promotions put into place to help alleviate the impact of the pandemic and its restrictions on our business.

Commissions expense as a percent of total revenue declined to 43.4% from 48.7% in the prior year quarter as a result of our proactive efforts to reduce incentive costs. Selling, general and administrative expenses decreased 35% to \$4.3 million from \$6.6 million a year ago, reflecting our proactive cost reduction measures that reduced employee-related costs, professional fees and event spending. The highly variable nature of our cost structure affords us the flexibility to continue adapting expenses in line with order volume as evidenced by the 37% year-over-year decline in our total operating expenses for the second quarter.

As a result of these actions, despite the challenging operating environment that has persisted over the past several months, we were able to return to profitability in the second quarter. Operating income totaled \$183,000 compared to an operating loss of \$4,000 in the second quarter last year.

We recorded an income tax provision of \$274,000 for the quarter compared to an income tax benefit of \$28,000 in the second quarter last year. Net income totaled \$34,000 or breakeven per diluted share, compared to net income of \$397,000 or \$0.04 per diluted share in the second quarter last year.

I will now turn to our balance sheet and cash flow. Total cash and cash equivalents were \$93.2 million at June 30, down slightly from \$95.4 million at March 31. Net cash used in operating activities was \$28,000 in the second quarter compared to \$3.7 million in the second quarter of last year.

We have a strong balance sheet and a conservative capital allocation philosophy designed to help support our members and business. Further, we have ample liquidity with 0 debt and no bank loans of any kind.

I am pleased to announce that this strong liquidity position has enabled us to maintain our dividend. On August 3, our Board of Directors declared another quarterly cash dividend of \$0.20 per share, which will be payable on August 28 to stockholders of record as of August 18, 2020. Our Board of Directors will continue to monitor the economic environment and evaluate our capital allocation strategy going forward to determine the most efficient use of capital to drive shareholder value.

While we are continuing to execute through this uncertain and volatile environment, we remain highly focused on the fundamentals of our business including supporting our members, maintaining our strong balance sheet, and ensuring proactive expense management. These elements position us to benefit from any economic recovery that is to come.



I'd like to echo Chris' comment and that I'm extremely proud of our employees' dedication to our business and the commitment and support shown by our members during these difficult times.

That completes our prepared remarks. I will now turn the call back over to the operator.

Operator

Ladies and gentlemen, that concludes today's conference. Thank you for joining us. You may now disconnect your line.

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