

USANA HEALTH SCIENCES INC

Form 10-Q

August 07, 2008

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR
15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 28, 2008

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR
15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission file number: 0-21116

USANA HEALTH SCIENCES, INC.

(Exact name of registrant as specified in its charter)

Utah
(State or other jurisdiction
of incorporation or organization)

87-0500306
(I.R.S. Employer
Identification No.)

3838 West Parkway Blvd., Salt Lake City, Utah 84120

(Address of principal executive offices, Zip Code)

(801) 954-7100

(Registrant's telephone number, including area code)

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The number of shares outstanding of the registrant's common stock as of July 30, 2008 was 16,301,934.

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USANA HEALTH SCIENCES, INC.

FORM 10-Q

For the Quarterly Period Ended June 28, 2008

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands)

	December 29, 2007 (1)	June 28, 2008 (unaudited)
ASSETS		
Current assets		
Cash and cash equivalents	\$ 12,865	\$ 9,982
Inventories	19,439	22,038
Prepaid expenses and other current assets	11,639	9,545
Deferred income taxes	2,049	2,711
Total current assets	45,992	44,276
Property and equipment, net	52,061	60,163
Assets held for sale	607	607
Goodwill	5,690	5,690
Other assets	4,778	5,409
	\$ 109,128	\$ 116,145
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
Accounts payable	\$ 8,111	\$ 8,753
Other current liabilities	32,074	33,326
Total current liabilities	40,185	42,079
Line of credit	28,000	9,835
Other long-term liabilities	2,305	2,820
Stockholders equity		
Common stock, \$0.001 par value; authorized 50,000 shares, issued and outstanding 16,198 as of December 29, 2007 and 16,413 as of June 28, 2008	16	16
Additional paid-in capital	7,525	11,759
Retained earnings	30,108	47,803
Accumulated other comprehensive income	989	1,833
Total stockholders equity	38,638	61,411
	\$ 109,128	\$ 116,145

(1) Derived from audited financial statements.

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(in thousands, except per share data)

(unaudited)

	Quarter Ended	
	June 30, 2007	June 28, 2008
Net sales	\$ 107,542	\$ 109,208
Cost of sales	22,443	21,884
Gross profit	85,099	87,324
Operating expenses:		
Associate incentives	43,280	45,603
Selling, general and administrative	22,531	25,135
Research and development	902	618
Total operating expenses	66,713	71,356
Earnings from operations	18,386	15,968
Other income (expense):		
Interest income	87	85
Interest expense	(403)	(123)
Other, net	303	(27)
Other income (expense), net	(13)	(65)
Earnings from continuing operations before income taxes	18,373	15,903
Income taxes	6,966	5,755
Income from continuing operations	11,407	10,148
Loss from discontinued operations, net of tax benefit	(93)	
Net earnings	\$ 11,314	\$ 10,148
Earnings per common share		
Basic		
Continuing operations	\$ 0.68	\$ 0.62

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Discontinued operations			
Net earnings	\$	0.68	\$ 0.62
Diluted			
Continuing operations	\$	0.66	\$ 0.62
Discontinued operations			
Net earnings	\$	0.66	\$ 0.62
Weighted average common shares outstanding			
Basic		16,709	16,393
Diluted		17,163	16,460

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(in thousands, except per share data)

(unaudited)

	Six Months Ended	
	June 30, 2007	June 28, 2008
Net sales	\$ 208,220	\$ 210,778
Cost of sales	43,029	43,386
Gross profit	165,191	167,392
Operating expenses:		
Associate incentives	82,829	86,967
Selling, general and administrative	44,032	50,909
Research and development	1,832	1,591
Total operating expenses	128,693	139,467
Earnings from operations	36,498	27,925
Other income (expense):		
Interest income	394	183
Interest expense	(408)	(362)
Other, net	472	43
Other income (expense), net	458	(136)
Earnings from continuing operations before income taxes	36,956	27,789
Income taxes	13,749	10,094
Income from continuing operations	23,207	17,695
Loss from discontinued operations, net of tax benefit	(207)	
Net earnings	\$ 23,000	\$ 17,695
Earnings per common share		
Basic		
Continuing operations	\$ 1.34	\$ 1.08

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Discontinued operations		(0.01)	
Net earnings	\$	1.33	\$ 1.08
Diluted			
Continuing operations	\$	1.30	\$ 1.08
Discontinued operations		(0.01)	
Net earnings	\$	1.29	\$ 1.08
Weighted average common shares outstanding			
Basic		17,302	16,378
Diluted		17,813	16,460

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

Six Months Ended June 30, 2007 and June 28, 2008

(in thousands)

(unaudited)

	Common Stock Shares	Common Stock Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
For the Six Months June 30, 2007						
Balance at December 30, 2006	17,859	\$ 18	\$ 15,573	\$ 44,251	\$ 355	\$ 60,197
Comprehensive income						
Net earnings				23,000		23,000
Foreign currency translation adjustment, net of tax benefit of \$184					253	253
Comprehensive income						23,253
Common stock retired	(1,712)	(2)	(18,958)	(54,038)		(72,998)
Common stock awarded to Associates	1		47			47
Equity-based compensation expense			3,220			3,220
Common stock exercised under equity award plan, including tax benefit of \$1,031	117		3,232			3,232
Balance at June 30, 2007	16,265	\$ 16	\$ 3,114	\$ 13,213	\$ 608	\$ 16,951
For the Six Months Ended June 28, 2008						
Balance at December 29, 2007	16,198	\$ 16	\$ 7,525	\$ 30,108	\$ 989	\$ 38,638
Comprehensive income						

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Net earnings				17,695			17,695
Foreign currency translation adjustment, net of tax benefit of \$438						844	844
Comprehensive income							18,539
Equity-based compensation expense				2,858			2,858
Common stock exercised under equity award plan, including tax benefit of \$1,028			215	1,376			1,376
Balance at June 28, 2008	16,413	\$	16	\$	11,759	\$	47,803
						\$	1,833
							61,411

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Six Months Ended	
	June 30, 2007	June 28, 2008
Increase (decrease) in cash and cash equivalents		
Cash flows from operating activities		
Net earnings	\$ 23,000	\$ 17,695
Adjustments to reconcile net earnings to net cash provided by operating activities		
Depreciation and amortization	2,457	3,171
(Gain) loss on disposition of property and equipment	73	(78)
Write-down of assets held for sale	25	
Equity-based compensation expense	3,220	2,858
Excess tax benefit from equity-based payment arrangements	(977)	(1,028)
Common stock awarded to Associates	47	
Deferred income taxes	(844)	(1,791)
Provision for inventory valuation	691	400
Changes in operating assets and liabilities:		
Inventories	26	(2,563)
Prepaid expenses and other assets	106	2,291
Accounts payable	(1,371)	1,705
Other liabilities	6,167	2,535
Total adjustments	9,599	7,500
Net cash provided by operating activities	32,599	25,195
Cash flows from investing activities		
Receipts on notes receivable	60	57
Increase in notes receivable	(65)	(16)
Proceeds from the sale of property and equipment	23	119
Purchases of property and equipment	(14,271)	(11,582)
Net cash used in investing activities	(14,253)	(11,422)
Cash flows from financing activities		
Proceeds from equity awards exercised	2,201	348
Excess tax benefit from equity-based payment arrangements	844	1,028
Repurchase of common stock	(72,998)	
Borrowings on line of credit	62,410	2,655
Payments on line of credit	(27,895)	(20,820)

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Net cash used in financing activities	(35,438)	(16,789)
Effect of exchange rate changes on cash and cash equivalents	(61)	133
Net decrease in cash and cash equivalents	(17,153)	(2,883)
Cash and cash equivalents, beginning of period	27,029	12,865
Cash and cash equivalents, end of period	\$ 9,876	\$ 9,982
<u>Supplemental disclosures of cash flow information</u>		
Cash paid during the period for:		
Interest, net of amount capitalized	\$ 201	\$ 371
Income taxes	11,343	9,948

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

(unaudited)

Basis of Presentation

The unaudited interim consolidated financial information of USANA Health Sciences, Inc. and its subsidiaries (collectively, the Company or USANA) has been prepared in accordance with Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission. Certain information and footnote disclosures that are normally included in financial statements that have been prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the accompanying interim consolidated financial information contains all adjustments, consisting of normal recurring adjustments that are necessary to present fairly the Company's financial position as of June 28, 2008, and results of operations for the quarters and six months ended June 30, 2007 and June 28, 2008. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto that are included in the Company's Annual Report on Form 10-K for the year ended December 29, 2007. The results of operations for the quarter and six months ended June 28, 2008 may not be indicative of the results that may be expected for the fiscal year ending January 3, 2009.

NOTE A ORGANIZATION

USANA develops and manufactures high-quality nutritional and personal care products that are sold internationally through a network marketing system, which is a form of direct selling. The Company's products are sold throughout the United States, Canada, Mexico, Australia, New Zealand, Singapore, Malaysia, Hong Kong, Taiwan, Japan, South Korea, the United Kingdom, and the Netherlands.

NOTE B DISCONTINUED OPERATIONS

Consistent with the Company's long-term objectives of focusing on its direct selling business, on August 10, 2007, the Company sold certain assets of its third-party contract manufacturing business. The Company retained assets that are associated with manufacturing and packaging its Sensé skin and beauty care products and continues to manufacture these products at the Draper, Utah facility. Results of the third-party contract manufacturing operations have been classified as discontinued operations for all periods.

The Company's sales that are reported in discontinued operations for the quarter and six months ended June 30, 2007 were \$1,865 and \$3,754 respectively. For the quarter ended June 30, 2007, the loss from discontinued operations was \$150 and the related income tax benefit was \$57. For the six months ended June 30, 2007, the loss from discontinued operations was \$330 and the related income tax benefit was \$123.

NOTE C INVENTORIES

Inventories consist of the following:

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	December 29, 2007	June 28, 2008
Raw materials	\$ 5,730	\$ 5,603
Work in progress	5,825	5,609
Finished goods	7,884	10,826
	\$ 19,439	\$ 22,038

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE D PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets consist of the following:

	December 29, 2007	June 28, 2008
Prepaid insurance	\$ 1,300	\$ 608
Other prepaid expenses	1,646	1,532
Federal income taxes receivable	2,754	1,169
Miscellaneous receivables, net	4,109	3,912
Deferred commissions	1,179	1,717
Other current assets	651	607
	\$ 11,639	\$ 9,545

NOTE E PROPERTY AND EQUIPMENT

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	Years	December 29, 2007	June 28, 2008
Buildings	40	\$ 23,466	\$ 23,609
Laboratory and production equipment	5-7	11,563	11,676
Sound and video library	5	600	600
Computer equipment and software	3-5	25,745	27,793
Furniture and fixtures	3-5	3,839	4,063
Automobiles	3-5	198	201
Leasehold improvements	3-5	3,700	4,137
Land improvements	15	1,579	1,565
		70,690	73,644
Less accumulated depreciation and amortization		36,459	38,921
		34,231	34,723
Land		1,956	1,968
Deposits and projects in process		15,874	23,472
		\$ 52,061	\$ 60,163

At June 28, 2008, the Company had a balance of \$9,835 on its line of credit, which was used to expand its facilities in Salt Lake City, Utah, and in Sydney, Australia. The interest expense that is associated with these projects has been capitalized as part of the asset to which it relates and will be amortized over the asset's estimated useful life. Total interest expense that was incurred during the first six months of 2008 was \$642, of which \$280 was capitalized.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE F OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

	December 29, 2007	June 28, 2008
Associate incentives	\$ 4,733	\$ 6,234
Accrued employee compensation	10,139	6,559
Income taxes	2,106	1,365
Sales taxes	4,111	4,569
Associate promotions	917	1,419
Deferred revenue	4,302	5,760
Provision for returns and allowances	931	1,093
All other	4,835	6,327
	\$ 32,074	\$ 33,326

NOTE G LONG TERM DEBT AND LINE OF CREDIT

The Company has a \$40,000 line of credit, which had a balance of \$9,835 at June 28, 2008. The Company will be required to pay the balance on this line of credit in full at the time of maturity in May 2011.

The weighted-average interest rate on this line of credit at June 28, 2008, was 4.16%. The interest rate is computed at the bank's Prime Rate or LIBOR and is adjusted according to the related Credit Agreement. The collateral for this line of credit is the pledge of the capital stock of certain subsidiaries of the Company, as set forth in a separate pledge agreement with the bank. The Credit Agreement contains restrictive covenants that are based on the Company's EBITDA and on the Company's debt coverage ratio.

NOTE H COMMITMENTS AND CONTINGENCIES

Contingencies

As of June 28, 2008, the Company was named as a defendant in two class action lawsuits, which were filed in 2007 and were later consolidated. The Company is also involved in other various disputes arising in the normal course of business. In the opinion of management, based upon advice of counsel, the ultimate outcome of these lawsuits will not have a material impact on the Company's financial position or results of operations.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE I EQUITY-BASED COMPENSATION

Equity-based compensation expense relating to equity awards under the current and previous plans of the Company, together with the related tax benefit recognized in earnings for the periods ended as of the dates indicated is as follows:

	Quarter Ended		Six Months Ended	
	June 30, 2007	June 28, 2008	June 30, 2007	June 28, 2008
Cost of sales	\$ 172	\$ 150	\$ 315	\$ 331
Selling, general and administrative	1,303	1,169	2,612	2,422
Research and development	154	51	293	105
	1,629	1,370	3,220	2,858
Related tax benefit	529	479	1,105	1,048
Net equity-based compensation expense	\$ 1,100	\$ 891	\$ 2,115	\$ 1,810

The following table shows the remaining unrecognized compensation expense on a pre-tax basis for all types of equity awards that were outstanding as of June 28, 2008. This table does not include an estimate for future grants that may be issued.

Remainder of 2008	\$ 2,945
2009	3,773
2010	3,316
2011 +	2,307
	\$ 12,341

The cost above is expected to be recognized over a weighted-average period of 1.9 years.

The Company uses the Black-Scholes option pricing model to estimate the fair value of its equity awards, which requires the input of highly subjective assumptions, including expected stock price volatility. The only awards granted by the Company during the six months ended June 28, 2008, were deferred stock units, which are full-value shares at the date of grant. For awards granted by the Company during 2007, expected volatility was calculated by averaging the historical volatility of the Company and a peer group index, and the risk-free interest rate was based on the U.S. Treasury yield curve on the date of grant with respect to the expected life of the award. Due to the plain vanilla characteristics of the Company's equity awards, the simplified method, as permitted by the guidance in Staff Accounting Bulletin No. 107, was used to determine the expected life of these awards.

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Weighted-average assumptions that were used to calculate the fair value of awards that were granted during the quarter and six months ended June 30, 2007, are included in the table below. Because deferred stock units are full-value shares at the date of grant they have been excluded.

	Quarter	Six Months
Expected volatility	41.9%	41.9%
Risk-free interest rate	4.6%	4.6%
Expected life	4.2 yrs.	4.2 yrs.
Expected dividend yield		
Grant price	\$ 40.51	\$ 42.10

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE I EQUITY-BASED COMPENSATION CONTINUED

A summary of the Company's stock option and stock-settled stock appreciation right activity for the six months ended June 28, 2008, is as follows:

	Shares	Weighted-average exercise price	Weighted-average remaining contractual term	Aggregate intrinsic value*
Outstanding at December 29, 2007	1,864	\$ 32.18	4.9	\$ 12,606
Granted		\$		
Exercised	(215)	\$ 1.62		
Canceled or expired	(35)	\$ 44.09		
Outstanding at June 28, 2008	1,614	\$ 35.99	4.5	\$ 1,805
Exercisable at June 28, 2008	844	\$ 33.85	5.2	\$ 1,778

* Aggregate intrinsic value is defined as the difference between the current market value at the reporting date and the exercise price of awards that were in-the-money. It is estimated using the closing price of the Company's common stock on the last trading day of the period reported.

The weighted-average fair value of stock options and stock-settled stock appreciation rights that were granted during the six months ended June 30, 2007, was \$16.79. The total intrinsic value of awards that were exercised during the six month periods ended June 30, 2007, and June 28, 2008, was \$4,745 and \$7,096, respectively.

The total fair value of awards that vested during the six month periods ended June 30, 2007, and June 28, 2008, was \$4,397 and \$5,381, respectively. This total fair value includes equity awards that were issued in the form of stock options, stock-settled stock appreciation rights, and deferred stock units.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE J COMMON STOCK AND EARNINGS PER SHARE

Basic earnings per share are based on the weighted-average number of shares outstanding for each period. Shares that have been repurchased and retired during the periods specified below have been included in the calculation of the number of weighted-average shares that are outstanding for the calculation of basic earnings per share. Diluted earnings per common share are based on shares that are outstanding (computed under basic EPS) and on potentially dilutive shares. Shares that are included in the diluted earnings per share calculations include equity awards that are in-the-money but have not yet been exercised.

	For the Quarter Ended	
	June 30, 2007	June 28, 2008
Earnings from continuing operations available to common shareholders	\$ 11,407	\$ 10,148
Loss from discontinued operations available to common shareholders	(93)	
Net earnings available to common shareholders	\$ 11,314	\$ 10,148
Basic EPS		
Shares		
Common shares outstanding - entire period	17,859	16,198
Weighted-average common shares:		
Issued during period	116	195
Canceled during period	(1,266)	
Weighted-average common shares outstanding during period	16,709	16,393
Earnings per common share from continuing operations - basic	\$ 0.68	\$ 0.62
Loss per common share from discontinued operations - basic		
Earnings per common share from net earnings - basic	\$ 0.68	\$ 0.62
Diluted EPS		
Shares		
Weighted-average shares outstanding during period - basic	16,709	16,393
Dilutive effect of equity awards	454	67
Weighted-average shares outstanding during period - diluted	17,163	16,460
Earnings per common share from continuing operations - diluted	\$ 0.66	\$ 0.62
Loss per common share from discontinued operations - diluted		
Earnings per common share from net earnings - diluted	\$ 0.66	\$ 0.62

Equity awards for 58 and 1,539 shares of stock were not included in the computation of diluted EPS for the quarters ended June 30, 2007, and June 28, 2008, respectively, due to the fact that their exercise prices were greater than the average market price of the shares.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE J COMMON STOCK AND EARNINGS PER SHARE CONTINUED

	For the Six Months Ended	
	June 30, 2007	June 28, 2008
Earnings from continuing operations available to common shareholders	\$ 23,207	\$ 17,695
Loss from discontinued operations available to common shareholders	(207)	
Net earnings available to common shareholders	\$ 23,000	\$ 17,695
Basic EPS		
Shares		
Common shares outstanding - entire period	17,859	16,198
Weighted-average common shares:		
Issued during period	84	180
Canceled during period	(641)	
Weighted-average common shares outstanding during period	17,302	16,378
Earnings per common share from continuing operations - basic	\$ 1.34	\$ 1.08
Loss per common share from discontinued operations - basic	(0.01)	
Earnings per common share from net earnings - basic	\$ 1.33	\$ 1.08
Diluted EPS		
Shares		
Weighted-average shares outstanding during period - basic	17,302	16,378
Dilutive effect of equity awards	511	82
Weighted-average shares outstanding during period - diluted	17,813	16,460
Earnings per common share from continuing operations - diluted	\$ 1.30	\$ 1.08
Loss per common share from discontinued operations - diluted	(0.01)	
Earnings per common share from net earnings - diluted	\$ 1.29	\$ 1.08

Equity awards for 42 and 1,400 shares of stock were not included in the computation of diluted EPS for the six months ended June 30, 2007, and June 28, 2008, respectively, due to the fact that their exercise prices were greater than the average market price of the shares.

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During the six months ended June 30, 2007, the Company expended \$72,998 to purchase 1,712 shares under the Company's share repurchase plan. No shares were purchased under the Company's share repurchase plan during the six months ended June 28, 2008. The purchase of shares under this plan reduces the number of shares issued and outstanding in the above calculations.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE K SEGMENT INFORMATION

USANA operates as a direct selling company that develops, manufactures, and distributes high-quality nutritional and personal care products that are sold through a global network marketing system of independent distributors (Associates). During the six months ended June 30, 2007, and June 28, 2008, the Company s nutritional products represented 86% and 88% of product sales, respectively. The Company s personal care products represented 10% of product sales during both of the six month periods ended June 30, 2007, and June 28, 2008.

The Company s primary business is to manage its worldwide Associate base. As such, management has determined that the Company operates in one reportable business segment as defined in SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. Resources are allocated to markets for the purpose of developing an infrastructure that supports the Associates and sales in that market. The Company does not use profitability reports on a regional or market basis for making business decisions. Performance for a region or market is primarily evaluated based on sales. No single customer accounted for 10% or more of net sales for the periods presented.

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In the table below, selected financial information is presented in four geographic regions: North America, Southeast Asia/Pacific, East Asia, and North Asia. North America includes our operations in the United States, Canada, Mexico, and direct sales from the United States to the United Kingdom and the Netherlands. Southeast Asia/Pacific includes our operations in Australia, New Zealand, Singapore, and Malaysia. East Asia includes our operations in Hong Kong and Taiwan. North Asia includes our operations in Japan and South Korea.

Selected Financial Information

Selected financial information, presented by geographic region, is listed below for the periods ended as of the dates indicated:

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	Quarter ended		Six Months Ended	
	June 30, 2007	June 28, 2008	June 30, 2007	June 28, 2008
Net Sales to External Customers				
North America	\$ 68,156	\$ 65,921	\$ 132,709	\$ 128,196
Southeast Asia/Pacific	23,570	24,170	44,203	45,715
East Asia	11,631	15,057	23,516	28,672
North Asia	4,185	4,060	7,792	8,195
Consolidated Total	\$ 107,542	\$ 109,208	\$ 208,220	\$ 210,778
Total Assets				
North America	\$ 69,134	\$ 81,750	\$ 69,134	\$ 81,750
Southeast Asia/Pacific	15,579	22,610	15,579	22,610
East Asia	7,320	7,637	7,320	7,637
North Asia	3,935	4,148	3,935	4,148
Consolidated Total	\$ 95,968	\$ 116,145	\$ 95,968	\$ 116,145

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE K SEGMENT INFORMATION CONTINUED

The following table provides further information on markets representing ten percent or more of consolidated net sales:

	Quarter ended		Six Months ended	
	June 30, 2007	June 28, 2008	June 30, 2007	June 28, 2008
Net sales:				
United States	\$ 43,433	\$ 40,125	\$ 85,493	\$ 78,675
Canada	18,965	19,527	36,106	38,110
Australia-New Zealand	14,630	14,068	27,656	27,446

Due to the centralized structure of the Company's manufacturing operations and its corporate headquarters in the United States, a significant concentration of assets exists in this market. As of June 30, 2007, and June 28, 2008, long-lived assets in the United States totaled \$39,023 and \$49,633, respectively. Additionally, due to the purchase, remodel, and fit-out of a new facility in Sydney, Australia during 2007, long-lived assets in the Australia-New Zealand market as of June 30, 2007 and June 28, 2008 totaled \$7,009 and \$13,626, respectively. There is no significant concentration of long-lived assets in any other market.

NOTE L SUBSEQUENT EVENTS

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On July 21, 2008, the Company's Compensation Committee of the Board of Directors issued approximately 2,500 SSARs to certain members of senior management that vest over five years. These grants will have a significant impact on the Company's future equity-based compensation expense and, consequently, results of operations.

As of June 28, 2008, a consolidated shareholder class action lawsuit was pending in the United States District Court, District of Utah, Central Division, against the Company and certain of its officers. On July 23, 2008, the district court granted the Company's motion to dismiss this litigation with prejudice. The plaintiff has the right to appeal the court's order within 30 days of the date of the order.

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

The following discussion and analysis of USANA's financial condition and results of operations should be read in conjunction with the Unaudited Consolidated Financial Statements and Notes thereto that are contained in this quarterly report, as well as Management's Discussion and Analysis of Financial Condition and Results of Operations that are included in our Annual Report on Form 10-K for the year ended December 29, 2007, and our other filings, including Current Reports on Form 8-K, that have been filed with the Securities and Exchange Commission (SEC) through the date of this report.

Our fiscal year end is the Saturday closest to December 31st of each year. Fiscal year 2008 will end on January 3, 2009, and is a 53-week year. Fiscal year 2007 ended on December 29, 2007, and was a 52-week year.

Presentation

Due to the sale of certain assets related to the third-party contract manufacturing business on August 10, 2007, we now operate as one reportable business segment, Direct Selling. Our financial results reflect the reclassification of sales and related expenses in the former Contract Manufacturing segment to discontinued operations.

General

USANA develops and manufactures high-quality nutritional and personal care products. We market our products on the basis of high levels of bioavailability, safety, and quality. We distribute our products through a network marketing system, which is a form of direct selling. Our customer base comprises two types of customers: Associates and Preferred Customers. Associates are independent distributors of our products who also purchase our products for their personal use. Preferred Customers purchase our products strictly for their personal use and are not permitted to resell or to distribute the products. As of June 28, 2008, we had approximately 169,000 active Associates and approximately 77,000 active Preferred Customers worldwide. During the six months ended June 28, 2008, sales to Associates accounted for approximately 87% of product sales. For purposes of this report, we only count as active customers those Associates and Preferred Customers who have purchased product from USANA at any time during the most recent three-month period, either for personal use or for resale.

We have ongoing operations in the following markets, which are grouped and presented in four geographic regions:

- North America – United States, Canada, Mexico, and direct sales from the United States to the United Kingdom and the Netherlands;
- Southeast Asia/Pacific – Australia-New Zealand, Singapore, and Malaysia;

- East Asia Hong Kong and Taiwan; and
- North Asia Japan and South Korea.

Our primary product lines consist of USANA® Nutritionals and Sensé beautiful science® (Sensé). The USANA Nutritionals product line is further categorized into three separate classifications:

- Essentials core vitamin and mineral supplements that provide a foundation of advanced nutrition for every age group;
- Optimizers targeted supplements that are designed to meet individual health and nutritional needs; and
- Macro Optimizers healthy, low-glycemic functional foods and other related products.

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The following tables summarize the approximate percentage of total product revenue that has been contributed by our major product lines and our top-selling products for the current and prior year periods indicated:

Product Line	Six Months Ended	
	June 30, 2007	June 28, 2008
USANA® Nutritionals		
Essentials	36%	35%
Optimizers	36%	40%
Macro Optimizers	14%	13%
Sensé beautiful science®	10%	10%
All Other *	4%	2%

* Includes items such as resource materials and services, sales tools, and logo merchandise.

Key Product	Six Months Ended	
	June 30, 2007	June 28, 2008
USANA® Essentials	21%	20%
HealthPak 100	13%	12%
Proflavanol®	10%	10%

As both a manufacturer and direct seller of nutritional and personal care products, we compete within two industries: nutrition and direct selling. We believe that the most significant industry-wide factors affecting us are the aging of the worldwide population and the general public's heightened awareness and understanding of the connection between diet and health, as well as attracting and retaining Associates and Preferred Customers.

Our results of operations and financial condition are directly related to changes in the number of Associates and Preferred Customers purchasing our products. We believe that our high-quality products and our financially rewarding Compensation Plan are the key components to attracting and retaining Associates. Additionally, we sponsor meetings and events throughout the year, which offer information about our products and our network marketing system. These meetings are designed to assist Associates in business development and to provide a forum for interaction with successful Associates and members of the USANA management team. We also provide low cost sales tools, which we believe are an integral part of building and maintaining a successful home-based business for Associates.

In addition to Company-sponsored meetings and sales tools, we maintain a website exclusively for our Associates where they can keep up on the latest USANA news, obtain training materials, manage their business information, enroll new customers, shop, and register for Company-sponsored events. Additionally, through this website, Associates can access other online services to which they may subscribe. For example, we offer an online business management service, which includes a tool that helps Associates track and manage their business activity, a personal webpage to which their prospects or retail customers can be directed, e-cards for advertising, and a tax management tool.

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The number of active Associates and Preferred Customers is used by management as a key non-financial measure because it is a leading indicator of net sales. The tables below summarize the changes in our active customer base by geographic region, which are further discussed in the Summary of Financial Results section below. These numbers have been rounded to the nearest thousand as of the dates indicated.

Active Associates By Region

	As of June 30, 2007		As of June 28, 2008		Change from Prior Year	Percent Change
North America	104,000	58.5%	96,000	56.8%	(8,000)	(7.7)%
Southeast						
Asia/Pacific	40,000	22.5%	39,000	23.1%	(1,000)	(2.5)%
East Asia	28,000	15.7%	27,000	16.0%	(1,000)	(3.6)%
North Asia	6,000	3.3%	7,000	4.1%	1,000	16.7%
	178,000	100.0%	169,000	100.0%	(9,000)	(5.1)%

Active Preferred Customers By Region

	As of June 30, 2007		As of June 28, 2008		Change from Prior Year	Percent Change
North America	71,000	89.9%	69,000	89.6%	(2,000)	(2.8)%
Southeast						
Asia/Pacific	6,000	7.5%	6,000	7.8%		0.0%
East Asia	1,000	1.3%	1,000	1.3%		0.0%
North Asia	1,000	1.3%	1,000	1.3%		0.0%
	79,000	100.0%	77,000	100.0%	(2,000)	(2.5)%

Total Active Customers By Region

	As of June 30, 2007		As of June 28, 2008		Change from Prior Year	Percent Change
North America	175,000	68.1%	165,000	67.1%	(10,000)	(5.7)%
Southeast						
Asia/Pacific	46,000	17.9%	45,000	18.3%	(1,000)	(2.2)%
East Asia	29,000	11.2%	28,000	11.4%	(1,000)	(3.4)%
North Asia	7,000	2.8%	8,000	3.2%	1,000	14.3%
	257,000	100.0%	246,000	100.0%	(11,000)	(4.3)%

Forward-Looking Statements and Certain Risks

The statements contained in this report that are not purely historical are considered to be forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act. These statements represent our expectations, beliefs, anticipations, commitments, intentions, and strategies regarding the future. They may be identified by the use of words or phrases such as believes, expects, anticipates, should, plans, estimates, and potential, among others. Forward-looking statements include, but are not limited to, statements contained in Management's Discussion and Analysis of Financial Condition and Results of Operations regarding our financial performance, revenue, and expense levels in the future and the sufficiency of our existing assets to fund our future operations and capital

spending needs. Readers are cautioned that actual results could differ materially from the anticipated results or other expectations that are expressed in these forward-looking statements for the reasons that are detailed in our most recent Annual Report on Form 10-K at pages 21 through 31. The fact that some of these risk factors may be the same or similar to those in our past SEC reports means only that

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the risks are present in multiple periods. We believe that many of the risks detailed here and in our other SEC filings are part of doing business in the industry in which we operate and will likely be present in all periods reported. The fact that certain risks are common in the industry does not lessen their significance. The forward-looking statements contained in this report, are made as of the date of this report, and we assume no obligation to update them or to update the reasons why our actual results could differ from those that we have projected. Among others, risks and uncertainties that may affect our business, financial condition, performance, development, and results of operations include:

- Our ability to attract and maintain a sufficient number of Associates;

- Our dependence upon a network marketing system to distribute our products;

