

FINAL TRANSCRIPT

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HLF - Q1 2010 Herbalife Ltd. Earnings Conference Call

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Herbalife Ltd. - Chairman, CEO

Des Walsh

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PRESENTATION

Operator

Good morning and thank you for joining the first quarter 2010 earnings conference call for Herbalife Ltd. On the call today is Michael Johnson, the Company's Chairman and CEO, the Company's President, Des Walsh, John DeSimone, the Company's CFO and Brett Chapman, the Company's General Counsel. I would now like to turn the call over to Brett Chapman to read the Company's Safe Harbor language.

Brett Chapman - Herbalife Ltd. - General Counsel

Before we begin, as a reminder, during this conference call, comments may be made that include some forward-looking statements. These statements involve risk and uncertainty and as you know, actual results may differ materially from those discussed or anticipated. We encourage you to refer to yesterday's earnings release and our SEC filings for a complete discussion of risks associated with these forward-looking statements and our business.

In addition, during this call, certain financial performance measures may be discussed that differ from comparable measures contained in our financial statements, which are prepared in accordance with the US Generally Accepted Accounting Principals, referred to by the Securities and Exchange Commission as non-GAAP financial measures. We believe these non-GAAP financial measures assist management and investors in evaluating and comparing period to period results of operations in a more meaningful and consistent manner. Please refer to the Investor Relations section of our Web site, herbalife.com, to find our first quarter 2010 press release containing our reconciliation of these measures. Additionally, when management makes reference to volume during this conference call, they are referring to volume points. I'll now turn the call over to Michael.



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Michael Johnson - Herbalife Ltd. - Chairman, CEO

Thanks, Brett, and good morning everyone and welcome to our first quarter 2010 earnings call. We kicked off our 30th anniversary with a record first quarter. We experienced stronger volume in margins exceeding the guidance that we provided to you in February. 2010 is a year of opportunity as our business continues to gain momentum, led by engaged distributors who are driving daily use of Herbalife products to more consumers and expanding deeper into markets throughout the world.

Herbalife is in a unique competitive position with the direct selling industry. Our distributors have developed an economically attractive business method which comes in the form of nutrition clubs or weight loss challenges that emphasize daily consumption of our products. We believe these business methods, which provide a daily price point to consumers is transforming our business. Millions of people can now access Herbalife products and the business opportunities, especially in emerging markets, where they have the ability to pay a daily fee to our distributors for access to our great products. Yesterday we reported adjusted EPS of \$0.98, which was \$0.30 above our first quarter 2009 results. The improvement in earnings was driven primarily by revenue growth. Our reported net sales in the quarter increased 19% compared to the same period in 2009, again reflecting the strong growth in local currency sales, coupled with an FX tail wind of 530 basis points.

In terms of local currency, we experienced sales growth of 13% versus the same period in 2009 led by a 21% increase in the US Latino market and a 14% increase in the US general market. Growth in the general market is most encouraging and as we believe, unique in our industry. Des will provide you with additional detail regarding the general market in just a few moments. In total, our top five markets, which comprise almost 55% of our revenue, were up 15% in local currency sales in the first quarter. This growth was led by a 12% increase in new distributors, primarily reflecting recent changes we made in our marketing plan. Additionally, we experienced an increase in average active sales leaders of 11% compared to the same period in 2009, reflecting their focus on daily consumption business methods.

The breadth of our strong performance in the first quarter results can be seen in the fact that all six of our regions posted net sales growth. Turning to free cash flow, Herbalife's business model generates a large amount of free cash. We generated \$87.4 million in cash flow from operations in the quarter. And compared to last year's first quarter, we lowered our net debt by \$17.4 million to \$82.1 million while we repurchased \$28 million in stock and paid out \$12.1 million in dividends during that quarter. We remain in an enviable position with a conservatively levered balance sheet. Yesterday our Board of Directors approved an expansion and extension of our current share repurchase authorization, reflecting our belief that we will continue to generate significant cash in excess of our needs. This expansion represents a \$700 million increase to the prior \$300 million program, bringing the total authorization to \$1 billion.

This authorization runs through December 31st, 2014. As of March 31st, 2010, we have already used slightly more than \$100 million of the previous \$300 million buyback authorization, leaving approximately \$900 million. This expanded repurchase authorization is on top of the \$760 million we have returned to investors since the inception of our buyback and dividend program three years ago.

On a product front, we continue to target the global obesity epidemic around the world. As many of you have read in this weekend's "Wall Street Journal," more than a third of the adult population of America is, sadly, obese, a significant increase from even a decade ago. The annual health costs of obesity in America have risen from \$74 billion in 1998 to \$147 billion in 2008, and this is no longer an epidemic unique to the US. We have tremendous head room to grow our weight management category. This past quarter our weight management business increased 18% and comprised 63% of our business.

We introduced two new and improved products in the US and continue the globalization of key products this quarter. Throughout 2010, we are upgrading key products for release in both our weight management and targeted nutrition lines and as we enter our Herbalife decade, we are highly focused on innovation, recruiting new, outstanding talent in product research and development for sports nutrition, skin care, anti-aging and brain health. We also continue to increase our commitment to vertical



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integration and best manufacturing practices. Our expectation for Herbalife is to be recognized as the premiere nutrition company in the industry for product innovation, quality, efficacy and safety.

In quality assurance and safety new talent such as former FDA director Bill Frankos, who joined us recently as our Senior Vice President of Product Compliance and Safety, will also contribute credibility to our efforts to educate regulatory and government bodies around the world. As will activities such as the Global Nutrition Transition Conference for physicians that we held in Orlando, prior to the leadership summit in March. The world is still upside down about nutrition. Our shake, with the best protein, healthy carbohydrates, balanced vitamins, minerals and antioxidants is called a meal replacement, while a burger, fries and soda is called a meal. Hard for me to figure out, maybe you can. As more people become educated about healthy nutrition, we are here, ready to support them in their pursuit of healthy, active lifestyles.

Our continued confidence in the future of Herbalife is reflected in our 2010 guidance. We are raising our full-year 2010 EPS estimates to a range of \$3.80 to \$3.90, a 16% to 19% increase over our 2009 results. Our financial performance is directly attributable to the ongoing success and increased engagement of our independent distributors. Since January we've hosted distributor events in Ecuador, Brazil and China and celebrated our 30th anniversary at our leadership summit in Orlando, Florida. Some of our sales side analysts and top investors were in Orlando and experienced firsthand our distributors' passion for Herbalife. Their engagement with the business is higher than at any other point we can recall and there are more Herbalife meetings of every size, from Herbalife opportunity meetings, to success training seminars to leadership development weekends, taking place around the world than anytime before.

In two weeks we'll be in Singapore with our distributors from Asia-Pacific for the annual Extravaganza. We've sold nearly 15,000 tickets, putting this event on track to be the largest Herbalife event ever hosted in Asia. Our distributors will be exchanging ideas, learning from our most successful distributors and leaving with a new energy and a call to action that they will take back to their respective markets to continue to drive our wonderful momentum. Before I turn over to Des, let me repeat, we are confident 2010 is a year of opportunity for Herbalife and while we celebrate our 30th year in business, we truly believe that we're just getting started. Now let me turn it over to Des for specific

Des Walsh - Herbalife Ltd. - President

Thank you, Michael. The momentum we are seeing in our business is being driven by two key elements, the ongoing successful expansion of daily consumption business methods around the world, and the increased level of distributor engagement. We continue to see the expansion in daily consumption business methods as the largest driver of our distributors' businesses and Herbalife's growth. We believe that the momentum behind this evolution will continue to accelerate as more distributors and more markets have success acculturating daily consumption business methods in their markets.

We estimate that daily consumption business methods comprise approximately 30% of our current sales, but believe that these business methods can add significant incremental growth as distributors take daily consumption deeper into their respective markets. We believe that the other key driver behind our growth is the increased level of distributor engagement. Let me give you an example. Last December we hosted a leadership meeting for future President's Team members within the US general market. At that meeting, our Chairman's Club members challenged the future President's Team members to reengage in their markets and commit to scheduling additional Herbalife training sessions for their distributors, or STS to use our internal terminology.

The idea was to reengage distributors in cities around the country that had not been actively hosting meetings. These training meetings are the backbone to building a strong engaged distributor group and an infrastructure for training new distributors on the product and provide the business knowledge they need to take their businesses to the next level. The future President's Team members not only accepted the challenge, but they took it to heart. In the months following that December meeting, those US general market leaders held substantially more meetings in multiple cities throughout the US, reenergizing and reengaging more general market distributors around the country.



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It is not a coincidence that the general market posted such strong growth this quarter. The US general market has posted five consecutive months of growth, with the year-on-year rate of growth increasing as we move through the quarter. Momentum begins with engagement. We believe that the engagement level of our distributors has increased substantially and we commend our distributor leaders on their success in making this happen. While we are always looking at new countries in which to expand, our distributor leaders are taking the mantra of "going deeper" to heart with our new City by City program. This program encourages distributors in each city to work together, to create and implement a plan for growth in their city. The plan can include a range of elements such as a schedule of regular Herbalife opportunity meetings, success training seminars, and product and business opportunity trainings. Herbalife was founded as a person to person business, based around culture of meetings and now we are seeing a return to this with increased distributor engagement as a result.

Now let me provide regional highlights and color on some key markets. North America posted strong growth compared to the prior year period in both local currency net sales and volume points with increases of 22% and 18% respectively. One of the measurements that we used to gauge distributor engagement, average active sales leaders, increased 14% in the region compared to last year's first quarter results. This was an exceptionally strong quarter in the US, which benefited from growth in both the general and Latin markets and exceeded our internal expectations. US net sales grew 23% and volume points increased 19% versus the same quarter last year, well ahead of our expectations.

In the first quarter of 2010, the Latin market represented 65% of the US business. Volume points increased 21% compared to the first quarter 2009 results. We were pleased to see that new distributors and average active sales leaders both increased in the quarter. New distributors were up 15%, while average active sales leaders increased 22% over the prior-year period. We are enthusiastic about the ongoing growth opportunities in this market. While this has been and continues to be one of our most exciting markets, we believe that there remains large untapped areas of opportunity throughout the US Latin market.

Volume points in the general segment of the US market were up 14%, versus the first quarter in 2009. Both new distributors and average active sales leaders increased in the quarter by 29% and 2% respectively. We have been saying for the past several quarters that we believe that the general market was poised for growth.

The increased activity and engagement level is beginning to translate into a resumption of growth for the segment of the US market. We believe that the general market has likely turned the corner. Distributor leadership is engaged and is augmenting their traditional business methods with elements of daily consumption methods and achieving considerable success as a result.

Let's move now to Mexico, where local currency net sales for the quarter increased 8% and volume points increased 3%. New distributors increased 7% year over year in the quarter and we are pleased to see active average sales leaders increase by 4%, compared to the prior year period. Since Mexico's growth was substantially based on the successful expansion of nutrition clubs, one of our largest logistical challenges in Mexico has been improving distributor access to Herbalife products. As we have discussed in the past, we've expanded a number of Herbalife distribution centers in Mexico over the past several years. But even with more than 20 centers, there were still many under served areas around the country. In late 2009, we tested a pilot program in more than 30 locations in Mexico, where distributors who ordered their products from the Company could choose to pick up the order at a customer service counter within a non-Herbalife Mexican retail chain. In the first quarter, we rolled this program out in more than 300 outlets. Distributor acceptance has been outstanding with an increasing percentage of distributor orders going through these locations.

The Asia Pacific region continues to be a key growth driver for the Company. During the first quarter, local currency net sales increased 11% and volume points grew 5% compared to the prior-year period. New distributors in the region increased 38%. Of the 12 countries in the region, three posted more than 50% growth in local currency sales. South Korea, India, and Indonesia. We believe that the growth within the region continues to be driven by the expansion of daily consumption business methods, and the high degree of distributor engagement. Average active sales leaders increased 19% in the quarter.

Looking at key markets within the region, let me spend a few minutes discussing South Korea, Taiwan and India. All three markets have continued to increase the adoption of daily consumption methods and this continues to be a key driver of their



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growth. During the first quarter, local currency sales were up 69% in Korea, due to their expansion of daily consumption in the market. Average active sales leaders in Korea increased 72% in the first quarter, compared to the prior-year period. We believe that the momentum in Korea shows no signs of slowing. The country had an all-time record volume point month in March.

India is benefiting greatly with the increase in the addressable audience, who can partake in the daily price point made available by our independent distributors through the nutrition club model. We believe that within India our addressable audience is approximately 300 million people, and that the country has the potential for significant future growth. Local currency net sales and volume points increased 86% and 52% respectively in the quarter. Distributor engagement continues to grow as well with an 89% increase in average active sales leaders. Daily consumption and the replication of nutrition clubs continue to be the drivers of growth in India.

As we have mentioned in the past, the first quarter was a challenge for Taiwan, as they lapped a very difficult comparison in 2009. In the prior-year period, the Taiwanese government had a stimulus program in effect, which we estimate drove an incremental 12 million to 15 million volume points in the quarter. Volume points in Taiwan were down 28%, compared to the prior year. And while this quarter's comparison was negatively impacted by that one-time event, we were pleased to see average active sales leaders remain positive in the quarter.

Local currency net sales in the South and Central American region increased 30% due to timing, and volume points in the region were down 2% in the quarter. Average active sales leaders in the region increased 2% over last year's first quarter. In the quarter the region benefited from continuing its successful evolution to the daily consumption model. While there are 16 countries within the region, the key drivers remain Brazil and Venezuela. During the quarter we continue to see growth in Brazil and Venezuela, with slight volume point increases in both markets. During the quarter also the Company hosted its South American Extravaganza in Quito, Ecuador, and sold a record 13,000 tickets. This engagement level and the excitement of the distributor dealership in many markets around the region is very encouraging.

EMEA has been a challenging region for Herbalife as well as for most of our competitors over the past several years. Local currency net sales declined 2%, and volume points in the region declined 4% in the quarter, largely weighed down by continuing pressures in Western European countries, which muted the growth we've seen in some of the Eastern European markets. Average active sales leaders were essentially flat in the quarter. But there are markets within the region that are beginning to emerge with implementation of daily consumption through weight loss challenges and in some instances nutrition clubs.

Now let's turn to China, where local currency net sales increased 20% and volume points increased 23% in the first quarter compared to the prior-year period. A little over a year ago, we began to introduce the club concept into this unique market because of the strong success that clubs were demonstrating in Korea and Taiwan. As we have seen in other markets, including Brazil, the process takes up to 24 months to localize, train and replicate before we begin to see what we believe to be strong, sustainable growth.

We believe that our sales leaders in China are making progress acculturating the concept of daily consumption and we are now seeing clubs open in locations that are more like those which have been successful and duplicable in other markets. We currently have 11 provincial licenses within China and have applications in for five additional licenses.

As we have been discussing with you for the past several quarters, we believe that there's an ongoing transformation within our business. The daily consumption model has taken hold in some of our largest markets, and it continues to expand into more of our existing markets every day. Nutrition clubs in their various forms around the world are driving a significant portion of our volume growth. While we talk about the localization of clubs across the globe, it is important to understand that we believe we are in the early innings of their growth in most of our markets. In closing, let me congratulate our distributor leadership for their wonderful achievements in expanding daily consumption, increasing distributor engagement, hosting more meetings and driving the wonderful momentum we are seeing around the world. Now let me pass the call over to John to review the financials.



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John DeSimone - Herbalife, Ltd. - CFO

Thank you, Des. We'll start the financial portion of this call by giving you some of the highlights of the first quarter results compared to both last year and the guidance we provided in February. And we'll conclude with the review of our guidance for the second quarter and for full year 2010. Compared to prior year, first quarter net sales increased 18.6%. Local currency sales accounted for 13.3% of the increase, while a currency tailwind accounted for the remaining 530 basis point improvement of the increase.

The 13.3% local currency growth was comprised of the following growth by region. North America was up 22.4%, that was comprised of Latin American growth of 21.3% and the US general market growth of 14.3%, which is the largest growth in the general market since we began bifurcating the market in 2005. Asia Pacific increased 10.6%, despite Taiwan reporting a 17.3% decline due to the lapping of the one-time benefit to last year's results as a result of the government stimulus coupon. If we normalize for that event, Asia Pacific local currency net sales would have increased 22.3%. That increase was led by Korea and India which reported 69.1% and 85.9% increases respectively. Mexico was up 7.8%, China increased 20.4%, South and Central America increased 29.6%, led by Brazil, which increased 10.9% and Venezuela which increased 50.8%, which was due mostly to price increases. And lastly EMEA declined 2%.

Before turning to our margin and EPS results, I'm happy to say that we believe at this point that this is the last quarter we'll be spending time discussing the accounting treatment of Venezuela. In yesterday's earnings release, the income statement we provided contained footnotes detailing a line by line reconciliation related to the one-time impact from the implementation of highly inflationary accounting for Venezuela. As I discuss the Company's margin and EPS results for the quarter, I'll be referencing those which exclude this one-time impact.

Turning to gross margin for the quarter, adjusted gross margin was approximately 100 basis points below last year, driven mostly by currency. Specifically, the accounting for Venezuela at the curb rate, as supposed to the official rate, which is how we accounted for it last year, negatively impacted gross margins by 60 basis points.

Operating margin, on an adjusted basis, improved by 210 basis points versus last year. 37 basis points was a result of a weaker dollar, the remaining improvement was primarily a result of leverage from the revenue growth. Turning to EPS, the \$0.30 improvement in Q1 versus the prior year was largely a result of increase in volume. However, a weaker dollar did contribute \$0.07 to the quarter and a change in the effective tax rate contributed \$0.04 to the quarter. These items were partially offset by a higher share base, which negatively impacted EPS by \$0.02.

With respect to cash flow, our Company produced cash flow in the quarter of \$87.4 million from operations. We returned \$40.1 million to investors through a quarterly dividend of \$12.1 million and a share repurchase of \$28 million. We invested \$11.6 million in capital expenditures and our net debt as of March 31 was \$82.1 million, a \$17.4 million improvement compared to year-end 2009.

Let me now discuss our results compared to the guidance we provided in February. In comparing our first quarter results to our previous guidance, adjusted EPS of \$0.98 was \$0.18 above the high end of our guidance range, primarily reflecting a benefit from the contribution margins associated with higher than expected volume point growth. Also impacting the quarter was the timing of shipments and the timing of the tax rate. These timing related items contributed about \$0.07 to the quarter, \$0.04 from the timing of shipments and \$0.03 from the timing of tax-related items.

Now let me discuss our guidance for the second quarter and the full-year 2010. For the second quarter, our guidance reflect current FX rates and our expectations that the momentum in the business we have been seeing will continue. The guidance includes volume point growth of 8% to 9% and net sales growth of 12% to 13% above the prior-year period. We expect our effective tax rate to be in the 30.5% to 31.5% range and therefore our EPS guidance for the second quarter is expected to be in



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the range of \$0.89 to \$0.92. It is important to remember that while our first quarter was favorably impacted by \$0.07 of timing items, our second quarter is negatively impacted by \$0.05 of that \$0.07.

Turning to the full-year. We are raising our guidance for volume point growth to 6.5% to 7.5%. Additionally, we're raising our net sales guidance to 11% to 12% compared to the previous guidance of 8.5% to 9.5%. We expect our effective tax rate to be in the 30.0% to 31.0% range for the full year. In terms of EPS we are raising our guidance range to \$3.80 to \$3.90 compared to the previous guidance range of \$3.58 to \$3.70. This increase reflects a \$0.22 increase in the low end of our guidance range and a \$0.20 increase to the high end. This increase is a result of the \$0.18 beat in Q1 plus a \$0.09 increase in the improvement from currency, partially offset by a \$0.07 negative impact from the timing of certain items previously mentioned. From a capital expenditure standpoint, we continue to anticipate 2010 capital expenditures to be in the range of \$65 million to \$75 million, which includes capital to improve and expand our new US manufacturing facility, investments in technology to improve our distributor experience, and also the capital required to open up new countries over the course of the year.

Lastly, I'll conclude the prepared remarks with some additional comments regarding share repurchase. As Michael stated earlier, our Board of Directors approved an expansion and extension of our current share repurchase authorization, reflecting our belief in our ability to generate significant cash in excess of our needs. Since 2007 through the end of the first quarter of this year, the Company has returned over \$600 million to shareholders through the repurchase of approximately 16 million shares. This latest authorization provides the Company with an opportunity to return an additional \$900 million to shareholders over the next 19 quarters. We expect to execute this new program from cash flows generated from operations, but portions of the repurchase could be accelerated if we believe it's appropriate in the future. This new authorization is an indication in our belief in the long-term health of Herbalife and its ability to generate excess cash and our commitment to the utilization of a significant portion of that excess cash to enhance returns to our shareholders.

We will now open this call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). And your first question comes from Doug Lane with Jeffries & Company.

Doug Lane - *Jeffries & Company, Inc. - Analyst*

Yes, hi. Good morning, everybody.

John DeSimone - *Herbalife, Ltd. - CFO*

Good morning, Doug.

Doug Lane - *Jeffries & Company, Inc. - Analyst*

John, I get the increase in the stock buyback given the free cash flow. Can you elaborate on the implications for your dividend policy going forward?



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John DeSimone - Herbalife, Ltd. - CFO

Well, the increase in the authorization of the buyback does not prevent us from increasing our dividend yield in the future. So we thought our yield at this point was appropriate. It's in line with our peer group. It's ahead of the S&P 500. And if we believe we have a need to increase the dividend, we can still do that.

Doug Lane - Jeffries & Company, Inc. - Analyst

Okay. Fair enough. And then, Des, on nutrition clubs, at 30% of the model, obviously not everybody everywhere -- this would be the right model for everybody everywhere. Where do you see nutrition clubs eventually getting to maybe in the next two or three years?

Des Walsh - Herbalife Ltd. - President

So I think, Doug, we're going to see them continue to grow. You know, our distributors are prudent business people. In certain markets they're clearly waiting to see the adoption, the acculturation be successful before they adopt. But there's no question that the continuing success around the world is substantially driven by the nutrition clubs. (inaudible - technical difficulty) that have so far been waiting back and seeing the results.

Doug Lane - Jeffries & Company, Inc. - Analyst

So you think then they could get over 50% in the next couple of years?

Des Walsh - Herbalife Ltd. - President

I think that's absolutely achievable. And certainly we're already seeing that come to that in certain areas. So I think we're going to see 50%, maybe as high as 70% in the years to come.

Doug Lane - Jeffries & Company, Inc. - Analyst

This one leads into my next question. In the United States, where we haven't seen the traditional market growing at these kind of rates in the past. Is some of that -- you mentioned your training sessions, but is a lot of that market moving over to nutrition clubs as well?

Des Walsh - Herbalife Ltd. - President

Yes, it's really two things, Doug. First of all, it's obviously the expansion of nutrition clubs. But also it's in general more meetings, more activity, more distributor engagement. And the other important thing to remember, Doug, is that when we talk about the nutrition clubs, I think it will be helpful to think of these in many cases as similar to the distributor offices of old, in that all of the different methods of doing the business are being conducted from the nutrition clubs, all that simply is being added is the fact that on a daily basis, customers are being invited to experience the products, to get on programs and so on. So it's really a combination of all different methods, just simply operated from distributors working together. The other thing obviously is that we're just getting start with the clubs in the general market in the US and so, huge, huge head room for that as we progress through the years to come.



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Doug Lane - *Jeffries & Company, Inc. - Analyst*

Okay. And then just lastly with Waldo's in Mexico. Is that pretty much up and running now heading into the second quarter? Or are you still building out that distribution opportunity?

Des Walsh - *Herbalife Ltd. - President*

No. It's up and running. We have over 300 locations currently operating. And what we're now seeing is that we've got as high as 18% of the volume in Mexico, orders are actually being picked up through those centers.

Doug Lane - *Jeffries & Company, Inc. - Analyst*

Already. Okay. Thanks.

Operator

Your next question comes from Brett Jordan with Avondale Partners.

Brett Jordan - *Avondale Partners - Analyst*

Hi. Good morning. Just looking at some of the markets that have really seemed to turn on with the daily consumption model. Could you talk about what percentage of India is going through daily right now?

John DeSimone - *Herbalife, Ltd. - CFO*

Hi, this is John. I'll take that question. Most of the growth in India is being driven by clubs and the adoption of daily consumption. It's the benefit of the daily price point that's really driving growth in India. It's a culture that's very accustomed to paying for product on a daily basis. And not on a monthly basis.

Brett Jordan - *Avondale Partners - Analyst*

So I guess what percentage of the volume would be going on daily versus monthly?

Des Walsh - *Herbalife Ltd. - President*

You know, it's tough to tell. About all we can say is this. For the last number of years, India has been a flat market essentially doing 1 million volume points per month. What we've seen is that the clubs began there about four years ago. We go through this normal two year period of acculturation, finding out how the clubs work in the market, and now we're doing about 5 million volume points a month. So clearly you look at that 1 million to 5 million and certainly the bulk of that is being driven by the adoption of the clubs.

Brett Jordan - *Avondale Partners - Analyst*

Okay.



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Des Walsh - Herbalife Ltd. - President

The other thing as we mentioned is, we've identified that in India we now have an addressable population of about 300 million people, substantially because now we have a price point which is affordable on a daily basis to that huge group of Indian consumers. And so that's one of the reasons obviously we're so excited about what's happening in India today and what the prospects are for India down the road.

Brett Jordan - Avondale Partners - Analyst

Okay. Great. On Waldo's, just a little bit more color there, you said 18% of the volume points in Mexico are going through the Waldo's distribution channel. How many distributors are they buying from? Is it an 80/20 rule where the minority of the population does the majority of the volume? Or is that reasonably well adopted across the population of the distributors?

Des Walsh - Herbalife Ltd. - President

So in Mexico because of the nutrition clubs, we have a huge number of distributors that are very active. So obviously we have over 30,000 clubs operating in Mexico. And all of those have individual or multiple distributors associated with them, depending on whether they're home or office clubs. What Waldo's has done, obviously is greatly increase the efficiency for those distributors who now can place an order over the phone and then just go to a center in their community, rather than some considerable distance to a sales center, some distance away. So we believe that obviously this is hugely beneficial for distributors in terms of making their time more productive and therefore enable them to do more business more effectively.

Brett Jordan - Avondale Partners - Analyst

Okay. So do you have a feeling for the percentage of the distributors that are using Waldo's now?

Des Walsh - Herbalife Ltd. - President

I don't know that we have an exact statistic on that but I think we'd be happy to --

John DeSimone - Herbalife, Ltd. - CFO

I'll look that up and get back to you, Brett.

Brett Jordan - Avondale Partners - Analyst

All right, great. And then one last question. Singapore coming up in May for the Extravaganza. Is there incremental overhead attached to the promotions that you're going to be running in the second quarter? Just costs associated, driving business forward. Is that a meaning (inaudible) to run your largest Asian show in history I guess is the question.

John DeSimone - Herbalife, Ltd. - CFO

This timing event that changed year to year and in the second quarter in general and in the third quarter we have more events than we do in the first and the fourth quarter. So if you're looking to model SG&A, you can expect that there will be a spike in both Q2 and Q3 and it will be higher than in it was in Q1. And that's reflected in the guidance that we provided.



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Brett Jordan - Avondale Partners - Analyst

All right. Great. Thank you.

Operator

Your next question comes from Tim Ramey with D.A. Davidson & Company.

Tim Ramey - D.A. Davidson & Co. - Analyst

Hi. Good morning. Congratulations. The whole concept of distributor engagement sounds kind of touchy-feely and soft. But it's easy to see how that, with daily consumption is perhaps just top of mind every day to the people in your organization. How do you kind of manage that distributor engagement level? It was somewhat of a fluke that it rose due to the change in the daily consumption model. I'll let you talk. Sorry.

Des Walsh - Herbalife Ltd. - President

Sure. No worries, Tim. So touchy-feely is probably a good term. But it's obviously one of the things that drives this business. We are a driven business, which is driven by confidence and passion. And both of those thrive in an environment where you have got people meeting face-to-face, sharing success, sharing stories of how they're achieving that success. So what we're doing, Tim, in order to support our distributors in this, is that we're sharing the statistics. So one of the statistics that we shared at that December future President's Team meeting is that we contrasted the Latin business in the US, where as of the end of last year, they had approximately 90 what we call success training seminars attended by about 20,000 people a month, compared to the general market, where we had less than 20 and less than 1,000 people.

And so while the distributor leadership in the general market, it was they learned from that and they said let's go back and reengage and dramatically increase the number of meetings. That's what happened in the first quarter this year. Dramatic increase in terms of number of monthly training sessions, similar increase in number of attendees and we see the business go up. What we're now doing is that we're actually expanding this concept, what we refer to as the City by City program, around the world, where we're encouraging distributors in all cities to embrace their fellow distributors in that city and to think not just organizationally, but now also to think geographically and so we believe that distributor engagement City by City around the world can have more meetings, more activity, and therefore more sales as a result.

Tim Ramey - D.A. Davidson & Co. - Analyst

Thanks Des. Maybe just a quick update on the progress of verticalization.

John DeSimone - Herbalife, Ltd. - CFO

I'll take that. This is John. We're on track with what we've communicated in the past. We purchased our facility in the second half of last year. We're in the process of upgrading that facility and moving products in, but the meaningful amount of products going into that factory doesn't happen until the third quarter. And we're on track with that.

Tim Ramey - D.A. Davidson & Co. - Analyst

So is there any meaningful production right now?



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John DeSimone - Herbalife, Ltd. - CFO

There is production. It's not meaningful. So you're not going to see any margin enhancement from that facility probably until Q4. It will kick in, the production, in Q3 in a big way and then you have to get through one inventory turn before you start seeing the benefit. Right now it's somewhere between 10% and 15% of our US production going through that facility. It's a small number.

Tim Ramey - D.A. Davidson & Co. - Analyst

Thanks, John.

Operator

Your next question comes from Scott VanWinkle with Canaccord.

Scott VanWinkle - Canaccord - Analyst

Hi. Congratulations. Sticking on the Waldo Mexico questions. What percent complete are you in building out that network? I believe not all of the provinces have been rolled out. And can I simply say that a high percentage of the improvement we're seeing in Mexico is driven by that distribution improvement and therefore really focus on that build-out as being a driver.

John DeSimone - Herbalife, Ltd. - CFO

Well, first of all, it's fully implemented. It became fully operational in the middle of the first quarter. So we're in 300, a little over 300 stores now. And from an access standpoint, we do believe that ultimately will be a driver of growth from Mexico. There is a short-term inventory burnoff that needs to take place for inventory that was in the field, that now distributors are buying from Waldo's instead of from local warehouses. So there will be a little bit of an inventory correction that took place in Q1, maybe a little bit into Q2. Nothing meaningful. Just increased access is a strategy we have both from a business opportunity standpoint and a product standpoint. And Waldo's helps accomplish that in a country that was really difficult to reach a number of our distributors.

Des Walsh - Herbalife Ltd. - President

But, Scott, as well as that obviously it's not just that that's obviously helping the business recover. What we've got is we've got distributor leadership extremely engaged. In addition, we've just completed a nutrition club, almost a relaunch in Mexico with the unified training program, which was given by leaders throughout the country, it was attended by over 25,000 distributors. And it focused on a variety of different areas, it focused on new business building areas, how to invite new customers, new merchandising, ethics, a whole variety of different issues. And in fact we're watching that with great interest, because based on what we see the impact of that in Mexico, we'll consider adopting and rolling that out in other markets where we now have mature nutrition club businesses.

Scott VanWinkle - Canaccord - Analyst

Thank you. And on the US general market two questions. One, obviously there's always little differences here and there with nutrition clubs. Are the same products being offered in a general market club as the Hispanic side? And then second, I think you said that the growth in new distributors in the general market was 29%. And average active were up 2%. Did I get those numbers right and what does that big disparity mean between those two numbers?



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Des Walsh - Herbalife Ltd. - President

So going from back to front -- so in relation to -- so it's correct. New distributors up 29%, average active sales leaders up 2%. So new distributors effectively is an indication of people coming into the business. That's our future pipeline. Obviously we're very encouraged with that, because particularly with our new -- the addition to the marketing plan of the 5K cumulative supervisor method, it means that every one of those new distributors has the potential to become a supervisor over a period of up to 12 months. So we're very encouraged by that in terms of future pipeline. Average active sales leaders is really a measure of activity and engagement, because that reflects the average number of, certainly in the US general market we refer to them as supervisors, who are ordering each month. So that the fact that that's trending upwards is an indication of a more consistent stable business, as more of our supervisors are actually purchasing each month. And as far as the future expansion of the clubs and the products, so effectively 51% globally, our Formula 1, tea and aloe represent about 51% of our business in 2010 compared to 50% in 2009. So what we're seeing is that as the clubs grow and evolve, the focus in terms of those three core club products becomes stronger.

Scott VanWinkle - Canaccord - Analyst

And for John, or I guess anyone. If global currencies were to stay where they are today for the next 12 months, would there be any intention to change pricing to alleviate pressure on gross margin or differences in each markets now with payout, given where currencies have been volatile over the last 12 to 18 months.

John DeSimone - Herbalife, Ltd. - CFO

First, if currencies stay where they are right now, then there's no change to our current forecast. So our forecast reflects current exchange rates. From a pricing standpoint, we try not to price necessarily with currency. We'd much rather price with inflation and commodity and price increases if that happens to take place. Because currencies change all the time. So it's really difficult for us to change prices up when the dollar strengthens and change it back down when it weakens. So we stick to pricing in a market based on inflation and purchasing power.

Scott VanWinkle - Canaccord - Analyst

Okay. Thank you.

Operator

(Operator Instructions.) Your next question comes from Chris Ferrara with Merrill Lynch.

Chris Ferrara - Merrill Lynch - Analyst

Hey, guys. I know you said in Mexico the Waldo's transition resulted in some burnoff of inventory. But can you explain a little bit better why that would be and then also was volume of 3% in Mexico, was that what you thought it would be? Was that as good as you had expected it to be?

Des Walsh - Herbalife Ltd. - President

In relation to the inventory issue, Chris, so historically if you think about us, for our lower level distributors, operators and nutrition clubs, essentially they're operating on a cash and carry basis, because they don't have the funds to actually fund the timeline between ordering a product, paying for it and having it delivered. So in remote areas, where it may take several days for product to reach them, and where it's not practical for them to have visited in person one of our 20 sales centers, what would



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happen in that area is that an upline distributor would effectively carry an inventory of product and they would actually sell that to their downline and that's obviously a part of our marketing plan.

What is happening now, of course, is that through the Waldo's program, there's now over 300 additional locations, where our distributors in those areas can go to pick up product. In addition, with the change of the marketing plan, whereby either the 5K cumulative or the qualified producer, there's now a second incentive for that distributor to buy directly from the Company. So you have the combination of an incentive now to buy directly from the Company and you've got the increased access with the additional Waldo's locations that are causing those distributors to switch their patterns and buy directly from the Company and pick up at a Waldo's. What that means is that distributor leaders who had a small warehouse and were supplying that inventory effectively are selling off that inventory, because they no longer need to provide that service to their downline.

John DeSimone - Herbalife, Ltd. - CFO

Chris, this is John. Mexico did achieve what we had expected them to achieve in Q1, to answer the second part of your question.

Chris Ferrera - Merrill Lynch - Analyst

Great. That helps. I guess how do you guys -- just give an updated thought process on how you think about Mexico growth in the long run. I suspect 3% volume growth -- you do expect it to recover to I guess somewhat of a higher growth rate than that or is that off base?

John DeSimone - Herbalife, Ltd. - CFO

You know, we've never guided by market. I shouldn't say never, but I think it's a practice that stopped a few years ago. But we do expect growth from Mexico. I would say that Mexico is underpenetrated relative to the US Latino market. The US Latino market has a penetration rate of over 10% and Mexico is under 5%. So we think there's still quite a bit of opportunity left. But we're not going to give out specific numbers by market.

Chris Ferrera - Merrill Lynch - Analyst

Okay. Great. And actually that was a perfect segway into my last question, if you'll humor me. The Latino portion of the US business, I guess you just said volume penetration is like 10%. I think you had said in the past that 10% is really kind of a mixed bag, some markets are much higher than that and some cities in the US really have very little penetration. Can you talk about what you're doing to drive penetration in cities where there is very little penetration. And I guess why is there little penetration in the cities where there is?

Des Walsh - Herbalife Ltd. - President

What we're doing is this, Chris. We are sharing with our distributor leaders the areas of opportunity. For example, we had a presentation just internally yesterday, where we reviewed states around the US, where we have significant Latino populations, but today we don't have that infrastructure in terms of STS, in terms of opportunity meetings and so on. So we're doing two things. One is we are highlighting those areas with our distributor leadership so that they're aware of the opportunity. And then we're supporting them in terms of support to host meetings in those areas. And then the last thing, of course, is that even in our major metropolitan markets, there are considerable differences from one distributor -- from one area to another. And again that's what the City by City program is all about, where we're encouraging friendly competition between those cities because we know that our distributors are very competitive and that really helps them focus on the opportunity that lies in those cities.



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Chris Ferrera - *Merrill Lynch - Analyst*

Should you expect a big portion of your growth in the Latino portion of the US to come from increased penetration of underpenetrated cities? I mean, is it that simple or is that a tougher slog than driving, if it's 10% on average, maybe it's 15% in some cities, is it going to be -- is it possible to drive that 15% to 20%, or are there other cities even with high penetration levels where you think you could get even more?

Des Walsh - *Herbalife Ltd. - President*

We think there's opportunity everywhere, Chris. And it's balanced throughout the country, it's not only in those areas where we have very little penetration, even in the cities frankly where we have high penetration, we believe there's still significant upside.

Chris Ferrera - *Merrill Lynch - Analyst*

Great, thanks guys.

John DeSimone - *Herbalife, Ltd. - CFO*

I don't think we have any more questions. So I'll pass it over to Michael for closing comments.

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

Well, first of all, I want to congratulate everyone on the team. The thing I'm congratulating you on is I didn't have to handle one single question this morning. I think that's fabulous. It shows the strength of our team, not only in this room, but globally in what's taking place.

Barb Anderson, who is the head of our communications, handed me a book review this morning. It was called -- Muhammad Yunus, and it's "Building a Social Business". And I read this early this morning. And there's a quote in here, a line in here that's just amazing. It says, "In just a few short years, social business has developed from a mere idea to a living, rapidly growing, reality," Dr. Yunus says. "It is already bringing improvements into the lives of many people and is now on the verge of exploding into one of the world's most important social and economic trends."

What we have in Herbalife is momentum. We have this tremendous momentum to fix a social problem, which is nutrition that is plaguing the world. Obesity is, if you caught the article in the "Wall Street Journal" on Saturday in the weekend edition, obesity is now a \$174 billion problem in the medical costs of this country, and it's exploding on a global basis. What we're doing at Herbalife is we're building the best business opportunity on the face of the Earth, combined with the best products, we're vertically integrating this Company to build a stronger infrastructure for our distributors to take and exploit these products, get them to people on a daily basis for a low-cost, an opportunity that we're starting to see explode in marketplaces like India. Des downplayed it a little bit, but I'm very excited about India and what's taking place there. And what we're seeing happen in the US general marketplace are all signals of great momentum. The market places where daily consumption is lagging, it will improve. When we have our meetings, we show people who have success.

There are new faces on stage every single event. Faces that people don't know, who are collecting large checks, bonuses, building our Company to a higher and more significant level. Because they're on the mission for nutrition and it's an opportunity to not only be an economic personal opportunity, but a social mission and a real mission for nutrition. We've got something really special here. Our verticalization is going to continue to improve this Company. The opportunity that distributors are



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seeing and seizing is going to continue to grow this Company. We thank you for your confidence. We're excited about the future of Herbalife. We're excited about the days ahead. So thank you for being with us today. We appreciate it.

Operator

This concludes the first quarter 2010 earnings conference call for Herbalife Ltd. You may now disconnect.

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