

## Herbalife Ltd.(Q1 2023 Earnings)

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### Corporate Speakers:

- Erin Banyas; Herbalife Ltd.; Head of IR
- Michael Johnson; Herbalife Ltd.; Chairman & CEO
- Alexander Amezquita; Herbalife Ltd.; CFO
- Mark Schissel; Herbalife Ltd.; COO

### Participants:

- Chasen Bender; Citigroup Inc.; Assistant VP
- Jeffrey Van Sinderen; B. Riley Securities, Inc.; Senior Analyst
- William Reuter; BofA Securities; MD & Research Analyst
- Hale Holden; Barclays Bank PLC; MD
- Unidentified Participant; Bank of America; Analyst
- Karu Martinson; Jefferies LLC; Analyst

## PRESENTATION

Operator^ Good afternoon, and thank you for joining the first quarter 2023 Earnings Conference Call for Herbalife Limited. (Operator Instructions) As a reminder, today's conference call is being recorded. I would now like to turn the conference over to Erin Banyas, Vice President and Head of Investor Relations, to begin today's call.

Erin Banyas^ Thank you, Twanda, and good afternoon and good evening, everyone. Joining us today are Michael Johnson, our Chairman and CEO; and Alex Amezquita, our Chief Financial Officer.

Before we begin today's call, I would like to direct you to the forward-looking statements on Page 2 of our presentation and in our earnings release issued earlier today, which is available under the Investor Relations section of our website.

The earnings release includes a discussion of some of the more important factors that could cause results to differ from those expressed in any forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 as amended and Section 21E of the Securities Exchange Act of 1934 as amended. As is customary, the content of today's call and presentation will be governed by this language.

In addition, during today's call, we will be discussing certain non-GAAP financial measures. These non-GAAP financial measures exclude certain unusual or nonrecurring items that management believes impact the comparability of the period's preference. Please refer to our earnings release for additional information regarding these non-GAAP financial measures and the reconciliations to the most directly comparable GAAP measure.

Following today's call, the presentation materials will also be made available under the Investor Relations section of our website. And with that, I will now turn the call over to Chairman and CEO, Michael Johnson.

Michael Johnson^ Thanks, Erin, and welcome to Herbalife on behalf of all of us. Good afternoon to our investors and shareholders and all of our stakeholders. Thanks for joining us today. This is my second call back after my return.

We joined you in February and -- February 14, and then and now we are in the midst of a significant change, and we're more comfortable with that than we have been in a long time. And I'm going to continue on the promise that we made in our last call in February that our sales will grow and our results will improve. We're evolving. And that's what's been happening over the last six months, and it's going to continue.

We still aren't where we want to be, but we have embarked on a significant journey as we laid out on our earnings call in February. Since then, we've engaged more closely with our distributors than we have since 2019. That's hard to believe. We launched our new brand. We've seen net sales trends improve, and we are full steam ahead on executing Herbalife ONE, our new digital platform.

By working closely with our distributor digital team to make sure Herbalife ONE provides the content data and transaction capabilities to grow their business, I'm excited and, frankly, very confident that executing on this transformation, we will build our business stronger, reduce our costs and focus us on all the important elements and metrics in our business.

We've secured the balance sheet since then. We've made management changes to align key talent with key initiatives. We are streamlining our team for better operations, product innovation, data and sales analytics and improve productivity. We have worked very hard to make sure our distributor and customer engagement has increased. We are embracing on change as a company, recognizing we need to continue modernizing and evolving our way of doing business.

Since 1980, Herbalife has evolved with product and innovation, brand creation, distributor methods of operation, compensation plan enhancements and customer engagement. We will continue to evolve. We have consistently involved, adjusted and grown Herbalife because the need for great nutritional products and personalized selling that has created a community for nutrition and business opportunity that is unique to our culture and to our market opportunity.

Our transformation, it will take time, but we are working together. We have implemented new initiatives, and we have the right team in place, and we are highly energized. We're beginning to see some early rays of light, some bright spots. We are encouraged by improving trends. Our rate of decline has decreased significantly. And as I said in our last

call, our results and sales will improve. Our trends tell us we will see growth in the fourth quarter.

On to the numbers. Starting with our first quarter net sales of \$1.3 billion, we are down 6.3% compared to first quarter 2022 and down 2.6% on a constant currency basis. Our year-over-year reported net sales trends have improved in all five regions from quarter four. The 2.6% constant currency year-over-year quarter decline is trending better than it has in seven quarters. Our new distributor and customer trends are also showing improvement. Quarter one is up 7% sequentially compared to Q4 and only down 2% from Q1 2022.

Our first quarter 2023 reported diluted EPS of \$0.29 and adjusted diluted EPS is \$0.54. Adjusted diluted EPS was impacted by a \$0.32 currency headwind. With that said, we are fully focused on both volume and margin improvements.

We took steps to secure our balance sheet and improve our financial flexibility. We are well positioned financially to execute our strategic plan. Alex will give you more details on that financial movement soon.

We are seeing increased distributor focus and improved engagement that I will discuss in just a moment. Many of our leading indicators are promising, including high attendance at our events. These are wonderfully positive trends, which takes us to the basics.

Let's talk about our distributor and event highlights. Last quarter, I talked to you about the key pillars of our business, content and distribution. We are expanding and enhancing the content we bring to market to strengthen our distributors with new tools and opportunities to leverage data and analytics.

As we have previously discussed with a group of distributors, that we didn't have -- we had -- excuse me, we had a group of distributors that didn't have the opportunity to be engaged and trained by our senior distributors. They joined us in a time when person to person was replaced by virtual training. We know and part of our DNA is that in-person is way more valuable.

Let me pause here and tell you a little story. When I was at Disney, we did a deal with McDonald's, and we were going to be involved very closely with McDonald's and all marketing efforts around their Happy Meals for all of our films. When we met with McDonald's, it was clear to us that we didn't have an understanding of their culture and they did not have an understanding of ours.

So many of us at Disney embarked on a journey to Oak Park in Illinois to go to McDonald's to understand their culture, to understand their tools, to understand how they train. It was an in-person three-day event that a new franchisee goes through. It was highly valuable for us to understand their culture and to see us.

This impact was huge for all of us. It helped us understand the McDonald's customer, the way McDonald's operated, and how to best put our products inside their products to achieve the goals we wanted. We have a similar situation here at Herbalife today.

Our new distributors were impacted in a time when they could not receive person-to-person training. These impacted new distributors and almost everyone they sponsored, because a few of them had the opportunity to receive in-person training, did not achieve the level of engagement that comes with the result of being person-to-person, attending live events and having the metric necessary for them to succeed.

So what we're seeing today is that we are encouraged by the activity level of the new people now coming into the business, who are able to receive person-to-person training and able to attend in-person events.

Once this new cohort builds their skills and sales teams during the remainder of this year, we expect to see a positive impact on our sales performance. When you think about a distributor Herbalife, think of a retail outlet. Every time we recruit a new distributor, we are basically recruiting a new retail outfit. The difference is it's more than that.

They are retailers, but they're also recruiters. They are the people who build hands-on training, and they project the opportunity for people in meetings to be part of our DNA. In person trainings create a forum for learning, mentoring and driving engagement. In person events are critical. Herbalife distributors learn best from face-to-face training and proper mentoring.

Since the beginning of this year, we have held over 700 in-person meetings and reached more than 400,000 attendees, including our annual leadership training event, which was held last month for the first global in-person event since 2019. That's almost hard to believe.

Many distributors are attending an in-person event for the first time in their lives. In fact, at the upcoming Singapore event of the 22,000 tickets purchased, approximately 70% of the ticket sales are for distributors attending for the first time. The impact and the opportunity for this group is enormous. We've seen it in the past, and we'll see it again.

We have 10 major regional events planned for the remainder of this year. In the next three months alone, we will be traveling to Singapore, Nanjing, Lima, Bangalore and San Antonio to meet with our distributors face-to-face, share our vision for Herbalife 2.0 and learn from distributors as we launch regional products, promotions and give them support. We expect to engage over 140,000 distributors. You heard that right, 140,000 distributors at these events.

Distributors will leave these events more energized and motivated with enhanced knowledge, training and an opportunity and a plan to expand their businesses. We will be exchanging different unique successful sales methods, opportunities for distributors to train, mentor, motivate, inspire, learn from distributors, distributors to distributors, where

learning is key. These events give new distributors the opportunity to better understand the big picture, to see where they fit and to see what the opportunity looks like at Herbalife for each and every one of them.

We find that distributors who attend our events are more active and productive in their businesses. Our brand modernization. Many of you are seeing our new modernized brand for the first time today. As part of the rebranding, we unveiled a new name, yet an old name, Herbalife. But in brand mark and our new brand mark represents the company's modernization into a new era focused on health and wellness.

We will speed up our vertical platforms around product and biz opportunity. The evolution of our symbol placed tribute to our legacy while inviting new audiences to connect meaningful with this brand. It's refreshed. It looks great and the opportunity is there in front of us.

We will be able to use our new brand mark in a more meaningful way. We feel this is the beginning of our new era, Herbalife 2.0. Our healthy active lifestyle approach has returned as refreshed as we are seeing more distributor activity and engagement with fit camps, fit clubs and community workouts that open the door to recruiting and retailing. And add a foundation to our moniker Live Your Best Life.

Our digital transformation, where we're full speed ahead. Our brand enhancements will be seen through our modernized digital platform. Herbalife ONE is progressing and progressing well. Our this platform is transformational. It will accelerate data utilization and actions. As we have reported Herbalife ONE is creating a modern, harmonized user-friendly and integrated experience packed with key data and insights to grow and support our customers and distributors needs globally.

Our early progress is to launch a modernized and cohesive website in 40 markets that represents 80% of our sales by the end of this year. We also have plans to launch a brand-new e-commerce platform in two markets this year with the majority of the remaining markets in 2024 to enhance ease of recruiting sign-ups and retail transactions.

On to business revitalization. One of the places that pandemic hurt us was Nutrition Clubs, especially in China. Nutrition Clubs are coming back to life. Distributors are leveraging new creative ideas and success stories implemented in their marketplaces. Operators and distributors are becoming more sophisticated in maximizing Nutrition Club volume, defining metrics on a per-serving basis.

Working with regional management and distributors to be and enforce a data-driven approach to identifying new geographies for Nutrition Club expansion is part of our utilization. We want to give them data for where to go and how to operate clubs that are evolving, providing distributors with information they need to determine which markets are ideal opportunities, and what methods that they put into those marketplaces will maximize sales.

We have more methods to the marketplace than ever before. Person to person is where the company started. We moved on to Nutrition Club, hybrids, fit camps, social media cell and challenges, marathons, offices and evolving models around preferred members. We are working with distributors to maximize the opportunities we have with their preferred customers.

We are working with distributors to activate upselling with their customers, focused with a team here internally to maximize that opportunity. We are enhancing our data analytics and our ability to take action on the data we are collecting to increase preferred customer sales, reminders, suggestive selling, all of the opportunities that are ahead of us and with us today. We have taken steps to modernize our distributors' compensation structure. These are huge.

New programs launched on February 1 are designed to consistently enhance the economic opportunity for up-and-coming distributor leaders. We want them to earn faster. We want to stimulate success earlier in their HLF journey. We are continuing. We currently have two months of results, which are hitting our initial expectations. We're seeing an increase in qualifiers, and we're beginning to see early signs of some organizations increasing their royalties and personal production. We're monitoring this closely to see if the results continue as expected or if tweaks are necessary, so we can evolve this program for success.

Let me get on to some organization changes. I've been back for 6 months now. This is Michael 3.0. And I think my team can attest to the fact that I've never been more focused, more passionate about Herbalife than I am today. I've had time to assess, focus and understand who and what we need to do in order to build a team to have a success built into our DNA deep into the future.

We have a deep and incredibly talented team here. I can't mention everyone, but last quarter, we laid out a strategic plan and our team is completely aligned on our brand, our digital information, information innovation, our distributor engagement, our focused on recruiting, retailing and retention.

So now I'm announcing that we're making changes to speed this plan to our marketplace. It's with a little bit of regret and probably deep regret that I announce Mark Schissel's retirement. Mark has been with us for 16 years of dedicated service. Today, we announced a new organization structure that will provide efficiency, scale and position us for long-term growth. But Mark, you've been a super trooper here. You've been a friend of me. You've been a colleague to our distributors and an incredible contributor to this company.

As I said before, I'm super proud of this team, but the one wonderful thing we have here is a deep bench. We have appointed Frank Lamberti, who has 18 years of tenure to Chief Operating Officer. This is a huge job, but Frank is the right person.

He's got a great team with him and he is focused on building Herbalife bigger, better and stronger. The cool thing about Frank is he is a fitness freak, he's health focused and he's obsessed with his food intake. That makes him a perfect Herbalife executive.

Frank joined Herbalife in 2005 as Vice President of Investor Relations, has served in numerous leadership positions, including most recently as the Regional President of the Americas working closely with distributors and their customers. Prior to that, Frank worked as Executive Vice President of Distributor and Customer Experience. He also worked abroad as Senior Vice President and Managing Director of North Asia.

Frank has a big job ahead of them. He will be handling all of our digital content, our product innovation, supply chain, sales, data analytics, manage our vertical process and manage our back office. Frank, you're the right man at the right time for the right job. Thank you very much for stepping up.

Ibi Montesino is a Herbalife success story, 24 years of tenure. We have expanded her role to Executive Vice President and Chief of Staff. She is an inspiration to our distributors and to all of our employees. As she joined Herbalife in 1998 as an assistant for Personal Care, transitioned to product marketing before joining the North American region where she served in multiple capacities, including Director -- Senior Director, Vice President of Sales, Marketing for the U.S. Latin market and eventually heading in a growth period, the entire North American market.

Ibi's expanded management authorities is a voice to all employees and distributors through human resources, brand marketing, social media, corporate communications and our very important worldwide events and sales. Ibi, congratulations, and welcome again to your new role.

On top of all this, we've appointed Rob Levy to President of the Americas. Rob has been on a partner to me for over 20 years. He's a proven leader, trusted by distributors and his colleagues, a long time Herbalife and industry veteran with 28 years at the company. Rob has run every region during his tenure. He has been responsible for all distributor-facing businesses, including sales, marketing, distributor operations and functions.

I took a long time to announce these folks, because this group has 70 years of combined experience. Their energy and passion belies their time here. Their wisdom will help get us back to growth, innovate and expand Herbalife.

I told you when I started -- I told you when I came back that I had started 20 years ago in this company. This is an amazing place, and we have built an incredible community here. The friendships that I have built among our team and our distributors are frankly just amazing. We've had some Board of Director changes, and I want to thank John Tartol, who has been a distributor member of our Board for 18 years. I want to thank you, John, not only for your service, but your friendship.

And I want to welcome Stefan Graziani, who joins Juan Miguel Mendoza. They are 2 of our most data and analytics-driven distributors, and they're going to help us on our digital journey. Their friendship, their consult and their wisdom will help us move forward faster. So Alex, let me turn it over to you for some financials, and we'll come back to me for a close.

Alexander Amezquita^ Thank you, Michael. I'll begin my section with key financial highlights for the quarter. First, quarter net sales of \$1.3 billion were down 6.3% compared to the prior year. Year-over-year reported net sales trends in all 5 regions improved compared to the fourth quarter trends. Currency pressure continued to weigh on our results during the quarter resulting in a 370 basis points currency headwind to net sales.

Q1 gross profit margin of 76.2% was approximately 80 basis points below prior year. Currency movement drove significant pressure on our gross profit margin, resulting in an approximately 150 basis point headwind compared to the first quarter of '22. Over the past year, our pricing actions have outpaced input cost inflation, and if not for currency, we would have had year-over-year gross profit margin expansion this quarter.

While the U.S. dollar has been on a weakening trend since the third quarter of 2022, it is still stronger than currency rates during the first quarter a year ago. Should rates stay relatively constant, we anticipate gross profit margin improvement to Q1 in the balance of the year.

First quarter adjusted EBITDA of \$129 million was below first quarter of last year. This reduction was driven primarily by the lower top line in the quarter and a currency headwind of approximately \$37 million. Additionally, as Michael mentioned, our in-person events have increased in 2023 with event spending up \$20 million in the first quarter of 2013 compared to the same period last year. Note that approximately half of the \$20 million is due to the timing events that occurred in Q1 of this year as compared to Q2 of last year.

Adjusted diluted EPS of \$0.54 was negatively impacted by a \$0.32 currency headwind. Adjusting for the currency headwind and the timing of event spend, as previously mentioned, Q1 adjusted EPS would have been relatively flat compared to prior year.

During the first quarter, we made significant progress on our previously announced Transformation program to strategically improve our productivity. Our actions taken to date have unlocked approximately \$35 million of savings for 2023 with the total program expected to deliver annual savings in excess of \$70 million in 2024 and beyond.

And sixth, we took proactive steps last week to ensure we provided ourselves greater financial flexibility to make investments in key initiatives by amending our senior secured credit facility to increase the gross leverage ratio covenant, which we will discuss in more details in the following slides. It is important to note that we were within compliance with all covenants as of March 31, 2023.



We continue to manage our balance sheet towards investment-grade metrics and a 3x gross leverage ratio as evidenced by our repayment of approximately \$67 million of our outstanding debt.

Reported net sales for the first quarter declined 6.3% from a year ago. However, on a constant currency basis, sales were down 2.6%. The year-over-year reported net sales trends for the quarter improved in all 5 of our geographic regions compared to the year-over-year results for the fourth quarter of 2022.

Reported net income for the first quarter was \$29 million, with adjusted EBITDA of \$129 million. Adjusted EBITDA margin was 10.3%, which was weighed down by negative FX impacts, higher input costs and distributor event spending in the quarter. As I previously stated, some of the pressure to adjusted EBITDA and gross profit in the quarter was purely due to timing.

Reported diluted EPS was \$0.29 for the quarter, with adjusted diluted earnings per share of \$0.54. Reported diluted EPS was impacted by a onetime charge of \$0.21 due to separation and retention, and executing of the Transformation program.

Adjusted diluted EPS was negatively impacted by a year-over-year currency headwind of approximately \$0.32, primarily driven by a stronger U.S. dollar compared to the first quarter of '22. Assuming rates hold at current levels, we expect a smaller currency headwind in '22 -- I mean we expect a smaller currency headwind in the second quarter, followed by a tailwind in the back half of the year.

During the first quarter, the company strategically paid down approximately \$67 million of its outstanding debt. We ended the quarter at 3.6x gross debt to adjusted EBITDA, which is above our targeted leverage ratio of 3x. We plan to use free cash flow generated in 2023 to continue to reduce our nominal debt levels as we work towards our long-term target leverage.

First quarter net sales benefited from 13 percentage points of pricing as a result of price increases implemented over the past 12 months. Local currency net sales for the first quarter were down 2.6% compared to the prior year. The U.S. dollar weakened toward the end of the first quarter against most major currencies, but was still elevated compared to the first quarter.

Moving to adjusted EBITDA margins, where adjusted EBITDA of \$129 million resulted in adjusted EBITDA margin of 10.3%, 360 basis points below prior year. Adjusted EBITDA margin benefited by approximately 480 basis points as a result of our recent price increases. However, we continue to be impacted by elevated raw materials and manufacturing overhead costs, which drove an adjusted EBITDA margin headwind versus prior year of approximately 220 basis points.

Inventory write-downs were slightly elevated in the quarter due to recent sales trends, which combined with other cost items, combined to a 60 base impact to EBITDA margin.

Within SG&A, we experienced approximately 220 basis point headwind related to promotional spend, largely to the return of in-person events in most regions as well as the timing of our major annual global event, which we held in-person in March this year versus virtually in the second quarter of 2022.

As Michael referenced, we believe the energy and engagement being generated at our in-person events will translate into improving metrics as the year progresses. As mentioned earlier, currency had a significant impact and led to an additional headwind of approximately 240 basis points on adjusted EBITDA margin.

For the quarter, active sales leaders of approximately 462,000 was 6% below last year. Although this number has come down from its peak in 2021, we are still 7% above first quarter of 2020 and 14% above the first quarter of 2019. While the Q1 new distributor and preferred customer metric followed the usual seasonality and increased sequentially, new entrants declined about 2% compared to the first quarter of 2022.

Turning to our regional results for the quarter, where the Asia Pacific region was up 1% on a reported basis and 9% on a local currency basis. The region was led by continued strength in India, which grew 18% on a reported basis and 28% in local currency.

Taiwan was up 4% or 13% in local currency. The EMEA region saw a 3% decline in local currency net sales, which was amplified by approximately 600 basis points of currency pressure in the quarter as reported net sales were down 9%.

Within the LatAm region, Mexico's reported net sales grew 8% compared to the prior year. Brazil's reported net sales grew 4% in the quarter, returning to growth after several challenging years.

Moving to the next slide. I will recap the status of our Transformation program that we initiated in 2021 to strategically optimize our global processes for future growth. As a reminder, the Transformation program involves both the realignment of infrastructure as well as locations of certain functions in order to better support our distributors and customers.

In the first quarter, we made significant progress on this initiative. The actions we have taken to date will result in approximately \$35 million of savings in 2023, and we are now on track to exceed \$70 million of total program run rate savings in 2024 and beyond.

During the quarter, we recognized onetime pretax expenses of approximately \$27 million or \$0.27 in SG&A. These nonrecurring expenses are excluded from our adjusted results. In total, we have incurred \$52 million of at least \$60 million we expect to incur in order to realize the expected full run rate savings of the program.

Turning to our capital structure and cash position. During the quarter, we strategically paid down our nominal debt by \$67 million, including a full repayment of our revolving credit facility. The \$330 million revolving credit facility remains fully undrawn and available for future borrowings. At the end of first quarter, our gross leverage ratio was 3.6x, and we are fully compliant with all debt covenants.

As I mentioned earlier, in April, we amended our senior credit facility to increase our gross leverage ratio covenant in order to provide greater financial flexibility as we invest in the business for growth. Our gross leverage ratio covenant was raised from 3.75x and to 4.5x through December of 2023, stepping down to 4.25 as of the end of the first quarter and 4x thereafter.

Turning to cash flow. And while our cash generation ability remains strong, free cash flow in the first quarter was below historical run rates. For 2023, we will continue to execute on the initiatives to optimize working capital. Our capital allocation and long-term views of cash priorities remain unchanged.

As always, our number one priority is to service our debt as we work towards our targeted gross leverage of 3x. We plan to use free cash flow generated in 2023 to continue to reduce our nominal debt levels. This concludes our prepared remarks. Operator, please open the line for questions.

## QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) Our first question comes from the line of Chasen Bender with Citi.

Chasen Bender^ I'd just like to start on the distributor trends, specifically, just in context of the historical quarter over -- quarter-over-quarter change we usually see from 4Q to 1Q. Active sales leaders trends actually look to be improving for a couple of your markets like North America, which I think probably reflects all the work you're doing.

But they actually step back in a couple of others like EMEA and LatAm. So I'm just wondering, is there something unique to those markets that are inhibiting the stabilization relative to North America? Or is it just macro? Just any comment you can provide there would be great.

Alexander Amezcuita^ Yes. So generally, the trends of our active sales leaders are going to be a lagging effect of what you see on the new distributors and preferred members. And as you saw for much of '22 and particularly the markets that you've noted, the funnel for those for our active sales leaders has been our new member KPIs have been in decline.

So the funnel for filling those active sales leaders I think it would be natural to expect some softness in our active sales leaders. With that said, there's still significant strength, I think, in the number of active sales leaders that are still participating in the business.

So where we currently sit with the strategic initiatives in place, our current level of active sales leaders and the trends that we expect it can still set us up for overall growth by the end of the year. I don't think that, that is something that we think of as prohibitive, but clearly, those are metrics and those are KPIs that we're focused on as we think about how to implement our overall strategic initiatives.

Chasen Bender^ Got it. I appreciate that color. And then just on the pretax charges related to the Transformation program. Can you remind us exactly what is in that \$27 million bucket? And it sounds like there's just a little bit of cleanup left relative to the \$60 million expectation. But just relative to the 7% global reduction in workforce that you announced last quarter, are those costs part of that? Or are there additional charges related to that program that we've yet to see?

Alexander Amezquita^ So the lion's share of that \$27 million is personnel cost. We talked about retention, separation costs, those types of things. As we mentioned in the last quarter, this was a pretty significant portion of this broader plan where there's overall a net workforce reduction of about 7%, 13% growth, 7% net. So the \$27 million is the execution of those personnel changes.

Chasen Bender^ Okay. So the 7% reduction in global workforce that \$27 mil and total \$60 million captures that. There's not an additional charge coming as you continue to work through personnel. Did I understand that correctly?

Alexander Amezquita^ There will continue to be incremental expenses, but the \$27 million that you referenced is largely execution on a personnel level, so for separation and retention purposes.

Chasen Bender^ Okay. Got it. And then just on the credit amendment, obviously, increasing the leverage covenant gives you a lot of breathing room in 2Q, but in the second half, as you roll off some of the stronger 22 years old implies a big step-up in EBITDA, ostensibly like that's when the business is -- has had time to digest a lot of the changes you've made and more of the cost savings are going through. But can you just speak to your confidence in staying within the leverage covenant leverage covenant? And just remind us if there are any other covenants that are at risk of being tripped?

Alexander Amezquita^ Yes, so the covenant that we had amended was the default covenant on our senior credit facility. And we don't see any risk of that -- of breaching that covenant in 2023 or beyond. Even when we step down in 2024, we're stepping down after our 2024 converts are paid down. We actually have even with the step down more financial flexibility post that date with a step down than we do for the remainder of 2023. So we feel highly confident of those levels. I'll just leave it at that.

Operator^ Please stand by for our next question. Our next question comes from the line of Jeff Van Sinderen with B. Riley.

Jeffrey Van Sinderen^ And kind of if you can bear with me as a little bit of a multipart question here, but can you speak more about what you're seeing in North America, what you're hearing from kind of your key North American distributors, what the new distributor adds and overall distributor retention metrics look like in North America.

I'm not sure if I saw that maybe buried somewhere. And then I know you said you expect year-over-year sales growth for the whole company in Q4. Do you expect North America segment to inflect year-over-year growth in Q4 as well? Or if not, what do you think needs to happen to return to growth in North America?

Alexander Amezquita^ Yes. So I think overall -- so first, let's start with the retention metric. The retention metric that we provide is an annual metric. So you could keep digging for it, but you're not going to find it. It's only in our case that we provide that. We provide that on an annual basis. If you look in our supplementals, you can look at something that approximates retention as we go along, which is activity or activity percentage. And again, that's provided in our supplemental on our website. So you can kind of get an idea of that in between those annual retention tests.

As it relates to overall growth, we're not providing market-by-market guidance, but obviously, what would be instrumental in achieving overall growth in the company by the fourth quarter would be significant improvement in North America. I think that is a core tenet in our overall expectation of overall company growth is we're going to have to see significant improvement in North America. Will that translate into specific growth in North America at that time? I think we'll have to see. But obviously, significant recovery as part of that overall thesis.

Jeffrey Van Sinderen^ And I mean you have some regions, I think you called out Mexico and maybe it was Brazil that were actually positive. So as we think about the other part of North America, and I don't know, maybe Michael wants to speak to this, but what do you believe needs to happen to get North America back to, let's say, close to flattish or hopefully closer to flattish as we exit the year?

Michael Johnson^ So thank you. We're so engaged with our distributors right now in North America. It's hard for me to imagine a time when we've been more analytically data-driven, engaged with that group of distributors than ever before. So we have taken each state and broken it into sections in terms of to try to validate and understand what models are working. We have been working with a group of distributors in the Southeast, into New York and in Texas and then here in California.

We're very energized and excited about what they see in the business, especially around Nutrition Clubs, fit clubs and getting the healthy active lifestyle back into our business that kind of fell apart during the pandemic, and we're seeing an uptick in that. But the overall strength is going to be one that is going to have to take place across a lot of states and across a lot of regions in a very short period of time. And so I wouldn't predict that, that's going to happen quickly. I think it's going to happen systematically.

It takes 12 months for a new distributor to open up a Nutrition Club. So we have a lag there. It takes a little time for them to understand how to operate these clubs most effectively. Our social media selling is on the uptick, but it needs to be refurbished. And we are building -- we have a San Antonio Extravaganza coming up. We'll launch an extremely positive new line there of products that we think will enhance and help Nutrition Club operators build out their customers even stronger, but this takes time.

So I don't want to use the word lag, because I never liked that word much, but it's a reality right now that once we get these in place, it takes a little time for them to have effect. The energy and excitement among our distributors is super high. And how that translates into numbers will take a little time.

Jeffrey Van Sinderen^ Okay. That's fair. And then if I could, just wanted to get a sense, I guess, of what trends you're seeing even just sequentially in terms of weight management products, maybe how that -- if there's anything to call out by region.

I know India has been really strong. And then maybe just touch on kind of key new product rollouts for 2023 and then any new products that you have rolled out so far, kind of traction you're getting there so far this year? And then also, as part of that, just if you could just update us on the SKU rationalization process.

Alexander Amezcuita^ Yes. So I'll take just overall, I think the bright spot of our product categories that we think about it is still in the energy fitness category. If you look in the, we actually are having positive year-over-year net sales growth in that category. And that's primarily being led by the energy products within that category and predominantly led by India as a region in driving that growth. I think for the rest of weight management and some of the other products, they're just holding serve with the overall with the -- how the overall markets are trending.

So we'll continue to -- our product rollouts I think you've seen some of them. We've talked about some of the vegan line coming out in North America, and some of our other products are really incremental to our existing product philosophies. But more to come on with products as we are launching Herbalife 2.0. I know we have -- I don't know if we want to mention you'd like to...

Michael Johnson^ How many cats do you want to let out of the bag? You just mentioned the vegan line. So, that's okay. All right. So I'm looking at Frank, who's our Chief Operating Officer now and also the former Head of North America and the Americas. We've got a lot of products in the pipeline right now. Our product release program is extensive in this company. The SK -- the SKU rat that is going on inside the company is going to remove Mark, you're sitting here, how many -- what is the SKU rationalization number exactly?

Mark Schissel^ 15% of our portfolio.

Michael Johnson^ 15% of our portfolio is going to be reduced, and that's going to allow us more innovation, the use of resources to put towards innovation. We have a new member, and I mentioned it last time of our product development team and innovation team here, the gentleman who brought us Herbalife24, Dr. John Hiss, who's looking at every piece of our product portfolio right now.

We have a couple of major, what should I say, product innovations that I don't want to tip right now that are going to be released in the near future. We'll test a few in some marketplaces. This is our new mentality and here is to test it to make sure it works.

We have a couple of products in Europe, Vital Complete, that's delivering some very early positive numbers to us. India has a self-contained product line there. They continue to enhance and create new products. We're looking at our innovation center in Asia as a huge opportunity for us. I just don't want to tip the hat on some of these products that are coming because our distributors don't know about them yet.

We work closely with the distributors to make sure that everything we're bringing to the marketplace has a distributor method of operation that it fits in and works closely with their business. I know that's a little bit of a political answer for you, but that's the best you're going to get right now.

Operator^ Please stand by for our next question. Our next question comes from the line of William Reuter with Bank of America.

William Reuter^ Firstly, you commented that the benefit of pricing was 13% in the quarter. I know you've been hesitant to take additional price increases after the large 1 last summer. Where are you guys in terms of additional price increases for the remainder of the year?

Alexander Amezquita^ Yes. Obviously, 13% quarter-over-quarter is a massive number. I think if you look at sort of the performance post that -- post the price increases, that we predominantly took mid last year, there is some level of demand elasticity and there's some level of market saturation, particularly in the U.S. and some Western European markets in terms of the ability to continue to take price.

And so while we're not necessarily made whole from a gross profit margin on all the input supply chain escalations that we've seen over the past year and change, there does seem to be a limitation for how much pricing we can continue to pass on to the market.

So I think what you're going to see from us in 2023 is some level of price increases on a lot lower level than what we executed on in 2022. And we're just really going to monitor it closely and see how -- on a market-by-market basis, how those price increases are being impacted. But -- so overall, I would summarize much more conservative in terms of the amount of price increases we're going to be taking and really taking a more prudent view on demand elasticity as we move through 2023.

William Reuter^ Okay. Previously, you had noted that free cash flow this year should be above 2022. I don't think I heard an update, Alex, in your prepared remarks on that. I know your first quarter, you said, was below kind of historical levels. Where are you on that thought process?

Alexander Amezquita^ Yes. So the first quarter free cash flow is going to look unseasonably low. There are some timing impacts on that. So for example, some big cash flow items, a bonus that we paid in Q2 to distributor as part of their compensation program. We did that in Q2 last year, we did it in Q1 this year. That's a \$70 million item. And there's a handful of other smaller costs that we saw in Q1 that's disproportionately bringing our first quarter free cash flow down.

Overall, we expect for 2023, our operating cash flow to still be in excess of where we were in 2022. The variable then on free cash flow would just be how we execute against the Herbalife ONE and the CapEx we put against that whether or not we'll be above or below our free cash flow. So long story short, OCF higher than 2022. And one of the variables that we still have is on the execution of H1 on where the free cash flow will actually land for the year.

William Reuter^ Got it. And then just lastly for me. In terms of the debt that was repaid in the quarter, I have not seen that. It may be in the supplemental slides. But what debt did you target? Was it just the credit facility, the revolver?

Alexander Amezquita^ That's correct. We had \$60 million drawn on the revolver and then there's a balance of about \$7 million of just your standard term loan amor.

Operator^ Please for our next question. Our next question comes from the line of Hale Holden with Barclays.

Hale Holden^ I had two quick ones. Am I supposed to understand the \$20 million of additional kind of event spending in the first quarter was just a timing shift from 2Q last year to 1Q this year, and so that's why SG&A looks a little elevated from, I guess, where we might have thought it would have been?

Alexander Amezquita^ That's right. Well, \$10 million of the \$20 million. So \$10 million relate to an event, primarily the event held in Los Angeles that we call Honors. Last year, it was in the second quarter, this year, it's in the first quarter. So \$10 million of it is just timing and then \$10 million of it is more activity engagement around events as a method of promotional spend and engagement spend.

Hale Holden^ Got it. And so the other question I had was on the leverage covenant increase that you got. If we're going to get back to revenue growth, is this a function of additional investment over the next six to nine months to kind of get the flywheel going faster that should be a drag to margins? Or is it just simply an LTM timing from highs from last year that you're just trying to make sure that you have room for?



Alexander Amezquita^ More of the latter. It's just simply as we move through the year, there may be some LTM flexibility that we would want as we go forward. By the way, removing the covenants to places that would still -- particularly where it lands at 4x, I mean, still consistent with the covenant of an investment-grade covenant. So it's really just actually getting -- what I would say kind of getting our credit facility with covenants that probably should have been more representative of what we should have been in the first quarter.

Operator^ Please stand by for our next question. Our next question comes from the line of Anna Lizzul with Bank of America.

Unidentified Participant^ This is Yasmin on for Anna. So given that Asia Pacific outperformed the rest of your geographies on regional volume point metrics, are there any learnings you can take from that region and apply to regions where you see steeper declines?

Alexander Amezquita^ 100%. I mean that is one of the things that we do well as a management team. As we look at what's working well in any particular region, and we work with our distributors and get those best practices in other places of the world. Now the principal driver of that in the APAC region is India.

That is the principal driver of the overall regional growth where India was up significantly Q1 over Q1. India has been a growth driver now for us for a number of years and for at least the past handful of quarters. We've been taking deep dives in the Indian market and what's working well there and working with our distributors to have some of those best practices communicated to other markets around the world.

Michael Johnson^ And I'd say just to add to that, it's not just India. It is in marketplaces where we see distributors succeeding, even though the overall market may be down. We are working very closely with those distributors, both with data analytics practices, where they are in the marketplace, getting down to the grassroots with them.

We have some distributors who are doing fabulous in North America, doing fabulous in Europe. And we want to make sure we're exporting those ideas as fast and furiously as we possibly can. That's what these Extravanzas are about. That's what these big meetings are about is to bring in voices from distributors who are successfully employing the Herbalife business model in their marketplace to train and teach other distributors on how to do the same.

So while India is a success story, and we love it, and it's doing great there because the energy, enthusiasm and business practices there are fantastic. We have pockets of success all over the world. In Brazil, Mexico, North America, Europe, Asia, we're seeing all sorts of things. It's just -- we now need to globalize those as fast as we can in the marketplace.

Unidentified Participant^ Got it. Okay. That's great. And I know earlier in this call, you guys talked a little bit about just regional performance. And I guess with the reopening in

China, would you mind providing some color on why China results were weak this quarter?

Alexander Amezcuita^ Well, on a year-over-year basis, certainly, they were down. I mean I actually look at it sequentially from where they were in the fourth quarter. And actually, you had volume increase in the Q1 versus volume in Q4. You typically don't see that because in the first quarter, Chinese New Year, Lunar New Year significantly impacts not just the week but almost the whole month for the first quarter.

And so to see sequential improvement in a quarter when you have the market really not fully engaged. And further, we know in China, even though that zero COVID policy was lifted during the quarter, there was really a month where a large swath of the population actually contracted COVID and was out of work. People were down and out of the count to the extent that we actually had to close our manufacturing facilities for the month of February. There were so many citizens that were impacted.

So to have those sort of headwinds and to still have sequential volume increase, I actually am quite pleased with how China actually rebounded from that. I'm looking forward to see how the second quarter goes there.

Michael Johnson^ Yes. We have an impact in China where now we are just getting back to live meetings in the last couple of months where Nutrition Clubs are starting to reopen in that marketplace. You've got to realize that in China, when they went into lockdown, it was much different than any place on the face of the earth. It was a true lockdown. Our clubs were heavily and highly impacted.

We didn't have the ability to get to the digital platform as fast as we would have liked. We're working on that right now. But I think without being too positive here or too negative, I think we're going to see some interesting news out of China over the next couple of quarters.

Operator^ Please stand by for our next question. Our next question comes from the line of Karru Martinson with Jefferies.

Karru Martinson^ When you look at the cost for distributor events, do you feel that, that's on par with kind of what you were spending pre-pandemic? Or does this represent a step up from that period as well?

Alexander Amezcuita^ I think it represents what's consistent with pre-pandemic, particularly in the event spend. It's a little bit more than the pandemic times. Particularly, we had a pretty significant shift from events to some other types of promotional spending. So I don't think it's that aligned with historical run rates. And quite frankly, it's what the business needs more than anything right now. So I think it's -- as we think about where to put the spend, this is, I think, an effective use of it.

Karru Martinson^ Okay. And then have you seen the changes in the new distributor compensation start to kind of impact that sign up? Or is it just too early in that process?

Alexander Amezquita^ Yes. So yes. So we've seen -- I mean it's early stages, but we have seen positive impacts from both of the marketing plan changes that we made in February. It's less around sign-ups. Those marketing plan changes that we made is really about motivational impacts in distributors that already have their feet wet are looking to really grow their organizations into larger substantial business. It's really for that sort of middle distributor, I would say.

And so we're seeing good signs of those impacts taking hold. It is going to be something that is going to take months, if not quarters for it to really full bear fruit, but we're very pleased with the progress so far.

Operator^ I'm showing no further questions in the queue. I would now like to turn the call back to Chairman and CEO, Michael Johnson.

Michael Johnson^ Thank you all very much. Thanks for being on this call. I get pretty excited during my presentation because we're seeing positive trends here. We've got a management team and a distributor base that's fully energized. We've said that before, but we're really starting to see some changes in the atmosphere here. We're excited about the new digital platform. We've got some wonderful products rolling out. Our distributors, our Board, our investors, employees, super excited and aligned on where we are.

These have been a tough couple of years for Herbalife without a doubt. Not in my experience, have I ever seen this happen in our company, but I know, and I know everybody else knows in here that we're on a pathway to improve success in the company.

We're on a pathway to, frankly, improve a lot of lives in this company. This is a super unique company. I am really excited to be back here. I said that six months ago, I'm going to say it today. And probably say it again in six months. This company is just something special, and we know that the best days of Herbalife are ahead of us.

So thank you for being with us. We're looking forward to seeing you next quarter. Hopefully, we'll be here with some better numbers. It's going to take a little patience and time, but we know Herbalife is on a path to success. So thank you all very much. Thanks for being with us, and I wouldn't be me if I didn't say let's go Herbalife.

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