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Q1 2022 Herbalife Nutrition Ltd Earnings Call

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PRESENTATION

Operator

Good afternoon, and thank you for joining the First Quarter 2022 Earnings Conference Call for Herbalife Nutrition Ltd. On the call today is Dr. John Agwunobi, the company's Chairman and CEO; John DeSimone, the company's President; Alex Amezcuita, the company's Chief Financial Officer; and Eric Monroe, the company's Senior Director, Investor Relations.

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

Eric Monroe Herbalife Nutrition Ltd. - Senior Director of IR

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

In addition, during this call, certain financial performance measures may be discussed that differ from comparable measures contained in our financial statements prepared in accordance with U.S. generally accepted accounting principles referred to by the Securities and Exchange Commission as non-GAAP financial measures. We believe that these non-GAAP financial measures assist management and investors in evaluating our performance and preparing period-to-period results of operations in a more meaningful and consistent manner as discussed in greater detail in the supplemental schedules to our earnings release. A reconciliation of these non-GAAP measures to the most comparable GAAP financial measures is included in our earnings press release submitted to the SEC. These reconciliations, together with additional supplemental information, are available at the Investor Relations section of our website, herbalife.com. Additionally, when management makes reference to volumes during this conference call, they are referring to volume points.

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

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

Good afternoon. Thank you for joining us on the call today. I'll jump right into our Q1 performance, where volume points for the quarter declined 7% compared to the prior year. This result was within our Q1 guidance range of down 9.5% to down 3.5%. Reported net sales for the first quarter declined 11% compared to the prior year, which was below our guidance range. The bridge between volume point and net sales results was driven by the unfavorable impact of foreign exchange rates during the quarter as well as a shift in the geographic mix of revenue compared to our projections.

We were able to deliver bottom line results at the high end of our guidance range. Reported earnings per share for the first quarter was \$0.96, and adjusted earnings per diluted share was \$0.99, near the top of our adjusted earnings per share guidance range of \$0.80 to

\$1. Net income during the quarter was \$98.2 million, resulting in adjusted EBITDA of \$185.6 million, just above our adjusted EBITDA guidance range of \$165 million to \$185 million.

Overall, top line results fell short of our expectations. From a macro perspective, we believe economic pressures from the inflationary environment and widespread geopolitical uncertainty has had an impact on our channel. Additionally, the current wave of the COVID-19 crisis in Asia Pacific and South and Central America negatively impacted the business during the quarter. And in China, the latest lockdowns have added to ongoing challenges in that market.

Despite the adaptability and ingenuity of our distributor base, we've begun to see an emerging shift in behavior. Specifically, we've begun to see that as a group, the behavior of distributors that joined the business during the pandemic has diverged from historic trends. The number of distributors from this cohort that are ordering and recruiting is below last year and below expectations.

However, on the positive side, this slowdown is primarily isolated to the collective performance of this pandemic era group. As those that joined the business pre-pandemic continue to order at historical levels. Also on the positive side, we've not seen a material change in the behavior in our preferred customer segment as a whole.

We believe this data, which shows consistent behavior within the pre-pandemic distributor cohort and our total preferred customer segment demonstrates the continued strength of the foundation of our business. It also makes us believe that the return of in-person events and the numerous sales initiatives that we've implemented at a local level will act as a catalyst to improve the results.

Most of the distributors that joined Herbalife during the pandemic have never been to an in-person event, and there is no substitute for gathering in person for learning, collaborating and motivating.

As a result of the top line trends observed during the first quarter and year-to-date, we are updating our guidance for the year. For the full year, we are lowering our net sales guidance to a range of down 10% to down 4%. The volume point guidance is being reduced to a range of down 12.5% to down 6.5%. Our updated guidance implies year-over-year net sales will be flat in the second half of the year, and we will show growth for the fourth quarter. Our teams here at corporate and around the world are laser-focused on achieving this growth.

We are also focused on improving margins and controlling costs. As we discussed in detail last quarter, input cost inflation continues to be at historic levels, driving a significant rise in costs for ingredients, production and transportation of product. We are actively engaged on multiple fronts to support margin accretion. Today, we're announcing that incremental pricing actions will be implemented globally in the second quarter. These price increases will partially offset the ongoing increases in input and freight costs.

In addition to price, we are implementing cost control measures. We're being surgical in our approach to avoid any negative impact on sales or service to our distributors. These actions are in addition to the transformation program we announced last quarter. As such, we expect to see an improving EBITDA margin trend in the back half of 2022 compared to the first half of the year and an accretive full year margin in 2023 compared to full year 2022.

Before I turn it over to Alex, I want to say that we have an unwavering confidence in the resilience and strength of our business, and we're keenly focused on creating shareholder value through driving performance and returning to growth. I will now turn the call over to Alex.

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

First quarter net sales of \$1.3 billion represents a decline of 11% on a reported basis compared to the first quarter in 2021. As John mentioned, although volume points landed near the midpoint of our guidance range, net sales were negatively impacted by currency movement and country mix. The unfavorable country mix impact was largely driven by India outperforming our expectation, while China, Western Europe and the U.S. underperformed.

Currency was a headwind to net sales in the quarter, representing a drag of approximately 320 basis points, which was 80 basis points unfavorable than what was assumed in Q1 guidance. As you are aware, the Q1 year-over-year trend was impacted by a challenging

comparison period. When comparing to the last quarter that was largely unimpacted by the pandemic, our 2-year stack grew approximately 6%.

Reported gross margin for the first quarter of 77% decreased by approximately 210 basis points compared to the prior year period. The decrease was largely driven by increased costs in our supply chain, lower production volume at our facilities and the unfavorable impact of country mix. The decreases were partially offset by the impact of our price increases, which were taken in line with our historical strategy to increase prices in line with local CPI.

First quarter 2022 reported and adjusted SG&A as a percentage of net sales were 34% and 33.8%, respectively. Excluding China member payments, adjusted SG&A as a percentage of net sales was 29.8%, approximately 250 basis points unfavorable compared to the first quarter 2021. This was primarily driven by the reduction in net sales as nominal spend was down year-over-year, partially due to the timing of distributor events that took place in Q1 last year and will take place in Q2 this year. For the first quarter, we reported net income of approximately \$98.2 million or \$0.96 per diluted share. This resulted in adjusted earnings per share of \$0.99 and adjusted EBITDA of \$185.6 million.

Both adjusted EPS and adjusted EBITDA results finished at the high end of our guidance range for the quarter. Note that Q1 benefited from approximately \$0.10 of China grant income that we had previously projected to occur in the second quarter.

We are issuing guidance for the second quarter 2022 as well as revising our full year '22 guidance. For the second quarter, we estimate net sales to be in the range down 17.5% to down 11.5%, which includes an approximately 270 basis point currency headwind versus the prior year. For context, the midpoint of this guidance range is an increase of approximately 7% over the second quarter of 2019, which was the last second quarter prior to the pandemic.

Second quarter adjusted diluted EPS is estimated to be in the range of \$0.60 to \$0.80. Adjusted EBITDA is expected to be in the range of \$135 million to \$155 million. Adjusted EPS and EBITDA include a projected currency headwind of \$0.07 and \$9 million, respectively, compared to the second quarter of 2021.

For the full year, we are reducing our net sales estimates to be in a range of down 10% to down 4% on a reported basis. The revised guidance implied an approximately flat second half of '22. And as John stated, we expect to return to year-over-year net sales growth in the fourth quarter.

The strengthening of the dollar has resulted in an expected full year currency headwind to net sales of 230 basis points compared to the expected 160 basis points headwind from a quarter ago. As a reminder, the projected currency headwind is reflected of the average U.S. dollar to foreign currency exchange rates for the first 2 weeks of April.

We are reducing full year '22 guidance for adjusted diluted EPS to a range of \$3.50 to \$4. This \$0.75 reduction to the midpoint of our prior adjusted EPS guidance is primarily driven by reduced sales expectations for the remainder of the year, partially offset by the incremental pricing actions and cost control measures. FX now represents an approximately \$0.23 headwind for the year, \$0.06 unfavorable from the \$0.17 headwind assumed a quarter ago.

For the year, we now expect adjusted EBITDA to be in a range of \$680 million to \$740 million. While organic sales growth remains our top priority, we are taking meaningful steps to improve margins. We implemented price increases in the majority of our markets in the first quarter that were consistent with our practice of keeping in line with local CPI. Given the unprecedented increase in our input and freight costs that are substantially in excess of current CPI levels, we will be taking incremental pricing actions during the second quarter. We are also implementing short-term and long-term cost control measures. These actions are in addition to the previously announced transformation program to optimize global processes for future growth while improving margins through productivity and efficiency enhancements within our business.

As I discussed last quarter, the company expects the first phase of the program to result in annual incremental savings in the range of \$10 million to \$15 million with some savings beginning in 2022. We are actively looking to accelerate the second phase of the program to

begin in late 2022 with expected ongoing annualized savings in the same magnitude as Phase 1.

Turning to our cash position and our share repurchase activity. We began '22 by generating \$130.5 million in operating cash flow in the first quarter. This was above our cash flow generation in the first quarter of '21. However, the first quarter benefited by the timing of our annual distributor bonus, which will be paid in the second quarter of '22, where it was paid during the first quarter last year.

We currently have \$570 million of cash on hand. This cash balance is after our execution of approximately \$102 million in share repurchases during the first quarter. We continue to believe the repurchase of common shares is consistent with the company's long-term goal of maximizing shareholder value. We remain committed to returning our excess cash flow to shareholders through share repurchases.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will come from Steph Wissink with Jefferies.

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

I'm wondering if we can talk about that pandemic recruited cohort. And if you can give us some sense of how much more burden on the model you expect to see before you digest through kind of a baselining of that cohort engagement?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

Yes. Steph, that's a great question. I think I'll kind of build up to that just to make sure the answer is clear. So I'll repeat some of what John said in the opening. First is we believe the foundation of the business is strong. And one of the reasons we believe that is when we look at the cohorts, those cohorts that have been in the business for a while are performing very well and that we can isolate -- at least predominantly isolate in most countries that the performance issue of those cohorts that came in during the pandemic.

We can also look at the history of our performance in various countries and see that as markets have grown pretty quickly in the past, it's not uncommon to see some of the newer cohorts underperform the older cohorts. And we know that we've been very resilient and been able to bounce back from that in the past.

Further, when you think of what has the pandemic cohorts kind of been exposed to, it's been exposed to a very limited amount of the Herbalife Nutrition business. You can almost put a fence around it. They've been only Zoom, only virtual, have not experienced the energy of Herbalife Nutrition. Has not had the cross-pollination of ideas that you get at events with both the people that are on stage training but also the other distributors and the energy you get from the other distributors and the confidence you get. And so they haven't had that exposure. So that's also some of what we're seeing. And what makes us believe that when you think of this as a layered business, right, the cohorts think of them as layers, right, the foundation being strong and some of the layers above it, collectively not being as strong, we think that in-person events can reengage some of the cohort that came in through the pandemic, but also we have to bring in new layers, and that's the key. And we're in this position where live events are starting up again.

And so we think that based on our long-term experience on what happens at events that we can reengage these folks quickly. So I think it's a matter of reengaging the cohort that's underperforming and bringing in new layers of new distributors into this new environment. So that's what we're expecting. It's not an overnight switch, right? This is a gradual improvement, but hopefully, we can start seeing some of that gradual improvements soon, certainly this year, and we expect the back half of this year to see some improvement over what we're seeing now.

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

Okay. That actually leads into my second question, which is the stabilization in the back half with the fourth quarter returning to growth. If you could just give us some degree of what's underlying that assumption base. What are you seeing that gives you confidence in the

ability to kind of return to growth in the fourth quarter? Or what would you be watching for that might change the trajectory, either higher or lower as we progress over the course of the next several months?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

Yes, that makes sense, Steph. I'll take that question. And I'll answer it as it relates to our guidance. So our guidance for the rest of this year reflects what we saw this emerging trend that John A. articulated and that John D. just explained with the new cohort, it reflects the run rate that we saw largely in March, but even more so in April. And the rest of the guide reflects the behavior of that month taken forward. So if we just assume that the channel and our distributors and the business markets behave the same way that we're currently seeing because of the comps, the first half of this year comping over what was still a lot of demand in the first half of 2021 versus how it compares against the second half of 2021 with the same run rate that we're seeing over the past 2 months, you will see back half -- you'll see it flat in the back half from a net sales perspective, and that should imply some growth in the fourth quarter.

John G. DeSimone Herbalife Nutrition Ltd. - President

No, I was going to add one of the things that we look for, which is what I think was part of your question, and they fall into 2 categories. There's lots of metrics within these 2 categories, and our metrics or puzzle that we build based on all the metrics collectively. But think of it as activity and productivity and activity is a term -- it's an internal term we look at for measuring engagement, and it's a collective engagement, but it's also an individual distributor metric. And it can be how often they order, how often their organization orders, how many new recruits are coming in from the distributor level, how are those new distributors progressing up the marketing plan to sales leader and how their customer profile is looking and are they bringing in new preferred customers if that program is available in their market. So there's lots of metrics we look at, and we'll look at shifts in those metrics to determine if we're on track to the latest guidance.

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

I would just add that we're not looking at this passively. We have an active -- some might even say, aggressive plan to promote sales to -- in terms of around the world. Each market has a plan in place to drive sales across the course of the remainder of the year. But we also have a number of -- a large number of scheduled events that are scheduled to drop into place throughout the second, third, fourth quarter of this year. We're very confident as we look at that schedule of events and as we look at the schedule of sales-related activities that are happening in each of our markets around the world that, that, too, will help make sure we deliver on our guidance.

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

Last really quick one is just the risk parameters around could the business actually progressively get a bit worse before it gets a bit better. What are the conditions of the backdrop that you're seeing that give you confidence that the March/April trend line is suitable to just kind of straight line go forward from here?

John G. DeSimone Herbalife Nutrition Ltd. - President

Yes, Steph, this is John D. I'll take that one. So I'm in the belief -- we are in the belief that our return to live events is really the key, absent any other kind of global event, right? So what's happened since February, of course, is we've had the Russia, Ukraine event. And it's not localized to just Russia and Ukraine, right, the sentiment at the consumer and distributor level that could have had an impact on our activity levels across a lot of countries. And so absent any new event or any worsening of that particular conflict, we think that in-person events will be a kind of catalyst, almost an inflection point for our improving activity levels.

Operator

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

Douglas Matthai Lane Lane Research - Principal & Director of Research

Just looking at our forecast in the first quarter, which, as you pointed out, was a little miss on the top line. It wasn't a huge miss. But the biggest divergence from what I was looking for, I think, really was in North America. Can you talk then in a little more detail on what's going on in North America with regards to the volume points and the distributor trends?

John G. DeSimone Herbalife Nutrition Ltd. - President

Doug, this is John D. again. I'll take that one. So you're right in highlighting that, that may have been the market with the -- let's say, that underperformed the most versus our expectations. Now exactly what has already been described is what's going on in the U.S. When we

look at our performance by cohort, those distributors, those sales leaders that have been in the business for 2 years or more performing really well. It's the -- it's that newer cohort, the pandemic cohort, if you call that are underperforming. And it's not just limited to the U.S., but it's really seen in the markets that had the most growth during the pandemic, which is why you're seeing the most impact in the U.S. because it had 50%, 60% growth for a few quarters from the pandemic, and now we're giving some of that back because the group that came in at that time are the ones that are underperforming. So that's why you see an outweighed impact in the U.S. because it was outweighed on the other side, too, on the positive side when the pandemic initiated.

Douglas Matthai Lane Lane Research - Principal & Director of Research

Yes. I mean we're not seeing the same thing in Europe. Europe also had some good quarters there, maybe not 50%, but certainly 20%, 30%. And their declines from volume points anyway is pretty consistent the last 3 quarters in that high single-digit area. So why is the U.S. and North America acting so much more differently than Europe, for instance?

John G. DeSimone Herbalife Nutrition Ltd. - President

Well, it's not as much as it looks, right? So Europe is made up of 50-something countries, and it's a pool of countries, and it's got a basket effect that the U.S. doesn't have, right? The U.S. is a country, and even North America is in itself almost entirely just the U.S. for our business. So you're really looking at one country versus a basket of country. So if you look in Europe, the countries that grew the most during the pandemic, the U.K., South Africa, Spain, Italy, they're also having pretty steep declines. And so you're getting a basket effect. Plus you're offsetting a little bit of some of the decline in Europe with some pull forward in Russia, Ukraine business that happened in Q1.

Douglas Matthai Lane Lane Research - Principal & Director of Research

Speaking of that, you announced you're exiting Russia. Can you just walk us through what the dynamics are there just as far as logistics and timing and how you're going to handle -- I mean, does your forecast include Russia, not include Russia? How should we look at that?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

Yes. So as we said in our press release just after the onset of the war, we have stopped shipping product into Russia. So the inventory that was in market is expected to run off. I think there's still a handful of months left of inventory there as that inventory runs off. With respect to our full year as compared to the February guidance that we provided, about 120 million volume points isolated to Russia and then also to Ukraine, which obviously that market is not operating for all the obvious reasons. There's about \$120 million of volume points that are no longer in our forecast attributed to those 2 specific markets. Now obviously, the impact of Russia, Ukraine is beyond the borders of those 2 markets, but I think your question was specific to those markets. And so about 120 million volume points are attributed to those.

Douglas Matthai Lane Lane Research - Principal & Director of Research

And I assume there's some EPS impact to those volume points. I mean, obviously, a \$0.75 reduction, could we say \$0.10 of that is Russia?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

I mean you could just follow down the P&L and take our average and kind of back into the EPS impact.

Douglas Matthai Lane Lane Research - Principal & Director of Research

Okay. Fair enough. And just lastly, on stock buyback here. We talked about the \$50 million a quarter run rate is kind of a baseline that you have in your forecast. And you did \$100 million, which makes sense given where the stock price is. Any other kind of guidelines we should think about? Should we still be using a \$50 million a quarter baseline and then expect that there's opportunity for opportunistic upside depending upon how the quarter goes with regards to your stock?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

Yes. So we've indicated in our guidance package that the guidance package does still include the same assumptions, the \$50 million guide per quarter. So that's still in place. Nothing changes with respect to that.

Operator

Our next question will come from Hale Holden with Barclays.

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

I had a couple of questions. I guess, John, what gives you confidence that you're going to be able to add new layers on top of the base that are stronger as we go forward given the churn off from the pandemic cohort? I would just think it's sort of difficult to go out and recruit when you've got sort of a turn off of one tier coming.

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

Well, I think our -- the tier that's underperforming is a tier that probably was least exposed to methods of how to recruit -- how to bring in. And the foundation -- I'm going to call the foundation, again, the people that have been in the business since pre-pandemic that are actually the numbers of people ordering in that group are up. Their experts, they've been through a lot, they've seen a lot. They've been very resilient to things like the implementation of the FTC order and other very unique -- Herbalife unique and global situations that were challenging. And every time, they were resilient enough to re-recruit and reengage people. So I have that level of confidence in that group provided that we can get that group together in person with -- at events, I think that's going to be the key.

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

I'll just add, if I may, Hale. Over the years, 42 years now in the business, 95 different countries, we've had events in the past. I think this is where John was saying, where we had cohorts or air pockets in the pipeline, so to speak, that were weaker than their predecessor layers or the layers that followed. And the system is built in such a way that so long as our sponsor leaders are strong and they are, we're very resilient. They pull them in. They give them extra attention and time. And that's what these live events are all about.

It's one of the reasons we're so confident that, that's where we'll turn that around. The point being, we've seen on a smaller scale -- we've never seen a pandemic before, but on a country-by-country, market-by-market basis, we've seen these kinds of cohort-type dynamics occur in the past. And we've always fought through them. We're confident we'll do that with this cohort as well.

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

And actually, what you're looking at is really a bunch of synchronized events, right? Normally, the events that can drive inflections in growth or switch it to a decline unique to a country or a handful of countries, and we've always had the basket effect because we're in so many countries, where it doesn't have an overweighting impact on the overperformance. But with the pandemic, there were so many countries that grew at the same time and grew tremendously, and those are the ones that are suffering now that you're seeing a more collective impact on the overall performance of the company than you would normally see when these kinds of behavior shifts happened in the past.

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

Okay. My second question was, I guess, the opposite of what Doug just asked you, which is on your EBITDA guide, it looks like you'll be over your leverage started for the first time in some time on a gross basis. And I was wondering how that sort of played into your thinking on buybacks and capital allocation and what should be doing with your cash.

Alexander R. Amezcua *Herbalife Nutrition Ltd. - CFO*

Yes. The business is still going to generate cash and still has a profitability level that we feel comfortable with. So we feel very comfortable with keeping the \$50 million guide. Obviously, there's an opportunistic piece of our share repurchase program. So we're just going to have to monitor that as the year progresses to see how opportunistic we can be. But certainly, even with the revised level of EBITDA, we feel comfortable with the guide we've put out.

Operator

Our next question will come from Jeff Van Sinderen from B. Riley.

Jeffrey Wallin Van Sinderen *B. Riley Securities, Inc., Research Division - Senior Analyst*

Let me say this is a multipart question, if you can just bear with me a little bit. As you look at your major regions and contemplate a return to growth year-over-year in Q4, which regions do you see driving that growth? Is that really just a big bounce back in the U.S.? And

then maybe if you could touch on your thinking about perhaps a little bit longer term when each major region might return to growth that isn't growing now, even if that's beyond Q4. And then also maybe if you could remind us how the company has performed in a macroeconomic recession in the past.

John G. DeSimone Herbalife Nutrition Ltd. - President

This is John D. I'll take that. So we don't give specific guidance by region. So I think when you just go back for the last couple of years and look at the regions that had very meaningful growth caused by new cohorts coming in during the pandemic, those are the ones that are suffering the most now, and those are the ones that have benefited most from live events. Now there's some uniqueness in that live events are allowed in most places. There's still some places where it's not. There's still some countries that there's shutdowns and some countries are dealing with pandemic results right now. And so in those countries, it may take a little longer. So again, I don't want to go against our historical practice and not guiding by region, but I'm giving you some of the variables to look at. And I think through -- just through that lens, you'll be able to determine about when we think different regions will grow. And what was the last part of your question?

Jeffrey Wallin Van Sinderen B. Riley Securities, Inc., Research Division - Senior Analyst

So I just wonder...

John G. DeSimone Herbalife Nutrition Ltd. - President

Yes, yes, I'm sorry. So look, you only have to look at Herbalife Nutrition. You can look at direct selling in general. And it's been very countercyclical. That's been a positive element to direct sales during a recession and people looking to generally supplement their income, more than just look for a new income. It's -- in the U.S., we'll see where that goes. Obviously, that's been a little different lately. But globally, based on the last 100 years of direct selling, it's been very countercyclical. Now Herbalife has been able to perform well in both up and down cycles because we also offer nutrition products, which is a macro trend that really favors our product line. So we've been able to perform well during both.

Jeffrey Wallin Van Sinderen B. Riley Securities, Inc., Research Division - Senior Analyst

So is it possible that, let's just say we had a global economic recession -- possible that some of the new cohorts that come in because they are looking for a way to supplement their income, perhaps those are more, I don't know if the word is right, but non-pandemic type of cohorts that perhaps are more robust than the pandemic type of cohorts?

John G. DeSimone Herbalife Nutrition Ltd. - President

They may be more sticky, right? Now I want to be clear, right? I think the distributors that came in and the ones that came -- seeing sales leaders that came into the pandemic probably would have still been sticky have we returned to live events much sooner when they were active, right? I don't know that it was a mindset, right? I think the people that came in during the pandemic are probably also looking for incremental income, right, during the time that was very challenging. But there wasn't this infrastructure built in a way that could cross-train them and cross-pollinate them with our distributor base in general. And so I think the current cohort that comes in that will have access to our historical way of doing business with the added benefit of some virtual training, right, by not having that be the primary way to learn, I think, will likely be more sticky than the group that came in over the last 2 years.

Jeffrey Wallin Van Sinderen B. Riley Securities, Inc., Research Division - Senior Analyst

Okay. That's helpful. And then just if I could ask one more around kind of the input costs. And I know you mentioned cutting some costs or cutting some expenses. If you could elaborate a little bit more on that. I know you mentioned shipping is one, obviously, a pressure point for a lot of folks. Maybe if you could just touch a little bit more on where you're seeing the most pressure. And then any more color you could give us on where you're cutting costs or expenses.

Alexander R. Amezquita Herbalife Nutrition Ltd. - CFO

I'll take that one. So the biggest driver is in the gross -- when we think about our margins overall is in our gross profit line. So you'll see in the first quarter, we had gross profit down to 77.0%. That is a fair way off where our historical run rate has been, which is really a reflection of all of those input costs, all of the headlines that you've been -- we've been reading about in sort of how that is now capitalizing into the P&L. I think it's clear. I think the world is clear that input cost inflation sort of the world that we're living in is

sustained in nature.

And so in addition to our traditional pricing strategy, where we, in most markets, price consistent with local CPI, we need to do something more to recover some of that input cost inflation. And so we are implementing pricing actions to go into place by the end of the second quarter to help recover some of that input cost inflation. It doesn't get us all the way there because clearly, we have to thread the needle between pricing, demand and making sure that the channel can still be successful because the way through this is for organic net sales growth, organic volume growth.

So we want to make sure that we thread that needle carefully. But clearly, there has to be some actions that we need to take that depart from our traditional pricing strategy to recover some of that margin. It's probably about -- if you just look at the back half P&L, these pricing actions are expected to impact gross margins by an incremental 100 basis points in the back half of this year. So that's where we're going to start and kind of see how that plays out and see how the macro plays out in addition to our pricing actions to see where we move from there.

Jeffrey Wallin Van Sinderen B. Riley Securities, Inc., Research Division - Senior Analyst

Okay. And then as far as some of the programs you're working on to just reduce overall expenses.

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

So there's the transformation program that we've announced last quarter expected to yield \$10 million to \$15 million of run rate savings. We are accelerating a Phase 2 to that program, kicking that off similar magnitude of run rate savings. We're anticipating kicking that program off later this year. So that is productivity and efficiency enhancements primarily in our share -- primarily in our infrastructure-type operations, finance, HR, member operations, those types of things. And so we're going to accelerate that.

And then we're also just being very prudent on where we're spending dollars in our discretionary SG&A pool. We don't want to compromise distributor service. We don't want to compromise any of the things, promotion activity, those types of things that drive top line and that support our distributors around the world, but what we can do internally to just make sure that we're directing dollars to the right programs. We're just going to be more mindful of that and sort of delay growth projects until the right time.

Operator

Our next question will come from Karru Martinson with Jefferies.

Karru Martinson Jefferies LLC, Research Division - Analyst

Just a follow-up on Al's question. So are we moving the gross leverage target? Or are we just -- is it a question that we're just comfortable being above it right now, and then we will try to work back down to that 3x target at some point in the future?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

That's right. Nothing changes about the target. The target always has ebbs and flows. I think for the most part, if you look at the prior quarters and years, we've been a little bit below that gross target leverage. I think we've been [2.8]. So just a function of our denominator having a shift right now primarily as a result of our gross profit getting squeezed from the dramatic increase in input costs is creating some compression on our -- ultimately, our EBITDA margin as a result of our gross profit margin. That's just the denominator issue, and we'll -- we're a bit over 3x. And when that corrects, we'll try to work our way back to 3x.

Karru Martinson Jefferies LLC, Research Division - Analyst

And when you look at the pricing that you're taking, what are the thoughts in terms of the elasticity there in your respective markets of the consumer response to it? Is it that we just have to take it? Or is that there is a volume that you're willing to give up with those price increases?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

I mean ideally, it's not a volume that we want to give up. I mean I think it's going to be a market-by-market decision as we navigate it. Our pricing point in each market is a little bit different. So I'm sure there are going to be some markets that can absorb it and others that

will be more of a challenge. But we're going to just have to see how this plays out. Clearly, there needs to be some action taken to the input cost inflation. By the way, we're not unique in this. I think this is a pretty common issue that globally, companies are trying to deal with.

Karru Martinson Jefferies LLC, Research Division - Analyst

And just lastly, on the cohorts. I mean I think we're somewhat in a strange time in the sense that we're having the pressured consumer who would be looking for supplemental income, but at the same time, we have a very robust job environment. I mean do you find that there is competition for that distributor base out there in terms of getting them signed up?

Alexander R. Amezcua Herbalife Nutrition Ltd. - CFO

I think it's real opportunity -- it is a real issue that we're looking at. It's really hard to obviously give with any specific attribution to that fact. But clearly, the job market is tight as it ever has been. The jobs report that came out this morning is showing that is not going to abate anytime soon. So that is an issue when you think of all of the opportunity costs that an individual has where our business opportunity has to compete with all of those opportunities, clearly, that's going to be a bit of a headwind. But how much of that is contributing to the activity rates that we are seeing in the past 1.5 months versus other factors like the lack of training that has largely been present, it's really hard to pinpoint the why to one or the other with any specificity.

What we do know is that we see the KPIs. We see the activity KPIs. So we know what the problem is, and we've been through these issues before historically, and we know how to -- we know how to address those. And so the local sales initiatives in addition to all of the live event catalysts that John D. and John A. has mentioned, we think that's going to address those types of issues as we move forward here.

Operator

I'm showing no further questions in the queue at this time. I will now turn the call back over to Chairman and CEO, John Agwunobi, for any closing remarks.

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

Thank you. I know that many of our shareholders are disappointed with these results. We are, too. Let me be very clear on that. It's true that we, along with many other companies around the world, are facing -- I think it's safe to say an unprecedented time in the macro sense. There's lots of stuff happening out there at the same time. We're not going to let those things stop us from pushing aggressively towards our goals. I've spoken with our distributor leaders around the world. I mean in fact, we're meeting with them in person here in Los Angeles next week to double down on our strategy for the rest of the year.

We are as confident today about our future as we've ever been. There are real plans in place, real actions being taken on the top line and real actions being taken down below within the P&L to help push through this storm that is out there. So I would just urge everyone who's listening to recognize that the team realizes that this is a time for us all to kind of step up and lean forward, and we're doing just that. Thank you for joining us.

Operator

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

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