

NU SKIN ENTERPRISES INC  
Form 10-Q  
August 03, 2018

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

Commission File Number: 001-12421

	NU SKIN ENTERPRISES, INC. (Exact name of registrant as specified in its charter)	
Delaware		87-0565309
(State or other jurisdiction of incorporation or organization)	75 WEST CENTER STREET PROVO, UTAH 84601 (Address of principal executive offices, including zip code) (801) 345-1000 (Registrant's telephone number, including area code)	(IRS Employer Identification No.)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes    No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes

No

As of July 31, 2018, 55,530,464 shares of the registrant's Class A common stock, \$.001 par value per share, were outstanding.

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NU SKIN ENTERPRISES, INC.

QUARTERLY REPORT ON FORM 10-Q – SECOND QUARTER 2018

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In this Quarterly Report on Form 10-Q, references to "dollars" and "\$" are to United States ("U.S.") dollars.

Nu Skin, Pharmanex, and ageLOC are our trademarks. The italicized product names used in this Quarterly Report on Form 10-Q are product names and also, in certain cases, our trademarks.

## PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

## NU SKIN ENTERPRISES, INC.

Consolidated Balance Sheets (Unaudited)

(U.S. dollars in thousands)

	June 30, 2018	December 31, 2017
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$402,031	\$426,399
Current investments	8,200	11,847
Accounts receivable	50,180	33,196
Inventories, net	283,730	253,454
Prepaid expenses and other	70,898	52,893
	815,039	777,789
Property and equipment, net	503,452	464,587
Goodwill	187,423	114,954
Other intangible assets, net	95,887	67,647
Other assets	144,562	164,895
Total assets	\$1,746,363	\$1,589,872
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$58,920	\$50,341
Accrued expenses	290,653	319,189
Current portion of long-term debt	97,481	77,840
	447,054	447,370
Long-term debt	370,525	310,790
Other liabilities	125,250	127,116
Total liabilities	942,829	885,276
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Class A common stock – 500 million shares authorized, \$.001 par value, 90.6 million shares issued	91	91
Additional paid-in capital	532,996	466,349
Treasury stock, at cost – 35.0 million and 37.9 million shares	(1,296,628)	(1,304,694)
Accumulated other comprehensive loss	(75,460)	(66,318)
Retained earnings	1,642,535	1,609,168
	803,534	704,596
Total liabilities and stockholders' equity	\$1,746,363	\$1,589,872

The accompanying notes are an integral part of these consolidated financial statements.

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NU SKIN ENTERPRISES, INC.  
Consolidated Statements of Income (Unaudited)  
(U.S. dollars in thousands, except per share amounts)

	Three Months Ended		Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
	2018	2017	2018	2017
Revenue	\$704,190	\$550,101	\$1,320,409	\$1,049,200
Cost of sales	168,549	121,521	314,830	232,787
Gross profit	535,641	428,580	1,005,579	816,413
Operating expenses:				
Selling expenses	272,757	228,353	530,459	437,361
General and administrative expenses	180,120	135,488	333,366	268,051
Total operating expenses	452,877	363,841	863,825	705,412
Operating income	82,764	64,739	141,754	111,001
Other income (expense), net	(11,165 )	(2,731 )	(9,958 )	(7,298 )
Income before provision for income taxes	71,599	62,008	131,796	103,703
Provision for income taxes	20,638	19,967	45,296	34,173
Net income	\$50,961	\$42,041	\$86,500	\$69,530
Net income per share (Note 2):				
Basic	\$0.92	\$0.79	\$1.58	\$1.32
Diluted	\$0.90	\$0.77	\$1.53	\$1.28
Weighted-average common shares outstanding (000s):				
Basic	55,608	52,929	54,807	52,804
Diluted	56,713	54,839	56,430	54,466

The accompanying notes are an integral part of these consolidated financial statements.

## NU SKIN ENTERPRISES, INC.

## Consolidated Statements of Comprehensive Income (Unaudited)

(U.S. dollars in thousands)

	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
Net income	\$50,961	\$42,041	\$86,500	\$69,530
Other comprehensive income, net of tax:				
Foreign currency translation adjustment, net of taxes of \$(558) and \$1,901 for the three months ended June 30, 2018 and 2017, respectively, and \$296 and \$1,679 for the six months ended June 30, 2018 and 2017, respectively	(20,047)	81	(9,000)	9,776
Net unrealized gains/(losses) on foreign currency cash flow hedges, net of taxes of \$(10) and \$(114) for the three months ended June 30, 2018 and 2017, respectively, and \$18 and \$99 for the six months ended June 30, 2018 and 2017, respectively	87	207	(160)	(180)
Reclassification adjustment for realized losses/(gains) in current earnings, net of taxes of \$3 and \$143 for the three months ended June 30, 2018 and 2017, respectively, and \$(2) and \$120 for the six months ended June 30, 2018 and 2017, respectively	(26)	(260)	18	(217)
	(19,986)	28	(9,142)	9,379
Comprehensive income	\$30,975	\$42,069	\$77,358	\$78,909

The accompanying notes are an integral part of these consolidated financial statements.

NU SKIN ENTERPRISES, INC.  
Consolidated Statements of Cash Flows (Unaudited)  
(U.S. dollars in thousands)

	Six Months Ended	
	June 30,	
	2018	2017
Cash flows from operating activities:		
Net income	\$86,500	\$69,530
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	40,142	35,080
Equity method earnings	(43 )	(358 )
Gain on step acquisitions	(13,644 )	—
Loss on extinguishment of debt	7,220	—
Foreign currency losses	10,194	(256 )
Stock-based compensation	13,267	7,581
Deferred taxes	3,023	5,390
Changes in operating assets and liabilities:		
Accounts receivable	(6,775 )	(2,812 )
Inventories, net	(16,743 )	8,706
Prepaid expenses and other	(19,676 )	(15,140 )
Other assets	(546 )	(2,567 )
Accounts payable	1,040	(4,357 )
Accrued expenses	(45,363 )	(21,607 )
Other liabilities	(6,663 )	4,839
Net cash provided by operating activities	51,933	84,029
Cash flows from investing activities:		
Purchases of property and equipment	(28,429 )	(27,751 )
Proceeds on investment sales	7,964	7,741
Purchases of investments	(4,722 )	(4,716 )
Acquisitions (net of cash acquired)	(28,311 )	(25,095 )
Investment in equity investee	(4,750 )	—
Net cash used in investing activities	(58,248 )	(49,821 )
Cash flows from financing activities:		
Exercise of employee stock options and taxes paid related to the net shares settlement of stock awards	5,951	7,795
Payments on long-term debt	(514,177)	(64,495 )
Payment of cash dividends	(40,091 )	(38,042 )
Payment of debt issuance costs	(7,243 )	—
Proceeds from debt	582,398	67,000
Repurchases of shares of common stock	(35,823 )	(22,135 )
Net cash (used in) in financing activities	(8,985 )	(49,877 )
Effect of exchange rate changes on cash	(9,068 )	3,525



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Net (decrease) in cash and cash equivalents	(24,368 )	(12,144 )
Cash and cash equivalents, beginning of period	426,399	357,246
Cash and cash equivalents, end of period	\$402,031	\$345,102

The accompanying notes are an integral part of these consolidated financial statements.

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NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

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## 1. THE COMPANY

Nu Skin Enterprises, Inc. (the "Company") is a leading, global direct selling company that develops and distributes premium-quality, innovative personal care products and nutritional supplements that are sold worldwide under the Nu Skin and Pharmanex brands and a small number of other products and services. Over the last several years, the Company has introduced new Pharmanex nutritional supplements and Nu Skin personal care products under its ageLOC anti-aging brand. The Company reports revenue from seven segments: Mainland China; South Korea; Southeast Asia, which consists of Brunei, French Polynesia, Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam; Americas/Pacific, which consists of Australia, Canada, Latin America, New Caledonia, New Zealand and the United States; Japan; Hong Kong/Taiwan; and Europe, Middle East and Africa ("EMEA"), which consists of several markets in Europe as well as Israel, Russia, Ukraine and South Africa (the Company's subsidiaries operating in these countries in each segment are collectively referred to as the "Subsidiaries").

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. The unaudited consolidated financial statements include the accounts of the Company and its Subsidiaries. All significant intercompany accounts and transactions are eliminated in consolidation. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, considered necessary for a fair statement of the Company's financial information as of June 30, 2018, and for the three- and six-month periods ended June 30, 2018 and 2017. The results of operations of any interim period are not necessarily indicative of the results of operations to be expected for the fiscal year. The consolidated balance sheet as of December 31, 2017 has been prepared using information from the audited financial statements at that date. For further information, refer to the consolidated financial statements and accompanying footnotes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

## 2. NET INCOME PER SHARE

Net income per share is computed based on the weighted-average number of common shares outstanding during the periods presented. Additionally, diluted earnings per share data gives effect to all potentially dilutive common shares that were outstanding during the periods presented. For the three-month periods ended June 30, 2018 and 2017, stock options of 0.3 million and 0.2 million, respectively, and for the six-month periods ended June 30, 2018 and 2017, stock options of 0.9 million and 0.6 million, respectively, were excluded from the calculation of diluted earnings per share because they were anti-dilutive.

## 3. DIVIDENDS PER SHARE

In February and April 2018, the Company's board of directors declared a quarterly cash dividend of \$0.365 per share. These quarterly cash dividends of \$19.8 and \$20.3 million were paid on March 14, 2018 and June 13, 2018 to stockholders of record on February 26, 2018 and May 25, 2018. In July 2018, the Company's board of directors declared a quarterly cash dividend of \$0.365 per share to be paid on September 12, 2018 to stockholders of record on August 31, 2018.

## 4. DERIVATIVE FINANCIAL INSTRUMENTS

The Company enters into non-designated foreign currency derivatives, primarily comprised of foreign currency forward contracts, for which hedge accounting does not apply. The changes in the fair market value of these non-designated derivatives are included in other income/expense in the Company's consolidated statements of income. The Company uses non-designated foreign currency derivatives to hedge foreign-currency-denominated intercompany transactions and to partially mitigate the impact of foreign-currency fluctuations. The fair value of the non-designated foreign currency derivatives is based on third-party quotes.

NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

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The following table summarizes gains (losses) related to derivative instruments not designated as hedging instruments during the three- and six-month periods ended June 30, 2018 and 2017 (U.S. dollars in thousands):

	Location of Gain (Loss) Recognized in Income	Amount of Gain (Loss) Recognized in Income	
		Three Months Ended June 30, 2018	Six Months Ended June 30, 2017
Derivatives not designated as hedging instruments:			
Foreign currency contracts	Other income (expense)	\$—	\$—
			\$(485)

The Company designates as cash-flow hedges those foreign currency forward contracts it enters to hedge forecasted intercompany transactions that are subject to foreign currency exposures. Changes in the fair value of these forward contracts designated as cash-flow hedges are recorded as a component of accumulated other comprehensive income (loss) within shareholders' equity (deficit), and are recognized in the consolidated statement of income during the period which approximates the time the hedged transaction is settled.

As of June 30, 2018, the Company held no forward contracts designated as foreign currency cash flow hedges compared to notional amounts of 2.2 billion Japanese yen and 1.0 million Euros (\$19.6 million and \$1.1 million, respectively) as of June 30, 2017, to hedge forecasted foreign-currency-denominated intercompany transactions. The fair value of these hedges were zero and \$0.3 million as of June 30, 2018 and 2017, respectively.

The following table summarizes gains (losses) related to derivative instruments recorded in other comprehensive income (loss) during the three- and six-month periods ended June 30, 2018 and 2017 (U.S. dollars in thousands):

	Derivatives designated as hedging instruments:	Amount of Gain (Loss) Recognized in Other Comprehensive Loss			
		Three Months Ended June 30, 2018		Six Months Ended June 30, 2017	
Foreign currency forward contracts related to intercompany license fee, product sales, and selling expense hedges		\$87	\$207	\$(160)	\$(180)

NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

The following table summarizes gains (losses) relating to derivative instruments reclassified from accumulated other comprehensive loss into income during the three- and six-month periods ended June 30, 2018 and 2017 (U.S. dollars in thousands):

	Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income	Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income			
		Three Months Ended		Six Months Ended	
Derivatives designated as hedging instruments:		June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Foreign currency forward contracts related to intercompany license fees and product sales hedges	Revenue	\$(26)	\$134	\$18	\$109
Foreign currency forward contracts related to intercompany selling expense hedges	Selling expenses	\$—	\$269	\$—	\$228

As of June 30, 2018 and December 31, 2017, there were zero and \$0.1 million, respectively, of unrealized gains/(losses) included in accumulated other comprehensive loss related to foreign currency cash flow hedges. The remaining \$75.5 million and \$66.4 million as of June 30, 2018 and December 31, 2017, respectively, in accumulated other comprehensive loss are related to cumulative translation adjustments. The Company assesses hedge effectiveness at least quarterly. During the three- and six- month periods ended June 30, 2018 and 2017, all hedges were determined to be effective.

The Company reports its derivatives at fair value as either other current assets or accrued expenses within its consolidated balance sheet. See Note 12 - Fair Value.

## 5. REPURCHASES OF COMMON STOCK

During the three-month periods ended June 30, 2018 and 2017, the Company repurchased 0.2 million and 0.3 million shares of its Class A common stock under its open market stock repurchase plan for \$18.4 million and \$15.3 million, respectively. During the six-month periods ended June 30, 2018 and June 30, 2017, the Company repurchased 0.5 million and 0.4 million shares of its Class A common stock under its open market repurchase plans for \$35.8 million and \$22.1 million, respectively. As of June 30, 2018, \$92.2 million was available for repurchases under the Company's open market stock repurchase plan. In July 2018, the previous stock repurchase plan was terminated and replaced by a new repurchase plan with an initial authorization amount of \$500 million.

## 6. SEGMENT INFORMATION

As a result of the Company's management changes in the first quarter of 2017, the Company concluded that the Chief Operating Decision Maker, as defined in ASC 280, is now comprised of the CEO, President and CFO. This change required the Company to reevaluate its determination of operating segments. The Company's operating segments are based on geographic regions that generate revenue and hold its long-lived assets. The Company sells and distributes its products through a global network of customers and sales leaders in approximately 50 markets. The Company has divided these markets into seven operating segments, which are the Company's reportable segments: Mainland China, Hong Kong/Taiwan, South Korea, Japan, Southeast Asia, Americas/Pacific and EMEA. The reportable segments generate revenue from the sale of personal care products and nutritional supplements under the Nu Skin and Pharmanex brands, have similar business characteristics and align with how the CODM function began assessing performance and allocating resources in the first quarter of 2017. The Other category includes the manufacturing and product-packaging companies that the Company acquired during the first quarter of 2018.

NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

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Segment information for the three- and six-month periods ended June 30, 2017 has been recast to reflect the move of the Pacific components from the "Southeast Asia/Pacific" operating segment to the "Americas/Pacific" operating segment. Consolidated financial information is not affected.

Profitability by segment as reported under US GAAP is driven primarily by the Company's transfer pricing policies. Segment contribution, which is the Company's segment profitability metric presented in the table below, excludes certain intercompany charges, specifically royalties, license fees, transfer pricing, discrete charges and other miscellaneous items. These charges have been included in Corporate and other expenses. Corporate and other expenses also include costs related to the Company's executive and administrative offices, information technology, research and development, and marketing and supply chain functions not recorded at the segment level.

The accounting policies of the segments are the same as those described in Note 1 – The Company. The Company evaluates the performance of its segments based on revenue and segment contribution. Each segment records direct expenses related to its employees and its operations.

Summarized financial information for the Company's reportable segments is shown in the following tables. Asset information is not reviewed or included with the Company's internal management reporting. Therefore, the Company has not disclosed asset information for each reportable segment.

Revenue by Segment

(U.S. dollars in thousands)	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
Mainland China	\$245,256	\$172,098	\$442,787	\$322,102
Americas/Pacific	103,990	82,997	196,279	154,422
South Korea	91,624	86,917	180,554	169,388
Southeast Asia	79,223	60,545	150,083	123,570
Japan	64,113	64,796	127,337	125,952
Hong Kong/Taiwan	52,206	43,071	93,198	79,019
EMEA	44,010	38,188	88,991	72,252
Other	23,768	1,489	41,180	2,495
Total	\$704,190	\$550,101	\$1,320,409	\$1,049,200

NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

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## Segment Contribution

(U.S. dollars in thousands)	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
Mainland China	\$73,899	\$52,283	\$118,716	\$87,710
Americas/Pacific	17,068	12,718	26,240	23,777
South Korea	24,880	22,278	51,081	46,790
Southeast Asia	20,639	13,367	37,041	26,384
Japan	13,377	10,922	26,615	23,348
Hong Kong/Taiwan	7,835	7,766	15,681	12,849
EMEA	3,069	3,617	7,823	5,408
Total segment contribution	160,767	122,951	283,197	226,266
Corporate and other	(78,003 )	(58,212 )	(141,443 )	(115,265 )
Operating income	82,764	64,739	141,754	111,001
Other income (expense)	(11,165 )	(2,731 )	(9,958 )	(7,298 )
Income before provision for income taxes	\$71,599	\$62,008	\$131,796	\$103,703

## Depreciation and Amortization

(U.S. dollars in thousands)	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
Mainland China	\$3,444	\$3,681	\$6,931	\$7,652
Americas/Pacific	279	484	493	1,050
South Korea	1,576	1,654	3,243	3,286
Southeast Asia	564	550	1,123	1,077
Japan	900	899	1,815	1,779
Hong Kong/Taiwan	321	344	644	646
EMEA	175	322	351	594
Other	13,976	9,521	25,542	18,996
Total	\$21,235	\$17,455	\$40,142	\$35,080

## Capital Expenditures

(U.S. dollars in thousands)	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
Mainland China	\$1,029	\$760	\$2,898	\$1,663



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Americas/Pacific	240	327	429	561
South Korea	44	16	44	464
Southeast Asia	144	333	195	533
Japan	72	21	383	97
Hong Kong/Taiwan	116	511	598	1,117
EMEA	42	118	77	311
Other	14,090	9,737	23,805	23,005
Total	\$15,777	\$11,823	\$28,429	\$27,751

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NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

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### Revenue by Major Market

A major market is defined as one with total revenue greater than 10% of consolidated total revenue. Based on this criteria, the Company has identified three major markets: Mainland China, South Korea and Japan. There are approximately 50 other markets, each of which individually is less than 10%. No single customer accounted for 10% or more of net sales for the periods presented. Sales are recorded in the jurisdiction in which the transactions occurred.

### Revenue by Product Line

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Nu Skin	\$466,462	\$345,287	\$852,912	\$647,160
Pharmanex	212,998	202,912	425,897	399,015
Other	24,730	1,902	41,600	3,025
Totals	\$704,190	\$550,101	\$1,320,409	\$1,049,200

### Long-Lived Assets by Major Market

A major market is defined as a market with long-lived assets greater than 10% of consolidated long-lived assets and also includes the Company's country of domicile (the U.S.). Long-lived assets in Mainland China consist primarily of property, plant and equipment related to manufacturing, distribution facilities and the Mainland China headquarters. Long-lived assets in the U.S. consist primarily of property, plant and equipment, including the Company's corporate offices and distribution facilities. Long-lived assets by major markets are set forth below for the periods ended June 30, 2018 and December 31, 2017 (U.S. dollars in thousands):

	June 30,	December
	2018	31, 2017
United States	\$357,043	\$302,884
Mainland China	89,529	97,046
South Korea	37,462	42,211
Japan	8,122	9,342
All others	11,296	13,104
Total	\$503,452	\$464,587

## 7. GOODWILL

During the first quarter of 2017, the Company realigned its operational segments and reporting structure to reflect how the business will be managed going forward. As part of this realignment, the Company divided its single operating segment into seven geographical reporting segments. The Company's reporting units for goodwill are its operating segments, which are also its reportable segments. As a result of the segment changes, the historical goodwill of \$115.0

million was allocated to the seven reportable segments.

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NU SKIN ENTERPRISES, INC.  
Notes to Consolidated Financial Statements

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The following table presents goodwill allocated to the Company's reportable segments for the periods ended June 30, 2018 and December 31, 2017 (U.S. dollars in thousands):

	June 30, 2018	December 31, 2017
Mainland China	\$32,179	\$32,179
Americas/Pacific	9,449	9,449
South Korea	29,261	29,261
Southeast Asia	18,537	18,537
Japan	16,019	16,019
Hong Kong/Taiwan	6,634	6,634
EMEA	2,875	2,875
Other	72,469	—
Total	\$187,423	\$114,954

The Other category represents goodwill allocated to the companies acquired in the first quarter of 2018 (see Note 15 – Acquisitions).

## 8. INVENTORY

Inventories consist of the following (U.S. dollars in thousands):

	June 30, 2018	December 31, 2017
Raw materials	\$99,984	\$87,683
Finished goods	183,746	165,771
	\$283,730	\$253,454

The total inventory balance as of June 30, 2018 includes \$23.1 million of inventory held by the companies acquired in the first quarter of 2018 (see Note 15 - Acquisitions).

## 9. INCOME TAXES

Provision for income taxes for the three- and six-month periods of 2018 was \$20.6 million and \$45.3 million, compared to \$20.0 million and \$34.2 million for the prior-year periods. The effective tax rates for the three- and six-month periods were 28.8% and 34.4% of pre-tax income compared to 32.2% and 33.0% in the prior-year periods. The decrease in the effective tax rate in the second quarter of 2018 reflects a benefit due to permanent reinvestment of \$60.0 million in Mainland China as well as reduced withholding tax liabilities related to foreign currency exchange rates.

The Company accounts for income taxes in accordance with the Income Taxes Topic of the Financial Accounting Standards Codification. These standards establish financial accounting and reporting standards for the effects of

income taxes that result from an enterprise's activities during the current and preceding years. The Company takes an asset and liability approach for financial accounting and reporting of income taxes. The Company pays income taxes in many foreign jurisdictions based on the profits realized in those jurisdictions, which can be significantly impacted by terms of intercompany transactions between the Company and its foreign affiliates. Deferred tax assets and liabilities are created in this process. The Company has netted these deferred tax assets and deferred tax liabilities by jurisdiction. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be ultimately realized. The Company had net deferred tax assets of \$1.4 million and net deferred tax liabilities of \$2.9 million as of June 30, 2018 and December 31, 2017, respectively.

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In accordance with ASU 2018-05 and SAB 118, the Company recognized the provisional tax impacts related to the re-measurement of our deferred income tax assets and liabilities and the one-time, mandatory transition tax on deemed repatriation during the year ended December 31, 2017. As of June 30, 2018, the Company has not made any additional measurement-period adjustments related to these items. Such adjustments may be necessary in future periods due to, among other things, the significant complexity of the Act and anticipated additional regulatory guidance that may be issued by the Internal Revenue Service ("IRS"), changes in analysis, interpretations and assumptions the Company has made and actions the Company may take as a result of the Act. The Company is continuing to gather information to assess the application of the Act and expects to complete its analysis with the filing of its 2017 income tax returns during the third quarter of 2018.

The Company files income tax returns in the U.S. federal jurisdiction, and in various state and foreign jurisdictions. The Company is no longer subject to tax examinations from the IRS for all years for which tax returns have been filed before 2011. With a few exceptions, the Company is no longer subject to state and local income tax examination by tax authorities for the years before 2011. In 2009, the Company entered into a voluntary program with the IRS called Compliance Assurance Process ("CAP"). The objective of CAP is to contemporaneously work with the IRS to achieve federal tax compliance and resolve all or most of the issues prior to filing of the tax return. The Company has elected to participate in the CAP program for 2018 and may elect to continue participating in CAP for future tax years; the Company may withdraw from the program at any time. In major foreign jurisdictions, the Company is generally no longer subject to income tax examinations for years before 2011. However, statutes in certain countries may be as long as ten years. Along with the IRS examination of 2011, the Company is currently under examination in certain foreign jurisdictions; however, the outcomes of those reviews are not yet determinable. In the first quarter of 2018 there was a discrete income tax charge of \$5.8 million booked. The charge was primarily related to additional reserves as the result of an Income Tax audit in Indonesia. The Company's unrecognized tax benefits relate to multiple jurisdictions. Due to potential increases in unrecognized tax benefits from the multiple jurisdictions in which the Company operates, as well as the expiration of various statutes of limitation, it is reasonably possible that the Company's gross unrecognized tax benefits, net of foreign currency adjustments, may decrease within the next 12 months by a range of approximately \$1 to \$2 million.

#### 10. COMMITMENTS AND CONTINGENCIES

The Company is subject to government regulations pertaining to product formulation, labeling and packaging, product claims and advertising, and the Company's direct selling system. The Company is also subject to the jurisdiction of numerous foreign tax and customs authorities. Any assertions or determination that either the Company or the Company's sales force is not in compliance with existing statutes, laws, rules or regulations could have a material adverse effect on the Company's operations. In addition, in any country or jurisdiction, the adoption of new statutes, laws, rules or regulations or changes in the interpretation of existing statutes, laws, rules or regulations could have a material adverse effect on the Company and its operations. No assurance can be given that the Company's compliance with applicable statutes, laws, rules and regulations will not be challenged by foreign authorities or that such challenges will not have a material adverse effect on the Company's financial position, results of operations or cash flows. The Company and its Subsidiaries are defendants in litigation, investigations and other proceedings involving various matters. In the opinion of the Company's management, based upon advice of its counsel handling such litigation, investigations and other proceedings, adverse outcomes, if any, are not currently expected to result in a material effect on the Company's consolidated financial condition, results of operations or cash flows.

The Company is subject to regular audits by federal, state and foreign tax authorities. These audits may result in additional tax liabilities. The Company believes it has appropriately provided for income taxes for all years. Several

factors drive the calculation of its tax reserves. Some of these factors include: (i) the expiration of various statutes of limitations; (ii) changes in tax law and regulations; (iii) issuance of tax rulings; and (iv) settlements with tax authorities. Changes in any of these factors may result in adjustments to the Company's reserves, which would impact its reported financial results.

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## 11. DEBT

### Existing Credit Agreement

On October 9, 2014, the Company entered into a Credit Agreement (the "Existing Credit Agreement") with various financial institutions, and Bank of America, N.A. as administrative agent. The Existing Credit Agreement provided for a \$127.5 million term loan facility, a 6.6 billion Japanese yen term loan facility and a \$187.5 million revolving credit facility, each with a term of five years. On October 10, 2014, the Company drew the full amount of the term loan facilities. On April 18, 2018, the Company repaid the full balance that was outstanding under the Existing Credit Agreement. As of June 30, 2018 and December 31, 2017, the Company had an outstanding balance of zero and \$47.5 million, respectively, on the revolving credit facility. The Existing Credit Agreement required that the Company maintain a consolidated leverage ratio not exceeding 2.25 to 1.00 and a consolidated interest coverage ratio of no less than 3.00 to 1.00.

### New Credit Agreement

On April 18, 2018, the Company entered into a Credit Agreement (the "New Credit Agreement") with several financial institutions as lenders and Bank of America, N.A., as administrative agent. The New Credit Agreement provides for a \$400 million term loan facility and a \$350 million revolving credit facility, each with a term of five years. Concurrently with the closing of the New Credit Agreement, the Company drew the full amount of the term loan facility and \$78.5 million of the revolving facility, each of which initially bear interest at the London Interbank Offered Rate ("LIBOR"), plus 2.25%. The interest rate applicable to the facilities is subject to adjustment based on the Company's consolidated leverage ratio. The term loan facility will amortize in quarterly installments in amounts resulting in an annual amortization of 5.0% during the first and second years, 7.5% during the third and fourth years and 10.0% during the fifth year after the closing date of the New Credit Agreement, with the remainder payable at final maturity. The New Credit Agreement requires the Company to maintain a consolidated leverage ratio not exceeding 2.25 to 1.00 and a consolidated interest coverage ratio of no less than 3.00 to 1.00.

### Convertible Note

On June 16, 2016, the Company issued \$210.0 million of convertible senior notes (the "Convertible Notes") in a private offering to a Chinese investor (the "Holder"). The Convertible Notes were senior unsecured obligations which ranked equal in right of payment to all senior unsecured indebtedness of the Company and ranked senior in right of payment to any indebtedness that was contractually subordinated to the Convertible Notes. Interest on the Convertible Notes was payable semiannually in arrears on June 15 and December 15 of each year at a rate of 4.75% per annum.

The Convertible Notes had a stated maturity date of June 15, 2020, unless repurchased or converted prior to maturity. Prior to the stated maturity date, the Company could, at its option, redeem all or part of the Convertible Notes at a price equal to 100% of the principal amount thereof, plus accrued and unpaid interest, if any, provided that its common stock share price was equal to or exceeded 180% of the applicable conversion price for 20 or more trading days (including the final three trading days) in the 30 consecutive trading days prior to the Company's exercise of such redemption right. The Holder of the Convertible Notes could, at its option, cause the Company to repurchase all of such Holder's Convertible Notes or any portion thereof that was equal to \$1,000 in principal amount or multiples of \$1,000 upon a change in control or a termination of trading of the Company's common stock, as those terms were defined in the indenture governing the Convertible Notes. In addition, each holder of the Convertible Notes had the right, at such holder's option, to convert all or any portion thereof that is equal to \$1,000 in principal amount or multiples of \$1,000 at any time beginning six calendar months following June 16, 2016, at the then-applicable



conversion rate. Upon conversion by the Holder, the Convertible Notes would be settled in cash with respect to principal and any accrued and unpaid interest to such date and in the Company's common shares with respect to any additional amounts, based on the applicable conversion rate at such time. The Convertible Notes had an initial conversion rate of 21.5054 common shares per \$1,000 principal amount of the Convertible Notes (which is equal to an initial conversion price of approximately \$46.50 per common share). Throughout the term of the Convertible Notes, the conversion rate could be adjusted upon the occurrence of certain specified events.

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Notes to Consolidated Financial Statements

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Of the \$210.0 million in proceeds received from the issuance of the Convertible Notes, \$199.1 million was originally allocated to long-term debt (the "Liability Component") and \$10.9 million was allocated to additional paid-in capital (the "Equity Component") within the Company's consolidated balance sheet. The Liability Component was calculated by measuring the fair value of a similar debt instrument that does not have an associated conversion feature. The amount allocated to the Equity Component, representing the conversion option, was calculated by deducting the fair value of the Liability Component from the par value of the Convertible Notes. The Company determined that the conversion option did not require separate accounting treatment as a derivative instrument because it was both indexed to the Company's own stock and would be classified in stockholders' equity if freestanding. The Equity Component would not be remeasured as long as it continued to meet the conditions for equity classification. The excess of the principal amount of the Liability Component over its carrying amount (the "Debt Discount") was amortized to interest expense over the term of the Convertible Notes. As a result, the Liability Component was accreted up to the Convertible Notes' \$210.0 million face value, resulting in additional non-cash interest expense being recognized within the Company's consolidated statement of income. The effective interest rate on the Convertible Notes was approximately 7.1% per annum.

The Company incurred approximately \$6.6 million of issuance costs related to the issuance of the Convertible Notes. Of the \$6.6 million in issuance costs incurred, \$6.3 million and \$0.3 million were recorded to deferred financing cost and additional paid-in capital, respectively, in proportion to the allocation of the proceeds of the Convertible Notes. The \$6.3 million recorded to deferred financing cost on the Company's consolidated balance sheet as a reduction of long-term debt was amortized over the contractual term of the Convertible Notes using the effective interest method. During the first quarter of 2018 the issuance costs were expensed due to the conversion of the Notes. During the three- and six-months ended June 30, 2018, the Company recognized \$0.5 million and \$3.5 million, respectively in interest expense related to the Convertible Notes, which included \$0.5 million and \$3.0 million, respectively of contractual interest and zero and \$0.5 million, respectively in amortization of debt issuance costs and in amortization of the Debt Discount prior to the conversion of the Notes.

During the first quarter of 2018, the Holder elected to convert the Convertible Notes pursuant to their terms in the indenture. The Company satisfied the equity portion of its conversion obligation on February 28, 2018 by issuing 1,535,652 shares of the Company's Class A Common Stock to the Holder and, on April 18, 2018, satisfied and discharged its obligations under the Convertible Notes and the indenture governing the Convertible Notes by paying the Holder \$213.4 million which included \$3.4 million of accrued interest from December 15, 2017 through April 17, 2018. The early conversion of the notes resulted in a \$7.2 million charge to other income (expense) during the first quarter of 2018 for a loss on extinguishment of debt.

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The following table summarizes the Company's debt facilities as of June 30, 2018 and December 31, 2017:

Facility or Arrangement	Original Principal Amount	Balance as of June 30, 2018 <sup>(1)(2)</sup>	Balance as of December 31, 2017 <sup>(2)</sup>	Interest Rate	Repayment terms
October 2014 Credit Agreement term loan facility:					
U.S. dollar denominated:	\$127.5 million	—	\$94.8 million	Variable 30 day: 4.627%	Principal amount was paid in full during April 2018.
Japanese yen denominated:	6.6 billion yen	—	4.9 billion yen (\$43.5 million as of December 31, 2017)	Variable 30 day: 2.7595%	Principal amount was paid in full during April 2018.
October 2014 Credit Agreement revolving credit facility:		—	\$47.5 million	Variable 30 day: 4.594%	Principal amount was paid in full during April 2018 and credit line was closed.
April 2018 Credit Agreement term loan facility:					
U.S. dollar denominated:	\$400.0 million	\$395.0 million	—	Variable 30 day: 4.344%	35% of the principal amount is payable in increasing quarterly installments over a five-year period beginning on June 30, 2018, with the remainder payable at the end of the five-year term.
April 2018 Credit Agreement revolving credit facility:		\$74.5 million	—	Variable 30 day: 4.344%	Revolving line of credit expires April 18, 2023.
Japan subsidiary loan:	2.1 billion yen	0.3 billion yen (\$3.0 million as of June 30, 2018)	0.7 billion yen (\$5.9 million as of December 31, 2017)	0.66%	Payable in semi-annual installments over three years that began on January 31, 2016.
Convertible note	\$210.0 million	—	\$210.0 million	4.75%	Principal amount was paid in full during April 2018.

As of June 30, 2018, the current portion of the Company's debt (i.e. becoming due in the next 12 months) included \$20.0 million of the balance of its U.S. dollar denominated debt under the New Credit Agreement facility and \$3.0 million of the Japan subsidiary loan. The Company has classified the \$74.5 million borrowed under the revolving line of credit as short term because it is the Company's intention to use the line of credit to borrow and pay back funds over short periods of time.

The carrying value of the debt reflects the amounts stated in the above table less debt issuance costs of \$4.5 million as of June 30, 2018 related to the credit agreement; and a debt discount of \$9.1 million and debt issuance costs of \$4.0 million (consisting of \$11.1 million related to the Convertible Note and \$2.0 million related to the credit agreement) as of December 31, 2017, which is not reflected in this table.

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Notes to Consolidated Financial Statements

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## 12. FAIR VALUE

The carrying value of financial instruments including cash and cash equivalents, accounts receivable and accounts payable approximate fair values due to the short-term nature of these instruments. The Company's current investments as of June 30, 2018 include certificates of deposits and pre-refunded municipal bonds that are classified by management as held-to-maturity as the Company had the positive intent and ability to hold to maturity. The carrying value of these current investments approximate fair values due to the short-term nature of these instruments. The Company has classified these instruments as Level 2 in the fair value hierarchy. Fair value estimates are made at a specific point in time, based on relevant market information.

The FASB Codification defines fair value as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. On a quarterly basis, the Company measures at fair value certain financial assets, including cash equivalents. Accounting standards specify a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs have created the following fair-value hierarchy:

Level 1 – quoted prices in active markets for identical assets or liabilities;

Level 2 – inputs, other than the quoted prices in active markets, that are observable either directly or indirectly;

Level 3 – unobservable inputs based on the Company's own assumptions.

Accounting standards permit companies, at their option, to measure certain financial instruments and other eligible items at fair value. The Company has elected not to apply the fair value option to existing eligible items beyond what is required by US GAAP.

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The following tables present the fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis (U.S. dollars in thousands):

	Fair Value at June 30, 2018			
	Level			Total
	Level 1	2	Level 3	
Financial assets (liabilities):				
Cash equivalents and current investments	\$79,249	\$ —	\$ —	\$79,249
Other long-term assets	3,566	—	—	3,566
Forward contracts	—	—	—	—
Life insurance contracts	—	—	38,232	38,232
Total	\$82,815	\$ —	\$38,232	\$121,047

	Fair Value at December 31, 2017			
	Level			Total
	Level 1	2	Level 3	
Financial assets (liabilities):				
Cash equivalents and current investments	\$36,531	\$ —	\$ —	\$36,531
Other long-term assets	3,726	—	—	3,726
Forward contracts	—	158	—	158
Life insurance contracts	—	—	37,737	37,737
Total	\$40,257	\$158	\$37,737	\$78,152

The following table provides a summary of changes in fair value of the Company's Level 3 marketable securities (U.S. dollars in thousands):

#### Life Insurance Contracts

Beginning balance at April 1, 2018	\$38,929
Actual return on plan assets:	
Relating to assets still held at the reporting date	(633 )
Purchases and issuances	—
Sales and settlements	(64 )
Transfers into Level 3	—
Ending balance at June 30, 2018	\$38,232

### 13. ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard was effective for the Company in the first quarter of 2018. As

a result of adopting this new accounting guidance, the Company has changed the method of accounting for its loyalty points program from a cost provision method to a deferred revenue method. The Company adopted the new standard effective January 1, 2018 using the modified retrospective transition method. The cumulative impact of adoption was a \$11.2 million net reduction to beginning retained earnings. See Note 16 – Revenue Recognition.

In February 2016, the FASB issued ASU 2016-02, Leases (Subtopic 842). ASU 2016-02 will require companies to recognize lease assets and lease liabilities on the balance sheet and disclose key information about leasing arrangements. For public companies, this standard is effective for annual reporting periods beginning after December 15, 2018, and early adoption is permitted. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

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In March 2016, the FASB issued ASU 2016-09, Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. The objective of this update was to simplify several aspects of the accounting for employee share-based payment transactions, including accounting for income taxes related to share-based compensation, the related classification in the statement of cash-flows, and accounting for share award forfeitures. This ASU was effective for the Company beginning on January 1, 2017. Prior to January 1, 2017, excess tax benefits were recognized in equity. As permitted, the Company elected to classify excess tax benefits as an operating activity in the Statement of Cash Flows instead of as a financing activity on a prospective basis and did not retroactively adjust prior periods. As also permitted by the new guidance, beginning January 1, 2017 the Company has elected to account for share award forfeitures as they occur. Previously, share-based compensation expense was recorded net of estimated forfeitures. A cumulative adjustment of \$2.8 million was recorded to retained earnings and additional paid-in capital as of January 1, 2017. Prior periods were not retroactively adjusted.

In the second half of 2016, the FASB issued ASU Nos. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, and 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash. The objective of these updates is to reduce the diversity in practice in the classification of certain cash receipts and cash payments, and the presentation of restricted cash within an entity's statement of cash flows, respectively. These ASUs are effective for interim and annual fiscal periods beginning after December 15, 2017. Early adoption is permitted. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business. This guidance revises the definition of a business as it relates to acquisitions, disposals, goodwill impairments and consolidations. This ASU is effective for annual periods beginning after December 15, 2017. Early adoption is permitted. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. This guidance simplifies the required test of goodwill for impairment by eliminating Step 2 from the goodwill impairment test. If a company determines in Step 1 of the goodwill impairment test that the carrying value of a reporting unit is less than the fair value, an impairment in that amount should be recorded to the income statement, rather than proceeding to Step 2. This ASU is effective for interim and annual impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

In December 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. The new standard makes more financial and non-financial hedging strategies eligible for hedge accounting. It also amends the presentation and disclosure requirements and changes how companies assess effectiveness. For public companies, the amendments in this ASU are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted in any interim period. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. This guidance provides an option to reclassify from accumulated other comprehensive income to retained earnings the stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017. This ASU is effective for interim and annual periods beginning



after December 15, 2018. Early adoption is permitted. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

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#### 14. COST OF SALES

The Tokyo District Court and, on appeal in 2017, the Tokyo High Court upheld the Japan customs authorities' customs assessments related to the importation of several of the Company's products into Japan. The Company appealed the High Court's decision to the Japan Supreme Court. In May 2018, the Japan Supreme Court declined to hear the Company's appeal. Accordingly, this matter is now closed.

As previously disclosed, the Company already recorded a charge of \$31.4 million to cost of sales in the first quarter of 2016, when the District Court issued its decision. This charge represents the full amount being disputed. It was a non-cash item because the Company was previously required to pay the assessments.

#### 15. ACQUISITIONS

On January 22, 2018, the Company acquired the remaining 73% ownership in Innuvate Health Sciences, LLC ("Innuvate"), which owns a 92% interest in a nutritional product manufacturer. Prior to this acquisition, the Company owned 27% of Innuvate and accounted for it using the equity method. The remaining 8% ownership in the manufacturer will continue to be held by an unrelated third party. Under the terms of the agreement, the Company paid \$23.5 million in cash and shares of the Company in exchange for the 73% ownership in Innuvate, subject to adjustment for certain closing items. Innuvate is a contract manufacturer that specializes in softgel and hardshell capsule manufacturing.

On February 12, 2018, the Company acquired the remaining 65% ownership in Treviso, LLC ("Treviso"), making Treviso a wholly owned subsidiary of the Company. Treviso is a personal care product manufacturer. Prior to this acquisition, the Company owned 35% of Treviso and accounted for it using the equity method. Under the terms of the purchase agreement, the Company has paid \$83.9 million in cash and shares of the Company in exchange for the 65% ownership in Treviso, subject to adjustment for certain closing items. Treviso is a liquid contract manufacturing laboratory for premium personal care products.

On February 12, 2018, the Company acquired 100% ownership in L&W Holdings, Inc. ("L&W") making L&W a wholly owned subsidiary of the Company. L&W is a packaging supplier company. Under the terms of the purchase agreement, the Company paid \$25.0 million in shares of the Company in exchange for 100% ownership in L&W, subject to adjustment for certain closing items. L&W specializes in the distribution and packaging of products in the cosmetic and nutritional industries.

The following table summarizes the fair value of consideration transferred for the acquisitions disclosed above (in thousands):

	Innuvate	Treviso	L&W Holdings	Total
Total cash consideration	\$ 17,587	\$ 14,648	\$ —	\$ 32,235
Shares issued in conjunction with acquisition	5,863	69,252	25,000	100,115
Total consideration	\$ 23,450	\$ 83,900	\$ 25,000	132,350
Previously held equity interest in equity method Investments <sup>(1)</sup>	8,748	30,281	—	39,029
Total	\$ 32,198	\$ 114,181	\$ 25,000	\$ 171,379

The acquisitions of Innuvate and Treviso are considered step acquisitions, and accordingly, the Company remeasured its pre-existing 27% equity interest in Innuvate and 35% of Treviso immediately prior to completion of the acquisition to its estimated fair value of approximately \$39.0 million. As a result of the remeasurement, the (1) Company recorded a gain of approximately \$13.6 million within other income (expense), during the first quarter of 2018, representing the excess of the approximate \$39.0 million estimated fair value of its pre-existing 27% equity interest in Innuvate and 35% equity interest of Treviso over its transaction date carrying value of approximately \$25.4 million.

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The following table summarizes the fair value of the assets acquired for the acquisitions disclosed above (in thousands):

	Innuvate Life Amount	Treviso Life Amount	L&W Holdings Life Amount
Total current assets	\$6,219	\$19,659	\$7,353
Fixed assets	9,291	33,282	114
Customer list	9 years5,100	9 years16,500	7 years6,500
Order backlog	5 month200	10 month1,700	4 month900
Trademarks	7 years900	6 years1,300	5 years600
Total current liabilities	(3,942 )	(3,740 )	(1,495 )
Other non-current liabilities	—	—	(1,731 )
Total identifiable net assets acquired	17,768	71,701	12,241
Goodwill	17,230	42,480	12,759
Fair value of noncontrolling interest	(2,800 )	—	—
Total consideration and value to be allocated to net assets	\$32,198	\$114,181	\$25,000

Pro forma and historical results of operations for the acquired companies have not been presented because they are not material, either individually or in the aggregate, to the company's consolidated financial statements.

## 16. REVENUE RECOGNITION

### Adoption of ASC Topic 606, "Revenue from Contracts with Customers"

On January 1, 2018, the Company adopted Topic 606 using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting under Topic 605.

The Company recorded a net reduction to opening retained earnings of \$11.2 million, net of tax, as of January 1, 2018 due to the cumulative impact of adopting Topic 606, with the impact primarily related to our loyalty point program deferrals. The impact to revenues as a result of applying Topic 606 for the three- and six-months ended June 30, 2018 was a decrease of \$0.6 million and \$1.2 million, respectively.

### Revenue Recognition

Net sales include products and shipping and handling charges, net of estimates for product returns and any related sales incentives. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring products. All revenue is recognized when we satisfy our performance obligations under the contract. The Company recognizes revenue by transferring the promised products to the customer, with revenue recognized at shipping point, the point in time the customer obtains control of the products. The Company recognizes revenue for shipping and handling charges at the time the products are delivered to or picked up by the customer. The Company

estimates product returns based on historical return rates. The majority of the Company's contracts have a single performance obligation and are short term in nature. Sales taxes and value added taxes in foreign jurisdictions that are collected from customers and remitted to governmental authorities are accounted for on a net basis and therefore are excluded from net sales.

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### Contract Liabilities – Customer Loyalty Programs

Contract liabilities, recorded as deferred revenue within the accrued expenses line in the Condensed Consolidated Balance Sheets, include loyalty point program deferrals with certain customers which are accounted for as a reduction in the transaction price and are generally recognized as points are redeemed for additional products on an annual basis. Significant changes in these contract liability balances were as follows for the six-month period ended June 30 (U.S. dollars in thousands):

	June 30, 2018
Outstanding at beginning of period	\$13,043 <sup>(1)</sup>
Increase (decrease) attributed to:	
Customer loyalty deferrals	3,029
Customer loyalty redemptions/expirations	(1,802)
Outstanding at end of period	\$14,270

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The company recorded customer loyalty points under the cost provision method prior to the adoption of Topic 606. <sup>(1)</sup>The loyalty point liability under the cost provision methodology was \$1.9 million as of December 31, 2017. The Company recorded an additional liability of \$11.2 million due to the cumulative impact of adopting Topic 606.

### Disaggregation of Revenue

Please refer to Note 6 - Segment Information for revenue by segment and product line.

### Arrangements with Multiple Performance Obligations

The Company's contracts with customers may include multiple performance obligations. For such arrangements, the Company allocates revenues to each performance obligation based on its relative standalone selling price. The Company generally determines standalone selling prices based on the prices charged to customers for individual products sales to customers.

### Practical Expedients and Exemptions

The Company generally expenses sales commissions when incurred because the amortization period would have been one year or less. These costs are recorded within selling expenses.

The Company does not disclose the value of unsatisfied performance obligations for contracts with an original expected length of one year or less.



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## 17. SUBSEQUENT EVENTS

During the second quarter of 2018, Argentina was determined to be a highly inflationary economy. Accordingly, the Company will apply highly inflationary accounting beginning July 1, 2018. From that date, the U.S. dollar will be used as the functional currency of the Argentina subsidiary. For the six months ended June 30, 2018, the Argentina subsidiary represented less than 2% of the Company's consolidated net revenues and less than 1% of total assets.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

This quarterly report on Form 10-Q (this "Quarterly Report") contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that represent our current expectations and beliefs. All statements other than statements of historical fact are "forward-looking statements" for purposes of federal and state securities laws and include, but are not limited to, statements of management's expectations regarding our performance, initiatives, strategies, product introductions and offerings, growth, opportunities and risks; statements of projections regarding future sales, expenses, operating results, taxes and duties, capital expenditures, sources and uses of cash, foreign currency fluctuations or devaluations, and other financial items; statements of management's expectations and beliefs regarding our markets; statements regarding the payment of future dividends and stock repurchases; statements regarding the outcome of litigation, audits or investigations; accounting estimates and assumptions; statements of belief; and statements of assumptions underlying any of the foregoing. In some cases, you can identify these statements by forward-looking words such as "believe," "expect," "project," "anticipate," "estimate," "intend," "plan," "targets," "likely," "will," "would," "could," "may," "might," the negative of these words and other similar words. We undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise, except as required by law. We caution and advise readers that these statements are based on assumptions that may not be realized and involve risks and uncertainties that could cause actual results to differ materially from the expectations and beliefs contained herein. For a summary of these risks, see the risk factors included in our Annual Report on Form 10-K for the 2017 fiscal year and in our subsequent reports.

The following Management's Discussion and Analysis should be read in conjunction with our consolidated financial statements and related notes and Management's Discussion and Analysis included in our Annual Report on Form 10-K for the 2017 fiscal year, and our other reports filed with the Securities and Exchange Commission through the date of this report on Form 10-Q.

Overview

Revenue for the three-month period ended June 30, 2018 increased 28% to \$704.2 million, compared to \$550.1 million in the prior-year period, and revenue for the six-month period ended June 30, 2018 increased 26% to \$1.3 billion, compared to \$1.0 billion in the prior-year period. Sales Leaders increased 21% and Customers increased 8% on a year-over-year basis.

The growth in our business reflects success with our growth strategy that focuses on products, programs and platforms. Our ageLOC LumiSpa skin treatment and cleansing device continues to generate strong sales and sales force engagement, particularly in our Mainland China and Southeast Asia segments. We believe that our Velocity enhanced sales compensation program, which we rolled out in North America, Taiwan and our Pacific region before or during the second quarter, also helped drive increases in Customer and Sales Leader activity. Our Sales Leaders also continued to have success with social selling initiatives, particularly in our Americas/Pacific, Southeast Asia and EMEA segments.

Our revenue also benefited 4% from foreign-currency fluctuations in the second quarter of 2018 and 5% in the first half of 2018 compared to the respective prior-year periods. In addition, our revenue benefited 4%, for both the second quarter and the first half of 2018 compared to the respective prior-year periods, from the businesses we acquired during the first quarter of 2018.

Earnings per share for the second quarter of 2018 increased 17% to \$0.90, compared to \$0.77 in the prior-year period. Earnings per share for the first half of 2018 increased 20% to \$1.53, compared to \$1.28 in the prior-year period. These increases primarily reflect the increased revenue in 2018, partially offset by a \$8.4 million foreign-currency charge during the second quarter of 2018. Earnings per share for the first half of 2018 additionally reflect the impact of \$4.7 million of purchase-accounting charges and the following items that occurred during the first quarter of 2018: a \$13.6 million gain from acquisitions of companies in which we held a minority interest, a \$7.2 million charge associated with the conversion of our convertible notes and a \$5.8 million charge related to our income taxes in Indonesia. For more information about these items, see "Segment Results—Other," "Other income (expense), net" and "Provision for income taxes," below.

## Segment Results

We report our business in seven segments to reflect our current management approach. Effective as of the first quarter of 2018, we reorganized the structure of our segments to reflect that our Pacific region, which was previously managed by our Southeast Asia regional management and was included in our South Asia/Pacific operating segment, is now managed by our Americas regional management and is included in our Americas/Pacific operating segment. Segment information for the three- and six-month periods ended June 30, 2017 has been recast to reflect this change. Consolidated financial information was not affected.

The following table sets forth revenue for the three- and six-month periods ended June 30, 2018 and 2017 for each of our reportable segments (U.S. dollars in thousands):

	Three Months Ended June 30,			Constant Currency Change <sup>(1)</sup>	Six Months Ended June 30,			Constant Currency Change <sup>(1)</sup>
	2018	2017	Change		2018	2017	Change	
Mainland China	\$245,256	\$172,098	43%	33%	\$442,787	\$322,102	37%	27%
Americas/Pacific	103,990	82,997	25%	31%	196,279	154,422	27%	31%
South Korea	91,624	86,917	5%	1%	180,554	169,388	7%	1%
Southeast Asia	79,223	60,545	31%	28%	150,083	123,570	21%	18%
Japan	64,113	64,796	(1%)	(3%)	127,337	125,952	1%	(2%)
Hong Kong/ Taiwan	52,206	43,071	21%	21%	93,198	79,019	18%	16%
EMEA	44,010	38,188	15%	7%	88,991	72,252	23%	11%
Other	23,768	1,489	1496%	1496%	41,180	2,495	1551%	1551%
Total	\$704,190	\$550,101	28%	24%	\$1,320,409	\$1,049,200	26%	21%

<sup>(1)</sup> Constant-currency revenue change is a non-GAAP financial measure. See "Non-GAAP Financial Measures," below.

The table below sets forth segment contribution for the three- and six-month periods ended June 30, 2018 and 2017 for each of our reportable segments (U.S. dollars in thousands). Segment contribution excludes certain intercompany charges, specifically royalties, license fees, transfer pricing and other miscellaneous items. We use segment contribution to measure the portion of profitability that the segment managers have the ability to control for their respective segments. For additional information regarding our segments and the calculation of segment contribution, see Note 6 to the consolidated financial statements contained in this report.

	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
Mainland China	\$73,899	\$52,283	\$118,716	\$87,710
Americas/Pacific	17,068	12,718	26,240	23,777
South Korea	24,880	22,278	51,081	46,790
Southeast Asia	20,639	13,367	37,041	26,384
Japan	13,377	10,922	26,615	23,348
Hong Kong/Taiwan	7,835	7,766	15,681	12,849
EMEA	3,069	3,617	7,823	5,408

The following table provides information concerning the number of Customers and Sales Leaders as of June 30, 2018 and 2017. "Customers" are persons who have purchased products directly from the Company during the three months ended as of the date indicated. "Sales Leaders" are independent distributors, and sales employees and independent marketers in Mainland China, who achieve certain qualification requirements.

	As of June 30, 2018		As of June 30, 2017		% Increase (Decrease)	
	Customers	Sales Leaders	Customers	Sales Leaders	Customers	Sales Leaders
Mainland China	209,000	33,400	207,000	22,600	1%	48%
Americas/Pacific	265,000	9,000	230,000	7,800	15%	15%
South Korea	184,000	6,900	188,000	7,700	(2%)	(10%)
Southeast Asia	135,000	7,500	104,000	6,300	30%	19%
Japan	132,000	6,000	134,000	6,400	(1%)	(6%)
Hong Kong/Taiwan	76,000	4,200	68,000	3,900	12%	8%
EMEA	147,000	4,300	129,000	4,200	14%	2%
Total	1,148,000	71,300	1,060,000	58,900	8%	21%

Following is a narrative discussion of our results in each segment, which supplements the tables above.

**Mainland China.** The year-over-year increases in revenue in Mainland China for the three- and six-month periods ended June 30, 2018 primarily reflect continued interest in LumiSpa and strong growth in Sales Leaders as more people were selling our products. The increases also reflect a favorable foreign-currency impact of 10% for both the second quarter and the first half of 2018. The Sales Leader growth is driven by strong interest in our products, particularly LumiSpa, and in the business opportunity we offer.

The year-over-year increase in segment contribution for the second quarter of 2018 primarily reflects higher revenue in 2018; revenue increased 43%, and segment contribution increased proportionately at 41%. The segment's gross margin decreased 2.7 percentage points in the second quarter of 2018 compared to the prior-year period, primarily reflecting sales of LumiSpa in 2018, which has a slightly lower gross margin than other products. The decrease in gross margin was offset primarily by lower selling expenses as a percentage of revenue. A portion of selling expenses includes the salaries and service fees of our sales force in Mainland China, which are fixed for a three-month period of time, until they are adjusted during a quarterly evaluation process. Based on our Mainland China segment's strong performance in the second quarter of 2018, we expect that, following the next evaluation, these salaries and service fees will adjust upward during the third quarter.

The year-over-year increase in segment contribution for the first half of 2018 primarily reflects higher revenue in 2018. It also reflects lower general and administrative expenses as a percentage of revenue in the first quarter of 2018 due to the fixed nature of certain of our general and administrative expenses as revenue increased in the first quarter. These improvements were partially offset by the second quarter's decrease in gross margin.

To date, the recently enacted tariffs and trade dispute between the United States and Mainland China have not materially impacted our business, although we believe it has impacted the foreign currency exchange rates which will have a negative impact on our revenue in Mainland China on a U.S. dollar basis if they do not return to prior levels. In the event the trade disputes between the United States and Mainland China continue or intensify, our business could be negatively impacted in the future. For more information, see Item 1A. Risk Factors—"Recently enacted tariffs, other potential changes to tariff and import/export regulations, and ongoing trade disputes between the United States and other jurisdictions may have a negative effect on global economic conditions and our business, financial results and financial condition."

Americas/Pacific. The year-over-year increases in Sales Leaders and Customers in our Americas/Pacific segment, as well as revenue for both the second quarter and the first half of 2018, reflect success with our growth strategy that focuses on products, programs and platforms. In North America, Sales Leaders had continued success with social-selling initiatives and products that are conducive to social selling, and we had a favorable response to our Velocity sales compensation program enhancements, which we launched in North America during the second quarter. We also believe that Velocity contributed to our continued growth in the Pacific region. In Latin America, we generated strong growth, particularly in Argentina and Chile; the growth in these markets accounted for approximately 44% of the Americas/Pacific segment's \$21 million revenue growth for the second quarter. However, revenue growth in Argentina has begun to flatten on a sequential basis. As discussed in Note 17 to the consolidated financial statements contained in this report, the Argentina economy was recently classified as a highly inflationary economy under U.S. accounting standards, and we will begin to apply highly inflationary accounting treatment in that market in the third quarter of 2018.

The year-over-year increases in segment contribution for both the second quarter and the first half of 2018 primarily reflect higher revenue in 2018, as well as higher gross margin. The increase in gross margin reflects changes in product mix and some increased prices in Argentina to follow inflation in that market. For the first half of 2018, these improvements in revenue and gross margin were partially offset by increased selling expenses as a percentage of revenue in the first quarter of 2018. Our selling expenses are impacted by the number of Sales Leaders qualifying for incentive trips and other promotional incentives and the cost of such trips and incentives, which were higher for the first quarter of 2018 in North America and Latin America on a year-over-year basis.

South Korea. Our business in the South Korea segment continued to be challenged in the second quarter and first half of 2018, with the year-over-year increases in revenue being almost entirely attributable to foreign-currency fluctuations and our Sales Leaders and Customers each decreasing. Although the political environment in South Korea has continued to negatively impact our performance in this market, and online competitive pressures have continued to affect our Customer acquisition, we generated slight sequential improvements in revenue and Customers as compared to the first quarter of 2018.

The year-over-year increases in segment contribution for both the second quarter and the first half of 2018 primarily reflect higher revenue in 2018, as well as slightly lower selling expenses as a percentage of revenue.

Southeast Asia. The year-over-year increases in Sales Leaders and Customers in our Southeast Asia segment, as well as revenue for both the second quarter and the first half of 2018, reflect growth in almost every market within this segment. The growth was primarily driven by successful social selling initiatives, interest in LumiSpa and distributor events during the quarter. In July 2018, we launched Velocity in certain markets of this segment.



The year-over-year increases in segment contribution for both the second quarter and the first half of 2018 primarily reflect higher revenue in 2018, as well as reduced general and administrative expenses as a percentage of revenue due to the fixed nature of certain of our general and administrative expenses as revenue increased. The increase in segment contribution for the second quarter also reflects a 1.4 percentage point improvement in gross margin due to changes in product mix. For the six-month period, the increase in segment contribution also reflects lower selling expenses as a percentage of revenue.

Japan. The year-over-year declines in Sales Leaders and Customers in our Japan segment, as well as constant-currency revenue for both the second quarter and the first half of 2018, continued to reflect a soft direct selling market in Japan, which could be attributable to a challenging regulatory environment and an aging demographic. The 1% year-over-year increase in reported revenue for the first half of 2018 reflects a favorable foreign-currency impact of 3%. In July 2018, we launched Velocity in this segment, with which we are aiming to drive Customer growth.

The year-over-year increases in segment contribution for both the second quarter and the first half of 2018 reflect a reduction in general and administrative expenses due to a sales force convention that was held in Japan in the prior year. The year-over-year increase in segment contribution for the first half of 2018 additionally reflects the positive foreign-currency impact on revenue and a 1.0 percentage point decrease in selling expenses as a percentage of revenue.

EMEA. The year-over-year growth in Sales Leaders and Customers in this segment, as well as revenue for both the second quarter and the first half of 2018, reflects continued success of Sales Leader social selling initiatives, as well as successful product initiatives, including products that are conducive to social selling. The increases in reported revenue of 15% for the second quarter and 23% for the first half also reflect favorable foreign-currency impacts of 8% and 12%, respectively.

Segment contribution for the second quarter of 2018 declined on a year-over-year basis despite increased revenue, primarily due to increased selling expenses as a percentage of revenue. Our selling expenses are impacted by the number of Sales Leaders qualifying for incentive trips and the cost of such trips. The year-over-year increase in segment contribution for the first half of 2018 reflects increased revenue and decreased general and administrative expenses as a percentage of revenue due to the fixed nature of certain of our general and administrative expenses as revenue increased.

Hong Kong/Taiwan. The year-over-year growth in revenue in our Hong Kong/Taiwan segment for both the second quarter and the first half of 2018 reflects strong interest in LumiSpa, which also contributed to Sales Leader and Customer growth. In addition, approximately half of the \$9 million increase in revenue in the second quarter is attributable to ticket sales for a regional convention in Hong Kong. We launched Velocity in Taiwan during the second quarter, which we believe has driven positive Customer acquisition.

The year-over-year increases in segment contribution for both the second quarter and the first half of 2018 primarily reflect higher revenue in 2018, partially offset by increased general and administrative expenses primarily due to the regional convention in Hong Kong.

Other. In addition to our seven segments, the manufacturing and product-packaging companies that we acquired during the first quarter of 2018 generated \$22.7 million of reported revenue in the second quarter and \$39.9 million in the first half of 2018. These companies provide products and services both to our company and to external customers; reported revenue includes only the revenue generated by sales to external customers.

As a result of these acquisitions, we incurred \$3.0 million of expense associated with the amortization of acquired intangible assets under acquisition accounting in the second quarter and \$4.7 million in the first half of 2018. We currently expect that we will continue to incur approximately \$2–3 million of these charges per quarter during 2018.



For information about these acquisitions, see Note 15 to the consolidated financial statements contained in this report.

## Consolidated Results

### Revenue

Revenue for the three-month period ended June 30, 2018 increased 28% to \$704.2 million, compared to \$550.1 million in the prior-year period. Revenue for the six-month period ended June 30, 2018 increased 26% to \$1.3 billion, compared to \$1.0 billion in the prior-year period. For a discussion and analysis of this increase in revenue, see "Overview" and "Segment Results," above.

### Gross profit

Gross profit as a percentage of revenue was 76.1% for the second quarter of 2018 compared to 77.9% for the prior-year period, and 76.2% for the first half of 2018 compared to 77.8% for the prior-year period. These year-over-year decreases were driven by negative impacts of 1.8 percentage points in the second quarter of 2018 and 1.7 percentage points in the first half of 2018 from the businesses we acquired in the first quarter of 2018; as previously disclosed, these businesses have lower gross margins than that of our core business, and therefore, we would expect to report a lower gross margin than we reported prior to the acquisitions. The gross margin of our core business remained relatively even with the prior year, as the decrease in gross margin in our Mainland China segment during the second quarter of 2018 was offset by increases in other markets and by other efficiencies.

### Selling expenses

Selling expenses as a percentage of revenue decreased to 38.7% for the second quarter of 2018 compared to 41.5% for the prior-year period, and they decreased to 40.2% for the first half of 2018 compared to 41.7% for the same period in 2017. The revenue from our acquired companies does not carry significant selling expenses; the impact from the acquisition of these companies lowered selling expenses as a percentage of revenue by 1.3 percentage points in the second quarter and by 1.2 percentage points in the first half. The decrease in selling expenses as a percentage of revenue in the second quarter of 2018 also reflects the fixed nature of a portion of the compensation for our Mainland China sales force, as discussed in the "Mainland China" discussion, above.

### General and administrative expenses

General and administrative expenses increased to \$180.1 million in the second quarter of 2018 and \$333.4 million in the first half of 2018 compared to \$135.5 million and \$268.1 million in the respective prior-year periods, primarily reflecting an increase in labor expenses of \$25.1 million for the second quarter of 2018 and \$38.8 million for the first half of 2018 due to increased employee headcount and the payment of increased employee incentive compensation upon achievement of performance goals. Promotion expenses also increased \$7.3 million in the second quarter of 2018, primarily due to the regional convention in Hong Kong. As a percentage of revenue, general and administrative expenses increased to 25.6% for the second quarter of 2018 from 24.6% for the prior-year period. For the first half 2018, general and administrative expenses as a percentage of revenue decreased to 25.2% compared to the prior-year period at 25.5%.

### Other income (expense), net

Other income (expense), net was \$11.2 million of expense for the second quarter of 2018 compared to \$2.7 million of expense for the prior-year period, and \$10.0 million of expense for the first half of 2018 compared to \$7.3 million of expense for the prior-year period. The increase in expense reflects a foreign-currency loss of \$8.4 million in the second quarter of 2018 resulting from the strengthening of the U.S. dollar against the China yuan and Argentina peso. The increase in expense for the first half additionally reflects a non-cash charge of \$7.2 million in the first quarter of 2018 related to the conversion of our then-outstanding convertible notes, offset by a non-cash gain of \$13.6 million on

our step acquisitions in the first quarter of 2018, as the fair value of our pre-acquisition interests in these companies exceeded the book value at the time of the acquisitions. For more information on these items, see Notes 11 and 15 to the consolidated financial statements contained in this report.

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### Provision for income taxes

Provision for income taxes for the three- and six-month periods ended June 30, 2018 was \$20.6 million and \$45.3 million, compared to \$20.0 million and \$34.2 million for the same periods in 2017. The effective tax rate was 28.8% and 34.4% of pre-tax income during the three- and six-month periods ended June 30, 2018, respectively, compared to 32.2% and 33.0%, respectively, in the prior-year periods. Our tax rates for the three- and six-month periods of 2018 reflect a benefit of 3.8% and 2.0%, respectively, from our decision in the second quarter of 2018 to designate \$60 million of our earnings in Mainland China as permanently reinvested, which allows us to remove a withholding tax liability on those earnings. The rates for the three- and six-month periods of 2018 also reflect a benefit from a reduction of our accrued withholding taxes due to foreign-currency fluctuations. The year-over-year changes in our tax rates also reflect a benefit that was recorded in the prior year due to a new accounting standard for stock-based compensation in 2017.

In addition to the foregoing factors, our tax rate for the first half of 2018 also reflects the impact of two items that occurred during the first quarter of 2018: an increase in our income tax reserves following an assessment we received from the Indonesia tax authorities during the first quarter of 2018, and a benefit from a deduction in Japan related to Japan customs assessments that were affirmed by the Tokyo District Court in 2011; in the first quarter of 2018, the Japan and U.S. tax authorities reached resolution as to the amount that would be deductible in each jurisdiction.

### Net income

As a result of the foregoing factors, net income for the second quarter of 2018 was \$51.0 million compared to \$42.0 million in the prior-year period. Net income for the first half of 2018 was \$86.5 million, compared to \$69.5 million for the first half of 2017.

### Liquidity and Capital Resources

Historically, our principal uses of cash have included operating expenses (particularly selling expenses) and working capital (principally inventory purchases), as well as capital expenditures, stock repurchases, dividends, debt repayment and the development of operations in new markets. We have at times incurred long-term debt, or drawn on our revolving line of credit, to fund strategic transactions and stock repurchases. We typically generate positive cash flow from operations due to favorable margins and have generally relied on cash from operations to fund operating activities. In the first half of 2018, we generated \$51.9 million in cash from operations compared to generating \$84.0 million in cash from operations during the prior-year period. This decrease in cash flow from operations reflects (1) the payment of significant accruals as of the end of 2017, particularly commissions based on the initial LumiSpa offerings in the fourth quarter of 2017 and taxes; and (2) payments to build up inventory for our increased sales, including of LumiSpa, in 2018.

As of June 30, 2018, working capital was \$368.0 million, compared to \$330.4 million as of December 31, 2017. Cash and cash equivalents, including current investments, as of June 30, 2018 and December 31, 2017 were \$410.2 million and \$438.2 million, respectively.

Capital expenditures. Capital expenditures in the first half of 2018 were \$28.4 million. Our 2018 capital expenditures include the following:

• the expansion and upgrade of facilities in our various markets; and

• purchases and expenditures for computer systems and equipment, software and application development, including for digital experience, social selling and technology modernization initiatives.



We estimate that capital expenditures for the uses listed above will total approximately \$45 million for the remainder of 2018. In addition, we are also in the planning phase for a new manufacturing plant in Mainland China. Although we are currently in the process of establishing a budget for this plant, we currently believe our 2018 expenditures will be approximately \$15 million to \$20 million. This amount could be lower if there is a delay in obtaining the necessary governmental approvals for the project.

Conversion and satisfaction of convertible notes. In June 2016, we issued \$210.0 million principal amount of convertible 4.75% senior notes due 2020 (the "Convertible Notes") to Ping An ZQ China Growth Opportunity Limited ("Ping An ZQ") at face value. During the first quarter of 2018, Ping An ZQ elected to convert the Convertible Notes pursuant to their terms. In connection with such conversion and pursuant to the terms of the indenture governing the Convertible Notes, we became obligated to deliver shares of Class A common stock and cash to Ping An ZQ. We satisfied our obligation to deliver shares of Class A common stock to Ping An ZQ during the first quarter of 2018 and, on April 18, 2018, satisfied our obligations under the Convertible Notes by paying Ping An ZQ \$213.4 million.

New credit agreement. On April 18, 2018, we entered into a Credit Agreement (the "New Credit Agreement") with several financial institutions as lenders and Bank of America, N.A., as administrative agent. The New Credit Agreement provides for a \$400 million term loan facility and a \$350 million revolving credit facility, each with a term of five years. Concurrently with the closing of the New Credit Agreement, we drew the full amount of the term loan facility and \$78.5 million of the revolving facility, each of which initially bear interest at the London Interbank Offered Rate ("LIBOR") plus 2.25%. We used the proceeds of the term loan and the draw on the revolving facility to pay off the Existing Credit Agreement, as defined below, and the outstanding balance on the Convertible Notes. The interest rate applicable to the facilities is subject to adjustment based on our consolidated leverage ratio. The term loan facility will amortize in quarterly installments in amounts resulting in an annual amortization of 5.0% during the first and second years, 7.5% during the third and fourth years and 10.0% during the fifth year after the closing date of the New Credit Agreement, with the remainder payable at final maturity. The New Credit Agreement requires us to maintain a consolidated leverage ratio not exceeding 2.25 to 1.00 and a consolidated interest coverage ratio of no less than 3.00 to 1.00. We are currently in compliance with these debt covenants.

Modification of previous credit agreement. On April 18, 2018, we repaid debt that was outstanding under our credit agreement, dated as of October 9, 2014, with several financial institutions as lenders and Bank of America, N.A., as administrative agent (the "Existing Credit Agreement"). We had indebtedness of \$257.6 million in principal amount outstanding under the Existing Credit Agreement as of both March 31, 2018 and April 18, 2018. See Note 11 to the consolidated financial statements contained in this report for further information regarding the New Credit Agreement, Convertible Notes and other debt.

Stock repurchase plan. In 2015, our board of directors approved a stock repurchase plan authorizing us to repurchase up to \$500 million of our outstanding shares of Class A common stock on the open market or in private transactions. During the first half of 2018, we repurchased approximately 0.5 million shares of Class A common stock under this plan for \$35.8 million. At June 30, 2018, \$92.2 million was available for repurchases under the 2015 stock repurchase plan. In July 2018, our board terminated the 2015 stock repurchase plan and approved a new repurchase plan with an initial authorization amount of \$500 million. Our stock repurchases are used primarily to offset dilution from our equity incentive plans and for strategic initiatives.

Dividends. In February and April 2018, our board of directors declared a quarterly cash dividend of \$0.365 per share. These quarterly cash dividends of \$19.8 million and \$20.3 were paid March 14, 2018 and June 13, 2018 to stockholders of record on February 26, 2018 and May 25, 2018. In July 2018, our board of directors declared a quarterly cash dividend of \$0.365 per share to be paid on September 12, 2018 to stockholders of record on August 31, 2018. Currently, we anticipate that our board of directors will continue to declare quarterly cash dividends and that the cash flows from operations will be sufficient to fund our future dividend payments. However, the continued declaration of dividends is subject to the discretion of our board of directors and will depend upon various factors,

including our net earnings, financial condition, cash requirements, future prospects and other relevant factors.

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Cash from foreign subsidiaries. As of June 30, 2018 and December 31, 2017, we held \$410.2 million and \$438.2 million, respectively, in cash and cash equivalents, including current investments. These amounts include \$334.2 million and \$413.8 million as of June 30, 2018 and December 31, 2017, respectively, held in our operations outside of the U.S. Substantially all of our non-U.S. cash and cash equivalents are readily convertible into U.S. dollars or other currencies, subject to procedural or other requirements in certain markets, as well as an indefinite-reinvestment designation, as described below.

We typically fund the cash requirements of our operations in the U.S. through intercompany dividends and intercompany charges for products, use of intangible property, and corporate services. Some markets impose government-approval or other requirements for the repatriation of dividends. For example, in Mainland China, we are unable to repatriate cash from current operations in the form of dividends until we file the necessary statutory financial statements for the relevant period. As of June 30, 2018, we had \$104.7 million in cash denominated in Chinese RMB. We also have intercompany loan arrangements with some of our markets, including Mainland China, that allow us to access available cash, subject to certain limits in Mainland China and other jurisdictions. We also have drawn on our revolving line of credit to address cash needs until we can repatriate cash from Mainland China or other markets, and we may continue to do so. Except for \$60 million of earnings in Mainland China that we designated as indefinitely reinvested during the second quarter of 2018, we currently plan to repatriate undistributed earnings from our non-U.S. operations as necessary, considering the cash needs of our non-U.S. operations and the cash needs of our U.S. operations for dividends, stock repurchases, capital investments, debt repayment and strategic transactions. Repatriation of non-U.S. earnings is subject to withholding taxes in certain foreign jurisdictions. Accordingly, we have accrued the necessary withholding taxes related to the non-U.S. earnings.

We currently believe that existing cash balances, future cash flows from operations and existing lines of credit will be adequate to fund our cash needs on both a short- and long-term basis. The majority of our historical expenses have been variable in nature, and as such, a potential reduction in the level of revenue would reduce our cash flow needs. In the event that our current cash balances, future cash flow from operations and current lines of credit are not sufficient to meet our obligations or strategic needs, we would consider raising additional funds in the debt or equity markets or restructuring our current debt obligations. Additionally, we would consider realigning our strategic plans, including a reduction in capital spending, stock repurchases or dividend payments.

#### Contingent Liabilities

Please refer to Note 10 to the consolidated financial statements contained in this report for information regarding our contingent liabilities.

#### Critical Accounting Policies

There were no significant changes in our critical accounting policies during the second quarter of 2018.

#### Seasonality and Cyclical

In addition to general economic factors, we are impacted by seasonal factors and trends such as major cultural events and vacation patterns. For example, most Asian markets celebrate their respective local New Year in the first quarter, which generally has a negative impact on that quarter. We believe that direct selling is also generally negatively impacted during the third quarter, when many individuals, including our sales force, traditionally take vacations.



Prior to making a product generally available for purchase, we often do one or more introductory offerings of the product, such as a preview of the product to our Sales Leaders, a limited-time offer, or other product introduction or promotion. These offerings may generate significant activity and a high level of purchasing, which can result in a higher-than-normal increase in revenue, Sales Leaders and/or Customers during the quarter and can skew year-over-year and sequential comparisons.

#### Currency Risk and Exchange Rate Information

A majority of our revenue and many of our expenses are recognized outside of the United States, except for inventory purchases, a significant portion of which are primarily transacted in U.S. dollars from vendors in the United States. The local currency of each of our Subsidiaries' primary markets is considered the functional currency with the exception of our Asia product-distribution subsidiary in Singapore and, beginning in the third quarter of 2018, our subsidiary in Argentina due to Argentina being designated as a highly inflationary economy under U.S. accounting standards. All revenue and expenses are translated at weighted-average exchange rates for the periods reported. Therefore, our reported revenue and earnings will be positively impacted by a weakening of the U.S. dollar and will be negatively impacted by a strengthening of the U.S. dollar. These impacts may be significant because a large portion of our business is derived from outside of the United States. Given the uncertainty of exchange rate fluctuations, it is difficult to predict the effect of these fluctuations on our future business, product pricing and results of operations or financial condition.

We may seek to reduce our exposure to fluctuations in foreign currency exchange rates through the use of foreign currency exchange contracts and through intercompany loans of foreign currency. We do not use derivative financial instruments for trading or speculative purposes. We regularly monitor our foreign currency risks and periodically take measures to reduce the impact of foreign exchange fluctuations on our operating results. As of June 30, 2018 and 2017, we did not hold non-designated mark-to-market forward derivative contracts to hedge foreign denominated intercompany positions or third party foreign debt. As of June 30, 2018 we did not hold any forward contracts designated as foreign currency cash flow hedges, compared to 2.2 billion Japanese yen and 1.0 million Euros (\$19.6 million and \$1.1 million, respectively) as of June 30, 2017, to hedge forecasted foreign-currency-denominated intercompany transactions. We continue to evaluate our foreign currency hedging policy.

#### Non-GAAP Financial Measures

Constant-currency revenue growth is a non-GAAP financial measure that removes the impact of fluctuations in foreign-currency exchange rates, thereby facilitating period-to-period comparisons of the company's performance. It is calculated by translating the current period's revenue at the same average exchange rates in effect during the applicable prior-year period and then comparing this amount to the prior-year period's revenue.

#### Available Information

Our website address is [www.nuskin.com](http://www.nuskin.com). We make available, free of charge on the Investor Relations portion of our website, [ir.nuskin.com](http://ir.nuskin.com), our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission.

We also use the Investor Relations portion of our website, [ir.nuskin.com](http://ir.nuskin.com), as a channel of distribution of additional Company information that may be deemed material. Accordingly, investors should monitor this channel, in addition to following our press releases, Securities and Exchange Commission filings and public conference calls and webcasts. The contents of our website shall not be deemed to be incorporated herein by reference.



### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information required by Item 3 of Part I of Form 10-Q is incorporated herein by reference from the section entitled "Currency Risk and Exchange Rate Information" in "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" of Part I and also from Note 4 to the consolidated financial statements contained in this report.

### ITEM 4. CONTROLS AND PROCEDURES

#### Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, under the supervision and with the participation of our management, including our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Based on that evaluation, our CEO and our CFO concluded that our disclosure controls and procedures were effective as of June 30, 2018.

#### Changes in Internal Controls Over Financial Reporting.

We made no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the fiscal quarter ended June 30, 2018 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

The following information supplements and amends our discussions set forth under "Legal Proceedings" in our Annual Report on Form 10-K for the 2017 fiscal year and our Quarterly Report on Form 10-Q for the first quarter of 2018. Except as discussed below, there have been no material developments concerning the matters discussed in those reports.

As previously disclosed, the Tokyo District Court and, on appeal in 2017, the Tokyo High Court upheld the Japan customs authorities' customs assessments related to the importation of several of our products into Japan. We appealed the High Court's decision to the Japan Supreme Court. In May 2018, the Japan Supreme Court declined to hear our appeal. Accordingly, this matter is now closed. We already recorded a charge of \$31.4 million to cost of sales in the first quarter of 2016, when the District Court issued its decision. This charge represents the full amount being disputed. It was a non-cash item because we were previously required to pay the assessments.

Please refer to Notes 10 and 14 to the consolidated financial statements contained in this report and to our discussions set forth under "Legal Proceedings" in our Annual Report on Form 10-K for the 2017 fiscal year for additional information regarding our legal proceedings.

### ITEM 1A. RISK FACTORS

The information presented below supplements and should be read in conjunction with the detailed discussion of risks associated with our business in our recent SEC filings, including our Annual Report on Form 10-K for the 2017 fiscal year.



Foreign-currency fluctuations and inflation in foreign markets could impact our financial position and results of operations.

In 2017, approximately 90% of our sales occurred in markets outside of the United States in each market's respective local currency. We purchase inventory primarily in the United States in U.S. dollars. In preparing our financial statements, we translate revenue and expenses in our markets outside the United States from their local currencies into U.S. dollars using weighted-average exchange rates. If the U.S. dollar strengthens relative to local currencies, our reported revenue, gross profit and net income will likely be reduced. For example, foreign-currency fluctuations negatively impacted our reported revenue by approximately 8% in 2015 compared to 2014. Foreign-currency fluctuations can also cause losses and gains resulting from translation of foreign-currency-denominated balances on our balance sheet.

In addition, high levels of inflation and currency devaluations in any of our markets could negatively impact our balance sheet and results of operations. Gains and losses resulting from the remeasurement of non-U.S. dollar monetary assets and liabilities of our subsidiaries operating in highly inflationary economies are recorded in our net earnings. For example, during 2014 and 2015, we recorded \$46.3 million and \$10.2 million, respectively, of non-cash foreign-currency charges related to the devaluation of the Venezuela currency after Venezuela was designated as a highly inflationary economy under U.S. generally accepted accounting principles. During the third quarter of 2016, we ceased business operations in Venezuela. Argentina also was recently designated as a highly inflationary economy; accordingly, beginning with the third quarter of 2018, we will apply highly inflationary accounting for our Argentina operations, which could result in additional foreign-currency charges. Other markets, including Ukraine, have experienced weakening currencies, and it is possible that this and other markets may be so designated in the future. Our Venezuela, Argentina and Ukraine subsidiaries' net sales revenue each represented less than 1.5% of consolidated net sales revenue during each of the periods ended December 31, 2015, 2016 and 2017.

Although we may engage in transactions intended to reduce our exposure to foreign-currency fluctuations, there can be no assurance that these transactions will be effective. Complex global political and economic dynamics can affect exchange rate fluctuations. For example, significant foreign-currency fluctuations occurred as a result of the June 2016 referendum in the United Kingdom in which voters approved an exit from the European Union. The recent U.S. Tax Cuts and Jobs Act also could affect foreign-currency fluctuations. In addition, members of the current U.S. presidential administration have expressed antipathy toward some international trade agreements and have suggested the implementation of tariffs, border taxes or other measures that could impact the level of trade between the U.S. and other markets. Any such proposal or measure could impact the value of the U.S. dollar. It is difficult to predict future fluctuations and the effect these fluctuations may have upon future reported results or our overall financial condition.

Recently enacted tariffs, other potential changes to tariff and import/export regulations, and ongoing trade disputes between the United States and other jurisdictions may have a negative effect on global economic conditions and our business, financial results and financial condition.

The United States recently proposed and enacted tariffs on certain items. Further, there have been ongoing discussions and activities regarding changes to other U.S. trade policies and treaties. In response, a number of our markets, including Mainland China, are threatening to impose tariffs on U.S. imports, or have already implemented tariffs on U.S. imports, or to take other measures in response to these U.S. actions. These developments may have a material adverse effect on global economic conditions and the stability of global financial markets, and they may significantly reduce global trade and, in particular, trade between Mainland China and the United States. Any of these factors could depress economic activity, create anti-American consumer sentiment, restrict our access to suppliers or customers and have a material adverse effect on our business, financial condition and results of operations. In addition, any actions by foreign markets to implement further trade policy changes, including limiting foreign investment or trade, increasing regulatory scrutiny or taking other actions which impact U.S. companies' ability to obtain necessary licenses or approvals could negatively impact our business.

These tariffs have just recently been announced and are subject to a number of uncertainties as they are implemented, including future adjustments and changes in the countries excluded from such tariffs. The ultimate reaction of other countries, and the individuals in each of these countries, and the impact of these tariffs or other actions on the United States, Mainland China, the global economy and our business, financial condition and results of operations, cannot be predicted at this time, nor can we predict the impact of any other developments with respect to global trade.

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**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

## Purchases of Equity Securities by the Issuer

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in millions) <sup>(1)</sup>
April 1 – 30, 2018	90,403	\$ 72.72	90,403	\$ 104.1
May 1 – 31, 2018	96,603	76.38	96,603	\$ 96.7
June 1 – 30, 2018	54,740	81.92	54,740	\$ 92.2
Total	241,746	\$ 76.27	241,746	

In October 2015, we announced that our board of directors approved a stock repurchase plan. Under this plan, our board of directors authorized the repurchase of up to \$500.0 million of our outstanding Class A common stock on the open market or in privately negotiated transactions. In July 2018, our board terminated the 2015 stock repurchase plan and approved a new repurchase plan with an initial authorization amount of \$500.0 million.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not Applicable.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

Exhibits

Regulation S-K

Number Description

10.1 Credit Agreement among the Company, various financial institutions, and Bank of America, N.A. as administrative agent, dated as of April 18, 2018 (incorporated by reference to Exhibit 10.1 to the Company's

Current Report on Form 8-K filed April 23, 2018).

31.1 Certification by Ritch N. Wood, Chief Executive Officer, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

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- 31.2 Certification by Mark H. Lawrence, Chief Financial Officer, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
  - 32.1 Certification by Ritch N. Wood, Chief Executive Officer, pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
  - 32.2 Certification by Mark H. Lawrence, Chief Financial Officer, pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INSXBRL Instance Document  
101.SCHXBRL Taxonomy Extension Schema Document  
101.CALXBRL Taxonomy Extension Calculation Linkbase Document  
101.DEF XBRL Taxonomy Extension Definition Linkbase Document  
101.LABXBRL Taxonomy Extension Label Linkbase Document  
101.PREXBRL Taxonomy Extension Presentation Linkbase Document

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

August 2, 2018

NU SKIN ENTERPRISES, INC.

By: /s/ Mark H. Lawrence  
Mark H. Lawrence  
Chief Financial Officer  
(Duly Authorized  
Officer and Principal  
Financial and  
Accounting Officer)