Overview

- Founded by Jean Nidetch
    - A Brooklyn homemaker
    - In 1963
        - Before that, she began weight-loss meetings
            - With a group of her overweight friends
            - In the basement of a New York apartment building
    - Heinz acquired in 1978
    - Artal Group acquired WTW from Heinz in 1999
        - $735 million leveraged buyout deal
            - Artal put down $224 million
        - Artal Group is run by Raymond Debbane
    - IPO in 2001
- Provides weight-loss meeting
    - In about 30 countries
    - For monthly pass fee of $42.95
        - A member stay for 8 months
        - A women can use Weight Watchers about 4 times during her lifetime
    - Each week, over **a million members** attend over **40,000 Weight Watchers meetings**
    - In each meetings
        - Weigh in
        - Members shares weight-loss experience, support, and advice
    - Very effective
        - Members lose more than twice as much weight as compared to those who try to lose weight with a doctor[i]
            - 3 times more likely to achieve 10% weight-loss
        - 5 times more weight loss than self-directed dieting[ii]
- Provide Weight Watchers program online
    - As of the end of fiscal 2012, Weight Watchers online had over **1.8 million** active subscribers
        - Monthly fee is $18.95
        - A member stays for 9 months
    - Weight Watchers online helps subscribers adopt a healthier lifestyle
        - Allows subscribers to track points through the web or apps

            - Point counting is a good self-monitoring habit
        - Help subscribers keep track of their weight loss effort
            - Weight trackers and progress chart
        - Help subscribers make smarter food choice
            - See new featured recipe daily
            - Create shopping lists from recipes
            - Interactive cheat sheets help to make better food choice at home or at restaurants, etc.
                - Meal ideas
                - Restaurant guides
- WTW has the best reputation in weight loss
    - License the brand to a lot of products
        - Apple bee’s
        - General Mills
            - Green giant frozen vegetables
            - Progresso light soups
            - Yoplait light yogurt
- WTW is a great investment by Artal Group
    - Since 1999, Artal group pocketed $3.8 billion
        - IPO
        - Dividend
        - Selling stocks
            - To keep 52% ownership
        - Selling WeightWatchers.com
            - To Weight Watchers
            - In 2005
            - For about $381 million
            - Before that, weightwatchers.com is a franchisee of WTW
                - WTW owned 20%
    - In an industry with a lot of fads, WTW’s ability to generate FCF is incredibly consistent
        - FCF was about $252 million in the last 10 years
            - Min: $210 million
            - Max: $360 million
            - Median: $252 million
            - Mean: $262 million

            - STDEV: $42 million
            - CV: 16% (stable)
    - This is thanks to WTW's terrific product economics
        - Low fixed cost
            - Fitting out a retail location cost less than $50,000
            - Usually in low-rent locations
        - Most meeting leaders work on a part-time basis
            - They don't work for money
            - They work because they love the job[iii]
        - So, with effective marketing, the offline business can earn about 30% operating margin
        - The online business is even more profitable
            - Over 50% operating margin
        - Return on capital is virtually infinite
            - EBIT/NTA is about 1,420%
    - WTW became Artal Group's cash cow
        - Regularly pay dividend
            - Total $376 million in the last 7 years
        - Repurchased share
            - Total $3,346 million since 2011
            - Artal Group got 52% of this amount
                - They sold an appropriate amount of shares to keep 52% ownership
            - Leveraged up and deleverage
                - Take cash out ahead of future FCF
                - Repurchased $1,034 million in 2007
                    - 19 million shares
                - Repurchased $1,504 million in 2012
                    - 18.3 million shares
- Should we become Artal's junior partners?
    - EV/EBITDA is about 8.8
    - Normal earnings power is about $5.32 per share
    - At EV/EBITDA of 12 that good consumer products companies usually trade at, the intrinsic value is $77
    - By our estimate, buying at less than $63 can give at least 10% annual return in 5 to 10 years

- At current price of $46 per share, we can get 20% annual return in the next 10 years
- Why is it so cheap?
  - Is EV/EBITDA too high?
  - Is the debt level too high?
  - Will free apps kill the online business and cannibalize the offline business?

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[i] "In September, we saw enrollment levels bounce back nicely as we benefitted from effective marketing as well as the publicity around the release of a clinical study published in the Lancet, globally one of the most respected medical journals. The Lancet study was a breakthrough publication for Weight Watchers. This large randomized clinical trial was led by investigators from the Medical Research Council of the University of Cambridge in the UK.

The study was conducted in the UK, Germany and Australia with close to 800 people on the sample. In the study, doctors would randomly refer an overweight and typically obese patient to either Weight Watchers meetings or to a standard care program led by a primary care provider. After 12 months, participants in the Weight Watchers arm achieved two times the weight loss and were more than three times more likely to achieve a 10% weight loss as compared to the standard care group.

The study demonstrated the power of the partnership between doctors and Weight Watchers to have significant impact on patient success. Moreover, just this past Friday another publication, The British Medical Journal released a new study further validating Weight Watchers superior to weight management. These studies clearly demonstrate our ability to be among the most effective tools for addressing part line obesity." – David Kirchhoff, CEO, 2011 Q3 Earnings Transcript

[ii] "We reacted quickly over the course of the first quarter and we were able to enter the spring campaign at the beginning of April with fresh advertising. **Our meeting star featuring Jennifer Hudson focused on a recent clinical study showing 5x more weight loss than self-directed dieting and we're much more direct in our messaging**." – David Kirchhoff, 2013 Q1 Earnings Transcript

[iii] "**Everyone who works for Weight Watchers lost their weight with the program. The connection that is made between the Service Providers and the Members is forged because of that commonality. This is not a "customer and vendor" relationship. It's much more familiar**.

Being a Weight Watchers Leader has been the most rewarding thing I've ever done. In my long and successful prior career, I don't recall ever

receiving a letter or email that said "thank you, you've changed my life", yet this now occurs on a regular basis.

Helping people reach their goals, regain confidence, see dramatic health benefits and embrace a healthier lifestyle is enormously rewarding. The relationships with our members go far beyond the meetings. There are Facebook Groups, Blogs, Emails and phone calls (unpaid but encouraged) that many of us maintain to help keep our members engaged and realize their goals.

We are often psychologists, nutritionists, motivational speakers, confidantes, subject-matter experts, sales people and facilitators. These are skills and traits that are difficult to quantify, and certainly not adequately compensated.

It is the passion for our members' success that has allowed the inadequacy of wages, lack of meritocracy and unpaid time to prevail for decades. What are we worth? We will find out." said one leader.

Durability

- Demand is durable
    - People eat more and work more in offices
    - Pay more attention to health and beauty
- The program is durable
    - There are a lot of fads in this business
        - Some fads in the past were
            - Atkin diets
            - South Beach diet
            - Slimfast
        - The reasons for a lot of fads include
            - The demand is high
            - Churn is high
                - Requires self-motivation to succeed
                - People tend to look for outside rather than inside reasons for failures
            - A customer doesn't stay in a program for a very long time
                - 9 months with Weight Watchers online
                - 8 months with Weight Watchers meetings
                - Customers come in and come out
                    - A women can use Weight Watchers about 4 times during her lifetime
                - 10-12 weeks with NutriSystem
            - So, customer acquisition cost is high in this business
                - NutriSystem spend about 25% of sales in advertising
                    - In 2007, spent $184 in marketing per new customer
                - Medifast spend
                    - 9-10% in advertising
                    - Pay over 20% commission to "health coaches"
                - Weight Watchers spend 14% of sales in marketing
            - So, program news and effective marketing drive customer acquisitions
    - WTW is stable than other programs
        - WTW has a general approach
            - Teach members to eat healthier

                - Counting calories
                - Watching weight
                - Peer pressure and support
            - Other programs focus on specific idea
                - Followers cannot eat like a normal person
        - Tweaks on programs are still based on a general theme
            - Momentum in 2008
            - PointPlus in 2010
        - Other programs need more changes in marketing to get people excited
- The brand is durable
    - Weight Watchers is like a religion
        - Meeting leaders are like preachers
            - Had over 54,000 employees and service providers in total
            - Meetings leaders usually work on a part-time basis
                - They are usually highly educated professional
                - They are all successful with Weight Watchers
                    - They are eager to help others lose weight
                    - They get formal training from Weight Watchers
                - Leaders can plays an important role in the weight loss process and getting customers[i]
                - Leaders don't make much money[ii]
                - But money doesn't have much to do with their motivation
                - They work because they love the job[iii]
        - The corporate focuses on promoting the brand
            - Program news & marketing buzz drives recruitment growth
    - Meeting leaders wouldn't hurt the brand
        - They're enthusiastic about helping members
            - They were members themselves[iv]
            - Money is not the biggest reason they work
        - They receive training
    - The risk that the management kill the brand isn't high
        - They may want to create a lot of buzz to drive sales
        - Only a very bad program can hurt the brand
            - But why would they introduce a bad program?

        - They can always find opportunities to improve the program[v]
  - The current management is good
    - Has a clear strategy to drive long-term growth
      - 4 drivers of growth[vi]
        - Marketing to differentiate the brand
        - Right leaders
        - Innovating programs
        - Identifying and implementing the best practices to improve service quality
    - Patient and careful with new program
      - The PointsPlus program was developed in 2007[vii]
      - They really wanted to launch the program a year ahead of when they launched[viii]
        - But they took time
        - Start with clinical trials and focus group
        - Rolled out the program in early 2010 at meeting sites in Manhattan, Los Angeles, and Morristown, N.J.
        - Gets 19,000 meetings leaders onboard
        - Lining up support from influential dietitians
        - Launched in December 2010
      - The CEO also believes that **“***good programs actually build over time as opposed to sort of one massive pop*”

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[i] “**The leader at my WW meetings is incredible: helpful, funny, and down-to-earth. And the receptionists are, too - I actually look forward to seeing them every week and they are so supportive and have made a huge difference in my weight loss and my attitude about it**. (Thank you, Helaine, Hilda and Cami!) I've always known that the employees push the products and make commissions, and it doesn't bother me. But it does bother me to hear how little they get paid. They deserve so much more.”, said a member, Low Pay at Weight Watchers Stirs Protest as Stars Rake It In, Steven Greenhouse, New York Times, 25 Feb 2013

[ii] “**But Ms. Williams complained that she was paid just $7,600 last year for leading four meetings a week in Wichita Falls, Tex**. She receives extra pay as

a local coordinator and commissions for selling company products like recipe books, scales and smoothie mixes.

While the company pays for two and a half hours of work to run a meeting, Ms. Williams, who is planning to quit, said it could take three hours or more to set up chairs, weigh in members, give talks, sell products and clean up. **(For meetings that attract 50 or 60 members, several leaders said that they received around $60 instead of the $18 base rate, and that receptionists for meetings received a base rate of $12 before commissions**.)" – Low Pay at Weight Watchers Stirs Protest as Stars Rake It In, Steven Greenhouse, New York Times, 25 Feb 2013

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It is the passion for our members' success that has allowed the inadequacy of wages, lack of meritocracy and unpaid time to prevail for decades. What are we worth? We will find out." said one leader.

[iv] "And then finally significant competitive advantages: Let me specific about this, is that every Weight Watchers meeting is led by a person who is a successful member. The reason that is important is that facilitating a group support experience requires that the facilitator have a high degree of empathy in

understanding and if you've never had a weight problem, you don't understand what it is.

What's another model that we can think about like this, AA; highly effective, really good at what they do. We don't tend to compare ourselves to them in marketing materials for a verity of different reasons, but specifically if you look at underlying, what's happening from a behavior modification point of view and why group support works, its sometimes a useful analog to think off and its very similar in terms of underlying philosophies that we apply in our means business." – David Kirchhoff, CEO, JP Morgan Global Health Conference 2012

[v] "**Chris Ferrara** - Merrill Lynch

That's really -- I appreciate all the color. I just wanted to ask I guess one follow-up to that, and I don't even know how you could answer this but just to sort of give color -- I mean, if you launch this campaign and it doesn't -- or this program and it doesn't go as you'd expect it to go. In other words, the results aren't as good, would you -- do you think hypothetically you would turn around and say we just didn't have the right innovation or might you draw another conclusion just on how viable the meeting business is in the long-term?

David P. Kirchhoff - President, Chief Executive Officer, Director

No, I would never come to that particular point of view. You know, the thing I would look at a program innovation is that what I would address, and certainly every time we launch a new program there's an opportunity to go back and take a look at it and say what are the elements of it that worked well and what are the elements that could have worked harder**. And if we are doing regular program development, we can always find an opportunity to further improve our program with subsequent releases**.

And so my view is that having the right kind of program development process means a willingness to constantly come out with new and better versions of the same and sometimes those are going to be tweaks and sometimes are going to be more major.

I think that if you see what a program does, I mean, if I thought that the only thing you had to do to drive this business was develop a good program, that would be a fairly simple thing to do in terms of driving the business. And the program is very important but it is not the only thing -- that if I'm going to drive the kind of growth that this business I believe is inherently capable of, it is going to be a function of us executing across all four different dimensions of the leader, marketing, program development, and service innovation." – 2008 Q1 Earnings Transcript

[vi] "Right. I mean, if I take a step back and look at what I believe is necessary to drive medium and long-term growth in the business, it continues to be -- and it's around these planks of retention relevance but it kind of boils down into sort of our areas. **The first is sharper, more differentiated advertising that does a better job of differentiating our brand equity. The second is right leader in the right meeting with the right training. The third is having innovative -- you know, a constant state of innovating programs that does a better and better job of addressing fundamental member needs, wants, and gets. And finally, there is innovating the service itself and finding, identifying, and implementing best practices in the actual meeting room environment.**

You know, the program innovation is one that can work really powerfully in tandem with marketing particularly if the program innovation addresses fundamental member needs and wants.

And as I've said in the past, our historic approach to program innovation, **we sometimes got ourselves into trouble because we could be accused of either not coming out with enough innovations or coming out with innovations that I think could have historically been argued as almost sometimes kind of a window dressing, if you will, used to fuel the marketing engine**.

The reason I feel good about this particular program we are working on is that I know the needs and wants that it's trying to assess. **I've had the opportunity to sit myself in research and focus groups, as I've listened to people go through pilot tests. And I've had enough exposure to it to believe that the things that it's trying to communicate and address are real**.

And on the basis of that, I feel good about it. Now, do I want to put sort of the future of humanity at stake with this new program? I mean, a couple of things on that -- first off, no, because **I think we have to execute against all four dimensions that I mentioned**. And secondly, I think the other thing that is very important for us to recognize is that good program innovations take time to build and the reason is that -- I'll always come back to the fact that give or take roughly six or seven out of 10 enrolments we get are at the recommendation of a friend or family member and that's word of mouth, and word of mouth frankly takes a while to build because word of mouth really starts to happen when members achieve success.

And what we see in good programs is that good programs actually build over time as opposed to sort of one massive pop. Now, all those caveats aside, I feel like if we have a program that innovation that is significant enough that we can build a marketing campaign around it that will address fundamental benefits for consumers, that that's reason to be excited about what we have for the winter campaign and everything I am seeing so far puts me in an on average more excited place." – David Kirchhoff, CEO, 2008 Q1 Earnings Call Transcript

[vii] "The original idea arose in 2007 when new CEO David Kirchhoff asked his team how they would design the program if it were created from scratch.

The answer was to create a system that tracked not just calories but the quality of calories. What emerged was "Points Plus," in which the amount of protein, carbohydrates, fat and fiber in foods are all considered.

The new system favors foods that make the body work harder to convert calories into energy, resulting in fewer calories absorbed.

For members, the change is profound. For example: Fruits and vegetables are now point-free. Orange juice, on the other hand, costs three points." – What Can You Learn From Weight-Loss Company's Shift to PointPlus? Patient, Advertising Age, 16 January 2012

[viii] "Weight Watchers made its move in December 2010, about three years after the drastic overhaul of its program was conceived. And the wait paid off. **By taking its time, the company was able to get its 19,000 meeting leaders--who would be influential in selling the changes to skeptical members--onboard, while lining up support from influential dietitians**.

A year later, the company is thriving. Analysts cited the program launch as a factor in boosting third-quarter 2011 revenue 30%, outperforming competitors, including Nutrisystem, which reported falling revenue.

In an age where so many corporations have failed and even backtracked on major changes that seem rushed--see Netflix, Bank of America--how did the company manage to remain on course? Ad Age talked to key members of the team to find out.

"**We really wanted to launch this program a year ahead of when we launched it**," Ms. Callan said. "It was tempting to do that. But we couldn't have pulled off this level of synchronization across the entire organization and the attention to detail."" – What Can You Learn From Weight-Loss Company's Shift to PointPlus? Patient, Advertising Age, 16 January 2012

Moat

- The weight-loss market is huge
    - 70% of all American are overweight or obese
    - 78.1 million American adults are obese
    - 90.6 million Americans are obese
    - 25 million American adults are diabetic
    - 78.5 million Americans are pre-diabetic
    - WHO projects that by 2015
        - 2.3 billion people will be overweight worldwide
        - 700 million people will be obese
    - Competitors include
        - Self-help weight management regimens, products, and services
            - Include diet schemes, books, magazines
                - The Paleo Diet
                - Atkins diet
                - Mediterranean diet
                - Glycemic index diet
                - South beach diet
            - 80% of weight loss attempts are on self-help basis
        - Food replacement companies
            - Jenny Craig
            - NutriSystem
            - Medifast
        - Pharmaceutical companies
- Weight Watchers has a general approach
    - Teach members to eat healthier
        - Counting calories
        - Watching weight
        - Peer pressure and support
- Weight Watchers' meeting business has a wide moat (in this approach)
    - Has a great brand name and reputation
        - License the brand to a lot of products
            - Apple bee's
            - General Mills
                - Green giant frozen vegetables
                - Progresso light soups

        - Yoplait light yogurt
  - Word-of-mouth
    - 60-70% of members came to Weight Watchers through word-of-mouth referrals[i]
  - The price may not be a big factor in choosing a program similar to WTW's
    - Low cost:
      - $42.95 meeting monthly pass fee
      - $18.95 online monthly fee
    - The benefit of successfully reducing weight is much higher
    - Once customers decide to go to a meeting, they'll choose the best program
  - Leaders wouldn't compete against Weight Watchers
    - Non-compete agreement
    - They usually work on part-time basis
      - They work for fun
        - Not for money
  - So, it's very difficult to duplicate WTW's meeting business
    - Competitors must enter the business by introducing something "new"
      - Base on specific ideas
        - Low carb diet
        - Food-replacement
        - Diet pills
        - Etc.
- Weight Watchers can protect its online business
  - The online business can cannibalize the offline business
    - From 2008 to 2012
      - Offline sales: declined 3.4%
      - Online sales: grew 269%
      - The economic condition had some impact on the offline business
        - But the online business might cannibalize somewhat
    - The introduction of online program is like a psychographic segmentation
      - Some people don't want to go to a group[ii]
      - Online is cheaper[iii]

            - Some people don't want to travel far to the meeting
            - Some people need peer pressure at the meeting[iv] [v]
    - So, the only threat to WTW's meeting business is
        - Online cannibalize offline
        - WTW's online business doesn't have a wide moat
    - Competitor is free apps
    - WTW online grew impressively in the last 3 years
        - 2010: 22%
        - 2011: 68%
        - 2012: 26%
    - But slowed down in the last quarter
        - Online paid weeks increased only 10.3% in Q1 2013
        - Due to the accelerated interests in free apps
    - WTW's advantages include
        - Being able to position the brand as a weight-loss program
            - Online competitors are at a disadvantage by focusing on a specific idea
                - They count specific measure like calorie
                    - Like My Fitness Pal
                        - Beside counting calories, they have a network like Facebook to help members share experience
                - People won't trust a point system from a unknown provider
                - It's difficult to teach people to eat healthier by counting calorie
                    - Weight Watchers assigns fewer points to healthier food with the same amount of calories[vi]
            - Weight Watchers has been advertise that people can lose weight successfully online
            - Free apps reduced the marketing effectiveness of this message[vii]
            - Now, Weight Watchers starts shifting to communicate the full value proposition of Weight Watchers Online
                - A behavior modification program
        - Being able to charge

            - “free” is one of the strongest marketing message[viii]
            - Once competitors choose to charge a fee, there won’t be any differentiation
                - Compete for people who are willing to pay
                    - They don’t really choose on price
                    - They will choose the best program
                        - Weight Watchers
        - Weight-loss success really depends on commitment
            - Some people are heavy users of free apps and succeed
                - Counting points or calories are very good self-monitoring habit
                    - It can be addicted like playing games
            - But it’s very hard to form this habit
            - But most people use free apps for only 1-2 weeks
                - They have higher commitment when use Weight Watchers online[ix]
    - Customers see the value proposition of WTW online program
        - Retention rate is high
            - Didn’t change despite free apps
            - Online members stay in the program for 9 months[x]
                - That means the online program works
                - Members see the program worth the money they pay[xi]
        - There are always people with high commitment to reduce weights
            - They see great value in reducing weights
            - They are willing to pay
            - Weight Watcher Online/Offline are great choices
- Weight Watchers doesn’t compete directly with other commercial programs
    - There is psychographic segmentation
    - Each person may prefer a different weight loss program
        - Some can do on their own
        - Some need help
        - Some want food replacement
- But has some advantages over other commercial programs
    - Is the biggest company by sales
        - Weight Watchers: $1.8 billion
        - Jenny Craig: $432 million

                - This was 2010 revenue
                - Compared to NutriSystem's $509 million in 2010 revenue
                - Sales declined in the last 2 years
            - NutriSystem: $397 million
            - Medifast: $357 million
    - Has the biggest marketing budget
        - Weight Watchers: $344 million
        - NutriSystem: $111 million
        - Medifast: $245 million total SG&A
            - Medifast actually has a direct-selling model
    - Words of mouth
        - 60-70% of members came to Weight Watchers through word-of-mouth referrals[xii]
    - Lower cost
        - Weight Watchers: $42.95 monthly pass fee
            - $18.95 online monthly fee
        - Jenny Craig: $400 monthly
        - Medifast: $250 monthly
        - NutriSystem: $250 monthly
        - People who live with family may find it expensive to spend hundreds of dollars on weight-loss each month

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[i] "I think the other thing that is very important for us to recognize is that good program innovations take time to build and the reason is that -- I'll always come back to the fact that **give or take roughly six or seven out of 10 enrolments we get are at the recommendation of a friend or family member and that's word of mouth, and word of mouth frankly takes a while to build because word of mouth really starts to happen when members achieve success**.

And what we see in good programs is that good programs actually build over time as opposed to sort of one massive pop. Now, all those caveats aside, I feel like if we have a program that innovation that is significant enough that we can build a marketing campaign around it that will address fundamental benefits for consumers, that that's reason to be excited about what we have for the winter campaign and everything I am seeing so far puts me in an on average more excited place." – David Kirchhoff, CEO, 2008 Q1 Earnings Call Transcript

[ii] "I love WW online! I started when DS was a week old, and I celebrated my 2nd anniversary in April.

It works for me because I'm not a group hug kind of person, had limited time with a newborn and it's a heck of a lot cheaper. I'm also on the computer a lot (especially when I returned to work) and it's so easy to track." said a member with nickname Zwalleby from babycenter.com. For more quotes, read "*Quotes on Different Offline & Online Customerss.docx*"

[iii] "I started the online program April 24th. **For me the issues were time and money. It is much cheaper to join online and since I spend a lot of time on-line anyway**. Not only that but I would have to get my mum who already watches Katie all day while I work etc. to watch her. I didn't think it was fair to my mum. So I figured, I would give it the 3 months online to see how I did and if I felt like I needed the meetings, I would change over.

I have lost 17.6 lbs. so far. (But am 26 lbs. down from what I was last December. Good Luck in whichever way you decide." Said a member from babycenter.com. For more quotes, read "*Quotes on Different Offline & Online Customerss.docx*"

[iv] **"**I do not do the online although I do have access. **Reason I will not hold myself accountable. I need to go to the meeting and have someone watching over me so to speak**. I swear it is like a confessional when I weigh in.

Oh I did bad this week because....LOL

Stephanie" said a member in babycenter.com. For more quotes, read "*Quotes on Different Offline & Online Customerss.docx*"

[v] **"I have been a member of MFP for 2 years now. By July 2012 I lost 20 pounds, but I was never able to fully commit to the MFP system. Even though I was provided with great tools for success, I still wasn't losing weight. A few weeks ago, I realized that this was because I had no real accountability. I personally joined Weight Watchers because it provides the accountability I am looking for**. My leader encourages us to have a fruit or veggie with every meal, exercise often, and even encourages eating back some of our exercise points. I like being able to see the same people every week and see how their journey is progressing and share in our triumphs (and failures). I have never felt like I am "dieting", just being cognizant of what I am eating. I do not plan on going to Weight Watchers forever. I plan on attending until I lose 50-70 pounds; since I don't think I could eat less than 30 points a day (right now I have 36 points a day which is about 1450-1600 calories). I say follow whichever "plan" you think you can stick to. For the stage of weight loss I am in right now, I

love Weight Watchers (even if I have to pay them $12 a week).", said a member from My Fitness Pal community, http://www.myfitnesspal.com/topics/show/881110-weight-watchers-v-calorie-counting

[vi] **"**I first joined WW back in May of 2011 and was successful at losing about 40 lbs. in 5 months....Then I decided to try and save a few bucks and quit WW... **Since then I bounced around between My fitness pal (great data base), lose it, spark people.com, calorie king (no mobile apps) and a couple of others....All have their good points and their shortcomings......but for some reason, they don't seem to work as well as WW....**

Why? ..Great question.....Maybe because they are all based on calorie counts and not all calories are created equal....Maybe it's because the WW program encourages you to eat fruit and vegetables by charging 0 points...Maybe it's because they have more resources and better support among its users....Perhaps it's as simple as the fact that it's not free....We have to pay for it and since we do, we try harder to get our money's worth out of it...." said a member from Weight Watchers community. For more quotes, read "Quotes on Counting Point being Better.docx"

[vii] **"**Our Weight Watchers Online advertising has done a great job over the past few years of creating awareness for losing weight online and driving trial of our online product **by advertising the fact that you could lose weight successfully online. This worked well for us over multiple years, a time during which there was no meaningful competitive online alternative**.

Over the past year, however, there's been an increase in proliferation of free applications, and Google Trends metrics indicate that consumer interest in these apps is up significantly this January. It's now clear that the weightwatchers.com awareness-driving strategy that has been so successful at driving millions of people in the weightwatchers.com started losing some effectiveness roughly 6 months ago. We now need to shift gears to leverage the groundswell of people interested in weight loss mobility tools by communicating the full value proposition of Weight Watchers Online, and the behavior modification approach on which it's based.

Our new goal is to convince the growing number of people who are inclined to seek online weight loss help that if they're going to invest their time and effort in trying to lose weight online, they should invest in the best method: Weight Watchers.

What we've been seeing this January is softness in never-member recruitment in Weight Watchers Online but continuing strength in recruiting rejoins and continuing strength in retention. To us this reflects the fact that people who have used Weight Watchers Online, and are therefore aware of the value proposition, are choosing to come back rather than turning to free apps. However, as to those who have not yet experienced the value proposition, we have not connected with them with our marketing.", David Kirchhoff, CEO, 2012 Q4 Earnings Call Transcript

[viii] "I did WW a couple of years ago and I loved it. I lost over 20 pounds, got my goal weight and maintained as long as I had my online membership. **It really taught me how to eat and I use those skills now on MFP. The reason I'm not on it now is simply because it's not free like this is**. I think I'm pretty much resigned to the fact that I will always need structure and accountability to maintain my weight." said a member in My Fitness Pal community. For more quotes, read "*Quotes from People Switching to MFP.docx*"

[ix] "**I found I was a little more accountable with WW because I'm cheap and I didn't want it to be a waste of money, I guess. I don't know why, really, I just had less trouble "falling off the wagon" with WW**. But I like MFP too; it all depends on your level of self-control. GL!" said a member from Theknot.com. For more quotes, read "*Quotes on Higher Commitment with Weight Watchers*.docx"

[x] "First quarter Internet revenues grew approximately 11% on a constant currency basis. Paid weeks rose 10%, which was somewhat ahead of our earlier expectations with growth in both the U.S. and International. Continental Europe and Canada had stand-out double-digit performance. That said, sign-ups grew weaker and turned negative in the U.S., though they were up strongly internationally. As a result, end-of-period active subscribers rose 6%. **Importantly, retention remains unchanged at 9 months**. We expect weightwatchers.com paid weeks growth in each quarter this year, albeit at decelerating rates, given the lower sign-up trend in the first quarter. For the year, paid weeks should now be up low-single digits, which is slightly ahead of our prior guidance of flat to up slightly. This outlook assumes the economic and competitive environment remains the same." – Nicholas Hotchkin, CFO, 2013 Q1 Earnings Transcript

[xi] **“**I love MFP. I use both MFP and WW. **I like WW for the recipes and that is enough to keep me paying. LOL I agree, MFP has more items listed and I love their bar code scanner, much better than the WW one**.” Said a member from Weight Watchers online. For more quotes, read “*Quote on Customers' Value Perception.docx*”

[xii] **“**I think the other thing that is very important for us to recognize is that good program innovations take time to build and the reason is that -- I’ll always come back to the fact that **give or take roughly six or seven out of 10 enrolments we get are at the recommendation of a friend or family member and that’s word of mouth, and word of mouth frankly takes a while to build because word of mouth really starts to happen when members achieve success**.

And what we see in good programs is that good programs actually build over time as opposed to sort of one massive pop. Now, all those caveats aside, I feel like if we have a program that innovation that is significant enough that we can build a marketing campaign around it that will address fundamental benefits for consumers, that that’s reason to be excited about what we have for the winter campaign and everything I am seeing so far puts me in an on average more excited place.” – David Kirchhoff, CEO, 2008 Q1 Earnings Call Transcript

Quality

- Industry quality
    - Solve the overweigh problem
    - Low fixed cost
    - The business is all about
        - Customer acquisition cost
        - Revenue per customer
    - So, any company that succeed in getting customers will make a lot of money
        - NutriSystem
            - Sales
                - 2004: $38 million
                - 2007: $777 million
            - EBITDA
                - 2004: $2 million
                - 2007: $174 million
            - EBIT
                - 2004: $2 million
                - 2007: $169 million
            - Driver of success was the increase in advertising
                - 2004: $8 million
                - 2007: $179 million
        - Medifast
            - Sales
                - 2008: $105 million
                - 2012: $357 million
            - EBITDA
                - 2008: $13 million
                - 2012: $34 million
            - EBIT
                - 2008: $8 million
                - 2012: $23 million
            - Driver of success was the increase in the number of direct sellers
                - 2008: 3,400 health coaches
                - 2012: 10,200 heath coaches

- WTW is the most profitable company in the industry
    - Low fixed cost investment
        - Fitting out a retail location historically cost $20,000-25,000
        - The revamp program now cost $50,000 per location
        - The online business has more significant upfront investment
            - Capitalized software and website development cost was $144 million in 2012
            - But get enough scale
                - Online sales was $508 million in 2012
                - Operating profit is over 50%
    - Negative working capital
        - Don't sell food replacement so don't have to keep high inventories
        - Receive a lot of deferred revenue
            - $83 million in 2012
        - Working capital in 2012 was -$102 million
    - As a result, WTW is much more profitable than NutriSystem and Medifast
        - WTW
            - EBITDA/NTA is about 1,454%
            - EBIT/NTA is about 1,420%
        - NTRI in best year
            - EBITDA/NTA: 400%
                - 2006
            - EBIT/NTA: 393%
                - 2006
        - Medifast in best year
            - EBITDA/NTA: 119%
                - 2010
            - EBIT/NTA: 100%
                - 2010
    - Generate a lot of FCF
        - FCF/Sales is about 20% since 2001
            - Min: 14%
            - Max: 24%
            - Median: 20%
            - Mean: 19%

                - STDEV: 3%
                - CV: 0.17
    - WTW has high and stable margin
        - Meeting gross margin was very stable
            - About 52% from 2001 to 2012
                - Min: 47%
                - Max: 54%
                - Median: 52%
                - Mean: 51%
                - STDEV: 2%
                - CV: 0.05
            - Despite the business is cyclical
                - Economic: spending in weight-loss program is discretionary
                    - NACO attendance declined 12% in 2009
                - Program & marketing
                    - New programs drive sales
                    - NACO attendance increased 18% in 2011 thanks to PointPlus introduce in late 2010
                - Fads of competing programs
                    - In 2004, NACO attendance declined 12% because of Atkins diet
            - Stable gross margin is due to the flexible business model
                - The main fixed costs are
                    - Rent
                        - Usually at low-cost locations
                    - Local managements
                    - Meeting leaders are paid on a part-time basis
                - So, in 2009
                    - NACO attendance declined 12%
                    - But offline gross margin declined only 4%
                        - 51% in 2008
                        - 47% in 2009
            - Offline operating margin is stable and high
                - About 29% since 2001
                    - Min: 19%
                    - Max: 37%

            - Median: 29%
            - Mean: 28%
            - STDEV: 5%
            - CV: 0.17
        - Gross profit pays for
            - Advertising
                - Manageable
                - Usually depend on sales
            - G&A
                - Is only about 12% of sales
    - Despite short-term fluctuation, attendance is stable around a level that allows WTW to make good profit margin
        - U.K. Meeting attendance since 2001
            - Min: 10 million
            - Max: 13 million
            - Median: 11.6 million
            - Mean: 11.6 million
            - STDEV: 0.93 million
            - CV: 8%
        - Continental Europe Meeting attendance since 2001
            - Min: 7 million
            - Max: 11.6 million
            - Median: 9.2 million
            - Mean: 9.3 million
            - STDEV: 1.54 million
            - CV: 17%
- Online business margin just gets better
    - Gross margin
        - 2005: 76%
        - 2012: 87%
    - Operating margin
        - 2005: -7%
        - 2012: 51%
    - Member growth leverages fixed cost

- As long as WTW can sell the program, the profitability remains unchanged
    - Durability makes it possible
    - But marketing effectiveness is still important

        - The management has been doing a good job
        - Local management has some freedom to try different marketing ideas
            - Local management can develop and test new ideas[i]
                - For example, the U.K team came up with continuity marketing[ii]
            - Refine and improve their marketing playbook[iii]
        - The management focus on return on marketing investment
            - Track the result of promotions[iv]
            - Test conventional assumption about banner ads
                - Decided to reduce banner ads[v]
- Some other quality
    - Global
        - About 30% of sales is outside of the North America
        - Online business can drive sales in international market
            - More accessible
            - Cheaper
    - Weight Watchers usually increase price after several year
        - 11% price increase in the U.K. in August 2007
        - Increased online monthly fee in 2011
            - $17.95 to $18.95
        - Increased monthly pass in the U.S.
            - PointPlus 2012
            - $39.95 to $42.95
            - Didn't increase since 2006

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[i] "**Bob Craig** - Stifel Nicolaus

David in hindsight what was the problem do you think with the UK marketing and looking at most of your countries now Germany, France, NACO obviously is what they are lacking an effective spokesperson.

David P. Kirchhoff - President and Chief Executive Officer

I think that is part of it. What they are lacking was, I think what an effective spokesperson does when he works for us is if you've someone who people can relate to is also having a weight issue, but their success is very visible, it's always a main thing how much inspiration people take from that. And they have tried something that was a little bit of a different approach they were real members, but they were using sort of lots of real members. **And they tried some different**

things that they thought was an appropriate reflection of kind of culturally where they thought the British consumer was. And they tried something that was a little bit different. And I think one of the balances that we're always trying to reach as an organization is that we want a management team and we want local management team that will try things, that will try to push the envelope and we are periodically try to take risks, and help us grow and develop the business.

And we are always trying to manage to what degree we sort off push things top down versus local management teams stretch their legs and try different things. **And in this case my judgment was to be supportive of the UK team and trying something a little bit different**. It didn't pan out and I think one of the broader statements that I would make about Weight Watchers is that I'm frustrated by the exclusion issues because there are things we could have avoid it, and that's disappointing.

At the same time, I don't want this organization becoming a risk of us. We're not going to get to where we need to go, but we're not willing to try things and we're not willing to push ourselves a little bit that does mean from time-to-time we're going to skin our knees. I think we need to sort of be more careful where we run, but we need to keep running.

And so when I look at the UK marketing, while I am disappointed and I think frankly, they look at what's happening for example in Germany where they are using celebrities spokesperson and their business is growing just great. Their online business in particularly is completely on fire right now. So they look at that and say, "Okay, we got it." And we know that we need to have something that looks like closer to that. They came to that conclusion on their own and as opposed to having a push down." – 2012 Q1 Earnings Call

[ii] **"**When I say continuity marketing what I mean is historically Weight Watchers would have a winter marketing campaign in which they might be on air say for most of the weeks of let's say January and February. Then we might go dark. In other words, we don't have any significant above the line marketing, TV, print, whatever, in the period beginning in March going into Easter. Then we might run the spring campaign which may go from Easter five or six weeks depending on the country. Then we would be effectively dark again throughout the course of the summer. Then in September again we would go back on air for say four, six or seven weeks depending on the country. Then we would go dark again throughout the rest of October, a chunk of October and November and then December.

We define continuity marketing as running marketing during traditionally sort of slow times. For example, running marketing in June and July, either prints, daytime TV or whatever the case may be. When I say continuity marketing that is what I mean.

So in the particular case of the U.K. what they were doing was they were running advertising during those summer months and they were combining it with some effective promotions that the depth of the discount was not that significant but the consumer response to the language being used was significant. In other words they were promotions that didn't cost us a lot of money but they drove a very good response rate and that allowed the continuity marketing effectively to work.

So that is basically what the U.K. did. **The obviously follow-up question to that is for us to contemplate how that could create opportunities to pursue similar strategies in other countries. That is something currently under evaluation.**" – David Kirchhoff, CEO, 2009 Q3 Earnings Call Transcript

[iii] **"**In our traditional business, we're frustrated that we did not execute our marketing consistently across our markets particularly in the U.K. **However, we continue to learn and refine our marketing playbook. the quality of our marketing has improved substantially over the past five years; we expected to keep improving over the next five years**." – David Kirchhoff, CEO, 2012 Q1 Earnings Transcript

[iv] **"**In early September we launched in NACO our first NACO promotion other than free registration. This particular promotion was a buy-one, get one free, BOGO, promotion in which new enrollees who purchase monthly pass would be credited their second month free. **This promotion had an immediate positive effect on our enrollment trends resulting in effectively a 10-15 percentage point improvement on the trend line during the 7-week promotion period**.

As we expected, we also saw a significant increase in the proportion of new enrollments who were signing up for monthly pass. **Prior to the promotion paid weeks and meetings were trending at 10-12% behind prior year. By the end of Q3 paid weeks were trending at roughly 6-7% behind the prior year.** This was the result of; one, improved enrollment trends. Two, a significant shift in monthly pass presentation.

Therefore, the most important learning from this effort was a confirmation that a more robust offering of promotion and value messages could have a meaningful impact on our volume trends in NACO. This was similar to what we have observed in our international markets. The most significant challenge of this specific BOGO promotion was the depth of the discount. **Assuming average**

retention of eight months per monthly pass subscriber, getting a free month amounts to effectively a 12.5% discount.

This in turn suggests this particular promotion is effectively breakeven on a revenue and contribution basis. As we noted on the last earnings call, the BOGO promotion would have a negative financial impact in Q3 and Q4 of this year due to the timing of revenue recognition. As a result, the BOGO unfavorably impacted our Q3 operating income by approximately $1.5 million and we predict another $3.5 million of negative impact in Q4 for a total of $5 million in 2009. This translates into roughly $0.04 per share for fiscal 2009. Of course, we will recoup this in 2010 when we will have the benefit of all of the incremental volume without having to take any additional revenue dilution associated with the discount.

While we were conducting the BOGO promotion this fall we were also taking a major market research effort to study other promotional messages that could have a positive impact on volumes. That work is now done and we have identified a variety of other new promotions that should drive volume as effectively as the BOGO but without nearly as steep a discount. We plan to launch one such promotion for the winter campaign in January 2010.

…

Jerry Herman - Stifel Nicolaus

Let's start with promotions if we can. I appreciate the feedback on that. You were good enough to quantify the impact of the promotional activity. Is there a way to quantify the volume impact? That is part A of the question. Part B is, you reference the possibility of doing some of that next year in the next diet season. Should we assume you are likely to do that throughout 2010 in the key diet seasons?

David Kirchhoff

The answer to your first question is as I mentioned during my remarks what we saw from a volume perspective, I mentioned two different metrics. **One I mentioned is during the 7 weeks in which we are running a promotion we estimate that we saw about a 10-15% improvement on the enrollment trend line**. So that was sort of an immediate like-for-like response to the promotional offer. That was the first metric we mentioned. **The second metric we mentioned was we started paid week in the beginning of the quarter as running at roughly Minus 10% to minus 12% and we ended the quarter at minus 6% to minus 7% and most of that, if not all of that, was a result of the promotion**. So that is the direct impact it had on volumes.

To answer your second question, we ran the BOGO knowing it was going to be a significant promotion and it felt like the right promotion for us to run during a typically slow season. **We knew it had a relatively high hurdle rate in terms of overcoming the discount in terms of the amount of lift it would have to provide but we really wanted to get a sense for it because we hadn't historically done promotions other than free registration**. We really wanted to get a sense for how this new kind of promotion could potentially impact our business as well as how we would execute it through the field because it was something different than what our service providers were used to. So it was a significant learning effort for us.

While we were doing it, as I mentioned during the remarks, we were doing some pretty comprehensive market research in which **we were testing 50-100 different potential promotional messages to understand which ones could potentially provide the most response to our business in terms of intent to purchase while also understanding the economic impact of each**. So we absolutely planned on running new promotions with perhaps new promotion language that you may not have seen before as we get into 2010, it would be our expectation we could do that identifying promotion that would have hopefully, and should have, similar effect on volume that we saw with the BOGO promotion but without nearly as much revenue dilution. So that work is still going in terms of planning at the calendar for 2010. We do see that as a growth lever as we go into next year" – David Kirchhoff, CEO, 2009 Q3 Earnings Transcript

[v] "Second, if you look at the digital side, what we -- what -- the conclusion we're increasingly coming to is that -- again, the point I would make with digital advertising is that **there's a presumption for years that if somebody merely saw a banner ad, in the way that the digital agencies do a lot of their analytics metrics, if somebody saw a digital banner and then 2 days later they signed up, that the digital banner would get credit for it, the banner will get credit for it and then you would continue advertising against that banner ad**. **We increasingly became skeptical that this was still true**. **And so we began a series of tests that ultimately led us to the conclusion that we could significantly tighten up and optimize our digital advertising with literally no lost volume**. **And so far, that's actually what we found, is that by the reductions we've made in digital advertising spend by optimizations has resulted in virtually no loss of volume**. So it's almost purely profit-accretive. In other words, that reduction in digital advertising spend is not having any impact on our ability to recruit people in. For the duration of the year, these are going to be that types of things that are going to be different. It's going to be a somewhat of a different advertising strategy in summer, which is typically a low-

enrollment period anyway, in addition to not having a men's campaign in fall. Other than that, throughout the course of the year, there's really no change other than the reduction in the digital advertising. And in that sense, what we have no interest in doing is pulling back on any of the things that we typically do to bring in our core market, either on the meeting business or online business. It was much more of a pre-calculated strategy that we were taking for tightening up how we do things from an advertising point of view." – David Kirchhoff, CEO, 2013 Q1 Earnings Transcript

Capital Allocation

- All acquisitions were for
    - Franchises
        - Attractive from a strategic and a financial standpoint
        - There are synergies in G&A
    - Weightwatchers.com
        - Paid $381 million for the remaining interests in Weightwatchers.com
            - Previously owned about 20%
        - This is a great investment
            - In 2012, Weightwatchers.com made
                - $508 million sales
                - $260 million operating income
    - From 2001 to 2012, Weight Watchers paid $1,046 million for acquisitions
        - Organic meeting attendance declined
            - Grew until 2008
        - EBITDA increased $339 million
            - $208 million in 2001
            - $547 million in 2012
        - A lot of the increase was thanks to the launch of monthly pass in 2006
            - Improve revenue per customers
        - But we can look at the period from 2001 to 2007
            - Weight Watchers spent $595 million in franchise acquisitions
            - Offline EBITDA increased $193 million
                - $208 million in 2001
                - $401 million in 2007
            - That suffices to say the acquisitions created great value
                - In 2012, less than 17% of worldwide attendance was at franchised operations
- Beside the acquisitions, Weight Watchers maximize shareholder value through leveraging and returning cash to shareholder
    - Paid about $52 million dividend annually
    - Return over $3.3 billion through share repurchase since 2001

        - Reduced over 47% of total outstanding shares
            - 105,600,658 outstanding shares in 2001
            - 55,754,372 outstanding shares in 2012
        - Don't pay attention to price with share repurchase[i]
- They increased debt to finance significant share repurchase twice
    - Increased almost $800 million debt in 2007
        - Repurchased over $1 billion
            - 19 million shares
    - Increased over 1.3 billion debt in 2012
        - Repurchased over 1.5 billion
            - 18.3 million shares
- Current debt to EBITDA is 4.7
- Total debt is $2.4 billion
    - Revolving credit facility
        - $250 million
            - Mature on April 2018
            - Current balance is 0
            - $249 million available to be used for working capital and other purposes
                - LIBOR + 2.25%
    - Term Facilities
        - $300 million due April 2016
            - Tranche B-1 Term Facility
            - 3.04% effective rate
                - LIBOR + 2.75%
                - Minimum 0.75%
        - $2.1 billion due April 2020
            - Tranche B-2 Term Facility
            - 3.75% effective rate
                - LIBOR + 3%
                - Minimum 1.75%
        - The applicable margin will increase 0.25% if WTW receive
            - BB- rating from S&P
            - Ba3 from Moody
    - The Term Facilities do not require the Company to maintain any financial ratios
    - WTW should have borrowed long-term fixed debt

        - A little bit more expensive
        - But safer
- We can expect future use of cash in
    - Franchise acquisition
    - Debt reduction
    - Dividend
        - No dividend in near term
    - Share repurchase
    - They will keep leveraging up and deleveraging
        - Controlled by Artal Group
            - Artal group bought Weight Watchers from Heinz in 1999
                - Took Weight Watchers public in 2001
            - Currently owns 52% of Weight Watchers
                - Able to control election and removal of directors
                - Determine corporate and management policies, including
                    - Mergers and acquisitions
                    - Payment of dividends
        - Whenever WTW repurchases shares, Artal Group sells an appropriate amount to maintain 52% ownership
            - They'll get 52% of the total cash return
            - Stock price is not important
        - Leveraging up allows Artal Group to take cash out ahead of future FCF

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[i] "With respect to the tender, keep in mind the reason for doing the tender was because **we've gone to a point that we had felt that our capital structure had become inefficient with relatively high weighted average cost to capital, because we are so much heavily weighted toward equity and so we felt that this was a business that could take on more leverage that could return and distribute back to shareholders and we could have done that in a special dividend or we could have done in the form of a share repurchase, we choose to do in the form of a share repurchase, as a way of returning value to shareholders, while improving the efficiency of our capital structure and we made the decision to do that when we did, because the debt markets was there and everything else was sort of the timing was appropriate and so we made a independently of that, we weren't trying to time the market and we believe that you know while again we are disappointed and**

frustrated by some of the specifics around Q1, it has not changed our perspective on the long-term and frankly medium-term growth prospects for those business which is all the reasons I have been incredibility excited about it throughout last year going into this year and going to next five years all those things are in place and I think ultimately I have absolutely no doubt in my mind what so ever that we are going to be driving significantly shareholder value that is going to continue to validate that the decision we made with the tender was a really smart one." – David Kirchhoff, 2012 Q1 Earnings Call Transcript

Value

- Private market price
    - No one would acquire WTW other than Artal Group
        - They control 52% of the company
    - WTW's strong FCF make it an ideal target for PE firms
    - WTW has a lot of debt now so PE firm wouldn't be able leverage more
        - 2.4 billion debt
        - 4.2 Net Debt/EBITDA
    - EV/EBIT is low on a normal basis
        - At $22.1 per share, market cap is $1,250 million
        - EV is $3,525 million
        - => EV/5-year average EBIT is 7.8
        - EV/5-year average EBITDA is 7.2
    - As EBITDA declines in near term, WTW can be acquired cheaply
        - EBITDA in near term might be between
            - $250 million, and
            - $340 million
        - At 10 times EBITDA, the price is between
            - $4 per share, and
            - $20 per share
    - => The risk is WTW would be acquired cheaply
        - At an adequate current EV/EBITDA
        - But low EV/normal EBITDA
- Absolute value
    - 5-year average EBIT is a good benchmark for normal earnings
    - WTW's marketing is cyclical
        - The business is marketing-driven
        - WTW refresh their programs every 4 or 5 years
        - WTW get a lot of members when
            - WTW has program news
            - Marketing is effective
        - After a peak, WTW can either
            - Spend more in marketing to maintain revenue
                - Lower operating income
            - Reduce marketing expend and see revenue decline
                - Lower operating income

- 5-year average EBIT has always increased
  - 2006: 13.1% growth
  - 2007: 8.7% growth
  - 2008: 6.3% growth
  - 2009: 2.7% growth
  - 2010: 4.6% growth
  - 2011: 8.4% growth
  - 2012: 3.5% growth
  - 2013: 1.6% growth
- 2014's normal earnings would decline if 2014 EBIT is lower than 2009 EBIT
  - It's likely
- There's good reason to expect 5-year average EBIT to increase overtime
  - New marketing up-cycle can reach higher than the last marketing up-cycle
    - Inflation
    - Bigger group of past members
    - Bigger addressable market
- At $22.1 per share, EV/normal EBIT is 7.8
  - => attractive
- WTW deserves 13 EV/normal EBIT

Growth

- The online business can continue to grow
    - Open up new market opportunities
    - Online subscribers are
        - Younger
        - Has less weight to lose
        - Higher than average income
        - Higher than average education
        - Seek a less intensive form of behavior modification[i]
    - Many people want to do weight loss programs in private
    - The online program can attract men
        - Men don't historically face the same kind of pressure around weight that women do
        - That can be changed due to
            - Health awareness
            - Media pressure
        - So, Weight Watchers is investing in advertising to men
            - Especially with Weight Watchers online
                - Men can do the program in private
                - 15% of online subscribers are men
            - Weight Watchers had Charles Barkley as the male spokesperson
            - In the U.S., they advertise to men during only 15 to 16 weeks a year[ii]
                - Can apply the marketing playbook and advertise in more weeks
- Online business profit will grow faster than sales
    - A lot of fixed cost is in
        - Software
        - Web development
    - There's no more cost to serve a new member
        - Need only customer acquisition cost
    - Operating profit grew tremendously
        - Sales
            - 2009: $198 million
            - 2012: $508 million

        - Operating profit
            - 2009: $63 million
            - 2012: $260 million
                - More than the offline business's $250 million
- The online business will somewhat cannibalize the offline business
- But there's also great potential in the B2B business
    - Subsidize model anywhere from 50% to 100% can increase 2 to 3 times the penetration[iii]
    - There's great benefit for healthcare plan to subsidize Weight Watchers
        - Obese has 40% higher health care cost than a healthy weight counterpart[iv]
        - There are about 25 million diabetic adults in the U.S.[v]
            - Healthcare cost is about $180 billion a year
            - 70 million America are now pre-diabetic
            - 10% sustained weight-loss can reduce the risk of Type 2 diabetes by close to 60%[vi]
        - In theory, healthcare plan can reduce cost by educating members
            - But studies show that using Weight Watchers is much more effective than trying to reduce weight on a self-help basis or with a doctor
    - Weight Watchers has the advantage over other commercial competitors in getting B2B customers
        - Lower cost
            - Weight Watchers: $42.95 monthly pass fee
                - $18.95 online monthly fee
            - Jenny Craig: $400 monthly
            - Medifast: $250 monthly
            - NutriSystem: $250 monthly
- It's worth mentioning that an online subscribers is as valuable as an offline member
    - Online subscribers stay for 9 months
        - Monthly fee is $18.95
        - Total revenue is $170.55
        - Operating profit is over $88
    - Monthly pass subscribers stay for 8 months
        - Monthly fee is $42.95
        - Total revenue is $343.6

        - Using high 30% operating margin
            - Operating profit is $103
        - Right now, offline operating margin is only 19%
            - Lower margin is partly due to investments in growing the B2B business[vii]
    - So, online growth can bring as much value as offline growth
- The market is so huge
    - 70% of all American are overweight or obese
    - 78.1 million American adults are obese
    - 90.6 million Americans are obese
    - 25 million American adults are diabetic
    - 78.5 million Americans are pre-diabetic
    - WHO projects that by 2015
        - 2.3 billion people will be overweight worldwide
        - 700 million people will be obese
- As of the end of fiscal 2012, Weight Watchers had
    - 1.8 million active online subscribers
    - 1.4 million Monthly Pass subscribers globally
- Future prospect in international markets is great
    - Both online and offline
- So, it's safe to expect long-term growth of 5%

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[i] "What we've seen is that, over and over again, is that **the kind of person that's gravitating toward online does tend to be somewhat different and have a somewhat different set of needs than the kind of people that are gravitating toward our meeting**. And so we have always believed that Weight Watchers online was a primarily incremental product in terms of the consumers that it was bringing in, based on everything we observed. **A little bit less weight to lose, looking for a little bit less intensive form of behavior modification, kind of wired in a different way**.

What I find interesting, I was just in a meeting out in Connecticut, a couple of weeks ago, and there was a guy, which I'm always glad to see, there was a guy who was having great success going to the meeting, and he had gone last year as well with maybe not quite as much success, but he is going gangbusters this year, and the leader asked him, what's working for you this year? He said, well, I'm tracking for the first time. She said, well, what were you doing last year? He said I wasn't tracking; I was sort of vaguely following the program. And she said, well what changed? He said the IPhone. He said it made it really easy to do it. It's right in my pocket. There's always a reason to track.

But he's the same guy who was also saying that he couldn't do it without the benefit of the weigh-in and the support of the group and everything you learn from the group. And so for him, didn't want to have to choose; he wanted it all. He wanted all the tools and all the resources.

And so what we find is that our most efficacious product is actually both. When I see social networking, I don't see it as a replacement to meetings; I see it as a complement to meetings. When I see tools like the iPhone and the Internet, I don't see it as a replacement to meetings, but I see it as a complement to meetings. And I continue to believe that it's going to be forever. **The gold standard is going to be a behavior therapy methodology that relies both on the benefit of face-to-face interaction, accountability and support that goes with it, along with the convenience and connectivity that you get from technology**.

And what I love of what we have at Weight Watchers in terms of our assets is we don't have to arbitrarily choose. We can let the Internet business grow to some tastes, and we can continue to support its growth in an aggressive way. And at the same time we'll also invest heavily in our face-to-face service, because we fundamentally believe in it as a behavior therapy methodology. And so, our view is that the right strategy is to push both and where possible find ways to connect the two." – David Kirchhoff, 2009 Q4 Earnings Call Transcript

[ii] **"Greg Badishkanian** - Citigroup

Great, thank you. If you look at just keeping on men's over the next year or two, how big do you think that could be as a percentage of your North American business?

David P. Kirchhoff - President and Chief Executive Officer

It's a tricky one to dimensionalize, but let me provide a couple of statistics for you to maybe help sort of ballpark it. And then I can talk a little bit about where we are right now versus what we haven't gotten to going forward. So first half, in terms of what is the aggregate theoretical potential. **Men are as likely to suffer from obesity as women and their health effects that they experience are the same is what woman experience, and so that kind of net aggregate need is at least as high for men as it is for women**.

However, they are about half as like we reduce something about it. **They tend not to face at least today the same sort of pressure around media and having a feel like they need to looks and everything else that you see with women. So they have been historically unlikely to take action**. **So if you take that 50% is likely to do something about it that would suggest that a**

theoretical mix of men would be say a third that's I believe that the willingness of men to be able to weight issue will increase over time as increased recognition of health effects of obesity would become more, more clear. Then there is what we are doing, if we're currently say for example, 15% in Q1 what stands between us in getting to that higher level as we go into the future. and **within the U.S., I would say that if you look at for example, 2012, we're going to be on I think with guys, men's advertising a total of 15, 16 weeks for the full year and still not a huge media weights. And so one opportunity for us is to use the same playbook we used for Weight Watchers Online to increase media weights into beyond more weeks, which is a formulative work really well for Weight Watchers Online. The other opportunity for us is that we have not yet launched Weight Watchers online for man in any of our international markets and that's also an opportunity that we believe is going to be in front of us.**" – 2012 Q1 Earnings Call Transcript

[iii] **"**And what I would tell you on the last point is that we have a number of large corporate clients now and in virtually every case where they go to a significantly subsidized model, so not even reimbursement, **subsidized model anywhere from 50% to 100% we almost always see a radical shift 2 to 3x in the penetration of the people within that population that are taking advantage of the services offered for example through Weight Watchers.**" – Credit Suisse Annual Health Conference, 10 November 2011

[iv] **"**I recently had the opportunity to participate and present at the CDC's first Annual Weight of the Nation conference in Washington, D.C. It was an honor for us to have the opportunity to be one of the very few for-profit companies invited to present. **During that conference several well-regarded economists presented their research demonstrating that obesity now accounts for approximately $137.0 billion a year in annual healthcare costs, or 10% of the total U.S. healthcare budget**.

The same research demonstrated how an obese individual has healthcare costs that are approximately 40% higher than their healthy-weight counterparts. This increased expanse has shown to have significant impact across payer groups, including private insurance, Medicaid, and Medicare." – David Kirchhoff, CEO, 2009 Q3 Earnings Call Transcript

[v] **"**Specifically you know when I think about diabetes, you know it's give or take 10% to 11% of the adult population, so about **25 million people**. The CDC came out with their forecast about a year ago that suggested by the year 2050, one out of every three Americans would be diabetic. **Today this is a $180 billion year condition**. Do the math and you can see the difficulty that is facing our healthcare system. You can begin to get an appreciation for why we're seeing

healthcare premiums for example in self-insured companies increasing 8% a year over the past 10 years. You can see how we now have an entitlement system that is very much at risk.

One way to kind of dimensionalize this is that in actually pre diabetics there's been a more recent forecast that it could be north of **70 million Americans are now pre diabetic**. **So as these folks get older, they will sadly be moving into this bucket of people who currently have diabetes. It is a significant issue.**", David Kirchhoff, CEO, JP Morgan Global HealthCare Conference, 11 January 2012

[vi] **"**The good news is, is that to affectively address this, you do not need to manufacture swimsuit models; that's not what this is about. **This is about helping people get to a 10% sustained weight loss. Doing so will reduce your risk of Type 2 diabetes by close to 60%.** It is absolutely possible, but it is not easy. And I think part of the problem with obesity is the entire way we conceptualize addressing the issue. I think in many respects, in many different pockets of the population, including in the healthcare community it's misunderstood and often wrong.", David Kirchhoff, CEO, JP Morgan Global HealthCare Conference, 11 January 2012

[vii] **"**David P. Kirchhoff - Chief Executive Officer, Executive Director, Chief Executive Officer of Weightwatchers Com and Acting President of North America

We're not ready to give a detailed breakout of what those things are, but let me describe thematically what we're spending on, which is 2 areas in the B2B space. It's principally 2 areas. **One is the -- this health services organization, which is a collection of professionals largely recruited from health services companies, account management, project management, technical expertise, marketing folks, people like that. We're virtually building a company within a company, if you will. And so part of what we've been adding therefore is sort of headcount associated with that, and that's going to be showing up in the G&A line**. **In addition, and ultimately this is going to be the biggest area of investment, is going to be the data collection, which is the outfitting of service providers with laptop computers, tablets, whatever the choice ultimately is going to be, to allow them to do real-time data capture at point of weigh-in**. We have been gradually scaling that effort up. A lot of the investment for that is going to be continuing to build somewhat in the second half with an eye toward probably a more aggressive rollout as we get into 2014 and maybe a little bit beyond. But that's -- those are really the primary areas of investment. **While we've been doing that, as you heard us mention, what's been good particularly in terms of the health services organizational**

investment, is that, that's been backed against the strategic sales revenue channel that we've now been bringing in, which has been growing sort of nice double-digit revenue as we've been going into this year." – David Kirchhoff, 2013 Q1 Earnings Transcript

Misjudgment

- We like family-controlled business
    - Weight Watchers has been controlled by Artal group since 1999
    - The biggest risk to Weight Watchers' business is the management doing something that damage the reputation
        - We think Artal group is a great guardian
- We don't know much about Artal Group
    - They kept constant ownership in WTW
    - But they can take the company private again
        - Current EV/EBITDA is not low
        - This can be a big risk
- Meeting attendance in other international markets doesn't reflect our expectation
    - 3.2 million in 2000
    - 3.4 million in 2004
    - 3.0 million in 2006
    - 2.1 million in 2008
    - 2.0 million in 2010
    - 1.7 million in 2012
    - Macro condition in other international market was better than the U.S, the U.K or the Continental Europe
    - The general trend is people are getting fatter
    - Meeting attendance should grow better in other international markets
- We don't know how much meeting attendance decline was due to online cannibalization
- We might be too optimistic about the online business
    - We don't have data about the strength in retention or recruiting rejoins
        - This is the key indicator of the online business's strength
    - We just have the management's words
    - We read blogs in Weight Watchers community
        - See that many people use both free apps and WW online
        - See some people return to WW online after switching to My Fitness Pal
    - So, our observation is in line with what the management said
    - But we might have looked at a skewed sample
        - Another extreme is reading threads in myfitnesspal.com
        - Many people there feel My Fitness Pal is good for them

    - We can confidently say that there will be many people see value in WW online and subscribe
        - The price is low compared to the benefit of successful weight-loss
        - WW online can effectively position as a program, not just an app
        - But we don't know for sure WW online will grow or decline
        - The huge weight loss market might make us more optimistic than we should otherwise
- We don't know exactly that share repurchase will create value
    - WTW consistently repurchase share
    - Two big purchases when leveraged up
        - 2007: 19 million shares
        - 2012: 18.3 million shares
    - They don't care about price
        - Artal Group always get 52% of the total cash return
    - So, the number of repurchased shares may really depend on the price at the time WTW leverages up
        - Investors can always sell if when the company repurchase at high price
- The stock went up and down at lot after earning releases
    - So, we might think the decline this time is merely the result of reaction to short-term problem
    - But the problem can be long-term
        - The online business cannibalize the offline business
        - The online business is less unique than the offline business

Conclusion

- WTW has one of the widest moat
- Durability is great
    - Better than consumer products company
    - No private label risk
- Product economics is terrific
    - Virtually infinite return on capital
    - Don't need to retain earnings
- The biggest risk is the stock price can decline and Artal acquires WTW at some premium
    - But why would they?
        - WTW already has a lot of debt
    - Suppose they acquire at 25% premium to $22
        - EV of the deal is $3,822 million
        - EV/5-year average EBIT would be 8.44
        - Unlevered yield is 0.65/8.43 = 7.7%
        - With leverage, the yield isn't terribly attractive
- Debt is quite safe
    - See the Debt Note
- The key questions are
    - Can WTW revive its brand?
        - No specific damage to the WTW brand recently
            - No negative publicity
        - More than 40 million people have used MyFitnessPal
            - A huge negative impact on WTW's recruitment recently
                - Influences people returning to WTW, words of mouth, etc.
    - Are free apps a long-term threat?
        - In 2018, free apps wouldn't be considered new and unique
        - WTW has always competed with free alternatives
            - It's always been the case that people can diet, exercise, etc. on their own
        - Is an app enough for WTW's core customers
            - An app makes it easier to keep track of diet and exercise
            - WTW's core customers can't maintain motivation/commitment on their own

        - Will they stick to MyFitnessPal more than two weeks?
    - Facts
        - There’re people successful with MyFitnessPal
        - Many people use MyFitnessPal for less than two weeks
- Quan’s best answers
    - There’re still people who need a weight-loss program
    - They’re the most profitable customers
    - WTW is now in a down marketing cycle
    - WTW can return to a new high
    - 5-year average EBIT is a good benchmark for normal earnings

Debt

- Total debt is $2.4 billion
  - Revolving credit facility
    - $250 million
      - Mature on April 2018
      - Current balance is 0
      - $249 million available to be used for working capital and other purposes
        - LIBOR + 2.25%
    - Requires WTW to maintain the Consolidated Leverage Ratio if the Revolving Facility exceed 20% of revolving commitments
      - => WTW can only count on access to $50 million of the revolving credit facility
  - Term Facilities
    - $300 million due April 2016
      - Tranche B-1 Term Facility
      - 3.04% effective rate
        - LIBOR + 2.75%
        - Minimum 0.75%
    - $2.1 billion due April 2020
      - Tranche B-2 Term Facility
      - 3.75% effective rate
        - LIBOR + 3%
        - Minimum 1.75%
    - The applicable margin will increase 0.25% if WTW receive
      - BB- rating from S&P
      - Ba3 from Moody
    - The Term Facilities do not require the Company to maintain any financial ratios
    - WTW must repay 0.25% per quarter
      - $24 million a year
- Total cash balance is $175 million
- WTW expect 2014 interest expense to be $125 million
  - Current EBIT is $461 million
    - 5.2 Debt/EBIT
    - 4.8 Net Debt/EBIT

- The lowest EBIT in history was in 2001
    - $195 million
- EBIT margin is about 30% since 2002
  - Min: 25%
  - Max: 37%
  - Median: 30%
  - Mean: 30%
  - STDEV: 3%
  - CV: 0.11
- If sales decline 50% and EBIT margin is 20%, EBIT would be
  - $1,827 * 0.5 * 0.2 = $183 million
    - => Able to survive
      - $125 million interest
      - $50 million CapEx
    - Interest rate can go up to about 6%
  - The management expect 2014 revenue to be $1.4 billion
    - 5% decline in gross margin
      - 58% in 2013
      - => 53% in 2014
    - Expect to cut
      - $60 million market expense
        - Realized in 2013
      - $90 million G&A
        - Realized between 2013 and 2015
    - => EBIT would be between
      - $201 million
        - = 1,400 * 0.53 – 296 (marketing) – 245 (G&A)
      - $291 million
        - = 1,400 * 0.53 – 296 (marketing) – (245-90) (G&A)
    - => able to pay interest expense before paying taxes
- Current net debt is $2,215 million
  - 3-year average EBIT is $506 million
  - 5-year average EBIT is $453 million
    - Conservative estimate of normal earnings given
      - The crisis
      - The growth in online business
        - 2008 EBIT: $63 million

            - 2012 EBIT: $260 million
- Earnings will be lower than normal in 2014 and 2015
- But if WTW has an up cycle, earnings and normal earnings will improve
    - WTW had $1.4 billion revenue in 2009
    - Never made more than $1.4 billion before 2007
    - EBIT margin was consistently over 30% before 2009
    - From 2002 to 2006, average EBIT was $320 million
    - WTW can cut a lot of costs today
    - But they're not reducing technology or B2B investment
    - They're spending a lot on marketing
    - They're trying to achieve a new peak revenue
        - That makes sense
            - Total addressable market grows overtime
            - The number of past WTW users grows overtime
            - Inflation
            - New channels like online and healthcare won't have 100% cannibalization rate
- @ $453 million average EBIT
    - From 2014 to 2020, total conservative EBIT would be $3,171 million
    - Total interest expense at 5% average rate would be
        - $120 million a year
        - $960 million in 8 years
            - Total interest expense would be lower when WTW reduces debt over the period
    - Estimate total FCF would be (3,171 – 960)*0.65 = $1,437 million
        - That's enough to bring debt to a safe level
        - There's no need to issue equity
- @ $300 million average EBIT
    - From 2014 to 2020, total conservative EBIT would be $2,100 million
    - Total interest expense at 5% average rate would be
        - $120 million a year
        - $960 million in 8 years
            - Total interest expense would be lower if WTW reduces debt over the period
    - Estimate total FCF would be (2,100 - 960)*0.65 = $741 million

- => $1,474 million net debt in 2020

Free Apps

- The treadmill to hell
  - Online solutions cannibalize the meeting solution
    - From 2008 to 2012
      - Offline sales: declined 3.4%
      - Online sales: grew 269%
      - The economic condition had some impact on the offline business
        - But the online business might cannibalize somewhat
    - The introduction of online program is like a psychographic segmentation
      - Some people don't want to go to a group[i]
      - Online is cheaper[ii]
      - Some people don't want to travel far to the meeting
      - Some people need peer pressure at the meeting[iii] [iv]
  - WTW's online business doesn't have a wide moat
    - Internet revenue declined for the first time in Q4 2013
    - Interests in free apps and activity monitors intensified[v]
  - WTW has $2.4 billion debt
  - Revolving credit facility
    - $250 million
      - Mature on April 2018
      - Current balance is 0
      - $249 million available to be used for working capital and other purposes
        - LIBOR + 2.25%
  - Term Facilities
    - $300 million due April 2016
      - Tranche B-1 Term Facility
      - 3.04% effective rate
        - LIBOR + 2.75%
        - Minimum 0.75%
    - $2.1 billion due April 2020
      - Tranche B-2 Term Facility
      - 3.75% effective rate
        - LIBOR + 3%

            - Minimum 1.75%
        - The applicable margin will increase 0.25% if WTW receive
            - BB- rating from S&P
            - Ba3 from Moody
        - The Term Facilities do not require the Company to maintain any financial ratios

- Can Weight Watcher survive?
    - WTW will have a safe balance sheet if they can have another up cycle
        - See Debt Notes
    - Why wouldn't WTW have another up cycle?
        - No specific damage to the WTW brand recently
            - No negative publicity
        - Free apps are not a long-term threat
- Free apps are not a long-term threat
    - More than 40 million people have used MyFitnessPal
        - A huge negative impact on WTW's recruitment recently
        - Impossible to have effective marketing and new sign-ups while tens of millions of people are trying something new
            - Too much noise
    - In 2018, free apps wouldn't be considered new and unique
    - There are fads for some apps
        - Farmville
        - Candy Crush Saga
        - Etc.
    - Why fads for games faded?
        - People completed the game
        - The game gets harder
        - People get bored
        - The game is no longer new[vi]
    - The similarities between MyFitnessPal and games
        - People uses until completion
        - People get bored
        - There are alternatives
            - But there are more competing games than weight-loss options
    - MyFitnessPal is not as addictive as games
    - Statistics on general free app use are poor

        - 20-30% of people who download a free app never actually uses it
        - 50% open it once or twice
    - Free online things that requires commitment has very poor rate of successful completion
        - MIT and Harvard Massive Online Open Course
            - 4% of people finished the course
            - 50% quit after the first one and two weeks
            - 1/3 got absolutely nothing out of the course
    - Weight-loss success really depends on commitment
        - Some people are heavy users of free apps and succeed
            - Counting points or calories are very good self-monitoring habit
                - It can be addictive like playing games
        - But it's very hard to form this habit
        - Most people use free apps for only 1-2 weeks[vii]
        - They have higher commitment when use Weight Watchers online[viii]
            - WTW's online members stay in the program for 9 months[ix]
- WTW is able to position the brand as a weight-loss program
    - Weight Watchers has been advertise that people can lose weight successfully online
    - Free apps reduced the marketing effectiveness of this message[x]
    - Now, Weight Watchers starts shifting to communicate the full value proposition of Weight Watchers Online
        - A behavior modification program[xi]
- **Conclusion**
    - There are people who succeed in using free apps to reduce weights
    - But it's always been the case that people can diet, exercise, etc. on their own
        - Free apps make it easier for these people
    - An app is not enough a guidance for WTW's core market
        - 4% successful rate of 40 million downloads still leaves 38.4 million potential customers to WTW
        - WTW's core customers can't maintain motivation/commitment on their own
    - WTW never had a big share of the total number of dieters
        - As of the end of FY 2012 (the peak)

            - 1.8 million active online members
            - 1.4 million Monthly Pass subscribers globally
    - WTW just has the biggest share of profits
        - WTW has the most profitable customers
    - The fad for free apps now is similar to the fad for the Atkins diet

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[i] **"**I love WW online! I started when DS was a week old, and I celebrated my 2nd anniversary in April.

It works for me because I'm not a group hug kind of person, had limited time with a newborn and it's a heck of a lot cheaper. I'm also on the computer a lot (especially when I returned to work) and it's so easy to track." said a member with nickname Zwalleby from babycenter.com. For more quotes, read "*Quotes on Different Offline & Online Customerss.docx*"

[ii] "I started the online program April 24th. **For me the issues were time and money. It is much cheaper to join online and since I spend a lot of time on-line anyway**. Not only that but I would have to get my mum who already watches Katie all day while I work etc. to watch her. I didn't think it was fair to my mum. So I figured, I would give it the 3 months online to see how I did and if I felt like I needed the meetings, I would change over.

I have lost 17.6 lbs. so far. (But am 26 lbs. down from what I was last December. Good Luck in whichever way you decide." Said a member from babycenter.com. For more quotes, read "*Quotes on Different Offline & Online Customerss.docx*"

[iii] **"**I do not do the online although I do have access. **Reason I will not hold myself accountable. I need to go to the meeting and have someone watching over me so to speak**. I swear it is like a confessional when I weigh in.

Oh I did bad this week because....LOL

Stephanie" said a member in babycenter.com. For more quotes, read "*Quotes on Different Offline & Online Customerss.docx*"

[iv] **"I have been a member of MFP for 2 years now. By July 2012 I lost 20 pounds, but I was never able to fully commit to the MFP system. Even though I was provided with great tools for success, I still wasn't losing weight. A few weeks ago, I realized that this was because I had no real accountability. I personally joined Weight Watchers because it provides the accountability I am looking for**. My leader encourages us to have a fruit or

veggie with every meal, exercise often, and even encourages eating back some of our exercise points. I like being able to see the same people every week and see how their journey is progressing and share in our triumphs (and failures). I have never felt like I am "dieting", just being cognizant of what I am eating. I do not plan on going to Weight Watchers forever. I plan on attending until I lose 50-70 pounds; since I don't think I could eat less than 30 points a day (right now I have 36 points a day which is about 1450-1600 calories). I say follow whichever "plan" you think you can stick to. For the stage of weight loss I am in right now, I love Weight Watchers (even if I have to pay them $12 a week).", said a member from My Fitness Pal community, http://www.myfitnesspal.com/topics/show/881110-weight-watchers-v-calorie-counting

[v] "At a high level, our Q4 performance of $0.54 per share was in line with expectations as good cost management was partially able to offset a deteriorating top line, **which included the first ever quarterly decline versus prior in Internet revenues. Furthermore, the start of the year is proving to be every bit as challenging as we thought, if not more so. The headwinds from free apps and activity monitors have only continued to intensify and are significantly impacting consumers**. And our marketing efforts in the early part of this year have been less effective than we had hoped putting our top and bottom lines under greater pressure." – Jim Chambers, CEO, 2013 Q4 Earnings Call Transcript

[vi] "Perhaps no company in recent memory epitomizes the mercurial nature of variable rewards quite like Zynga, makers of the hit Facebook game FarmVille. In 2009, FarmVille became an unmissable part of the global zeitgeist. The game smashed records as it quickly reached 83.8 million monthly active users by leveraging the Facebook platform to acquire new players. In 2010, as "farmers" tended their digital crops — while paying real money for virtual goods and levels — the company generated more than $36 million in revenue.

The company seemed invincible and set a course for growth by cloning its FarmVille success into a franchise. Zynga soon released CityVille, ChefVille, FrontierVille, and several more "-Ville" titles using familiar game mechanics in the hope that people would enjoy them as voraciously as

they had FarmVille. By March 2012, Zynga's stock was flying high and the company was valued at over $10 billion.

But by November of that same year, the stock was down over 80 percent. **It turned out that Zynga's new games were not really new at all. The company had simply re-skinned FarmVille, and soon players lost interest and investors followed suit. What was once novel and intriguing became rote and boring**. The "Villes" had lost their variability, and with it, their viability. As the Zynga story demonstrates, an element of mystery is an important component of continued user interest." – *Why Fads Fade: The Inevitable Death of Flappy Bird*, Nir Eyal, 14 Feb 2014, Techcrunch.com

[vii] "**David P. Kirchhoff** - Chief Executive Officer, Executive Director, Chief Executive Officer of Weightwatchers Com and Acting President of North America

No, I don't think it does. Not in the long term. I mean, and I -- so I think there's -- so part of this is there's a near-term issue, as well as, I think, opportunities that are emerging. Let me first off spend a little -- just a quick second, talking about kind of what I see in terms of the emergence of kind of the sort of morass of technology that has sort of encroached into the market at just an unprecedented pace. And what I would -- the way I would characterize it is in devices, as opposed to sort of what I'll call tangential apps as opposed to apps that, I think, try to offer something that's much -- feels much more directly akin to Weight Watchers. So the devices, of course, I'm talking about things like scales, activity monitors, fuel bands [ph], [indiscernible], all that kind of good stuff. The middle group of apps might be really interesting work being done in terms of dining out companion and ways of sort of searching for healthy restaurants and those types of things. And then, the sort of more direct, that feel like sort of closer in substitutes, would obviously be the Lose It!s and MyFitnessPals and those types of applications. The first 2 groups, we see a tremendous opportunity which we have not yet taken advantage of, to co-op them into what our offering, to add value to our offering, to make Weight Watchers Online that much more compelling. And effectively, the strategy was that, it was really going to be a much more aggressive approach in terms of pushing out an open API of strategy, and **that's something that we're working on right now as a way of sort of leveraging other people's technology efforts to add value to our offering.** In terms of kind of the core fundamental value proposition to consumers that fit with the middle Weight Watchers Online, I kind of go back to this: that when you talk to people who do Weight Watchers Online, **they're following a program and**

the technology merely makes it easier and more convenient and more fun for them to follow that program. And it's the combination of those things that ultimately provides the meaningful value that keeps people engaged once they start doing and keeps them engaged for a long time, because the only thing that matters in weight management is extended ongoing engagement, is the only thing that leads to the weight loss, which that is the only value proposition that wins in the long term. I think the question to ask with a lot of these other sort of offerings that are coming up, is that what we're seeing is that our -- and anecdotally, that **there are some people who are going to be hardcore users and some of these apps we're going to have good success with it. But frankly, we believe that the majority of people that are using them are probably using them, frankly, for 1 to 2 weeks and then not using them**. Now the implication of that is it creates near-term pressure on trials because effectively, that customer has been sort of taken out of the market, if you will. But to the extent that the idea of counting calories, which is effectively what you're doing if you're doing, for example, MyFitnessPal, starts to feel tedious and doesn't really recognize that calories are created equally and all those types of things that effectively, we would expect interest in those things to decline over time. I think that the opportunity for Weight Watchers to avoid that kind of commoditization is to continue focusing on what is at the core of us, which is the 50 years of accumulated IP science, the trust in the brand, everything else. Build on those things, more aggressively attach technology, both technology we develop, but also significantly, technology developed by others, in a way that creates a value proposition that is considerably superior to what you're going to get from any one of these individual little apps that's coming out." – David Kirchhoff, former CEO, 2013 Q1 Earnings Call Transcript

[viii] "**I found I was a little more accountable with WW because I'm cheap and I didn't want it to be a waste of money, I guess. I don't know why, really, I just had less trouble "falling off the wagon" with WW**. But I like MFP too; it all depends on your level of self-control. GL!" – *said a member from Theknot.com.*

"**I tried MFP last Jan but wasn't dedicated and didn't log in so through neglect gained another 7 or so pounds**. A friend of mine joined WW the fall and I decided to join as well. Since Oct I have lost 51.1 lbs. WW uses the points plus system. Just introduced the 360 program. I really don't see any difference in the two.

For me I couldn't do it on my own and needed a program to get me started. WW did it. I started out with 29 points a day and am now down to 26. It does cost money but I really needed help (I'm in the military and fitness is important and a big part of the routine. Getting older and with the 50 extra pounds I was carrying around I was afraid I'd have a heart attack or something) and was willing to pay the $50 a month. I like the weekly meetings and info I get. I was curious though to see how the points add up against calories. My 26 points a day work out to 1200 calories and i find that satisfying. I was eating so many empty calories before. WW has really helped me get the boost for a healthier lifestyle I needed

As for MFP I have to say I absolutely love this. It's great for the online support and I do like the online way better than WW. MFP is so much more user friendly and the message boards are awesome. **IMO WW still has work to do with their online program. Actual meetings are their on their strong point and I really enjoy my weekly weigh ins/meeting. So I will continue doing both."** – *Said a member from My Fitness Pal Community*

For more quotes, read "*Quotes on Higher Commitment with Weight Watchers*.docx"

[ix] **"**First quarter Internet revenues grew approximately 11% on a constant currency basis. Paid weeks rose 10%, which was somewhat ahead of our earlier expectations with growth in both the U.S. and International. Continental Europe and Canada had stand-out double-digit performance. That said, sign-ups grew weaker and turned negative in the U.S., though they were up strongly internationally. As a result, end-of-period active subscribers rose 6%. **Importantly, retention remains unchanged at 9 months**. We expect weightwatchers.com paid weeks growth in each quarter this year, albeit at decelerating rates, given the lower sign-up trend in the first quarter. For the year, paid weeks should now be up low-single digits, which is slightly ahead of our prior guidance of flat to up slightly. This outlook assumes the economic and competitive environment remains the same." – Nicholas Hotchkin, CFO, 2013 Q1 Earnings Transcript

[x] **"**Our Weight Watchers Online advertising has done a great job over the past few years of creating awareness for losing weight online and driving trial of our online product **by advertising the fact that you could lose weight successfully online. This worked well for us over multiple years, a time during which there was no meaningful competitive online alternative**.

Over the past year, however, there's been an increase in proliferation of free applications, and Google Trends metrics indicate that consumer interest in these apps is up significantly this January. It's now clear that the weightwatchers.com awareness-driving strategy that has been so successful at driving millions of people in the weightwatchers.com started

losing some effectiveness roughly 6 months ago. We now need to shift gears to leverage the groundswell of people interested in weight loss mobility tools by communicating the full value proposition of Weight Watchers Online, and the behavior modification approach on which it's based.

Our new goal is to convince the growing number of people who are inclined to seek online weight loss help that if they're going to invest their time and effort in trying to lose weight online, they should invest in the best method: Weight Watchers.

What we've been seeing this January is softness in never-member recruitment in Weight Watchers Online but continuing strength in recruiting rejoins and continuing strength in retention. To us this reflects the fact that people who have used Weight Watchers Online, and are therefore aware of the value proposition, are choosing to come back rather than turning to free apps. However, as to those who have not yet experienced the value proposition, we have not connected with them with our marketing.", David Kirchhoff, CEO, 2012 Q4 Earnings Call Transcript

[xi] **"Jerry Herman** - Stifel

Jim, question for you, I know you get this one a lot, but just wanted to get your updated thoughts here on your value proposition, and when I think about that I think about what you charge in price and what it costs you. And it sounds like you're talking about some enhanced services perhaps that implies higher cost. And then likewise can you just address your most recent thoughts on price relative to competition?

Jim Chambers - President & CEO

I won't say too much about price, yes we are looking a range of very significant potential product enhancements. Some would bring more cost and periodically more pricing potential, but that's down the road, we're not at that point of thinking about that yet.

With respect to the other side of the value proposition, if you will, there is a, when we do the research looking at our products, looking at competitive products, clearly at the level of tools versus having a program and a plan at the level of tools **there are things that are increasingly becoming available for free.**

There is a piece of this and it's becoming commoditized. I don't think that's the piece that drive success and therefore I don't think that's the piece that's going to determine the value proposition of our products going forward. We have to put more of the enhancements that you're referring to into the products but we have such a broad field of opportunity that I'm confident that we can do that. But I'm not going to talk too much to pricing in the short-term" – 2013 Q4 Earnings Call Transcript

Takeover

- Risk:
    - Artal Group acquire the remaining 48% of WTW at a cheap price
        - Based on a multiple of current EBITDA instead of normal EBITDA
- Why would they?
    - WTW is a big portion of Artal's portfolio[i]
    - WTW already has $2.4 billion debt
    - WTW is already like an LBO right now
        - This is the pattern
        - Artal keeps control of WTW since the IPO
            - Maintain about 52% ownership of the company
        - Leveraged up and down the company
            - Repurchased over $1 billion in 2007
            - Repurchased over $1.5 billion in 2012
        - Artal got 52% of the cash return by maintaining 52% ownership
    - Acquiring 48% of WTW would require Artal to put in a lot of money
        - Deleverage their own investment
            - => Reduce upside
        - Double risk
            - Double the equity in the stock
            - But solvency problem stays the same
        - Why would they risk more in an additional unleveraged investment but doesn't improve the balance sheet of the highly leveraged company?
    - Artal did a buyback at over $70 per share in 2012
        - That would be discussed in any considering of bids
- The bigger risk is the need for equity offerings to pay debt
    - See Debt Note

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[i] http://www.sec.gov/Archives/edgar/data/1053906/000114036114007106/xslForm13F_X01/form13fInfoTable.xml