

# FINAL TRANSCRIPT

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## HLF - Q4 2005 HERBALIFE LTD Earnings Conference Call

Event Date/Time: Feb. 22. 2006 / 11:00AM ET

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## CORPORATE PARTICIPANTS

**Brett Chapman**

*Herbalife Ltd. - General Counsel*

**Michael Johnson**

*Herbalife Ltd. - CEO*

**Greg Probert**

*Herbalife Ltd. - President & COO*

**Rich Goudis**

*Herbalife Ltd. - CFO*

## CONFERENCE CALL PARTICIPANTS

**Javier Escalante**

*Morgan Stanley - Analyst*

**Doug Lane**

*Avondale Partners - Analyst*

**Olivia Tong**

*Merrill Lynch - Analyst*

**Scott Van Winkle**

*Canaccord Adams - Analyst*

**Joe Norton**

*Banc of America - Analyst*

## PRESENTATION

**Operator**

Good morning, and thank you for joining the fourth quarter 2005 earnings conference call for Herbalife Limited. As a reminder, this conference is being recorded. On the call today is Michael O. Johnson, the Company's CEO; Greg Probert, the Company's President and COO; and Rich Goudis, the CFO. I would now like to turn the call over to Brett Chapman, the Company's General Counsel.

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**Brett Chapman - Herbalife Ltd. - General Counsel**

Good morning. Except for historical information contained herein, the matters set forth in this earnings call are forward-looking statements. All statements other than statements of historical fact are forward-looking statements for purposes of federal and state securities laws, including any projections of earnings, revenue or other financial items; any statements of the plans, strategies, and objectives of management for future operations; any statements concerning proposed new services or developments; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying all of the foregoing.

Forward-looking statements may include the words may, will, estimate, intend, continue, believe, expect, or anticipate, and any other similar words. Although we believe the expectations reflected in our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed in any of our forward-looking statements. Our future financial condition and results of operations as well as any forward-looking statements are subject to change and to inherent risks and uncertainties such as those disclosed on this earnings call.

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Important factors that could cause our actual results, performance and achievements or industry results to differ materially from our estimates or projections contained in forward-looking statements. We caution you that these statements should be considered in conjunction with the disclosures, including specific risk factors and financial data contained in our earnings release and in our most recent filings with the SEC. Now let me turn this over to Michael.

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

Thanks Brett. Good morning, everyone. Thank you very much for joining our call. I know we've got a big crowd today, so we're going to get through this. And I imagine there'll be a few questions at the end. We especially want to welcome our new investors who participated in our secondary stock offering completed in mid-December, and today I'm going to begin by running through our 2005 highlights of our fourth quarter and full year, and Greg will provide our 2006 objectives in the context of our five key strategies and update you on our key markets, and Rich, as usual, will walk you through our financial performance and provide guidance for the first quarter and full year 2006.

You know, we're really excited with our record revenue achieved in the fourth quarter. We're up 20% versus 2004, ahead of our expectations. And as you've noticed, in our press release issued yesterday afternoon, our sales and promotional expenses were also higher than expected. We want to address this straight on. On the surface, this might be viewed as a problem, but we believe that higher expenses in these two areas are contributing and continue to contribute to strong business building and it's created momentum within our distributor organization that is carried into 2006.

Let me explain. As you know, we conduct regional events such as World Team Schools and Leadership Development meetings to provide product best practice in business building training. It does more than that. It lifts the emotional level and momentum in our business. The expenses for these events are primarily borne by the Company, and during the fourth quarter, each event had higher than expected attendance. In Budapest, 9,000 distributors attended our World Team School. We had 15,000 distributors attend events in Kobe, Singapore and Anaheim -- 5,000 at each event. Finally, in Brazil, more than 13,000 distributors attended two events during the fourth quarter. We had record attendance for our World Team School events in 2005, up 30% versus the same events in 2004.

As for our promotional expenses in 2005, our Worldwide Cup promotion was a challenge promotion, which means that our distributors who achieved the rewards and prizes actually had to stretch over a previously defined baseline. As a result of this promotion, distributors retailed more products and built larger organizations. That's good news. In the fourth quarter, more distributors achieved the highest reward levels than we anticipated, which directly increased the cost of the promotion.

Since the fourth quarter, we have improved our ability to control sales event expenses, and planning and communicating better with our distributors, and by implementing a more formal review process. In addition, we will use our new business intelligence software to better track and calculate distributor performance and promotional expense. As I said earlier, we believe the higher expense in these two areas helped contribute to a higher sales in the fourth quarter and created positive sales momentum, which is very important to us, and that has carried into 2006. Rich will elaborate on that point in a moment.

Now let's review some of the other highlights of 2005. In each quarter of 2005, Herbalife distributors set new sales records, which led to our largest year ever with net sales of reaching \$1.6 billion, up 20% over 2004. Our 2005 operating profit margins improved 314 basis points. Our full year earnings per share in 2005 increased 75%. As many of you know, in April we celebrated the Company's 25th anniversary at our extravaganza in Atlanta. We had more than 35,000 distributors in attendance from more than 30 countries, the largest event in Herbalife's history.

In May, we opened in Hungary, our 60th market. We welcome three new members to our prestigious Chairman's Club, bringing our total members to 27, up 13% versus 2004. We added one to our exclusive Founder's Circle. These are highly, highly motivating for our other distributors to see. We added 97 - 97 - new members to our Presidents Team, one new member approximately

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every four days. That's up 13% since 2004. This has resulted in positive momentum in our revenue growth along with enthusiasm and success in our distributor organization.

We added more than 150,000 new supervisors in 2005, increasing our total supervisors to more than 334,000, up 12% versus 2004. We are proud of the outstanding financial performance and distributor growth achieved in 2005. And what truly excites me is the progress our distributors and employees have made in reinvigorating our great company.

Let me summarize our 2005 achievements in the context of our five key strategies. Our distributor strategy. Every decision in our organization is made with the consideration for our distributors first by supporting our three R's, recruiting, retailing, and retention. This past year we globalized key growth initiatives such as Generation H, that is, the initiative to bring younger distributors into Herbalife, the Total Plan and Nutrition Clubs. In fact, now we have more than 25,000 Nutrition Clubs operating in 26 markets.

We invested in regional business development staff to facilitate these initiatives worldwide. More than 23,000 distributors were trained at 45 Nutrition Club training sessions worldwide. We launched BizWorks, our online distributor tool, to improve the time efficiency and productivity of our distributors. Today, more than 6,000 supervisors are using BizWorks to grow their business.

We significantly expanded our branding efforts by creating partnerships with organizations such as the Association of Volleyball Professionals, known in the United States as the AVP, and Anschutz Entertainment Group. As a result, our brand is reaching millions through sporting events and on TV networks across five continents. Our distributors participated in these events, handing out tens of thousands of product samples and obtaining thousands of leads for new customers and distributors.

We also have accelerated our investments in grassroots and local initiatives to further strengthen our brand globally, primarily in the form of healthy, active lifestyle. Activities such as triathlon in London, in Malibu, Phuket, Thailand, and Santos, Brazil. And now, you will see it in Italy and in Australia in the future. These grassroots event helped activate our distributors.

Through our Herbalife Family Foundation, our distributors, employees and company donated almost \$1 million to emergency relief efforts in the U.S. and Mexico for Hurricane Katrina, Rita and Stan, and for tsunami relief in South Asia and Africa. We also launched our Herbalife Family Foundation, Casa Herbalife program in 2005. With this program, we help existing charitable organizations provide healthy and nutritious meals to children in need. We launched six locations in 2005, one here in Los Angeles, in Atlanta, Singapore, Budapest, Santos, Brazil, and in Kobe, Japan.

Our customer strategy. Improving the productivity of our distributors, retaining distributors and customers, and increasing product access points to potential consumers are fundamental elements to our customer strategy. In addition, we will obtain important consumer distributor insights to our products and our business opportunities that we anticipate will provide more stable, predictable revenue base for our company in the future.

In 2005, we selected technology partners to build our direct-to-consumer platform. We began the development of the platform, and Greg will elaborate on the timing and the rollout in a moment. We launched Liftoff.com in the fourth quarter as a beta test site. For the first time in our Company's history, consumers can purchase online and be linked to our distributors, while preserving the financial relationship.

Our product strategy. It continues through our commitment to selling high-quality, science-based efficacious products, and it's stronger than ever. In 2005, we hired Dr. Steve Henig, our Chief Scientific Officer. We doubled the size of our Medical Advisory Board. We entered the high growth energy drink category, with the launch of Liftoff, our patented effervescent energy drink in the U.S. and Canada.

We introduced NouriFusion, our new skincare line that incorporates vitamins A, C, and E in more than 25 markets, our largest individual product rollout across more countries than ever before. We launched our comprehensive Heart Health line in the

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U.S., containing Krill Oil, a higher bio-available form of Omega-3 fatty acids, endorsed by Nobel Laureate, Dr. Lou Ignarro. And we continued our global rollout of Shapeworks and Niteworks.

Our China strategy. Our expansion plans for China have progressed well, in spite of the delay of the issuance of the regulations for direct selling. In 2005, we assembled a very strong management team, headed by Percy Chin. We developed solid government relations. We licensed more than 25 products, half of which are outer nutrition SKUs. We opened up our corporate facility in Shanghai. We've opened 14 corporate stores in seven provinces, and we increased the production capacity of our plant in [Suzhou] nine-fold. We view China as a long range opportunity, and our expansion plans for the market are progressing well.

For infrastructure, which -- to support our growth initiatives, we continue to invest in our systems, our facilities and our people to execute our strategies timely and efficiently. In 2005, we continued executing our regionalization plans, building strength in local markets. We implemented Oracle distribution management and supply chain worldwide and we continue with the implementation of other Oracle modules, such as a general ledger and order management throughout the year. We implemented our business intelligence software to improve our analytical capabilities. We formalized our organizational development program with rigorous training, helping us organize for success, identify and develop future leaders in our company.

And we invested in our facilities, opening new sales offices, relocating offices to more prestigious locations and expanding our factory capacity to support future growth. Our distributors are excited. They're excited and they're executing a more balanced approach with the three Rs. They are focusing on recruiting new distributors, retailing products, and retaining existing distributors. We believe their confidence in our products and the company has never been higher, which has resulted in a tremendous year. And as I've said to many of you before, I really believe we're just getting started.

As we look to 2006, we will continue to prudently invest in our businesses to continue executing our five key strategies with the goal of sustaining positive momentum that has been created in 2004 and 2005. We are pleased to see progress in our three Rs, our recruiting, retailing and retention. We remain committed to driving sales growth, building brand awareness worldwide and producing high quality science-based products.

Now, I would like to turn the call over to my business partner, our President and Chief Operating Officer, Greg Probert for an update on our key markets and strategic initiatives for 2006.

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**Greg Probert** - *Herbalife Ltd. - President & COO*

Thank you, Michael. Let me begin with an update of our key markets and conclude with our 2006 initiatives in the context of our five key strategies. Then I'll turn it over to Rich for the financial review.

Core markets. Our core markets comprise more than 40 countries and are defined as countries that have been opened for at least five years. In the fourth quarter, this group of countries comprised approximately 39% of our sales and increased 5% versus the same period of 2004. We believe one of Herbalife's competitive advantages is that we are geographically diversified. For example in the fourth quarter, Europe contributed 31% of sales, the Americas contributed 47% of sales, and Asia, including Japan, contributed 22% of sales. As China sales grow, these percentages should become even more balanced.

This geographic portfolio minimizes the impact of volatility from any one region or country. We believe this is an important investment criterion. Periodically, countries in this group will grow or decline, but the balancing investments in these geographies allows our management to spend a disproportionate amount of time on countries that are materially impacting the business.

Our focus markets have been additionally classified as either high flyers or turnaround countries. Let's begin with the high flyers. In Mexico, our number one market based on volume points, volume was up 112% in the fourth quarter versus the same period of 2004. Beginning in June 2005, Mexico's year-over-year growth rate has consistently been triple digit, and we attribute this

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growth to the expansion of more than 23,000 Nutrition Clubs, along with distributor leadership that is unified and engaged in strong country management.

In Brazil, our number three market, volume increased by 21% in the fourth quarter versus the same period of 2004. We attribute this strong growth to the expansion of the total plan, strong country distributor leadership, a highly effective country management team and a competitive product performance. If you guys could just hang on for one second.

Okay. So the building is safe, guys. Taiwan -- back to our high flyers -- Taiwan, our number four market, volume points increased by 5% in the fourth quarter versus 2004. The growth rate in Taiwan have slowed as expected due to the impact of our distributors, moving the build businesses in China coupled with the high penetration of our business in this market. We expect Taiwan to report volume point declines for much of 2006.

Let's now review our turnaround markets which include the U.S., Japan, Germany, and the Netherlands. In the U.S., our number two market, volume points in the fourth quarter increased 17% versus the same period of 2004. This represents the fourth consecutive quarter of growth in the United States. Therefore going forward, we'll remove the US from our turnaround list. Total supervisors in the U.S. were up 5% year-over-year in the fourth quarter. This represents the third consecutive quarter of year-over-year supervisor growth with expanding growth rates. The rate of new supervisors in the U.S. continues to increase, up 16% in the fourth quarter.

Of our top 10 metro areas, eight were up versus the fourth quarter of 2004 and of our top 25 metro areas, 18 were up versus the fourth quarter of 2004. By comparison, a year ago only four of the top 10 metro areas were up and of the top 25 only six markets were reporting sales growth versus the fourth quarter of 2003. In 2006, we expect to open several satellite sales centers similar to the one opened in Dallas in March of 2005.

In Japan, volume points in the fourth quarter increased 2%, representing the second consecutive quarter of growth. These results are encouraging, however, we are not declaring a turnaround yet. Total supervisors were down 20% in the fourth quarter. However, new supervisors for the quarter were up 39%. This new supervisor statistic is very exciting as we expect Japan to post year-over-year volume growth in 2006 for the first time in over six years.

In Germany, volume points in the fourth quarter were down 16% versus 2004. Total supervisors declined 18% versus 2004, but for the first time since the first quarter of 2003, Germany actually reported an increase in new supervisors, up 4% versus the fourth quarter of 2004. This statistic is a leading indicator to us that efforts made last year are starting to gain traction. Last year we upgraded our Country Management, launched Niteworks at the summer spectacular, removed websites that were tarnishing the Herbalife brand in this market. In 2006, we expect Country Management to continue working closely with our local distributor leadership to implement concepts like Generation H, over-50 segment and enhanced brand imaging.

In the Netherlands, volume points in the fourth quarter were down 17% versus the same period of 2004. We are working diligently to stimulate this market, but it may take some time. Last year we hosted a summer spectacular in Anaheim with over 2,000 distributors in attendance, launched Niteworks, and formed a Gen H S&P team. Similar to the improvements we have made in Korea, the U.S. and Japan, we will continue to focus on Germany and the Netherlands to stem the declines over the next 12 to 18 months.

Now let me give you some insights into our key initiatives for 2006 in terms of our five key strategies. In our distributor strategy, we believe this strategy will be the strongest catalyst for both top and bottom line growth in 2006. We'll continue prioritizing initiatives in the context of the three Rs, recruiting, retailing and retention, with the goal of improving our distributors' return on investment and time. We are pleased with the expansion of our Nutrition Club party planning concept beyond Mexico to more than 25 additional markets in 2005.

As Michael mentioned earlier, we organized regional business development resources to help globalize and to acculturate this concept in our 60 markets. In 2006, we'll leverage our business development staff by continuing to seed Nutrition Clubs in

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additional markets and support that by providing regional training programs on best practices to our distributors. And the growth from these clubs will take a few years to reach the magnitude that we are experiencing in Mexico. Therefore we'll continue seeding this concept into new markets in 2006, fostering deeper penetration into existing markets with the anticipated positive revenue impact expected in the years to come.

We will leverage to the launch of BizWorks in 2006. As Michael mentioned earlier subscriptions for this tool will continue to gain traction. We will translate the distributor facing component into multiple languages to increase the adoption rate outside our English-speaking markets.

2005 was a very successful year in terms of increasing the branding efforts of our Company and products. And we'll continue this effort even more aggressively in 2006. Already this year, we have sponsored the Toray Pan Pacific Open Tennis Tournament in Japan; the Vodafone Beach Volleyball Tour in Australia; as we speak, the Amgen Tour of California is taking place, and we're the official nutrition sponsor of that event due to our multi-year agreement with the AEG. We extended our sponsorship to London and [volume] triathlons until 2008. We extended our nutrition sponsorship of Triathlete Olly Freeman, a genuine medal contender for the 2012 Olympics.

We'll continue to sponsor Casa Herbalife programs working with organizations worldwide helping to bring nutrition to children in need. We will leverage our new head of marketing allies to maximize the value of our current and future sponsorship assets. As well to provide innovative approach to the emerging health and women's categories to sports, entertainment and event marketing. We'll do this with partnerships like the one we announced yesterday with Velocity Sports.

Distributor segmentation such as Generation H, Latinos in the U.S., stay-at-home moms and the over-55 age group will also be areas of focus in 2006. Putting the considerations of our distributors first has been successful for us in the past few years, and in 2006 that focus will continue. Our distributors are the levers of growth for our Company.

Now, onto the customer strategy. Our customer strategy was developed as a longer term initiative to accelerate revenue growth by improving the productivity of our distributors, facilitating distributor retailing and broadening our consumer base. As Michael said, we launched our Liftoff.com beta site allowing the very first direct sales to a consumer on a website supported by the Company. We expect to significantly expand our e-commerce capabilities with a fully functional direct-to-consumer site expect in the U.S. by midyear.

Now onto our product strategy. Our product strategy supports our distributors and customer strategies and it has evolved into a build, buy, and partner approach to help accelerate products to market. Through our increased internal R&D staff, we hope to better identify and target launches to address global mega trends. Through our volume partnering efforts, we hope to accelerate new-product to local markets, leveraging our relationships with key regional suppliers and utilize our strong cash position to potentially purchase niche products.

In 2005, we have successfully launched such products as Liftoff and NouriFusion. While we continue introducing products like ShapeWorks, Niteworks, Liftoff and NouriFusion in key markets, our scientist and our new-product marketing team will be working closely to deliver new products in 2006. We plan to introduce a water-soluble formula one, a redesigned children's line and a redesigned Garden 7 club.

2006 will be a year of regional focus for product ideation. For example, Asian markets are likely to continue rolling out skin lighting products and possibly traditional Chinese medicine. Brazil is looking at local niche products to help continue driving excitement in that important growth market. And finally line extensions are also under development to upgrade and strengthen our existing products in terms of convenience and taste.

Our China strategy. We remain very committed to executing our China plan in an efficient planned and fiscally prudent manner. We expect 2006 to be another investment year for China as we plan to expand our presence, opening an additional 30 to 40 stores in approximately 20 provinces. In 2006 we currently anticipate an 8 to 10 million EBIT loss as we build out stores and

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expand our infrastructure to support future growth in China. We expect capital investment in 2006 to be approximately \$15 million.

We remain very conservative in our outlook for China as we gain a better understanding of the enforcement of the new regulations and build a business to compete effectively in the marketplace. We have submitted our application for our direct selling license and we are hopeful to be among the first group of direct selling companies to be granted a license.

Now onto our infrastructure strategy. Our infrastructure encompasses investment systems, technology, facilities, and our people to support our Company's strong double-digit growth. In 2006 the implementation of Oracle order management and GL modules will continue in key markets. We will be implementing a process tracking system, [Agile], to help support our regionalization efforts. We plan on leveraging our business intelligence tool to provide insight and statistical data related to distributor, product and other operational metrics that will help us better manage resources, target promotions and understand our distributors' order patterns more effectively.

We also [now] to relocation of regional staff for the Americas to a new facility in Torrance, California which will provide them with their own identity and increased autonomy. We will continue executing our organizational development initiative. We'll provide additional leadership development training. We're identifying clear, career [succession] plans, and we will transition to an MDO method of evaluation to insure compensation is probably aligned with Company goals.

As I stated earlier, we'll continue to invest in our business tools for distributors, a direct-to-consumer platform and our expansion of our business in China. To support our infrastructure strategy, we expect total Company capital expenditures to be in the range of \$35 million to \$45 million. Now let me turn it over to Rich who will review our financial performance and guidance for 2006.

**Rich Goudis** - Herbalife Ltd. - CFO

Thanks Greg. Let me walk you through our financial statements that were contained in the press release yesterday and also provide financial guidance for the first quarter and full year periods of 2006.

During the section, all references to sales are to net sales and volume is to Herbalife volume points. In the fourth quarter, net sales of 409 million were up 19.7% versus the fourth quarter of '04, reflecting continued strength in our key markets. Net sales in the Americas, which comprised 47.3% of our sales were 193.6 million, reflecting an increase of 55.1% versus the fourth quarter of '04. Without the impact of FX, sales would have been up 46.4%. Net sales in the U.S. were up 18.5% slightly ahead of our expectations. Additionally, net sales in Mexico were up 117.9% and Brazil was up 58.2%. These two countries expanded rapidly due to the success of Nutrition Clubs in Mexico and the total plan in Brazil coupled with unified distributor leadership and strong country management.

On a full year basis net sales for the Americas were 681.7 million an increase of 45.6% versus the same period of '04, primarily driven by strong growth in Mexico, up 113.8%, Brazil up 63.1%. And the turnaround in the U.S., up 12.6% versus the full year of '04. Excluding currency fluctuations, year-to-date net sales would have been up 39.2%.

European net sales of 127.7 million in the quarter, which comprised 31.2% of our sales, decreased 5.1% versus 134.5 million in the fourth quarter of '04. Without the impact of FX, sales would have increased 1.6%. While performance in Europe has essentially been flat this year, please keep in mind we are [comping] very strong year-over-year sales growth rates of up 21% in the fourth quarter of '04 versus '03, and up 19% in the fourth quarter of '03 versus '02.

It's important to note that these sales performances varied throughout our European portfolio, more than 30 countries. For example, with in our top six countries, three were down double digits and three were up double-digits versus the fourth quarter of '04. Net sales in Germany and the Netherlands were down 24% and 25.6% respectively versus the fourth quarter of '04.

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Comparatively, net sales in Italy, France, Turkey and Portugal were up 8.3%, 12.6%, 22.2% and 23.8%, respectively over the same period in '04. On a full-year basis, net sales in Europe increased 1.7% versus a full year of '04 to \$545.3 million. Excluding currency fluctuations as expected, full-year net sales increased about 1%.

Net sales in Asia-Pacific, which accounted for 15.7% of our sales, were 64.2 million, an increase of 11.6% versus the fourth quarter of '04. Taiwan was up 7.8%, and South Korea was up 22.9% versus the same period in '04. Excluding the impact of FX, sales for the region would have increased 11.7% versus the same period last year. China is included in these results, generating 3.7 million in net sales in the quarter. We will continue to invest and then capitalize upon this emerging opportunity in China. On a full-year basis, net sales in the region were 245.1 million, an increase of 18.7% over the comparative period in '04. Excluding the impact of foreign exchange, the region was up 14.2% versus the full year of '04.

Sales in Japan, which represents 5.8% of our sales, were 23.5 million, down 5.2% from the 24.8 million reported in the fourth quarter last year. Excluding the impact of FX, sales in Japan would have increased 5.4% compared to 2004. On a full-year basis, net sales in Japan were 94.7 million, down 4.1% from a year ago. Excluding the impact of currency fluctuation, Japan was down 2.3% for the year.

Gross profit in the fourth quarter was 325.9 million or 79.7% of sales. The year-to-date improvement -- year-over-year improvement, excuse me -- of 48 basis points primarily reflects country and product mix coupled with fewer inventory write-offs in '05 versus '04. On a full-year basis, gross profit was 1.3 billion or 79.8% of sales, which is 46 basis points improvement over the 79.4% reported in the full year of '04. Again, the improvement primarily reflects an improved country and product mix coupled with lower inventory write-down expenses in '05.

Royalty expense for the quarter was 144.8 million or 35.4% of sales, a 46 basis point improvement compared to the fourth quarter of '04. And on a full-year basis, royalty expense of 555.7 million or 35.5% of sales was flat essentially with the comparable period in '04, primarily reflecting the global nature of our marketing plan. SG&A in the quarter of 126.8 million was up 6.5 million or 5.4% compared to the 120.3 million reported in the fourth quarter of '04.

In absolute dollar spending, the increase reflects a 7.8 million increase in sales events and promotions. Sales events were up 3.7 million due to higher attendance, as Michael mentioned earlier, and promotion expense was up 4.1 million, primarily associated with the successful Worldwide Cup promotion, which ended in December. We had a \$2.8 million increase in depreciation associated with our investments in systems and in China and a 1.7 million increase in occupancy costs associated with the new offices worldwide. These increases in SG&A were partially offset by lower amortization expense of 4.7 million and a 4.3 million benefit due to the elimination of pre-IPO sponsor-related fees.

As a percentage of sales, SG&A improved 421 basis points to 31.0% of sales in the quarter. On a full-year basis, SG&A expense improved 290 basis points to 30.4% of sales. In absolute dollar spending, SG&A of 476.3 million was up 9.2% versus the 436.1 million reported in 2004, reflecting an increase of 23.1 million in labor, bonus and benefits, 19.5 million in sales events and promotions due to higher than expected attendance level at the events, and the Worldwide Cup promotion, and 5.6 million in occupancy costs associated with our new China properties and the relocation of our Japan office. These expenses were partially offset by 9.9 million of lower amortization expense and 9.2 million due to the elimination of the sponsor-related fees just mentioned.

On a reported basis, interest expense for the quarter was 6.3 million, a decrease of 61.8 million compared to the 68.1 million reported in the fourth quarter of '04, which included the transaction expenses of 56 million associated with our IPO recapitalization in the fourth quarter of '04. Excluding the 56 million of recap charges, interest expense would have decreased 5.7 million versus the fourth quarter of '04. For the full year 2005, interest expense was 43.9 million, which included 14.2 million of one-time expenses associated with the claw back of our 9.5% notes and was down 79.4 million versus the \$123.3 million reported for the full year 2004, which again included recapitalization expenses of 71.4 million, 15.4 million associated with the elimination of our high-yield debt in the first quarter, and \$56 million just mentioned related to the IPO recap in the fourth quarter.

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Excluding these adjustments, the 71.4 million in 2004 and the 15.4 million in '05, interest expenses was 29.7 million for the full year in '05, a decrease of 22.1 million compared to the 51.8 million in the same period of '04, again, reflecting the benefits from our IPO recap. Our effective interest rate in the fourth quarter was 8.1%, down 9.5% -- excuse me -- down from 9.5% during the fourth quarter of '04.

During the quarter, we prepaid 29 million of our \$200 million term facility, and for the full year, we repaid 109 million of that term facility. Our outstanding debt at the end of the year is now 255 million, comprised of a 165 million of our 9.5% notes due June 2011 and 90 million balance on our term loan tied to LIBOR plus 1.75 basis points. As you might recall our term loan is hedged with interest rate swaps minimizing the exposure to increasing rates. In the third quarter of '05, we renegotiated the covenants of our term loan to allow us to buy back up to 50 million of our bonds, however, during the period no buy-back of notes took place.

On a reported basis, our full year effective tax rate for 2005 was 46.8% compared to the 192.8% reported in 2004. The decrease in the effective tax rate for 2005 was caused primarily by the impact of significantly less nondeductible interest including the nondeductible recap charges in each period that I just mentioned. Offsetting these benefits was the \$5.5 million non-cash tax charge associated with moving our China subsidiary within our global corporate structure in the quarter -- in the second quarter of '05.

Additionally, stronger than expected revenue growth during the past several quarters, coupled with management's outlook that a mid-teens revenue growth will continue throughout 2006, caused a decrease in the valuation allowances required against certain deferred tax assets and an increase in current taxes in certain areas as our worldwide transfer pricing and overall tax structures were impacted. As a result of our tax planning and operating performance, our full-year effective tax rate on an adjusted basis was 40.4%, a slight improvement over our guidance of 41 to 42%.

Net income on a reported basis was 30 million in the quarter, compared to a net loss of 37.4 million reported in the fourth quarter of last year. Earnings per share of \$0.41 in the fourth quarter of '05 improved significantly compared to the net loss reported of \$0.68 in the fourth quarter of 2004. Excluding the expenses associated with our IPO recap in the fourth quarter of '04 of 56 million, earnings per share in the fourth quarter of '04 would have been \$0.13.

For the full year 2005, reported net income was 93.1 million and earnings per share reported was \$1.28. This compares favorably to a loss of \$0.27 per share reported for the full year of '04. Excluding the recap charges of 71.4 million in '04, 14.2 million of recap expenses in the first quarter of '05 and a non-cash tax charge of 5.5 million for China's movement within our global tax structure and the 4 million non-cash royalty expense adjustment in the third quarter of '05, our earnings per share adjusted in 2005 was \$1.52 for the full year versus \$0.87 in '04.

Turning to the balance sheet, the company ended 2005 with 88.2 million in cash, down 113 million compared to '04's ending balance of 201.6 million. The \$113 million reduction in the cash balance is due to the fact that in early 2004, we used \$110 million of our cash to claw back our 9.5% notes, which took place in February. Additionally, we prepaid 109 million against our \$200 million term facility throughout the course of 2005.

Inventory of 109.8 million increased 38.7 million compared to 71.1 million at the end of 2004. The increase during the year was intentional and needed to support our double-digit sales growth, the China expansion and build-out, the annual building of inventory in preparation for slow border crossings throughout most of Latin America, specifically Mexico, during the holiday period and to support the multiple new product rollouts globally. Inventory turnover was 3.0 compared to 4.0 turns in the fourth quarter of '04.

CapEx of 10.3 million in the quarter reflects our ongoing investments in infrastructure, which Greg mentioned earlier. We invested approximately 7.8 million in information technology, including Oracle, our Internet applications and our IT infrastructure. We also invested in facilities primarily related to China, our stores and our factory. On a full-year basis, we invested 32.6 million in capital.

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Now, let's turn towards our 2006 financial guidance. As Michael mentioned earlier, the record attendance at sales events in the fourth quarter, coupled with the success of the Worldwide Cup Promotion, has helped sustain strong volume growth into 2006. In fact in January, we had record volume point month, up 19% versus January 2005. And our top two countries, Mexico and the U.S., continued to grow at triple and double-digit growth rates, respectively through the first seven weeks of 2006.

Before I walk you through the guidance, let me first point out a correction to our press release issued yesterday. In the first quarter guidance section on the first line, the net sales growth rate should have been compared to 2005, not 2004. Additionally, let me point out that this is the first time the company has provided guidance for the first quarter. On our earnings call in November, we provided full year guidance for 2006 only.

Let me walk you down the guidance for the first quarter. Net sales growth versus '05, between 16% and 18% growth. Gross profit between 79.5% and 80% of sales. Royalty expense between 35.5% and 36.5% of sales. SG&A between 30.0% and 31.5% sales. Operating income as a percent of sales between 13.0% and 14.0% of sales. Interest expense between \$5 million and \$6 million. Our effective tax rate, we expect to improve to be between 30.5 and 40.5 as a percent of sales. EPS - excuse me, as a percent of pre-tax, EPS is in the range of \$0.37 to \$0.41 and CapEx between \$10 million and \$15 million.

Please keep in mind, the following items are contained in the first quarter 2006 guidance. Incrementally, \$3.5 million of SG&A expense versus 2004 related to our Latin America extravaganza, which happened in Chile in late January and our Herbalife Honors event, which will happen in March. If you recall, last year, our Honors event was part of our 25th year anniversary extravaganza, which occurred in April. The guidance for our effective tax rate is higher than the 36% effective rate reported in the first quarter of '05. And our diluted share base will increase to 74 million shares by the end of the first quarter 2006, reflecting the impact of a higher share price.

Now let's look at the full year guidance. Net sales growth versus 2005 in the range of 14% to 18% growth. Gross profit as a percent of sales between 79.5 and 80.5. Royalty expense as a percent of sales between 35.5 and 36.5. SG&A as a percent of sales between 30.2 and 31.8. Operating income as a percent of sales 13% to 14%. Interest expense \$20 million to \$24 million. Our effective tax rate 39.5% to 40.5% and our EPS range remains consistent with that - what we guided in November, which is \$1.80 to \$1.85 and lastly, our CapEx, between \$35 million and \$45 million.

And for the full year, please keep in mind that our guidance reflects \$8 million of stock option expense related to the implementation of FAS 123(R). And our EPS guidance reflects an increasing share base for dilutive purposes for calculation of approximately 250,000 incremental shares each quarter. Additionally, investors who are beginning to model the individual quarters in 2006 should be aware that expenses associated with our major extravaganza events will be reported in each of the three quarters -- the first three quarters this year -- our Honors event in the first quarter, and Asia Pacific extravaganza in the second quarter and our U.S. and European extravaganzas in the third quarter, compared to 2005, when all these events occurred in the second quarter at our Atlanta 25th anniversary extravaganza.

With that, that concludes our financial recap and prepared comments. Let's now open the call up to your questions.

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## QUESTIONS AND ANSWERS

### Operator

[OPERATOR INSTRUCTIONS] The first question is from Javier Escalante from Morgan Stanley.

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**Javier Escalante** - Morgan Stanley - Analyst

Hi, good morning, everyone. I have a quick question on the returns of your promotional or event spending in the quarter. It seems like your top-line came in stronger than expected but on the profit front, you came in a little bit light. What is your assessment of what happened in the fourth quarter? Is it that you spent as planned in terms of magnitude, but you didn't get the expected lift in revenues, or is it that the magnitude of the spending itself was ahead of plan?

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

Hello Javier, it's Michael. Javier, I think we broke it down for you. We had some over expenditures on events in the fourth quarter. We had a lot of the events, and we had some of over expenditures due to attendance. And I think to be very frank we had some people who added a few things to these events at the last minute that caused a little overspend on them. We have that well under control now. We actually just hired a new person in charge of all our event and event planning. Hopefully, and -- I'd not say hopefully -- I know for sure because I've already seen her in action on our upcoming Boca event that we will have our costs better planned and our budgets more focused on and lived to by everyone throughout the company. It's part of, frankly, it's part of the culture of the company of many years of these events taking place.

The second part of it is the promotion, which you went in on -- the promotion was oversubscribed. And you're absolutely right, we needed to have our pencils a little bit sharper on how we planned that oversubscription, which we did not do as good of a job as we should have. And I can guarantee you that that like these events is under deep, deep technical scrutiny in here and new -- what should I say, new guideposts has been set up before any promotion is approved or leaves any of these offices, to make sure that we have every pencil sharpened that there's been three extra looks at them.

But the reality was that more people qualified into the high level of these promotions than ever before, which is good for topline momentum. That's what helps build that topline. The downside of that was the event cost us more than we had anticipated. That won't happen again.

**Javier Escalante** - Morgan Stanley - Analyst

But, Michael, on a regional basis, you guys are thinking that this is -- that was mostly a problem in Europe, right?

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

No. No. This was a global event. This was a global promotion.

**Javier Escalante** - Morgan Stanley - Analyst

I see. And basically, the issue of the more expensive promotion that you guys expected is that -- is the -- the type of distributors that were incented to run the promotion? Was it that they had less of a retail focused, kind of, business mix or is it that basically, it was too incented toward the top of the organization basically -- the most expensive distributors so to speak?

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

The latter. It was too incented towards the top. We had vacations at the top-end of the promotional event and more people achieved those vacations. And we -- frankly, were not prepared for that number. We did not anticipate that number. And so to be very blunt, we made a mistake, and we're going to make sure that that mistake doesn't happen again.

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**Javier Escalante** - Morgan Stanley - Analyst

And Michael, turning back to China, it seems like you guys are progressing well if not ahead of plan. And I know that you guys are concentrating now on opening stores, but are you guys already recruiting distributors? And if so, how is recruitment relative to your expectations?

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

Well, let me start on that, and then let Greg give you -- fill in the details. I'm the -- I don't want to be overly bullish about China. I'm the most conservative one in here, and I think Greg is right there on my tail. We've both done a lot of business in China. We're in a build phase there. Yes, the building is going nicely, it's progressing but let's be very frank about China too. They still have not issued their licenses to operate. We are operating with the government's full blessing. They come visit us quite a bit, as they are doing to all multi-level sellers in the marketplace -- actually all direct sellers -- in the marketplace. So leaving it at that, I still -- I'm still bullish on China, but it's a 2007 story for me, not a '06 story. Greg, you want to add --

**Greg Probert** - Herbalife Ltd. - President & COO

Yes. Hi good morning, Javier.

**Javier Escalante** - Morgan Stanley - Analyst

Good morning, Greg.

**Greg Probert** - Herbalife Ltd. - President & COO

Just to add a little bit to what Michael said. Again, we're really focusing on the infrastructure build side of things, opening, I think as I said in my comments another 20 to 30 stores. We want to get a wide footprint across China so we want to enter another 20 provinces that will prevent importation of gray -- creating a gray market in China. So you're going to see a fairly rapid expansion of our store footprint across another 20 provinces.

We're building our manufacturing capabilities there to make sure that when we do get our license, sometimes probably, later this year -- you never know when you're going to get those in China. But, we have submitted the license along with a lot of other direct selling companies and continue to focus on our government relations. So yes, we're progressing, I would say, right on plan, slightly ahead of plan.

**Javier Escalante** - Morgan Stanley - Analyst

But Greg, is it your sense that as you understand the legislation, and for sure, I mean, probably it's something that is just still settling but as you understand the legislation, you made a comment that somehow, some of your distributors in Taiwan has been focusing on China themselves.

How do you feel whether the legislation actually creates an earnings opportunity that is attractive enough in China as to recruit -- eventually recruit independent distributors there? How is your strength - I mean, shall we just think that you find that the Taiwanese guys are now in China, it means that they feel that that is a good business for them, ahead of them? Is it that -- the right way to think about it?

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**Greg Probert** - Herbalife Ltd. - President & COO

Yes. I think that's one way - that's one indicator of the interest. I think we've been working very closely with our Chairmen's Club and our Pres. Team in Hong Kong and Taiwan to put together a very attractive marketing compensation plan. And as we've stated previously one of our -- we think one of our advantages is that we don't have to change our plan, that we're going in fresh.

Remember that we stayed on the sidelines until the regs were out so that we could launch a marketing plan that's one, compliant and two, competitive. So I think the simple answer is because we crafted that plan with our distributors and we've been making a few changes to it - we'll continue to modify it -- we feel that we have a very competitive opportunity in that market for distributors.

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**Javier Escalante** - Morgan Stanley - Analyst

And one more question, if I could, and it's just moving to another strong market, for sure, Mexico has been very good for you guys. We estimated that it's still driving close to 50% of the volume -- the incremental volume growth for you guys. If you give us a couple of data points that could help us understand the penetration achieved by the Nutritional Clubs.

For instance, of these 23,000 clubs that you guys have by the end of '05, how many of them opened in '05? And basically, my understanding also is that that you are expecting 30% sales growth in China. How many new club openings are you guys planning for '06? How do you understand the marketplace at this point?

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**Greg Probert** - Herbalife Ltd. - President & COO

Yes. You meant Mexico, right?

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**Javier Escalante** - Morgan Stanley - Analyst

Mexico, yes. I'm sorry -- I moved to Mexico on the Nutritional Club.

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**Greg Probert** - Herbalife Ltd. - President & COO

Right. So I think at the end of last year we had about 6,000 Nutrition Clubs and went up to about -- you add another I think, 18 in Mexico. So again, are we penetrated? We don't feel we're penetrated. A lot of those are in a couple of key markets. We have some major markets in Mexico that still are very underpenetrated in terms of Nutrition Clubs.

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**Javier Escalante** - Morgan Stanley - Analyst

So just to -- so just to see whether I heard that correctly, basically, you opened up -- you think that you opened up 18,000 clubs in '05?

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**Greg Probert** - Herbalife Ltd. - President & COO

Yes. Roughly that number. Yes.

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**Javier Escalante** - Morgan Stanley - Analyst

And basically in '04, you said that there were about 16,000 -- 6,000?

**Greg Probert** - Herbalife Ltd. - President & COO

About 6,000.

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

About 6,000.

**Javier Escalante** - Morgan Stanley - Analyst

So they tripled basically?

**Greg Probert** - Herbalife Ltd. - President & COO

Yes.

**Javier Escalante** - Morgan Stanley - Analyst

Okay. And basically, of these, what do you think is going to happen in '06? I know that you guys feel that -- and it's difficult for you guys to have a lot of visibility about penetration. But if you can tell us of the 30% growth that seems to be planned for '06, at least this is my understanding, what would be the equivalent new club opening number that sustained the 30% sales growth?

**Greg Probert** - Herbalife Ltd. - President & COO

Yes. Again, Javier, it's hard to tell because our distributors open this, we don't open them.

**Javier Escalante** - Morgan Stanley - Analyst

Yes.

**Greg Probert** - Herbalife Ltd. - President & COO

We support them. I think, probably a good number would be -- we'd expect to see 30,000 to 40,000 clubs by the end of this year. In total --

**Javier Escalante** - Morgan Stanley - Analyst

Okay.

**Greg Probert** - Herbalife Ltd. - President & COO

In total.

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**Javier Escalante** - *Morgan Stanley - Analyst*

Okay. Exactly. Well, thank you very much guys.

**Greg Probert** - *Herbalife Ltd. - President & COO*

Thanks Javier.

**Operator**

The next question is from Doug Lane from Avondale Partners.

**Doug Lane** - *Avondale Partners - Analyst*

Hi. Good morning everybody. While we're talking about Nutrition Clubs, can you give us an update on a progress of expanding that concept beyond Mexico?

**Greg Probert** - *Herbalife Ltd. - President & COO*

Yes, Doug it's Greg. How are you?

**Doug Lane** - *Avondale Partners - Analyst*

Hi, Greg.

**Greg Probert** - *Herbalife Ltd. - President & COO*

Yes. Like I said we've expanded this significantly outside of Mexico. So we're up to about 25 additional countries. And they're at various stages of being acculturated for the local markets. I think in the U.S., probably one very successful -- we have -- we think probably around 700 clubs in the U.S. now. We're in Jamaica, Venezuela, Brazil, five countries in Asia Pacific and probably another 10 or so in Europe.

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

Hey, Doug it's Michael. I just want to add one thing. When we're talking Nutrition Clubs, many times outside Mexico and I would say outside Brazil, we're talking about hybrids -- that this plan is now being localized we're seeing it in Japan and Russia has got weekend club in there, because there is a propensity of people not wanting to have people on their apartment and secure apartment complexes. So they're using the recreation areas.

And they're culturing these on a local basis to all sorts of things. We're seeing breakfast clubs. We're seeing lunch clubs. We're seeing after work clubs. We're seeing all sorts of things happen throughout the world. So it's not just Nutrition Clubs and we're not sure we're capturing all these numbers.

**Greg Probert** - *Herbalife Ltd. - President & COO*

I think -

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**Doug Lane** - *Avondale Partners - Analyst*

I was going to see if there's a way you could compare your success outside of Mexico with your success in Mexico.

**Greg Probert** - *Herbalife Ltd. - President & COO*

Well, it's not close yet, to be very blunt. I mean it's Mexico is its own phenomenon.

**Greg Probert** - *Herbalife Ltd. - President & COO*

I think, the other thing you have to remember Doug is -- it took several years for these to really emerge and blossom in Mexico. So if you just look at the numbers that I gave Javier. We had a rapid, rapid acceleration in '05 in the number of clubs. But that's after four or five years of those clubs being in existence.

So again, it's a real exponential ramp-up. I think we're going to accelerate that and work with our distributors, is to do distributor training. So like I mentioned in my comment, we trained over 45,000 distributors last year. We'll do probably a similar number this year. We've created three regional business development people whose focus is to work with distributor leadership to bring these concept to additional markets and make sure that they're properly aculturated and launched and sustained in those markets.

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

Doug I'll give you an example, and this captures two points, this captures one of our negative which is the overspend on events. But -- and here is a reason why, when we were in Budapest last year, we set up a training method. We rented a large hall that would seat about 500 people. Had all paid for and drinks and everything there ready to go. And when people signed up for Nutrition Club training, we anticipated 500 and something like 1,000 people signed up for it. So we had to leave the hall vacant and decide to use the main meeting room. And we announced it at the end of the meeting that we would do the Nutrition Club training there. And out of 9,000 people, estimate were somewhere around 4,000 stayed in that room to be trained. So it's a very -- again, we don't know out of those 4,000, how many walked out of there with Nutrition Clubs on their mind. It might be too much work for some distributors, and for others they might say, "I get it, I'm running with this, and I'm going to get them started."

**Greg Probert** - *Herbalife Ltd. - President & COO*

So just a closing comment, Doug. I would say there's a very high level of interest in the distributor -- in our distributor ranks is increasing. If you look at the growth of Mexico and the fact that we broke two Chairman's Clubs in Mexico in the past year. We have 16 Presidents, it's an incredible growth phenomenon. And I think our distributor leadership in other countries are certainly aware of that and are very interested to see if that concept can work in their local markets.

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

And I'll tell you and we're not going to beat this horse too dead here, but in Boca Raton, we're going to be in about a month, and we're going to hand out what is the corporate bonus, the Mark Hughes Bonus to main distributors, our distributors will see a lot of Mexicans faces on that stage.

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**Doug Lane** - *Avondale Partners - Analyst*

Okay. Thank you. Moving back to China, you mentioned - well just two questions on China. One is do you have any idea of when you expect to receive a direct selling license from the national government there -- this month, next month? And then secondly, do you think that you will turn profitable on an EBIT basis in '07, Mike?

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

You go ahead. I'm going to let Greg handle that, because he is much more tuned into China.

**Doug Lane** - *Avondale Partners - Analyst*

Okay.

**Greg Probert** - *Herbalife Ltd. - President & COO*

Yes. It's difficult to say, Doug, in China, when you're going to get a license. We know that's going to be at least 90 days from submission. So I guess the best case now would be probably end of Q2 or Q3. But we -- you tracked it along with us. The regs took an extra year to get out. We're in there, we're submitted, we're working with the government. Percy Chin has actually gone to Beijing and met with the government on the direct selling license. So we're comfortable that we're going everything we can, and we have no indications from the government that we won't have a license. We have every indication that we will get a license, and that we're -- that we'll get it at the same time as a lot of other companies.

**Doug Lane** - *Avondale Partners - Analyst*

And then assuming you get the license over the summer, do you think you could be breakeven on an EBIT basis in '07?

**Greg Probert** - *Herbalife Ltd. - President & COO*

In '07, yes.

**Doug Lane** - *Avondale Partners - Analyst*

Okay. And just one last question. You mentioned the difference in your spend this year on your big events, where it was focused on Atlanta in the second quarter of last year. This year it's more spread. Can you just put some numbers behind what you spent on Atlanta, and then how do you see those spendings being allocated in the first, second and third quarter of this year?

**Greg Probert** - *Herbalife Ltd. - President & COO*

Sure, Doug. Let me take you through it. Last year in Atlanta, we spent a little over \$8 million, and that was really four events rolled into one. This year we expect our Honors Awards or each of these events to be about \$2.5 million, reflecting the growth in our business. So Boca, our Honors Award in March, our Asia-Pacific extravaganza in June, and then we have two events in July, we have our European extravaganza and our U.S. extravaganza. So you'll see a little bit, 2.5 in Q1, 2.5 in Q2 and 5 in Q3 compared to a little over 8 in Q2 of a year ago.

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**Doug Lane** - *Avondale Partners - Analyst*

Okay. That's very helpful. Thank you.

**Greg Probert** - *Herbalife Ltd. - President & COO*

You're welcome.

**Operator**

Next question is from Olivia Tong from Merrill Lynch.

**Olivia Tong** - *Merrill Lynch - Analyst*

Hi. Good afternoon. You had mentioned previously that you're sort of moving away from challenge promotions in 2006. And also I noticed tough -- comps are getting much tougher as the year progresses. So I'm just trying to get comfortable with your metrics about -- with your sales growth estimates. How do you get comfort with that given those two factors?

**Rich Goudis** - *Herbalife Ltd. - CFO*

Let me start off first, Olivia, and refer to our guidance then I will turn over to Greg. As you seen our guidance we expect because of those comps, we're taking a conservative outlook now. And we expect that in the back half of the year our growth rate should slow into the middle teens.

You see in the first quarter, we have a higher expectation in topline growth, and we expect that that growth rate will slow as we head into the back half. Remember that Mexico started growing triple digits in the month of June, forward last year and the U.S. had its strongest quarters in Q3 and Q4. So with that let me just clarify that we do conservatively expect that revenue growth topline will continue to slow down to the mid teens level by middle and, call it, the latter part of the year.

**Olivia Tong** - *Merrill Lynch - Analyst*

And then also just wondering with the -- do you guys track margin generated on incremental challenge related sales? Clearly, the challenge was more successful than you would have expected. Is there any way to sort of quantify the impact of those sales?

**Greg Probert** - *Herbalife Ltd. - President & COO*

We -- again the good thing about a challenge promotion is that it challenges people to drive incrementally over a pre-defined base line. So from that standpoint the challenge promotion, if done probably, are self-funding and to drive incremental profitability to the Company, because it driving incremental volume.

With this promotion as Michael said there was a skew towards the higher end of the rewards and payouts, but net net while tais was a little bit more expensive than we expected in the fourth quarter overall. I think we are pleased with performance and I think that's why you saw a topline in the fourth quarter grew stronger than our expectations.

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**Olivia Tong** - Merrill Lynch - Analyst

Got it. Is there -- do you guys have systems in place to sort of get a read on the efficiency of each promotion or is that something that you're working on or anything like that?

**Greg Probert** - Herbalife Ltd. - President & COO

Well, with our business intelligence we're trying to improve how we track these promotions and really assess the real benefit. But at any one point in time, throughout the world, there are multiple promotions, local, regional and global promotions --

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

And distributor -- they do promotions within their own organizations.

**Greg Probert** - Herbalife Ltd. - President & COO

True -- that are going on, so it's very complex. It's akin to the auto dealership business, probably that there's a lot of promotion on the dealership floor.

**Olivia Tong** - Merrill Lynch - Analyst

Got it. And then just finally, are there markets, Nutritional Clubs have obviously been very successful in Mexico and you guys have mentioned that 34 Country Managers, had come to see the concept. Are there any markets where Country Managers just thought the concept won't work for them or it had very limited potential?

**Greg Probert** - Herbalife Ltd. - President & COO

I think that was one of the reasons we took people down to be truthful. Once you see the nutrition clubs, you understand that the basic tenants of the nutrition clubs do work in any culture. It's just really finding -- which is results on the product recognition a sense community and socialization. So those four tenants of the nutrition clubs work in any culture.

The trick is to figure how to acculturate it. And then Michael went through some of the examples of -- they don't have to be everyday, they don't have to necessarily be breakfast club. They are being changed and acculturated around the world. But I think there is tremendous interest from our country managers and I think a growing interest from our distributor leadership.

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

I just -- sorry Greg to jump in. But I think -- this is Michael -- and to answer that question in a little different way, it takes a little while for that acculturation to take place. And my former employer I remember, we were never going to serve wine in one of the theme parks. And it just wasn't going to happen, and then the locals started bringing their own wine in, in baskets. And so it was just a matter of time before that changed.

There was never going to be local Japanese cuisine served in Tokyo. And now there are sushi restaurants all over Tokyo Disneyland. So it takes a moment. I don't think there is any armed resistance if you will to Nutrition Clubs. But there was some mental resistance that this won't work in India, per se, because of the caste system and because of the different things going on there. I think that's going to change over time. But as Greg said earlier, it took three years for these to take hold in Mexico. We'll see the build over time.

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**Greg Probert** - Herbalife Ltd. - President & COO

This is Greg, again. I thought one of the toughest markets for us, personally would be Japan, and one of our distributors just opened there -- the first Nutrition Club in Japan, actually a few weeks ago. And it's a person that actually runs a retail, has another business and just is opening there, the retail store hour before they would open for normal business.

So again that idea has -- caught on in Japan. I thought with the size of houses there and the cost of real estate and the transportation issues that that might be a tough country, but even in Japan, we have a Nutrition Club open now, and I think, in the quarterly calls in 2006, you're going to see Japan emerge as -- also a country where Nutrition Clubs are working. So if they can work in 25 countries, then I think they can work in 60 countries.

**Rich Goudis** - Herbalife Ltd. - CFO

And Olivia, I think, as we shared with some people, last night some investors, there initially when this concept was introduced in Brazil, we had heard anecdotal stories of clubs opening and closing. Now six months later, what we're hearing is that they've fine tuned some of the aspects of the club. And now what we're hearing Brazil is going to be the next Mexico, as far as -- these are commons right out of the leadership, which is a very positive sentiment.

**Olivia Tong** - Merrill Lynch - Analyst

Thank you very much. I appreciate it.

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

Okay.

**Operator**

The next question from Scott Van Winkle from Canaccord Adams.

**Scott Van Winkle** - Canaccord Adams - Analyst

Hi. Most of my question have been asked and answered. But Rich, can you give us the number on amortization this year. Is there a reduction in amortization in '06 versus '05?

**Rich Goudis** - Herbalife Ltd. - CFO

In '06, it should only be about another \$2 million, I think, improvement over '05 Scott. That's a last piece of the go private transaction that [cliffs off].

**Scott Van Winkle** - Canaccord Adams - Analyst

Okay. Going back to a previous question on the promotional spending, when you do programs such as - what costs a little more in the fourth quarter, how do you measure what you want out of it versus near-term revenue impact and things like growing the supervisor count, which obviously has more of forward payoff and near-term payoff? How do you manage that and how

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do you roll that into maintaining expenses? Because obviously expenses against the near-term boost are significant while expenses again tomorrow's growth in supervisors isn't immediate payoff?

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**Rich Goudis** - Herbalife Ltd. - CFO

Well, I think, two aspects of this promotion were important. One, that it was a challenge promotion. So in and of itself, it drives people to do something incremental over their baseline. But even more important on this, this was a little more complex in the structure because there were rewards for building incrementally year volume points over a prior period, and volume points are primarily -- it really drives behavior at the beginning levels of the marketing plan, if you will, at the first level supervisor and the [world and get team].

But interesting this, it also had a royalty point component. So people who have large organizations, it gave them an incentive to build their business over their baseline as well. And that's the component that -- because this was a nine-month promotion, we didn't have real good visibility into those people that were going to exceed and then exceed by how much on a cumulative basis until really we had gotten through about half way through November. And we saw that people were moving up from Levels 3 and 4 to Level 5 pretty quickly.

The good thing about that, Scott, is that the business building aspect of it is more longer lasting than just retailing product because the retailing of product may not be as sticky unless it's a Nutrition Club type of concept. But the business building I think is really what we're seeing carrying into -- the success of that carrying into the first part of '06.

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**Greg Probert** - Herbalife Ltd. - President & COO

Scott, this is Greg. Let me add a couple of things. If you look at the supervisor growth, new supervisor growth, it was pretty staggering last year. It was over 20%. A lot of that's attributable in our opinion to this promotion. Also you hit on a very key point that all that -- the momentum from the promotion does not show up in the same period. So if you look at -- we ended last year with very, very strong momentum and really tremendous momentum driven by that promotion and a lot of other things. If you look at January sales, they're up almost 20% in volume points. So again, you're going to see that carry into 2006 and not only in January, but through. So again, as we bring new people into business through these promotions and they build their organizations, that's -you're building an annuity of business, not just the period business.

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**Rich Goudis** - Herbalife Ltd. - CFO

And to build on that, for the full year, new supervisors were up 21.4%, but the fourth quarter was up 34.8%. So we saw a bigger boost in the fourth quarter.

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**Scott Van Winkle** - Canaccord Adams - Analyst

And as you mentioned, that is your best leading indicator -- is kind of growth in new supervisor additions rather than some net new number?

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**Greg Probert** - Herbalife Ltd. - President & COO

Yes, I think that's one of our best leading indicators in terms of the health of the business and future growth of the business.

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**Scott Van Winkle** - *Canaccord Adams - Analyst*

And then just adding onto the several questions on Nutrition Clubs, you mentioned that Japan story. In I think it's 26 markets or whatever the number is outside Mexico, do you have anecdotal evidence thus far of successes in each of those markets?

**Greg Probert** - *Herbalife Ltd. - President & COO*

Yes, we do. And one of the - [Dez Walsh] who is our head of sales has someone that works for him, [Jack Divuich] whose job -- only job is to go around the world and train a Nutri Club work with our leadership and acculturating it to track the successes and share those. So we know the clubs that are open in these countries. We track them. We try and spread those best practices and share those with the leadership, so that they can see what works in other markets. So again, these are working and they're taking hold. And I think, in the future, you're going to see the exponential growth you saw in Mexico, start to take hold in other markets.

**Scott Van Winkle** - *Canaccord Adams - Analyst*

Thank you very much.

**Brett Chapman** - *Herbalife Ltd. - General Counsel*

Why don't we take two more phone calls -

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

Questions.

**Brett Chapman** - *Herbalife Ltd. - General Counsel*

-- two more questions.

**Operator**

The next question is from Joe Norton from Banc of America.

**Joe Norton** - *Banc of America - Analyst*

Thanks. Good morning. I just wanted to -- a little bit more clarification on the convention spending. So it sounds like in the second quarter, it should be down. So it was 8 million last year and then this year, 2.5.

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

Correct, Joe.

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**Joe Norton** - *Banc of America - Analyst*

And then in the third quarter, two events at 2.5 million, was there -- what is that up against? Was there anything in the third quarter last year or was that --

**Rich Goudis** - *Herbalife Ltd. - CFO*

We have regional, I'll say, summer spectaculars that go on both in Europe and the America. That should be other than, I'll say, the growth of the business that should be constant. But the spike or the lumpiness is the 5 million versus really nothing effectively last year.

**Joe Norton** - *Banc of America - Analyst*

In the third quarter?

**Rich Goudis** - *Herbalife Ltd. - CFO*

That's correct.

**Joe Norton** - *Banc of America - Analyst*

Okay. And then fourth quarter, anything unusual we should be thinking about?

**Rich Goudis** - *Herbalife Ltd. - CFO*

No. I think that a repeat of this year where we had six events and we spent probably almost \$10 million on those events.

**Joe Norton** - *Banc of America - Analyst*

Okay. And then I also wanted to ask a couple of questions about the Nutrition Club. I'm assuming in and this is just in Mexico right now. But is it do you guys know which distributors are running the Nutrition Club?

**Rich Goudis** - *Herbalife Ltd. - CFO*

Yes.

**Joe Norton** - *Banc of America - Analyst*

I mean, is that something you're able to track?

**Rich Goudis** - *Herbalife Ltd. - CFO*

At the senior level, we know and what we're trying to do, again, these are independent distributors. In Mexico, they do a sampling basis where at the last week of the month, they'll actually ask distributors that are placing their orders, "Are you running Nutrition Clubs?" So we have that type of information but we don't have -- it's not like retail store where we know exactly every single

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distributor ID who is running distribution clubs. Again, because of the independent nature of our business, there is certain information that people are willing to share and not share.

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

But we do know -- hi, Joe, it's Michael -- we do know the areas in which they're operating pretty well. Some distributors have focused in, and this is one of the duties of Nutrition Clubs from our aspect, is that in Herbalife in the past, the business tended to be broad and not very deep. And the Nutrition Clubs are taking them very deep. So we're penetrating communities where before we were kind of dancing along the top of communities. And it's really invigorating to us to see this.

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**Joe Norton** - Banc of America - Analyst

So does that mean -- is there anyway at all then to track the success rate of new clubs? I mean, you have some general members about how many there are and how many new ones there are, but do you know how many open and are very successful versus how many open and don't -- aren't successful or closed?

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**Greg Probert** - Herbalife Ltd. - President & COO

We don't have the detailed information, but our distributors certainly have that. So to Rich's point we have -- we had no information and we tried to track it. And one of the thing that Dez and Jack will look at is -- is there -- are there ways that we can gather more empirical data on exactly how many clubs there are and what those clubs are doing, and think of a POS type of -- because these are very stable businesses. They lend themselves to that type of gathering of empirical data. So we're looking at ways of doing that because we think that would be important data for us to have and share with distributors.

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**Joe Norton** - Banc of America - Analyst

Yes. And I mean, I guess, the reason I ask is because it seems like -- if it's - I mean what everybody, kind of wonders is is this mostly just kind of new club growth or it just seems these kind of growth rates it's, I'm sure you'll agree it's kind of risky as you look forward, and the more you could tell about how much repeat business you're getting versus just opening new clubs?

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**Rich Goudis** - Herbalife Ltd. - CFO

Joe, what we find out is that, we're seeing clubs start to move up. Clubs last year or in the first year when we started getting into this, we're charging 20 pesos in Mexico and it was primarily of formula one shake in a tea. Now, you go to some of these clubs, and it's 25 pesos, and they've added another product, which is our Aloe Concentrate. So people are finding ways on -- on a same-store sales basis to get more sales out of the people who are attending.

We still see that it's a very sticky concept that a large percentages of these people are attending throughout the course of the five or six days. And that there's actually people are more and more taking product home with them. As Greg mentioned, we're trying to get better intelligence as to better track this, but while we say that the majority of the growth, clearly, is expansion of the stores and you saw that in the earlier numbers, there is good movement and good anecdotal information that when you go back to this clubs, you actually see people are charging more and providing more services. So that's a good thing.

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**Joe Norton** - Banc of America - Analyst

Okay. Thank you.

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**Greg Probert** - Herbalife Ltd. - President & COO

You're welcome. Last question?

**Operator**

The last question is a follow-up from Javier Escalante.

**Greg Probert** - Herbalife Ltd. - President & COO

Okay.

**Javier Escalante** - Morgan Stanley - Analyst

Hi, guys. A quick question on Niteworks. Basically, if you can comment your communications strategy with distributors about the adverse scientific data, if any. How you guys are basically treating this?

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

We have a full -- frequently asked questions program for our distributor relations group to deal with any questions about any of our product Javier. And our science group publishes that on a, as-needed basis. And we have -- obviously, when we launch a product we have a complete backup to all the science that is available to us for our products.

**Javier Escalante** - Morgan Stanley - Analyst

But my understanding is that you -- I mean the distributors in general, at least they haven't come back to you with a lot of questions. That this mean that they just don't know, or if they know they are just well-informed and they just basically feel that they can manage the information by themselves. I mean how you characterize the status of awareness among distributors?

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

Well, I think that the whole issue there was overblown. And we had two calls from distributors.

**Javier Escalante** - Morgan Stanley - Analyst

Okay. And these two calls, so is that -- the way you guys interpreted this is that all the others know, and they just simply are fully educated on, then you wouldn't use your calling center, or is it that just simply the information hasn't gotten there and probably you'll expect some sort of more calls going forward?

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

Well, I think this is an extremely efficacious product. It's been proven out. There's thousands of papers in science about the impact and the effect of l-arginine. And I think that the thing you're referring to was to try to take l-arginine and test it in the very -- frankly, fractured people. And this is the issue in today's world of one small piece of information be coming overblown versus thousand of pieces of information being ignored.

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**Javier Escalante** - *Morgan Stanley - Analyst*

But do you say that your distributors now with that they shouldn't be indicating this product to, let's say, people with illnesses?

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

Yes. We have a warning on the label itself.

**Javier Escalante** - *Morgan Stanley - Analyst*

Okay. Thank you, guys.

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

Thank you.

**Brett Chapman** - *Herbalife Ltd. - General Counsel*

Okay. Thank you. Michael for close ...

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

Yes. I just -- I want to close. This has been a better great year for us in our company. We're very excited about what a fabulous year it's been. In the fourth quarter we've seen some of the comments and we've heard them from you. We will make sure that we guide you conservatively, and that we will deliver on the promises that we are putting forward to you. That is the style of this management and the style of this company.

And also I'd like to invite any of you to come and visit us, to spend time with us, to see our people, to see our process, to see what we believe in in this company. We're a fixer-upper, and I've said that 1,000 times. And this company continues to strive and move forward. And I'm very, very excited about the future that I see here.

Greg was in Malaysia last week, and fired me off with email last week and a lot of the senior staff that it was exciting, so positive and so up about the opening of the Malaysian marketplace, and the number of distributors that were there, and the Chairman's Club members were there, and the order that were being taken in the receiving, in our new distribution center in Malaysia. It got me -- I was tickled. I was very, very excited about the momentum to see a new market come on line and see distributors excited about our products and our process and our business opportunity.

Monday, I was in Santa Rosa, California, participated in the CEO Challenge for the Tour du California -- Tour of California. And we had a booth on Sunday that we think thousands of people came by in San Francisco, on the streets of San Francisco distributors, new customers. And in Santa Rosa on Monday, in this booth we have these great bicycles set up, and you can do a quarter mile challenge against someone else or against one of the Herbalife riders. And it gives people a chance to see, feel and touch us and touch our distributors. Our company has really got a great piece of momentum going. And I want to thank you guys for your support in our first year as a public company.

And our results, as you see it - we can continue to deliver as I said on our promises and we look forward to executing on our long-term strategy. And as I said before, I get even more excited about the health of this company. Our distributors, our products

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and our brand are all stronger than they were a year ago, and we're going to continue to build this brand and increase customer satisfaction.

We're entering 2006 with incredible momentum. Rich pointed out our January numbers and we've never done that before - pointed out what that great momentum is. We look forward to setting new records again this year, we're going to do it. We've got a great company and I'm glad you're part of it. And as I've always said, we're committed to changing peoples' lives. So thank you all very much.

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**Operator**

Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may now disconnect.

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