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China | Consumer

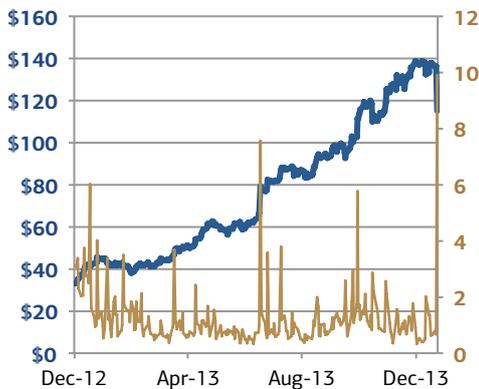
# Nu Skin Enterprises Inc. (NUS US)



## Heads up

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**Nu Skin Enterprises Inc. (NUS US) one-year share price in USD (blue) and volume (gold, in mln shares)**



Source: Bloomberg, January 16, 2013

### Nu Skin Enterprises (NUS US)

Price	USD 115.23
<b>Rating</b>	<b>UNRATED</b>
Market Cap	USD 6.85 bln
Simple Moving Avg.	1.37 mln
P/E	23.56x

Source: Bloomberg, January 16, 2013

### + Attack to be prolonged

China's Ministry of Commerce and the Administration of Industry and Commerce (AIC) have commenced an investigation of Nu Skin following two articles published in People's Daily that attacked the company for "brainwashing" and for stepping beyond the legal parameters of direct sales to engage in pyramid sales.

### + Backhanded compliment

We spoke with members of China's large "anti-multi-level marketing" community to ask "Why Nu Skin?" They said "because lately, the network is developing so fast, and the members who lose money on the products complain to the authorities." One "MLM Rescue Center" employee said that about one-fifth of the calls their center fields are about Nu Skin.

### + Easy target

We believe that the goal of the campaign is to collect fines from Nu Skin and to curtail its rate of growth. Members of the anti-MLM community pointed out that Nu Skin is no worse than the other 40 or so direct marketing companies licensed to operate in China and more law-abiding than many.

### + Valuation: Unrated

We believe that Nu Skin's reports contain significant problems that lead us to question the validity of the financials. As a result, we have been unable to value the company and set a price target.

## Too successful, too American

We believe that the recent attacks on Nu Skin China will be sustained and will curtail network growth but will not result in a revocation of the company's China license. Heightened legal scrutiny could reduce the Limited Time Offer sales that now make up to 22% of sales and about one-third of sales in China, because the products sold on LTO are not licensed for domestic distribution.

**The attacks are serious  
but do not allege law  
breaking.**

Given that China grew by 407% in Q3, this could significantly impact the company's 2014 Q1 results. Nevertheless, the attacks focus on well-known characteristics of all MLMs—the fervent, revival-type meetings they convene to juice sales, the disillusionment of the majority of participants who do not make money by participating in the network, and the misrepresentation of the products' mystical curative properties.

On January 15 and 16, the People's Daily ran articles criticizing Nu Skin for "brainwashing" at its sales meetings and for maintaining downlines that pay commissions. Although this is standard operating procedure for MLMs in China and elsewhere, technically, it violates China's direct sales regulations.

China's direct sales community believes that the People's Daily attack was prompted by Nu Skin's unusually fast growth. China has a large and vigilant community of anti-MLM activists who work with the police and the AIC in each province to identify any regulatory breaches by MLM companies. This is because, under the law, the companies must post large deposits against the eventuality that they may be fined, and authorities that prove cause even outside a legal proceeding may attach those deposits. This financial incentive has spawned entrepreneurial groups that volunteer to police the MLMs and potentially share in the fines.



Screenshot from People's Daily film of Nu Skin meeting | Xinhua

The articles fit well within a recent pattern of attacks on foreign-owned businesses in China, whether milk powder, pharmaceuticals, automobiles, or food. We regard this as a symptom of economic distress in which rent-seeking is sanctioned by a framing ideology that encourages xenophobia.



Nu Skin's wall of photos of prominent sales leaders | J Capital, August 2012

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