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Betterware de Mexico, S.A.P.I. de C.V.

First Quarter 2022 Earnings Conference Call

April 29, 2022

CORPORATE PARTICIPANTS

Luis Campos, *Executive Chairman*

Andres Campos, *Chief Executive Officer and Director*

Carlos Doormann, *Corporate Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Cristina Fernandez, *Telsey Advisory Group*

PRESENTATION

Operator

Thank you and welcome to Betterware's First Quarter 2022 Earnings Conference Call.

With me on the call today are Betterware's Executive Chairman Luis Campos, Chief Executive Officer Andres Campos, and Corporate Chief Financial Officer Carlos Doormann.

Before we get started I would like to remind you that this call will include forward-looking statements, which are subject to various risks and uncertainties that could cause actual results to differ materially from expectations. Any such statement should be considered in conjunction with the Cautionary Statements and the Safe Harbor statement in the earnings release and risk factors discussed in reports filed with the SEC. Betterware assumes no obligation to update any of these forward-looking statements or information. A reconciliation and other information regarding non-GAAP financial measures discussed on the call can be found in the earnings release issued yesterday, as well as the Investors section of the Company's website.

Now, I would like to turn the call over to the Company's Executive Chairman Luis Campos.

Luis Campos

Thank you, Operator. Good morning everyone and thank you for joining us today.

I would like to begin my remarks by highlighting the strength and resiliency of our company and its asset-light and agile business model which has allowed us to successfully navigate through an uncertain environment, both locally and globally, of high inflation, supply chain disruptions and changing consumer trends, and to recover our profitability levels after the extraordinary expenses experienced during the fourth quarter of last year. Compared to the preceding quarter, our gross and EBITDA margins expanded 993 and 1,003 basis points, respectively, which demonstrates the flexibility of our business to adapt promptly to different market conditions.

While we are operating in a dynamic and challenging environment, we remain focused on our long-term growth strategy and the opportunities ahead, as we have in the last 20 years, and we are confident that we have the right strategies in place to seize these opportunities to achieve a 40% household penetration in Mexico by the end of 2025. Later in the call, Andres will discuss some of these strategies in detail, which are based on our three strategic pillars of product innovation, technology, and business intelligence, and will pave the way for future growth. Carlos will discuss our quarterly financial results, our expectations for the rest of the year and the financial strength of our business.

Before turning the call to Andres, I would like to take the opportunity to welcome again all JAFRA employees, leaders and consultants to our company. As announced on April 7, we are very pleased to complete the acquisition of JAFRA's operations in Mexico and in the U.S., along with JAFRA's trademark rights worldwide, funded primarily by debt, taking advantage of our current low leverage ratio.

As previously mentioned, each company´s management team will operate as an independent subsidiary, remaining fully focused on its operations and growth strategies, and we will replicate Betterware's three strategic pillars across JAFRA´s operations to accelerate its future growth.

This acquisition expands our category and geographic reach, as JAFRA´s know-how and presence in the U.S. market of over 65 years will pave the way for us to enter the attractive U.S. market by the end of 2023. We will discuss in detail the strategy during our next conference call, when we have properly assessed potential synergies and its accretive impact to our results.

I will now turn the call to Andres to discuss our business strategies.

Andres Campos

Thank you, Luis, and good morning to everyone. Thank you for joining us today.

The COVID period, from 2020 to 2022, brought about an abnormal expansion of the market with the consequent, very positive impact on our revenues, which have now adjusted to back-to-normal conditions. Despite the adjustment, the secular trends on which we act continue to be valid and growing, namely: number one, people's living spaces are getting smaller and smaller; number two, people have more stuff everyday; number three, people´s lives are more and more hectic, so they need practical solutions for everything; number four, people are more and more in need of an extra income, opening a huge space for the gig economy. Therefore, we remain confident in our ability to return to year-on-year growth and we have the commercial strategies in place to achieve this.

First, we must remember our two main avenues of growth: number one, household penetration, and number two, share of wallet expansion. In terms of household penetration, we have different studies that show there is still room for growth. The latest study of May 2021 showed that with 1.2 million associates we reached almost 24% of Mexican households on a regular basis, or approximately 7 million households had purchased Betterware products in the prior 12 months. We are confident in our ability to reach 40% household penetration by 2025.

In terms of share of wallet expansion, there are two things to stand out. First, as we have mentioned before, we have deconstructed our complete product portfolio, reorganizing our product categories by functionality, rather than by areas of the home, elevating, thus, our innovation capabilities. Within these functional categories, we have identified more than 200 product concepts that we offer to the consumer, which will allow us to increase our growth opportunity going forward. With that in hand, we are in progress of making a thorough market analysis, that will be concluded by the end of the second quarter '2022. This will be ground-breaking information to drive concept and category growth. We plan to share information regarding this study in the second quarter 2022 earnings release.

Now, to seize these growth drivers, we are working within our three strategic pillars. On the innovation front, we´ve developed six main initiatives. First, we will strengthen our marketing effort, having recently hired a new Chief Marketing Officer, Gerardo Mier y Terán, who formerly led strategic Clorox brands for LatAm. Gerardo brings a strong experience of 15 years in category management, pricing and promotion development. Second, we are adjusting our strategy of doubling our innovation to focus on smarter innovation by concepts. As I mentioned before, we have segmented our portfolio into more than 200 concepts. We will develop these concepts thoroughly, making sure we are strong players in each one. Third, we are also strengthening our market research analysis and innovation process to make sure we have more assertiveness in all innovation initiatives. Fourth, we have created a category development team that is completely focused on new product category development. We are exploring different categories, such as smart home and home restoration, among others. At the same time, we have revised our pricing and promotion strategies, making sure we position each product in the right price and carry out creative promotions to spark demand. And sixth, we have integrated an Engineering and Manufacturing department, to make sure all designs are optimized in terms of costs.

As for our technology pillar, we are pleased to announce the launch of our new Betterware+ App on May 2022. This third version of our proprietary sales force app will help us to enhance support, training, and motivation of our distributors and associates. At the same time, we will roll out the first version of natural language processing technology within our service bots during the second quarter of ’22. We have also developed an intelligent outbound messaging system, which reminds all distributors and associates of specific actions they should take to continue growing. Additionally, we are also working on strengthening our digital catalogue design, so it can become a more productive tool for all associates and distributors.

Finally, regarding the Business Intelligence pillar, we have overhauled our rewards programs to continue motivating market penetration and sales force growth. We are also making progress on researching the associates’ behaviors and motivations to cater better programs and service to all of them, which we are sure will contribute to increase attraction and retention starting on May 2022 and going forward. Lastly, we are developing a stronger understanding of geographic expansion and the local actions we need to take to make sure every city grows according to its potential.

This entire set of initiatives is key to achieving a turning point between second quarter and third quarter of ‘22, which will help us return to year-over-year growth going forward.

Overall, as we mentioned before, we see the COVID and post-COVID period, meaning 2020 through 2022, as an abnormal period within our long-term focus on market penetration. We believe that there are still strong secular trends on which we can act to continue growing in the years to come, as we have done for the past 20 years before COVID.

We continue deepening our understanding of the market, and the most effective actions to seize existing opportunities. Thus, we are fully confident of our long-term target of reaching 40% market penetration remains valid.

I will now turn the call to Carlos, who will discuss our financial results for the quarter.

Carlos Doormann

Thank you, Andres, and good morning, everyone.

First, I would like to highlight that the first quarter of 2021 was the strongest quarter in the history of the Company in terms of net revenue, EBITDA and the size of our associates and distributors network, resulting in an extremely difficult comparison base for this year.

That said, during the first quarter of this year we experienced additional headwinds in our business. Globally, supply chain bottlenecks and input cost pressures continued, while in Mexico, the effects of the return to normality persist, coupled with a weaker than expected economic growth and the highest inflation rate since 2001. All these factors have negatively impacted the share of disposable income spent by consumers in discretionary products.

Given these factors, results were slightly below our expectations. Net revenues were 36% lower than comparable net revenues of the first quarter of 2021, given the extremely difficult comparison base following a 205% growth relative to first quarter 2020.

Efficient cost management and the 12% product price increase announced at the beginning of the year were key to expand our gross margin by 610 basis points compared to first quarter 2021, and 993 basis points compared to fourth quarter 2021

EBITDA for the quarter was 41% lower than the EBITDA for the first quarter of 2021, which was in turn 287% higher than EBITDA from first quarter 2020. EBITDA for the quarter was 30% higher than EBITDA for fourth quarter of 2021.

Our EBITDA margin was 29.3%, which represents a 1,003 basis points expansion quarter-on-quarter, mainly due to the gross margin expansion and the absence of extraordinary expenses seen in the fourth quarter of 2021, which clearly reflects that our expenses are under control.

Net income, which includes unrealized loss in mark-to-market of financial derivative instruments, was 58% lower than first quarter of 2021. Excluding the 99.4 million pesos negative impact due to unrealized loss in mark-to-market valuation of derivative instruments, which does not affect the Company´s cash flows or operating income, our adjusted net income was 27% lower than adjusted net income of the first quarter 2021. Adjusted earnings per share were $9.83 pesos for the quarter.

As we have mentioned before, our balance sheet and income statement reflect the strength of our differentiated business model. First, the flexibility of our asset-light business model and a relatively low fixed cost base allow us to quickly adapt to market conditions and changes in trends, as shown in our margin recovery for fourth quarter 2021 to first quarter 2022. To further enhance our profitability, we are currently undergoing a streamlining of our expense structure aimed at further EBITDA margin expansion.

Second, our cash conversion cycle stands strong at negative 16 days, due to favorable conditions with our suppliers and distributors, as well as an effective inventory management, allowing us to fully fund our working capital needs as we grow.

Finally, our leverage ratio remains at an extremely conservative level of 0.4x net debt to EBITDA as of the closing of first quarter 2022. Even considering the debt acquired to complete the purchase of JAFRA on April 6, our leverage ratio stands below 2x net debt to EBITDA. Given the high cash flow generation and the low capex requirement nature of both JAFRA and Betterware, we will gradually deleverage, while we continue with our dividend payments to our shareholders.

As mentioned in our earnings release yesterday, we are proposed the payment of a 350 million pesos dividend, or $9.38 pesos per share, which was approved at the next Ordinary General Shareholders´ meeting to be held on April, 28, 2022.

Regarding our full year expectations, at this point we anticipate, on the one hand, net revenues to be slightly below, and, on the other hand, EBITDA to be close to the previous guidance. We look forward to providing guidance for JAFRA, within our Q2 report, once we have more visibility into the external situation and have properly assessed JAFRA's synergies and its accretive impact within Betterware. For now, we can gladly share 2021 JAFRA's preliminary figures of net revenue at 5.8 billion pesos and EBITDA of 0.9 billion pesos, pending the release of audited financials from the external auditor and IFRS adoption.

We are committed to our cost control strategies and expect our gross margin for the year to be in the range of 58% and 60%, and our EBITDA margin to be in the range of 27% to 29%.

In the longer term, we remain confident in our ability to seize growth opportunities in the years to come, which will lead us to reach our target of household penetration and expand our geographic reach starting with expansion to the United States by the end of 2023.

I will now turn the call over to the operator and we will take any questions you may have. Thank you.

Operator

Thank you. We will now conduct a question-and-answer session.

Our first questions come from Cristina Fernandez with Telsey. Please proceed.

Cristina Fernandez

Hi, good morning. I had a couple of questions. I wanted to start if you can share some color on your expectations for 2022. The revision in the press release is for sales to be you know slightly below the prior guidance for flat, and EBITDA slightly below I guess flat year-over-year. With the first quarter results I guess I'm just wondering you know what exactly does that mean? Maybe if you can share some color what you're seeing in April so far. Thanks.

Luis Campos

Hi Cristina. This is Luis. What I can say is that our results for the first quarter are pretty much in line with our projections. If you remember, during the last conference regarding the fourth quarter results, we were very clear regarding we will have a progressive comparisons along the year beginning with a very, very extremely hard comparison in the first quarter since we grew 205% at the first quarter of last year as compared to 2020.

Then we said, what we would see is we will see progressively improvement along the year and begin growing as compared to last year sometime in the second half of the year. Which means very clearly that we would be below last year in the first two quarters and begin growing sometime in the second half.

Then what I can tell you is that, we are happy to see that our results in the first quarter are pretty much in line with our projections, and in terms of EBITDA, EBITDA margins, even better than what we expected.

Cristina Fernandez

Okay, that's helpful. Then I wanted to ask around the price increases. With the Mexican consumer being more cautious, I guess how were those received? Are you seeing any pushback in those higher prices from consumers or from associates and distributors?

Andres Campos

Hi Cristina. This is Andres. Obviously there's two parts to this. One is that we are not the only ones increasing prices. I think price increases are being generally held in Mexico across different categories of products. Obviously, that puts Betterware aligned with the general price increase.

Now, at the same time, obviously these inflationary pressures put pressure on the consumer, on their ability to keep the consumption going. So, that is still to be seen. There is not any formal numbers at the moment. We do believe it's going to put pressure to the consumer mainly in the first half of the year, but after that, we believe that the consumer could take these price increases and consumption could come back by the second half of the year.

Luis Campos

Something I could add to my previous answer, Cristina, related to what Andres is mentioning, this is the reason why we want to be conservative and say, slightly below in terms of sales and close to, in the case of EBITDA. Because if everything under our control internally, we have been taking care of it, and we are very confident about the positive impacts they will have.

What we cannot control is the external factors. This is a very important one. we prefer to be conservative and say, slightly below because we don't know whether or not these inflationary pressures could modify, a little bit our projections.

Our expectation with the review of our commercial strategies is that, this could neutralize the external factors—our internal strategies—but we still have to see the second quarter we will see how our strategies are working and what external factors—or the way external factors are improving or worsening.

Andres Campos

Just to wrap up the comment, Cristina. I think that these inflationary pressures are specifically a short-term impact, and we continue to believe that there are strong secular trends that will continue to project our growth in the long-term going forward. We talked about these secular trends in the call. Obviously, there is this short-term pressure with inflation and all this happening, but we believe that if we have the strategies in place, as we have done in the past, we will continue to achieve the long-term secular trends and be able to act on them and achieve this long-term growth.

Obviously, there are these short-term things we need to take care of, but it's very important, we believe, to keep our focus and our target also in these long-term trends that we have been able to capture in the past, and that we will continue to capture in the future.

Cristina Fernandez

That makes sense and very helpful.

I have one last question. I know in the JAFRA business you're not sharing guidance till next quarter, but anything you can share—at least high level—how that business is performing in this year so far? How confident are you in the—when the acquisition was announced, I think you had talked about 940 million in EBITDA. Is that still a good number to use on an annualized basis?

Luis Campos

I will make a comment and then I will turn to Carlos to make another comment regarding JAFRA.

The first one is, we are very happy and very confident about management of JAFRA. They have really, really a wide experience in the business. This is a very strong management team, both in the U.S. and in Mexico.

We are already working very intensively in our three strategic pillars, beginning with product innovation. Our management teams in JAFRA Mexico and JAFRA US are already working very enthusiastically and very hard already on improving. even improving our product innovation and our product innovation process. We are also already working on transferring as soon as possible in the next months and probably next year, the technology we have for the sales force which will also allow them to focus more on—the sales force in JAFRA Mexico and the U.S. to focus more on attracting people and improving sales.

And we are already working now, also, we already begun working on strengthening the Business Intelligence area on both Mexico and the U.S., which will also help to better focus on those concepts that will drive or accelerate growth.

Then all these together, we expect that will be very favorable for JAFRA's growth in the near, mid and long-term future. We will discuss more of these when we report the second quarter results.

Now, I will turn to Carlos that wants to comment also something on JAFRA.

Carlos Doormann

Yes. Thank you, Luis, and thank you, Cristina. I would like to comment that along with the synergies estimated in the $5 million to $10 million range, which we previously announced in January, we have identified additional opportunities which will allow us to improve their cost structure and margins in the short term, but these are still on the evaluation.

But additionally, we have already, as part of our endeavors on the integration of JAFRA identified opportunities to divest several of JAFRA's unproductive assets, which once completed, will release cash flow for better use. We will be glad to discuss both the synergies, and this sell off of unproductive assets in our next conference call. Thank you.

Cristina Fernandez

Thank you.

Luis Campos

Cristina, we are telling in our report that the 2021, before adapting to IFRS and before we receive a report from the external auditors, the EBITDA last year was like a little bit more than 900 million pesos, which is more or less 16% EBITDA margin.

Operator

There are no questions in queue. I would like to turn the call back over to Mr. Luis Campos for closing comments.

Luis Campos

Well, thank you for joining us today and we look forward to speaking with you when we report our next quarter results and meeting with many of you at the upcoming investor conferences. Thank you again.

Operator

Thank you. This does conclude today's teleconference. You may disconnect your lines at this time and thank you for your participation.