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Q3 2020 Herbalife Nutrition Ltd Earnings Call

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**Eric Monroe** Herbalife Nutrition Ltd. - Director of IR

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

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

## CONFERENCE CALL PARTICIPANTS

**Douglas Matthai Lane** Lane Research - Principal & Director of Research

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

**Ivan Philip Feinseth** Tigress Financial Partners LLC, Research Division - Director of Research

**Karru Martinson** Jefferies LLC, Research Division - Analyst

**Sebastian Barbero** Jefferies LLC, Research Division - Equity Associate

## PRESENTATION

### Operator

Good afternoon, and thank you for joining the Third Quarter 2020 Earnings Conference Call for Herbalife Nutrition Ltd.

On the call today is Dr. John Agwunobi, the company's Chairman and CEO; John DeSimone, the company's President; Alex Amezcuita, the company's Senior Vice President of Finance, Strategy and Investor Relations; and Eric Monroe, the company's Senior Director, Investor Relations.

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

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### **Eric Monroe Herbalife Nutrition Ltd. - Director of IR**

Before we begin as a reminder, during this conference call, we may make forward-looking statements within the meaning of the federal securities laws. These statements involve assumptions and are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those discussed or anticipated. For a complete discussion of risks associated with these forward-looking statements in our business, we encourage you to refer to today's earnings release and our SEC filings, including our most recent annual report on Form 10-K and quarterly report on Form 10-Q.

Our forward-looking statements are based upon information currently available to us. We do not undertake any obligation to update or release any revision to any forward-looking statement or to report any future events or circumstances or to reflect the occurrence of unanticipated events.

In addition, during this call, certain financial performance measures may be discussed that differ from comparable measures contained in our financial statements prepared in accordance with U.S. generally accepted accounting principles referred to by the Securities and Exchange Commission as non-GAAP financial measures. We believe that these non-GAAP financial measures assist management and investors in evaluating our performance and preparing period-to-period results of operations in a more meaningful and consistent manner as discussed in greater detail in the supplemental schedules to our earnings release.

A reconciliation of these non-GAAP measures to the most comparable GAAP financial measures is included in our earnings press release submitted to the SEC. These reconciliations, together with additional supplemental information, are available at the Investor Relations section of our website, [herbalife.com](http://herbalife.com). Additionally, when management makes reference to volumes during this conference call, they are referring to volume points.

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

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

Good afternoon, everyone. Thank you for joining us on the call today. During the third quarter, we achieved another worldwide sales record, with reported net sales exceeding \$1.5 billion and growth of 22.3% compared to the prior year. 3 of our 6 regions, North America, Asia Pacific and EMEA, along with 24 countries, set new quarterly net sales records.

Volume points grew for the tenth consecutive quarter. And for the third quarter in a row, we set a new record high. The success was broad-based as we had volume growth in all 6 of our regions for the first time since 2013. We have also seen growth in our sales force, which is now the largest it has ever been.

In the third quarter, new distributors and preferred members grew 57%, with increases in every region. Approximately 65% of these new distributors and preferred members are millennials or Gen Z, part of an increasingly health-conscious and younger demographic. We believe that an increased interest in health and wellness is continuing to drive demand for our nutrition products. Our products and our innovative direct sales channel allow us to help consumers reach their nutrition goals through education and community, healthier eating and a more active lifestyle.

Technology has been key during these times. We have seen our distributors turn to social media in higher numbers to reach new customers and to stay connected. We are empowering our distributors with enhanced technology tools for ordering, analyzing business performance and customer retailing. The combination of our traditional business methods and a more advanced digital infrastructure creates a more resilient sales force and channel.

Additionally, our training activities have shifted to a virtual online format, which has extended our reach to an even larger audience. At some of our larger events, attendance has been well above prior year levels. We expect to utilize an efficient hybrid event model in the coming years.

I now want to pivot to our outlook for the future. For the fourth quarter, we expect the momentum to continue, with net sales growth in the range of 10% to 20%. Looking ahead to 2021, we expect to build off this year's 13% year-to-date net sales growth and project full year 2021 net sales to increase between 3% and 11%. Alex will provide more details on our guidance.

We also announced today a distribution of warrants to our shareholders in an effort to provide the potential for enhanced value to all of our shareholders. Alex will also provide additional information on these warrants, and you can also find a Q&A document available now on our Investor Relations website.

Let's dig a little deeper into our regional results. Starting with the U.S., where volume points were at an all-time high and grew 50% for the quarter. We continue to see strength across all our channels in the U.S. led by customer direct shipping, which increased approximately 90% compared to the prior year. Sales coming from Nutrition Clubs also increased for the third quarter, including more home deliveries from Nutrition Clubs to their customers, an approach that has seen increased use as a response to the pandemic.

Over the past 2 quarters, we have seen a material acceleration in new distributors in the U.S. with year-over-year growth of 75% in Q2 and 85% in Q3. Our analysis into the behavior and ordering patterns of this new distributor cohort shows similar trends to distributors that entered the business prior to the pandemic. The activity rates and productivity of these new distributors gives us confidence in the future retention rates of the U.S. business.

In China, volume points grew 1% compared to the third quarter of 2019. Although meeting attendance is not back to historical levels, we are encouraged that certain cities in China are beginning to allow larger in-person group meetings to take place. These types of large gatherings have not taken place in China since last year's 100-day review, and we expect to utilize a combination of in-person and virtual meetings going forward in China.

India returned to growth in the quarter, increasing by 16% compared to the prior year. Restrictions imposed in the market due to the lockdown continue to ease. By the end of the quarter, our company locations were open to take orders, receive payments and to pick up product. However, we continued to see our members favor home delivery, where volumes still exceed pre-pandemic levels. The growth in India contributed to a record quarter for the Asia Pacific region, which increased 10% versus the third quarter of 2019.

In Mexico, volume points were up 7% in the quarter, following 5 quarters of single-digit declines. New members in Mexico grew 26% during the quarter, with 58% of new members coming from the millennial and Gen Z demographics compared to only 51% at the end of

last year.

The EMEA region set another volume point record and grew 34% in the quarter, the 42nd consecutive quarter of growth dating back to 2010. The growth came from countries such as Spain, which was up 43%; Turkey, up [6 -- 37%], increased 82%. And the united members are turning to social media to connect with their customers and are using technology to carry out their sales and training activities.

Finally, South and Central America returned to growth and were up 16% in the quarter. This was led by double-digit increases in Colombia, Chile and Peru, while Brazil was down just 1% in the quarter. Sales have rebounded as product access challenges from the pandemic have eased, and we're seeing distributors utilize virtual events, similar to what we've seen in other regions to improve the reach of their training.

Additionally, we have 2 leadership changes to share. Effective November 9, Bosco Chiu, who has been with Herbalife Nutrition for 27 years, has assumed the new role of Chief Risk Officer, where he will work across all business units to lead our enterprise risk management, internal controls, ethics and compliance strategy.

In conjunction with this move, Alex Amezcuita, who celebrated his 3-year anniversary with the company this week, will become our company's new Chief Financial Officer. He will now be responsible for all corporate financial functions at the highest level.

Both will report to me. And with these executive leadership transitions, we strengthen an already strong and high-performing senior management team. I look forward to working closely with Bosco and Alex as they assume their new responsibilities.

So what you've heard today is that in the third quarter of 2020, Herbalife Nutrition continues to set records. I am confident in the resilience and in the innovation of our distributors, the future of our business and our continued growth potential.

I now turn the call over to Alex to review the financials.

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**Alexander R. Amezcuita Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Thank you, John. Third quarter net sales of \$1.5 billion represented an increase of 22.3% on a reported basis compared to the third quarter in 2019. Currency normalized during the third quarter, but still drove a headwind of approximately 280 basis points. Adjusting for the change in foreign exchange rates, net sales for the quarter increased 25.1%.

We reported net income of approximately \$138.1 million or \$1.04 per diluted share. Adjusted earnings per diluted share were \$1.15, an increase of approximately 60% compared to adjusted EPS of \$0.72 for the third quarter last year. The impact of currency fluctuations represented a year-over-year headwind of approximately \$0.12 on results for the third quarter. Note that our reported and adjusted results this quarter include expenses related to the China Growth and Impact Investment Program of approximately \$3.2 million.

Reported gross margin for the third quarter of 78.8% decreased by approximately 165 basis points compared to the prior year period. The decrease was primarily driven by the unfavorable impact of foreign currency fluctuations and increased freight costs related to orders being shifted to home delivery versus member pickup as a result of COVID-19 that we called out a quarter ago.

Third quarter 2020 reported SG&A as a percentage of net sales was 34.8%, and adjusted SG&A as a percentage of net sales was 34.6%. Adjusted SG&A, excluding China member payments, was 26.5%, approximately 240 basis points lower than the third quarter 2019. This was largely driven by a decrease in member promotion and event costs as a result of delays, cancellations and reformatting of promotions and events due to the COVID-19 pandemic. A significant amount of the underspend on these items from the first 3 quarters of the year is projected to be spent in the fourth quarter.

Our third quarter reported effective tax rate was approximately 19.5%, and our adjusted effective tax rate was 16.3%, which was lower than the prior year, primarily due to favorable changes in the company's geographic mix of income and a reduction in the income tax rate of certain foreign jurisdictions.

As John mentioned, we are issuing guidance for the remainder of 2020 and providing initial guidance for 2021. While there is still uncertainty related to the impact that COVID-19 might have on the future performance of the business, we have gained increasing confidence in the business and operational trends in response to the impact of COVID-19 throughout 2020.

For the fourth quarter 2020, we estimate volume point growth in a range of 10% to 20%. Net sales are also expected to be in the range of 10% to 20% growth, which includes an approximate 350 basis points currency headwind versus the prior year.

Fourth quarter reported diluted EPS is estimated to be in a range of \$0.45 to \$0.75, and adjusted diluted EPS to be in a range of \$0.55 to \$0.85. Reported and adjusted diluted EPS includes a projected currency headwind of \$0.10 compared to the fourth quarter of 2019. The sequential reduction in EPS from Q3 to our fourth quarter guidance is primarily driven by the previously mentioned increase in SG&A due to advertising and promotion that was deferred from the first 3 quarters of the year. However, fourth quarter adjusted diluted EPS guidance implies full year 2020 adjusted diluted EPS guidance of \$3.48 to \$3.78, which implies 23% to 34% growth over 2019.

Initial guidance for 2021 builds off the double-digit top line growth implied in our full year 2020 guidance. 2021 worldwide volume points are estimated to be between flat and 8% growth, with worldwide net sales growth of 3% to 11% on a reported basis, which includes an approximate 80 basis points tailwind due to currency. Constant currency net sales are expected to be in a range of 2.2% to 10.2% growth.

Full year 2021 guidance for reported diluted EPS is in the range of \$3.50 to \$4, with adjusted diluted EPS in a range of \$3.65 to \$4.15. Reported and adjusted diluted EPS are expected to be currency-neutral compared to 2020. EPS guidance excludes the impact of any future expenses related to the China growth program, share repurchases, and excess tax benefits from equity exercises.

Turning to cash flow and our share repurchase activity. During the first 3 quarters this year, we generated over \$500 million in cash flow from operations, and we currently have over \$1 billion of cash on hand. During the third quarter, we also completed \$800 million in share repurchases, which included \$750 million from the modified Dutch auction self-tender offer completed in August, followed by \$50 million of open market repurchases over the remainder of the quarter. We have approximately \$700 million remaining on our existing share repurchase authorization, and we will prudently return excess cash to shareholders on a consistent basis.

To potentially unlock additional shareholder value, we are making a pro rata distribution of warrants, where shareholders of record will receive 1/4 of a warrant for each common share held. The warrants provide all of our shareholders the opportunity to potentially take advantage of the option value embedded in the warrant. The exercise price of the warrant is \$67.50 with a maturity of 7 years in which the warrant will only be exercisable at maturity. Should the warrants be exercised at maturity, the company has the ability to net settle the warrants and shares, which minimizes any impact on our diluted share count. The record date for the distribution is November 16, and the payment date will be December 14.

We continue to believe the repurchase of common shares, along with the distribution of warrants, is consistent with the company's long-term goal of maximizing shareholder value.

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

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) I show our first question comes from the line of Doug Lane from Lane Research.

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### Douglas Matthai Lane Lane Research - Principal & Director of Research

Congrats, Alex, on your promotion. Alex, can you elaborate on the warrants here and what the expected dilution is to your EPS count going forward?

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Doug, thanks for the well wishes. Sure. So the warrants themselves, so the exercise price is \$67.50. The way that the warrants will be accounted for is effectively treasury stock method. So while the share price is below the exercise price, there's actually no dilution at all to EPS. As our stock price becomes above the exercise price, again, we'll use treasury stock method in which that means the value above \$67.50 will be what is reflected into the denominator in calculating adjusted EPS.

It's also probably worth noting that while there is that potential dilutive effect to EPS, overall, shareholders, if you receive this warrant and you're holding both the warrant and the equity that you had, there's no dilution to your equity value that you withhold because the dilution that is in EPS is countered by the accretion of the ultimate underlying shares that you're holding. So effectively, if you hold the warrants, you're no different from an equity ownership in the company and effectively, no different from a value perspective from that lens.

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**Douglas Matthai Lane Lane Research - Principal & Director of Research**

Right. No, that's helpful. And how have you calculated the impact of warrants to your EPS guidance for next year?

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

They are not -- they had 0 impact on the EPS guidance of next year because, obviously, we are below the stock price or the exercise price. So that is a non-factor.

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**Douglas Matthai Lane Lane Research - Principal & Director of Research**

Okay. That makes sense. And then you mentioned \$700 million left on your stock buyback. I assume that no stock buyback is factored in your EPS guidance for next year as of yet as well.

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

That is correct. And as you probably heard in my remarks, post the tender offer, post the \$750 million of tender offer, we did do \$50 million worth of open market repurchases. I think going forward, again, I think this is a message we've been saying, that the company generates a lot of cash. We typically don't have a lot of uses for those cash. So excess cash, returning cash to shareholders by way of a repurchase is a good way to do that. I think those -- that \$50 million level that we did last quarter is probably a good level, generally speaking, as we look forward. Obviously, it might be less, it might be more depending on the facts and circumstances of the quarter. But back to your original question, guidance does not have any of those repurchases factored into the EPS guidance for 2021.

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**Douglas Matthai Lane Lane Research - Principal & Director of Research**

Okay. And then just lastly. I mean the acceleration in growth here has been pretty astounding. And I've dealt with these models for a long time, and I just need help understanding how you expect this momentum, this acceleration that we're seeing to revert back to the single digits so quickly in 2021.

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**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. Well, so I think if you look at the guidance range that we have in Q4, right, so Q4 is volume point growth between 10% and 20%. So I think even in Q4, what we're effectively saying is on the high end of the range, the business continues to perform, as you've seen through much of Q2 and through Q3. And in the low end of the range is a beginning of a deceleration to a more normal growth rate.

Now obviously, we're still in a circumstance where there's not as much visibility as we have historically had. But as we look at the sustainability metrics, as we look at the underlying metrics, we can see the top end of the range being a plausible outcome, and we could see the low end of the range be something as COVID might have some impact on the business.

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

Yes, Doug, this is John D. I'm going to jump in, just add to Alex' comment. Look, I mean the growth rates this year are tremendous, and you follow this industry for a long time, and it's -- there are spikes in growth and some leveling off. I like to look at our guidance and stack it up over 2 years to see that the sustained growth this year becomes part of the foundation. Once you stop comping the numbers we've had this year, it gets a lot harder. So I prefer to -- I think the easier way is to just look at 2 years back.

**Operator**

I show our next question comes from the line of Karru Martinson from Jefferies.

**Karru Martinson Jefferies LLC, Research Division - Analyst**

I'd like to offer my congratulations, Alex, as well on the promotion. Just in terms of the distributor growth, I mean, 85% in the U.S. What is the typical person coming in, in terms of their involvement here? You mentioned 65% globally, I think, millennial and Gen Zs. What are you seeing in the U.S.? And how are they spending?

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

Yes. This is John D. I'll take that one. I mean the mix is mixing younger, it's skewing younger, which is exciting for us as a company. And I know you're asking for the U.S. specific, I don't have the U.S. offhand. But in general, across almost all of our markets, the new members coming in are millennials or Gen Zs.

Mexico was a market that was kind of further behind some of the other markets. And in the third quarter, 65% of their new members were Gen Z and millennials. So that's a big pickup. So there's strength in our distributor base getting younger and that's exciting.

As far as their purchasing patterns, from an overall volume standpoint, not much different than what we had seen pre-COVID. So we've got a lot more people coming in. Productivity around those people are pretty standard, and the activity rates are pretty standard. So that's also encouraging. So it's not a short-term trial basis. So we're seeing pretty good sustainability from those people coming in that's not dissimilar from what we've seen in the past.

**Karru Martinson Jefferies LLC, Research Division - Analyst**

Okay. And then when we look at the product mix that you guys have during the quarter, are you still seeing kind of the immune essentials and things that are more COVID-related outpacing the rest of the portfolio or some shift on that? Or are you still seeing meal replacement and weight loss holding the bulk of the business?

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. It's still broad-based growth across the product portfolio. I don't think one particular product sector is disproportionately or just making a material difference in the mix. We're seeing all boats rise here.

**Karru Martinson Jefferies LLC, Research Division - Analyst**

Okay. And then when we look at the guidance for next year, how much is built in, in terms of new product introductions? Or how should we think about that pipeline as we go out to next year?

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. When we build guidance, we don't necessarily build guidance from a product standpoint. We look more from the distributor and sales metrics. So I don't have a great answer to that question in that way. I would say, generally speaking, though, the -- refreshing our product portfolio is instrumental for distributors to be successful out there in the field. That's part of their ability to be competitive and remain competitive. So I would say, generally, as we do product introductions, that is just an underlying assumption in the effectiveness that we see them out in the field.

But we continue to launch into different products as well to continue to penetrate different segments of the markets. As you know, we've been talking a lot about choice. So as we talk about clean label and those types of products, as we talk about further penetration into our sports line, and as we talk about further investing in localization of flavors specific to different markets, all of those aspects help to -- help our distributors be successful out there.

**Operator**

Our next question comes from the line of Hale Holden from Barclays.

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

I had two questions for you. Alex, I was just wondering the thought pattern behind the warrants. I'm sure you had multiple different things on the whiteboard that you were considering and why you thought the warrants were the most efficient sort of shareholder distribution method.

**Alexander R. Amezcua Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Sure. So there's no judgment on most or least. To me, the warrants become just another lever in unlocking shareholder value or the potential to unlock shareholder value. Obviously, there's a lot going on in the business. We had a great Q2, we continue to have a great Q3. And as we look into guidance of next year, the business is going to continue to grow. So from a company standpoint, the biggest way that we can return shareholder value is to make sure this business continues to grow.

There are other things that the company can do with its capital structure in the form of share repurchase, which is a leverage, and now we have this warrant distribution. And candidly, the warrant distribution provides an opportunity, not an obligation, but provides an opportunity for a shareholder to potentially take advantage of the option value embedded in the warrant. And so I don't think it's mutually exclusive. It's just another lever in the set that a shareholder may or may not take advantage of as we move forward. So that's sort of the rationale and how I would put the warrant in context with all of the other things available to a shareholder investing in Herbalife Nutrition.

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

Got it. And then my second question is we've been trying to track you guys on WeChat, and the level of activity seems like it's very high. And I was wondering, with the resumption of the bigger in-person China meetings, if that would be a growth accelerator in 2021. Or if alternatively, you guys think you did such a good job virtually this year that it was just sort of more additive? Or how I should think that through?

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

Yes. So this is John D. And so I assume when you're talking WeChat, you're talking the personal stores that we helped create for our members in China on WeChat. WeChat is used for a lot of things. That personal store -- the volume coming from that personal store in Q2 was in the low 20s; in Q3, it was in the mid-20s. So it's building, but it's still got a lot of growth left.

Meetings, by the way, are not fully back in China, not even close, the big cities, matter of fact. Meetings still have a lot of restrictions in some of the rural areas, which is where we're seeing some of the strength, is more in the rural areas and not in the big cities, is because the meetings are coming back. But I suspect over time, next year and the year after, you'll see a big acceleration in the sales that are coming from the digital platform as we enhance both the functionality because it's a fairly new tool and the training behind it.

**Operator**

Our next question comes from the line of Sebastian Barbero from Jefferies.

**Sebastian Barbero Jefferies LLC, Research Division - Equity Associate**

Congrats on a great quarter. Firstly, I was wondering if you could talk more about the trends in North America and Europe. I'm trying to understand what is leading to this sizable outperformance relative to other regions, and is it related to higher adoption of digital tools in these developed markets.

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

So this is John D. I'll take that one, too. So it's really a trifecta. It's 3 things. It's first and foremost, customer interest in the product, okay? That's the foundation. Behind that, of course, is distributor engagement, which is incredibly strong right now. And then the third, which is how do you combine those two, it is the use of technology, a bunch of different technology platforms and social media platforms. And in the developed markets, those are stronger. The infrastructure is stronger behind some of those tools. And certainly, even the ability to deliver the products and things like that are easier in more developed markets.



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

This is John A. I'd just add that within the distributor engagement piece, there's also the fact that there are many potential distributors sitting at home, looking for new ways to fill their day, to generate income for their families, to perhaps start new businesses. That makes it easier for distributors as they recruit their sales force, as they build their sales team.

**Sebastian Barbero Jefferies LLC, Research Division - Equity Associate**

And switching on to China. I was wondering what does your full year -- what does your 2021 guide embed for growth in the region?

**Alexander R. Amezcuita Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

No guideline. Yes, so we don't provide guidance by region. So just generally, I'd just point you to the overall volume growth of the -- of 2021.

**Sebastian Barbero Jefferies LLC, Research Division - Equity Associate**

Okay. And any -- many of your peers in the initial have cited issues with the supply chain. Anything to report here or has been pretty smooth for you guys?

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

Yes. Look, it's been pretty smooth. It has not been entirely smooth. That was mostly a reflection of just substantial sales growth that has created some out of stocks on some products, and it's been painful for some distributors who sell those products. It's been manageable. But certainly, we've had an impact from it. It's tough to quantify, but it's certainly something we've been able to overcome, but it's not non-existing.

**Sebastian Barbero Jefferies LLC, Research Division - Equity Associate**

Okay. And last one on CapEx for '21. Somewhat double what it was in 2019. But obviously, there was a bit of underinvestment in '20. Is that just a catch up effect?

**Alexander R. Amezcuita Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

That's right. It's a bit of a catch-up. Obviously, the volume this year, part of it is going to be into our manufacturing to help with being able to sustain that volume, not only for next year, but for our growth trajectory going forward. Part of it is for technology, continuing to invest in technology, particularly around distributor tools. And part of it is just spikiness.

**Operator**

I show our last question comes from the line of Ivan Feinseth from Tigress Financial.

**Ivan Philip Feinseth Tigress Financial Partners LLC, Research Division - Director of Research**

Congratulations on another incredible quarter, and congratulations to Alex and Bosco on their promotions.

**Alexander R. Amezcuita Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Thank you, Ivan.

**Ivan Philip Feinseth Tigress Financial Partners LLC, Research Division - Director of Research**

Now first of all, for the great growth, where do you see the drivers? Or where did you see the drivers coming from, especially since you say that the increase in distributors is breaking more toward younger people, toward millennials? What product lines are driving people to Herbalife to become a distributor, to become a customer? And so where do you see like the key drivers?

**Alexander R. Amezcuita Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Well, I mean, one thing -- that's a broad question, and there's a lot of different ways we can take it. But I think a piece of the question could be answered in some of the product categories that we are going in to attract different demographics and different folks. So

clearly, our H24 sports line attracts a younger demographic, an active -- healthy active lifestyle demographic that seems to resonate with all demographics, but particularly with that younger demographic. So we know it's a huge opportunity, and we're seeing that opportunity as we've rolled out that sort of sub brand, if you will, really resonating with the younger generation.

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

Yes. The other thing, by the way, Ivan, that we're pretty excited about on a go-forward basis is the fact that we've just launched in the U.S. 2 products that I think are going to appeal not only to Gen Z and millennials, but perhaps even to older customers as well. So this is less about the answer to your question on recruiting younger distributors and more to the fact that we were hoping to engage and retain a broad swath of customers as we go forward.

We're launching -- in fact, we've actually launched a couple of, I think, innovative products in the U.S. recently. MemoryArmor, which is a 300 milligrams of Bacopa, which is an Indian traditional herb with actually a fair amount of science behind it that is known to impact cognitive function and brain health. And then our very first entry into the cannabinoid marketplace with 2 topical products, a balm and a serum for outer use on the skin, and containing, I think, a really material amount of cannabinoid hemp extract. It's the beginning of our journey into that space. It's called Enrichual, and I think it's going to be an amazing product in the U.S. And at some point, we'll take it to other countries as regulation allows.

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**Ivan Philip Feinseth Tigress Financial Partners LLC, Research Division - Director of Research**

I would like to get into more specifics on some of the nutrition. I don't want to do it here. I welcome the opportunity to speak off-line. Then just two other things. When you spoke about there were some shortages of -- out of stock, do you think that the incredible results could have even been more incredible if the inventory was deeper?

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

So yes, there were some sales loss certainly when we were out of stock. I'm not going to get into quantifying, and I mean the results are great. And so probably would have been immaterial to the overall performance, but definitely lost some sales.

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**Ivan Philip Feinseth Tigress Financial Partners LLC, Research Division - Director of Research**

And what were some of the -- like the largest single items in the quarter? If you could just give us some overview or quick highlights.

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

Well, it's still Formula 1, which is a meal replacement shake. Our tea products and our aloe products still represent a huge portion of our sales.

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

Our Nutrition Clubs around the world has done very well in this last quarter, the last 2 or 3 quarters actually. And those are products that are their mainstays, F1, aloe and tea.

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**Alexander R. Amezcuita Herbalife Nutrition Ltd. - SVP of Finance, Strategic & IR**

Yes. And adding on to that, Ivan, really across all of our categories. I mentioned this in an earlier question, all of those have risen. Weight management is up 18%. Targeted nutrition is up 28%. Our energy line is up 32%. And so I mean that kind of gives you some perspective. It's really all boats rising.

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**Ivan Philip Feinseth Tigress Financial Partners LLC, Research Division - Director of Research**

And just quickly, as an example, there was an article in the Wall Street Journal that's saying one of the -- even younger people who have had COVID are experiencing memory loss. Do you think that's the driver of the new memory product or helping?

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

No. No. It's completely unrelated. We have actually very, very carefully thought to separate anything that we do from the pandemic. Our hearts go out to those that have lost loved ones or those that are suffering. And we've been very clear, the team and our distributors, on focusing on our traditional business, the traditional business that's performing. And it's not about a direct response to COVID in any way.

**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

Okay. And then my last question. You keep talking about digital tools and investments in digital tools. What are some of the areas you're going to expand?

And also, you have some great content that you have on this Herbalife fitness website with exercise videos. What are your thoughts -- how are you going to be incorporating that more into your customer engagement and giving ways to like monitor progress and things like that?

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

Yes. So this is John D. I'll take those. So first, on the technology side, they fall into a number of different buckets, by the way. Some of them is, in fact, capturing customer transaction data. Segmentation, as you know, has been rolled out a number of countries. It's in 8 countries as of today. Over the next 6 months, it will be in 8 more. By the end of next year, 80% of our volume -- maybe in excess of 80% of our volume will come from countries that have the preferred customer program, and that's -- there's a lot of programming in there country by country. It's not something you just turn on the switch and roll it out. So that's certainly one.

There are POS tools that we will roll out. So U.S. has a version of POS tool. We will look to roll that out in countries that want it, and there are a number of countries that want it because we think that's an efficiency tool for distributors that have clubs. But it could be used for more than just clubs, and I think it also can help increase the economic value of their customers.

There's also just general online tools. So we have tools that are online, sign up, online ordering. Those are the best-in-class for us, will get rolled out globally. So there's just a whole host of tools that we're going to invest in over the next year or plus. It will take more than a year, by the way, but a big investment comes next year.

And then there's, of course, on the sports side, we are going to look to make sure that, that portal that's got all that information is easy to use in different formats. So it could be mobile and things like that. And that's, I think, not only ties into our Herbalife24 program in general, but even those who are on Herbalife24, there will be a version on the fitness portal for them also to do some basic fitness.

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**Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research***

Congratulations again.

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**Operator**

I show no further questions in the queue at this time. I'd like to turn the call back over to the Chairman and CEO, John Agwunobi, for closing remarks.

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

Thank you. I'll keep this very quick. We're very proud of the work of our independent distributors around the world. They've really, I think, risen and grown their businesses and supported their customers in a way that makes us all extraordinarily proud.

I'm also particularly proud of our team and the way that it has responded to that growth and to that increase in demand for our services, our products. And when all is said and done, a big congratulations from myself to Alex Amezquita, our new CFO; and to Bosco Chiu, who's transitioning from CFO to what I think is going to be a critically important role as Chief Risk Officer, our goal being to be a model in that space in the future.

The future is bright. And as we say around here, we all feel like we've only just begun. And I'll end on that.

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**Operator**

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

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