



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

Third Quarter 2020 Earnings Results Conference Call

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CORPORATE PARTICIPANTS

Luis Campos, *Executive Chairman*

Andres Campos, *Chief Executive Officer*

Diana Jones, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Cristina Fernandez, *Telsey Advisory Group*

Eric Beder, *SCC Research*

Jorge Lagunas, *Apalache*

PRESENTATION

Operator

Thank you and welcome to Betterware's Third Quarter Fiscal 2020 Earnings Conference Call.

With me on the call today are Betterware's Executive Chairman, Luis Campos; Chief Executive Officer, Andres Campos; and Chief Financial Officer, Diana Jones.

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

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

Luis Campos

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

I will begin my remarks by providing a summary of our performance for the third quarter. Then Andres will discuss our competitive advantages and the work we have done to increase efficiency and elevate our

operating platform to support the strong growth we see ahead for the Company. Diana will then review our financial results and our updated Fiscal 2020 outlook.

We had an outstanding third quarter that included record sales and EBITDA and significant accomplishments toward our strategy. The momentum we have experienced in our business that has led to consistent sales and EBITDA growth over the past five years accelerated significantly this quarter generating a 199% increase in net sales, bringing to our Company 17,000 new distributors and 400,000 new associates and our growth drove a 234% increase in EBITDA.

Amidst a pandemic backdrop, Betterware successfully capitalized on the market opportunity driven by the increased demand for household and cleaning products and the increased desire for employment in home. We are very proud of our team's ability to adapt, meet the increased demand, and continue to serve our customers in a changing operating environment.

While Betterware has always been a great place to work, the pandemic gave us an even greater opportunity to add to our distributors and associates. Our outreach and the ability to have our associate and distributor networks conduct business digitally from home, fueled a 186% increase in distributors and 179% increase in associates during the quarter. As of quarter end, we had nearly 59,000 distributors and 1.2 million associates, which is the largest number of distributors and associates in the history of Betterware. We are confident in our ability to continue to grow our distributor and associate base and expect our larger and stronger team will help drive our business going forward.

Finally, during the quarter we made continued strides to improve our financial health and positioning. Namely, we reduced our leverage ratio of net debt to Adjusted EBITDA to minus 0.4x from minus 0.1x at the end of the second quarter, and increased our liquidity to Ps. \$1,155 million at quarter end. We continue to be focused on returning value to shareholders, and we again have proposed a dividend that is subject to approval at the next Ordinary General Shareholders' meeting.

In summary, we are very pleased with our ability to support the consumers' growing need for our products during the third quarter. Our strategic priorities, combined with our continued focus on managing expenses and working capital, have us poised to capitalize on the increased demand we are seeing across our business, and we believe we are in an enviable position moving forward.

With strong cash flow and positive business momentum, we have the ability to invest in support of our future growth while maintaining strong financial performance. As Diana will discuss, we expect our strong performance to continue in the final quarter of the year, which is reflected in our updated guidance.

I will now turn the call to Andres, our Chief Executive Officer, who will highlight our progress on our four strategic pillars.

Andres Campos

Thank you, Luis, and good morning to everyone.

Before I review our strategic growth pillars, I would like to commend our team for their unwavering dedication and hard work during this quarter.

We delivered an extremely strong third quarter performance well beyond our expectations that was supported by the efficiency and effectiveness of our robust operating platform. As you would expect, achieving the level of growth we experienced created some short-term impacts to the business in terms of delivery times and freight expense. Importantly, we reacted swiftly to expand our capabilities, with significant increases in our pick and pack lines, operations workforce, forklifts and trucks, as well as an

increased number of trucks moving between our warehouses daily. Our actions enabled us to return to optimal efficiency rates and on time deliveries that were back to pre-COVID levels by quarter end.

Now, I will review our four key strategic growth pillars, which are centered on market penetration, geographic expansion, category expansion, and business intelligence and technology investments. Then I will discuss our web marketing and new campus. These initiatives are expected to support our future growth and increase efficiency.

Starting with market penetration. We saw broad based strength across all categories during the quarter, which was spurred by the increased demand for our household and cleaning products as a result of the COVID-19 pandemic, and also our deliberate actions to drive growth with high impact innovation. This capability sets us apart from peers allowing Betterware to take a leadership position with new product introductions.

Our increased market penetration highlights our deep expertise in this category for which customers have learned to trust us and why we are the number one brand within the category in Mexico. Our constant focus on product innovation allows us to launch more and more successful products every day. This, combined with our unique multi-source design platform, generates more interest with customers, and allows us to continue to differentiate ourselves.

Our second strategic pillar is Geographic Expansion. During next quarter, we will introduce Betterware Guatemala following the successful pilot test. Our sales, EBITDA, distributor, and associate growth in this new market has been consistently growing each month. We are extremely pleased with the momentum of the business and the strong profitability of Guatemala. In fact, EBITDA margin reached 50% in September, demonstrating that we can successfully replicate our business model in other countries. Up until now, our operations in Guatemala have been through a concessionary.

In November, we will have a joint venture with the current concessionary as a minority partner to launch Betterware Guatemala as a subsidiary of Betterware Mexico. We expect its growth to accelerate towards 2022, and we look to expand to other countries in Central America, including Panama and Costa Rica. We are also targeting the expansion of Betterware into South America, specifically Colombia and Peru, in the coming years

Next, Category Expansion. We launched two catalogues during the third quarter, and we introduced 62 new products in these catalogues. Customer response to new categories has been strong.

Our last pillar is Business Intelligence and Technology Investments. We have been developing our Business Intelligence capability for many years, with an increased focus over the last seven years. These capabilities enable us to make smart decisions backed by technology in everything we do.

Regarding web marketing. In addition to showcasing our products, our new website is a tool for our distributors and associates to grow their sales and earnings by continuing to reach additional customers. Our new and improved transactional website, www.betterware.com, will help our distributors and associates reach more customers in two ways.

Number one; Connecting new customers based on location to a distributor or an associate if they don't already have an existing relationship with one. This makes the purchasing transaction easier for the customer and offers increased incentives and economics for the distributor or the associate.

Additionally, the distributors and associates will now be able to share a personal link that will automatically assign to them any purchase completed through their link, again generating increased economics for the distributor and the associates.

Turning to our new campus. The new campus, which is on track to open before year end, will be located in Huaxtla, Jalisco, on the outskirts of Guadalajara, and will become our national distribution center and headquarters, consolidating our operations to one location.

Our recent accelerated growth had us reaching full capacity at our existing facility, while the new facility has 2.5x the storage capacity and 5.3x the assortment capacity of our current locations, which is a significant increase. Some of the operational efficiencies that we expect to obtain from the new campus are consolidation of all our warehousing and distribution processes, optimization of space usage and inventory management efficiency all backed by new technology.

In support of our long-term growth planning, we recently completed a study by Bain & Company that identified opportunities to invest in future growth, improve service levels, and increase our competitive advantages. We are continuing to evaluate which investments make the most sense for the business, and we will continue to keep you posted.

Overall, we are excited about the operational initiatives planned for the remainder of this year and beyond as we continue to build a stronger Betterware positioned for sustained profitable growth. We look forward to updating you on our progress as we focus on building on our success to-date.

I will now turn the call over to Diana to review our third quarter financial results.

Diana Jones

Thank you, Andres. Good morning, everyone. I would like to take this time to review our third quarter 2020 results. I will then share perspectives regarding our outlook for the year.

Please keep in mind that the currency I will refer to when reviewing our results and guidance is the Mexican Peso, which is our functional and reporting currency.

Given the relevance of this matter, I would like to provide clarity regarding the accounting impacts of the warrants we inherited as a result of the merger with DD3 to our consolidated financial statements as of and for the nine-months ended September 30, 2020.

As reported in yesterday's 6-K and earnings release, our net income and earnings per share include a \$585 million non-cash expense related to the valuation of warrants. IFRS requires the warrants to be classified as a liability given that the functional currency of Betterware differs from the strike-price of the warrants, which is fixed in USD. Changes in the fair value of the liability are presented in the profit and loss statement under the heading, Changes in Fair Value of the Warrants.

IFRS requires the fair value of the warrants to be recorded in profit or loss for the period, however the Company's operating income and the financial position is not impacted. For purposes of the Company's EBITDA, the changes in the fair value of the liability are excluded as they represent non-cash charges.

In addition, when the warrants are exchanged for the Company's shares, the obligation associated with the liability will be extinguished with a corresponding increase in equity. Once the warrants have been redeemed, the net impact in the Company's equity is zero as the increase in their fair value is recorded in the profit and loss statement reducing retained earnings, offset by the equivalent increase in equity as a result of the issuance of the shares.

Turning to a review of the third quarter, I will provide highlights of our results which are detailed fully in our 6-K filed yesterday.

Total net revenues increased 199% to \$2,271 million from \$759 million in the prior period year.

Gross profit increased 173% to \$1,240 million. As a percent of sales, gross margin declined driven by unfavorable currency as we buy our products in U.S. dollars and sell them in Mexican Pesos and to a lesser extent, higher freight costs incurred to meet the surge in demand.

Selling expenses as a percent of sales were 10.7% of sales compared to 20.3% of sales in the year-ago period, driven by strong sales growth.

Higher Sales and SG&A leverage fueled a 244% increase in operating income to \$721 million from \$210 million. Operating margin as a percent of sales increased 410 basis points to 31.8% from 27.7%.

EBITDA for the third quarter 2020 increased 234% year-over-year to \$731 million, compared to \$219 million in the prior year, and EBITDA margin expanded 330 basis points to 32.2% due to the increase in operational leverage.

Finally, we reported \$13.22 in adjusted non-IFRS earnings per share.

Now, turning to the balance sheet, as of September 30, 2020, we had \$1,155 million in cash and cash equivalents, a 656% increase prior-year period and inventory growth supports our sales expectations.

At quarter end, our leverage ratio of net debt to EBITDA was -0.4x, down 0.3x from the end of the second quarter.

In the third quarter, we had \$182 million of capital expenditures. For the year, we anticipate that we'll invest \$794 million in Capex for the year, an increase from the \$267 million spent in 2019.

In terms of our outlook for 2020, as disclosed in our press release, we are providing a net revenue outlook and raising our EBITDA expectations for the year to reflect our robust third quarter performance and expectations for a strong end of the year. We expect revenue for 2020 to be approximately \$7,250 million, and expect EBITDA to be in the range of \$1,900 million to \$2,100 million up from \$1,450 million previously, and EBITDA margin to be 26.2% to 28.9% versus 26.7% to 28.3%.

We are pleased with our record growth, and over the long term, we expect our visible growth strategies supported by a strong infrastructure and talented team will enable our Company to deliver consistent growth in sales and EBITDA in future periods.

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

Operator

At this time, we will be conducting a question-and-answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two to remove yourself from the queue. For participants using speaker equipment, it may be necessary for you to pick up your handset before pressing the star key. One moment while we poll for questions.

Our first question comes from the line of Cristina Fernandez with Telsey Advisory Group. You may proceed with your question.

Cristina Fernandez

Hi. Good morning and congratulations on a good third quarter. We had a couple of questions. To start with the EBITDA guidance for 2020. Very strong increase, but when we look at the fourth quarter EBITDA margin, it is lower than what we saw last year, lower than for third quarter. Wanted to see if you could provide some color on any impact of air freight or effect that is weighting (phon) on the margin for the upcoming quarter. Thanks.

Luis Campos

Yes. This is Luis, Cristina. What we see is that we are expecting probably a lower gross margin due to the exchange rate volatility. If this doesn't happen, I think we could be better by the end of the year but we have to be a little bit cautious because of any potential pressure on the exchange rate peso/dollar. I think this is basically the reason.

The other thing is just taking care of consumption in Mexico. It has come down a little bit in the last few months. Even when we expect that it doesn't go further down, probably it's another opportunity we can have in the fourth quarter. This is why we are giving this range in the upper range, we could be in the upper range \$2,100, if everything goes well in this quarter.

Cristina Fernandez

Thank you. I wanted to ask about inventory availability. It seems like you've been able to get deliveries on track a bit. Any areas where you're seeing constraint in your ability to meet demand?

Andres Campos

We mentioned in the call, we have at the end of the third quarter, we are already meeting our pre-COVID service levels, and now we are prepared to attack all the service needed. We have increased our inventory levels for this quarter, so we believe that we are prepared on all fronts to comply with service levels.

Cristina Fernandez

Thank you. Then one last one from our team. The expansion to Guatemala, can you disclose the difference between working with a concession partner versus going the direct and what is the market opportunity you see there over the next, let's say, year or two?

Luis Campos

Yes, Cristina, this is Luis. We are on (phon) a very successful pilot test. We have two people in Guatemala, they are from Guatemala, and they did it very well. They are operating the business there. We appointed them as master distributors in Guatemala, and now what we are going to do is to have a joint venture, 70% owned (phon) by Betterware de Mexico and 30% owned by them. They will keep running the business down there, okay. One of them is Managing Director, and the other one is Commercial Director.

They are doing very well. We are very happy with their performance and they will continue running the Company. Hopefully in December this will be Betterware de Guatemala. They're operating the business, running the business there in Guatemala. This is going to be a subsidiary of the Betterware de Mexico.

Cristina Fernandez

Thank you and good luck here in the fourth quarter.

Luis Campos

Okay.

Operator

Our next question comes from the line of Eric Beder with SCC Research. You may proceed with your question.

Eric Beder

Good morning. Congratulations on a strong quarter. Could you talk a little bit about the distributors and associates, and you picked up more distributors and associates more than any time in your history. What are you seeing in terms of productivity from these new people, and how long does it take before they really ramp up to kind of where they should be? How should we be thinking about that?

Andres Campos

Hi. This is Andres. During the high growth in distributors and associates, we maintained, and even increased a little, the productivity for associates and for distributors. The distributors and associates are finding both the actual and the new that they're finding a good business at Betterware. We are not seeing any changes in that sense.

Eric Beder

Impressive. What is it going to be—I see you signed another dividend. What is going to be the dividend policy going forward, and what should we be expecting there?

Luis Campos

This is Luis. We are going to continue with our dividend policy. We do not foresee any change about that.

Eric Beder

Last question here. You've been using a lot of air freights, obviously, to keep up with demand. When should we be seeing kind of a slow down in air freight as a vehicle for sending products? Thank you.

Andres Campos

Hi. Andres, again. We are ready now for the fourth quarter with inventory levels and capacity in terms of delivery to sustain and deliver good service on demand. We don't expect to have any more of this during the fourth quarter unless something changes. With everything as it is now, we expect to comply without any extra charges.

Eric Beder

Great. Again, congrats on a good quarter. Good luck for the holidays.

Luis Campos

Thank you.

Andres Campos

Thank you.

Operator

As a reminder, if you would like to ask a question, please press star, one on your telephone keypad. One moment while we poll for questions.

Our next question comes from the line of Jorge Lagunas with Apalache. You may proceed with your question.

Jorge Lagunas

Thank you very much. Congratulations to all the teams, Luis, Diana, and Andres. My first question is with the recovery of the formal and informal employment in Mexico in this new normal, could we expect a (inaudible) scenario that grows in a number of associates and distributors for the next quarters?

Andres Campos

Hi, Jorge. This is Andres. Yes, we have a record net growth in associates and distributors during the pandemic. We are expecting that things going back to normal. We will continue to grow at more similar to historic levels of associates and distributor growth. Obviously, we are working to continue this strong growth in associates and distributors.

Luis Campos

This is Luis, Jorge. Would like to add something. Now, we are departing from a very all-time high level of distributors and associates. When we expect it to go back to normal growth in our salesforce, it is going to be substantial because we are departing from 1.2 million associates and 60,000 active distributors, both active. Then this is a wonderful platform to remain growing.

Jorge Lagunas

Perfect. That's very nice. Thank you very much. Last question is what is the status of your recent presence (phon) in Mexico. Is it going to (inaudible) this year?

Luis Campos

Excuse me? (Multiple speakers).

Jorge Lagunas

(Inaudible) of your (inaudible) process in exchanges in Mexico? Stock exchange.

Luis Campos

We will continue the process with the authorities in order to get listed in the Mexican stock market soon. We cannot give you a date, but we continue with the process, okay. Of course, we will let you know as soon as we have some clear idea about when we can get listed here in Mexico as we are now in the U.S.

Jorge Lagunas

Thank you very much, Luis, and congratulations again.

Luis Campos

Thank you.

Operator

As a reminder if you would like to ask a question, please press star, one on your telephone keypad. One moment while we poll for questions.

Ladies and gentlemen, we have reached the end of today's question-and-answer session. I would like to turn this call back over to Luis Campos for closing remarks.

Luis Campos

I would like to thank you for joining us today. We appreciate your interest in Betterware, and we look forward to speaking with you when we report our fourth quarter and year-end results, if not sooner if there is something else to announce.

Thank you, and see you for the report of the fourth quarter.

Operator

This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation. Have a great rest of your evening.