

NATURES SUNSHINE PRODUCTS INC
Form 10-Q
May 06, 2011
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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 March 31, 2011

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: 0-8707

NATURE S SUNSHINE PRODUCTS, INC.

(Exact name of Registrant as specified in its charter)

Utah
(State or other jurisdiction of
incorporation or organization)

87-0327982
(IRS Employer
Identification No.)

75 East 1700 South

Provo, Utah 84606

(Address of principal executive offices and zip code)

(801) 342-4300

(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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the 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

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Non-accelerated filer
(Do not check if a smaller reporting company)

Smaller reporting company

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

The number of shares of Common Stock, no par value, outstanding on April 29, 2011 was 15,532,909 shares.

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NATURE'S SUNSHINE PRODUCTS, INC.

FORM 10-Q

For the Quarter Ended March 31, 2011

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NATURE S SUNSHINE PRODUCTS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Amounts in thousands)

(Unaudited)

| | March 31, 2011 | December 31, 2010 |
|---------------------------------------------------------------------------------------------|-------------------|----------------------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 55,418 | \$ 47,604 |
| Accounts receivable, net of allowance for doubtful accounts of \$714 and \$918 respectively | 10,671 | 5,947 |
| Investments available for sale | 5,788 | 6,470 |
| Inventories | 35,665 | 36,235 |
| Deferred income tax assets | 4,564 | 4,582 |
| Prepaid expenses and other | 6,467 | 5,700 |
| Total current assets | 118,573 | 106,538 |
| Property, plant and equipment, net | 26,636 | 27,391 |
| Investment securities | 1,770 | 1,778 |
| Intangible assets, net | 1,266 | 1,303 |
| Deferred income tax assets | 12,945 | 12,916 |
| Other assets | 9,710 | 9,489 |
| | \$ 170,900 | \$ 159,415 |
| Liabilities and Shareholders' Equity | | |
| Current Liabilities: | | |
| Accounts payable | \$ 4,485 | \$ 4,855 |
| Accrued volume incentives | 22,065 | 18,619 |
| Accrued liabilities | 35,240 | 34,601 |
| Deferred revenue | 3,140 | 3,385 |
| Income taxes payable | 4,902 | 3,708 |
| Total current liabilities | 69,832 | 65,168 |
| Liability related to unrecognized tax benefits | 20,573 | 21,366 |
| Deferred compensation payable | 1,770 | 1,778 |
| Other liabilities | 3,124 | 2,721 |
| Total long-term liabilities | 25,467 | 25,865 |
| Commitments and Contingencies (Note 11) | | |
| Shareholders' Equity: | | |

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| | | |
|---------------------------------------------------------------------------------------------------------------------------------------|------------|------------|
| Common stock, no par value; 50,000 shares authorized, 15,533 shares issued and outstanding as of March 31, 2011 and December 31, 2010 | 67,840 | 67,752 |
| Retained earnings | 14,900 | 8,278 |
| Accumulated other comprehensive loss | (7,139) | (7,648) |
| Total shareholders' equity | 75,601 | 68,382 |
| | \$ 170,900 | \$ 159,415 |

See accompanying notes to condensed consolidated financial statements.

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NATURE S SUNSHINE PRODUCTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Amounts in thousands, except per share information)

(Unaudited)

| | Three Months Ended March 31, | |
|-----------------------------------------------------------------------------------------------------------|-----------------------------------------|-------------|
| | 2011 | 2010 |
| Net sales revenue (net of the rebate portion of volume incentives of \$11,582 and \$11,176, respectively) | \$ 92,844 | \$ 86,790 |
| Cost and expenses: | | |
| Cost of goods sold | 18,552 | 17,917 |
| Volume incentives | 34,298 | 32,551 |
| Selling, general and administrative | 32,373 | 35,752 |
| | 85,223 | 86,220 |
| Operating income | 7,621 | 570 |
| Other income, net | 265 | 2,901 |
| Income before provision (benefit) for income taxes | 7,886 | 3,471 |
| Provision (benefit) for income taxes | 1,264 | (1,300) |
| Net income from continuing operations | 6,622 | 4,771 |
| Loss from discontinued operations | | (618) |
| Net income | \$ 6,622 | \$ 4,153 |
| Basic and diluted net income per common share | | |
| Basic: | | |
| Net income from continuing operations | \$ 0.43 | \$ 0.31 |
| Loss from discontinued operations | \$ | \$ (0.04) |
| Net income | \$ 0.43 | \$ 0.27 |
| Diluted: | | |
| Net income from continuing operations | \$ 0.43 | \$ 0.31 |
| Loss from discontinued operations | \$ | \$ (0.04) |
| Net income | \$ 0.43 | \$ 0.27 |
| Weighted average basic common shares outstanding | 15,533 | 15,510 |
| Weighted average diluted common shares outstanding | 15,561 | 15,534 |

See accompanying notes to condensed consolidated financial statements.

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NATURE S SUNSHINE PRODUCTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)

(Unaudited)

| | Three Months Ended March 31, | |
|-----------------------------------------------------------------------------------|---------------------------------|-----------|
| | 2011 | 2010 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 6,622 | \$ 4,153 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for doubtful accounts | (61) | 6 |
| Depreciation and amortization | 1,054 | 1,118 |
| Share-based compensation expense | 88 | 69 |
| Loss on sale of property and equipment | | 31 |
| Deferred income taxes | 22 | 223 |
| Amortization of bond discount | 5 | 6 |
| Purchase of trading investment securities | (20) | (70) |
| Proceeds from sale of trading investment securities | 107 | 32 |
| Realized and unrealized gains on investments | (72) | (61) |
| Amortization of prepaid taxes related to gain on intercompany sales | | 271 |
| Foreign exchange (gains) losses | 589 | (2,869) |
| Changes in assets and liabilities: | | |
| Accounts receivable | (4,660) | (1,195) |
| Inventories | 713 | 2,052 |
| Prepaid expenses and other current assets | (733) | (78) |
| Other assets | (152) | 118 |
| Accounts payable | (298) | 1,330 |
| Accrued volume incentives | 3,340 | 2,670 |
| Accrued liabilities | 530 | 3,069 |
| Deferred revenue | (245) | (898) |
| Income taxes payable | 1,231 | (1,280) |
| Liability related to unrecognized tax benefits | (799) | (5,268) |
| Deferred compensation payable | (8) | 83 |
| Net cash provided by operating activities | 7,253 | 3,512 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of property, plant and equipment | (209) | (704) |
| Proceeds from sale of investments available for sale | 686 | |
| Net cash provided by (used in) by investing activities | 477 | (704) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Net cash provided by financing activities | | |
| Effect of exchange rates on cash and cash equivalents | 84 | 445 |
| Net increase in cash and cash equivalents | 7,814 | 3,253 |
| Cash and cash equivalents at the beginning of the period | 47,604 | 35,538 |
| Cash and cash equivalents at end of the period | \$ 55,418 | \$ 38,791 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION: | | |
| Cash paid for income taxes | \$ 650 | \$ 1,021 |

See accompanying notes to condensed consolidated financial statements.

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NATURE S SUNSHINE PRODUCTS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands, except per-share information)

(Unaudited)

(1) Basis of Presentation

Nature s Sunshine Products, Inc. and its subsidiaries (hereinafter referred to collectively as the Company) are primarily engaged in the manufacturing and marketing of nutritional, herbal, weight management, energy and other complementary products. Nature s Sunshine Products, Inc. is a Utah corporation with its principal place of business in Provo, Utah. The Company sells its products to a sales force of independent Distributors and Managers who use the products themselves or resell them to other Distributors or consumers. The formulation, manufacturing, packaging, labeling, advertising, distribution and sale of each of the Company s major product groups are subject to regulation by one or more governmental agencies.

The Company markets its products in Australia, Austria, Belarus, Canada, the Czech Republic, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Germany, Guatemala, Honduras, Hong Kong, Indonesia, Ireland, Israel, Japan, Kazakhstan, Latvia, Lithuania, Malaysia, Mexico, Mongolia, the Netherlands, Nicaragua, Norway, Panama, Peru, the Philippines, Poland, Russia, Singapore, South Korea, Sweden, Taiwan, Thailand, Ukraine, the United Kingdom, the United States, Venezuela and Vietnam. The Company also exports its products to several other countries, including Argentina, Australia, Chile, New Zealand and Norway.

Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions are eliminated in consolidation. In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the Company s financial information as of March 31, 2011, and for the three-month periods ended March 31, 2011 and 2010. The results of operations of any interim period are not necessarily indicative of the results of operations to be expected for the fiscal year ending December 31, 2011.

These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

Discontinued Operations

As more fully described in Note 2, Discontinued Operations, the Company ceased the operations of its Brazilian subsidiary in the third quarter of 2010, and the results of its operations are classified as discontinued operations in the Company's statements of operations and accompanying notes for all periods presented.

Classification of Venezuela as a Highly Inflationary Economy and Devaluation of Its Currency

As of January 1, 2010, Venezuela was designated as a highly inflationary economy. Accordingly, the U.S. dollar became the functional currency for the Company's subsidiary in Venezuela. All gains and losses resulting from the re-measurement of its financial statements are determined using official rates. On January 8, 2010, the Venezuelan government announced the devaluation of the bolivar against the U.S. dollar.

Currency restrictions enacted by the government of Venezuela require approval from the government's currency control agency organization in order for the Company's subsidiary in Venezuela to obtain U.S. dollars at the official exchange rate to pay for imported products or to repatriate dividends back to the Company. Prior to January 1, 2010, the market rate, which is substantially lower than the official rate, was available to obtain U.S. dollars or other currencies without approval of the government's currency control organization. In 2010, the government of Venezuela enacted additional currency restrictions, which effectively replaced the market rate with the System for Foreign Currency Denominated Securities (SITME), which is administered by the Venezuela Central Bank. Under SITME, entities domiciled in Venezuela can obtain U.S. dollar denominated securities in limited quantities each month through banking institutions approved by the government.

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At this time, the Company is not able to estimate reasonably the future state of exchange controls in Venezuela and its availability of U.S. dollars at the official exchange rate or at the SITME rate. However, the Company has been successful repatriating funds from Venezuela for imported products using the SITME rate. The Company re-measures its results in Venezuela at the SITME rate, which was approximately 5.30 bolivars per U.S. dollar as of March 31, 2011.

As a result of the events described in the preceding paragraphs, the Company recorded a gain of \$3,668 in the first quarter of 2010 in connection with the re-measurement of its balance sheet to reflect the highly inflationary designation and the devaluation due to the negative position of the Company's Venezuelan subsidiary's net monetary assets, which is recorded in foreign exchange gains or losses, a part of other income. The success of future operations will be affected by several factors, including the Company's ability to take actions to mitigate the effect of devaluation, further actions of the Venezuelan government and economic conditions in Venezuela, such as inflation and consumer spending.

During the three months ended March 31, 2011 and 2010, the Company's Venezuelan subsidiary's net sales revenue represented approximately 1.4 percent and 1.7 percent of consolidated net sales revenue, respectively. The Company's Venezuelan subsidiary held total assets of \$8,104 and \$8,024 (which includes an intercompany receivable denominated in U.S. dollars of \$2,010 and \$1,978) and net assets of \$5,205 and \$4,185 at March 31, 2011 and December 31, 2010, respectively.

Recent Accounting Pronouncements

In January 2010, the Financial Accounting Standards Board (FASB) issued authoritative guidance that requires new disclosures related to fair value measurements and clarifies existing disclosure requirements about the level of disaggregation, inputs and valuation techniques. Specifically, reporting entities now must disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. In addition, in the reconciliation for Level 3 fair value measurements, a reporting entity should present separately information about purchases, sales, issuances and settlements. The guidance clarifies that a reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities for disclosure of fair value measurement, considering the level of disaggregated information required by other applicable U.S. GAAP guidance and should also provide disclosures about the valuation techniques and inputs used to measure fair value for each class of assets and liabilities. This guidance was effective for the Company on January 1, 2010, except for the disclosures about purchases, sales, issuances and settlements in the reconciliation for Level 3 fair value measurements, which became effective for the Company on January 1, 2011. The adoption of the applicable sections of this guidance effective on January 1, 2010 and 2011 did not have a material impact on the Company's financial condition, results of operations, or cash flows.

(2) Discontinued Operations

During 2010, the Company ceased its operations in Brazil as a result of increased regulatory restrictions and declining sales, which made it difficult for the Company to register and sell key products in that market. This market was part of the Company's NSP International segment.

The following table summarizes the operating results of the Company's discontinued operations for the periods indicated:

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| | Three Months Ended March 31, | |
|-----------------------------------------------|---------------------------------|----------|
| | 2011 | 2010 |
| Net Sales Revenue | \$ | \$ 256 |
| Loss before income tax provision | \$ | \$ (618) |
| Income tax provision | | |
| Loss from discontinued operations, net of tax | \$ | \$ (618) |

The cash flows from our discontinued operations are included in the Company's operating cash flows, but were insignificant.

Table of Contents**(3) Inventories**

Inventories consist of the following:

| | March 31, 2011 | December 31, 2010 |
|------------------|---------------------------|------------------------------|
| Raw Materials | \$ 9,965 | \$ 9,177 |
| Work in Progress | 787 | 956 |
| Finished Goods | 24,913 | 26,102 |
| | \$ 35,665 | \$ 36,235 |

(4) Intangible Assets

At March 31, 2011 and December 31, 2010, intangibles for product formulations had a gross carrying amount of \$1,763 and \$1,763, accumulated amortization of \$497 and \$460, and a net amount of \$1,266 and \$1,303, respectively. The estimated useful lives of the product formulations range from 9 to 15 years.

Amortization expense for intangible assets for the three months ended March 31, 2011 and 2010 was \$37 and \$30, respectively. Estimated amortization expense for each of the five succeeding fiscal years is \$149.

(5) Investments

The amortized cost and estimated fair values of available-for-sale securities by balance sheet classification are as follows:

| As of March 31, 2011 | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|----------------------------------------|---------------------------|---------------------------------------|----------------------------------------|-----------------------|
| Municipal obligations | \$ 1,673 | \$ 65 | \$ | \$ 1,738 |
| U.S. government securities funds | 987 | | (17) | 970 |
| Short-term deposits | 2,663 | | | 2,663 |
| Equity securities | 228 | 189 | | 417 |
| Total short-term investment securities | \$ 5,551 | \$ 254 | \$ (17) | \$ 5,788 |

| As of December 31, 2010 | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|--------------------------------|---------------------------|---------------------------------------|----------------------------------------|-----------------------|
| Municipal obligations | \$ 1,883 | \$ 77 | \$ | \$ 1,960 |

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| | | | |
|----------------------------------------|----------|--------|---------------|
| U.S. government securities funds | 989 | (15) | 974 |
| Short-term deposits | 3,148 | | 3,148 |
| Equity securities | 228 | 160 | 388 |
| Total short-term investment securities | \$ 6,248 | \$ 237 | \$ (15) 6,470 |

The municipal obligations held at a fair value of \$1,738 at March 31, 2011 all mature in less than five years.

During the three-month periods ended March 31, 2011 and 2010, the proceeds from the sales of available-for-sale securities were \$686 and \$0, respectively. There were no gross realized gains (losses) on sales of available-for-sale securities (net of tax) for the three-month periods ended March 31, 2011 and 2010, respectively.

The Company's trading securities portfolio totaled \$1,770 at March 31, 2011 and \$1,778 at December 31, 2010, and generated gains of \$81 and \$44 for the three months ended March 31, 2011 and 2010, respectively.

As of March 31, 2011 and December 31, 2010, the Company had unrealized losses of \$17 and \$15, respectively, in its U.S. government securities funds. These losses are due to the interest rate sensitivity of the U.S. government securities funds.

(6) Net Income Per Share

Basic net income per common share (Basic EPS) is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per common share (Diluted EPS) reflects the potential dilution that could occur if stock options or other contracts to issue common stock were exercised or converted into common stock. The computation of Diluted EPS does not assume exercise or conversion of securities that would have an anti-dilutive effect on net income per common share.

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The following is a reconciliation of the numerator and denominator of Basic EPS to the numerator and denominator of Diluted EPS for the three months ended March 31, 2011 and 2010:

| | Three Months Ended March 31, | |
|----------------------------------------------------------------------------------|------------------------------|-----------|
| | 2011 | 2010 |
| Net income available to common stockholders | | |
| Net income from continuing operations | \$ 6,622 | \$ 4,771 |
| Loss from discontinued operations | | (618) |
| Net income | \$ 6,662 | \$ 4,153 |
| Basic weighted average shares outstanding | | |
| | 15,533 | 15,510 |
| Basic net income per common share: | | |
| Net income from continuing operations | \$ 0.43 | \$ 0.31 |
| Loss income from discontinued operations | \$ | \$ (0.04) |
| Net income | \$ 0.43 | \$ 0.27 |
| Diluted shares outstanding | | |
| Basic weighted average shares outstanding | 15,533 | 15,510 |
| Stock options | 28 | 24 |
| Diluted weighted average shares outstanding | 15,561 | 15,534 |
| Diluted net income per common share: | | |
| Net income from continuing operations | \$ 0.43 | \$ 0.31 |
| Loss from discontinued operations, net of tax | \$ | \$ (0.04) |
| Net income | \$ 0.43 | \$ 0.27 |
| Potentially dilutive shares excluded from diluted per share amounts: | | |
| Stock options | | |
| Potentially anti-dilutive shares excluded from diluted per share amounts: | | |
| Stock options | 995 | 394 |

Potentially dilutive shares excluded from diluted per share amounts include performance based options to purchase shares of common stock for which certain earnings metrics have not been achieved. Potentially anti-dilutive shares excluded from diluted per share amounts include both non-qualified stock options and unearned performance based options to purchase shares of common stock with exercise prices greater than the weighted-average share price during the period.

(7) **Comprehensive Income**

The components of comprehensive income, net of tax, for the three months ended March 31, 2011 and 2010, respectively, are as follows:

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| | Three Months Ended March 31, | | | |
|--------------------------------------------------------|---------------------------------|-------|------|-------|
| | 2011 | | 2010 | |
| Net income | \$ | 6,622 | \$ | 4,153 |
| Foreign currency translation gain | | 499 | | 1,277 |
| Net unrealized gains (losses) on investment securities | | 10 | | (2) |
| Total comprehensive income | \$ | 7,131 | \$ | 5,428 |

Table of Contents**(8) Share-based Compensation**

Stock option activity for the three months ended March 31, 2011 is as follows:

| | Number of Shares | Weighted Average Exercise Price Per Share |
|------------------------------------------|---------------------|-------------------------------------------------|
| Options outstanding at December 31, 2010 | 859 | \$ 9.20 |
| Granted | 405 | 8.88 |
| Expired | (74) | 9.70 |
| Exercised | | |
| Options outstanding at March 31, 2011 | 1,190 | 9.06 |

During the three-month period ended March 31, 2011, the Company issued options to purchase 405 shares of common stock under the 2009 Incentive Plan to the Company's executive officers and other employees, all of which were subject to achieving certain earnings metrics. These options were issued with an exercise price of \$8.88 per share, and a grant date fair value of \$4.02 per share. All of the options issued have an option termination date of ten years from the option grant date.

The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for the three-month period ended March 31, 2011:

| | 2011 |
|--------------------------|------|
| Expected life (in years) | 4.0 |
| Risk-free interest rate | 1.0 |
| Expected volatility | 58.4 |
| Dividend yield | 0.0 |

Expected option lives and volatilities are based on historical data of the Company. The risk free interest rate is calculated as the average U.S. Treasury obligation rate that corresponds with the option life.

Share-based compensation expense from qualified stock options for the three-month periods ended March 31, 2011 and 2010, was approximately \$88 and \$69, respectively; the related tax benefit was approximately \$34 and \$25, respectively. As of March 31, 2011 and December 31, 2010, the unrecognized share-based compensation cost related to the grants described above was \$325 and \$451, respectively. Should the Company attain all of the earnings metrics related to the metric based stock option grants, the Company could recognize up to \$2,800 of potential stock compensation expense.

At March 31, 2011, the aggregate intrinsic value of outstanding options to purchase 1,190 shares of common stock, the exercisable options to purchase 344 shares of common stock and options to purchase 185 shares of common stock expected to vest was \$802, \$396 and \$346, respectively. At December 31, 2010, the aggregate intrinsic value of options outstanding to purchase 859 shares of common stock was \$855.

(9) Segment Information

The Company has three business segments. These business segments are components of the Company for which separate information is available that is evaluated regularly by the chief executive officer in deciding how to allocate resources and in assessing relative performance.

The Company has two reportable business segments that operate under the Nature's Sunshine Products brand and are divided based on their geographic operations in the United States and in countries outside the United States. The Company's third reportable business segment operates under the Synergy Worldwide brand, which offers products with formulations that are sufficiently different from those of Nature's Sunshine Products and has marketing and Distributor compensation plans that are sufficiently different from those of Nature's Sunshine Products to warrant accounting for these operations as a separate business segment. Net sales revenues for each segment have been reduced by intercompany sales as they are not included in the measure of segment profit or loss reviewed by the chief executive officer. The Company evaluates performance based on operating income (loss) by segment before consideration of certain inter-segment transfers and expenses.

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Reportable business segment information is as follows:

| | Three Months Ended | |
|------------------------------------------|--------------------|-----------|
| | 2011 | 2010 |
| Net sales revenue: | | |
| Nature s Sunshine Products: | | |
| United States | \$ 35,645 | \$ 36,662 |
| International | 36,547 | 36,180 |
| | 72,192 | 72,842 |
| Synergy Worldwide | 20,652 | 13,948 |
| Total net sales revenue | 92,844 | 86,790 |
| Operating expenses: | | |
| Nature s Sunshine Products: | | |
| United States | 31,887 | 36,202 |
| International | 34,493 | 35,355 |
| | 66,380 | 71,557 |
| Synergy Worldwide | 18,843 | 14,663 |
| Total operating expenses | 85,223 | 86,220 |
| Operating income (loss): | | |
| Nature s Sunshine Products: | | |
| United States | 3,758 | 460 |
| International | 2,054 | 825 |
| | 5,812 | 1,285 |
| Synergy Worldwide | 1,809 | (715) |
| Total operating income (loss) | 7,621 | 570 |
| Other income, net | 265 | 2,901 |
| Income before provision for income taxes | \$ 7,886 | \$ 3,471 |

The Company moved its Dominican Republic market from the NSP United States segment to the NSP International segment during the quarter ended March 31, 2011, and has made conforming changes to the results presented above as of March 31, 2010. The net sales revenue and operating loss of this market were \$1,168 and (\$89) as of March 31, 2010, respectively.

From an individual country perspective, only the United States comprises approximately 10 percent or more of consolidated net sales revenue for either of the three-month periods ended March 31, 2011 and 2010 as follows:

| | Three Months Ended | |
|--------------------|--------------------|-----------|
| | 2011 | 2010 |
| Net sales revenue: | | |
| United States | \$ 40,787 | \$ 39,231 |
| Other | 52,057 | 47,559 |
| | \$ 92,844 | \$ 86,790 |

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Net sales revenue by product group has not been disclosed as management has determined that it is impracticable to accumulate such information.

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From an individual country perspective, only the United States and Venezuela comprise 10 percent or more of consolidated property, plant and equipment as follows:

| | March 31, 2011 | December 31, 2010 |
|-------------------------------------|-------------------|----------------------|
| Property, plant and equipment: | | |
| United States | \$ 19,805 | \$ 20,350 |
| Venezuela | 4,248 | 4,353 |
| Other | 2,583 | 2,688 |
| Total property, plant and equipment | \$ 26,636 | \$ 27,391 |

(10) Income Taxes

Interim income taxes are based on an estimated annualized effective tax rate applied to the respective quarterly periods, adjusted for discrete tax items in the period in which they occur. For the three months ended March 31, 2011 and 2010, the Company's provision (benefit) for income taxes, as a percentage of income before income taxes (benefit) was a provision of 16.0 percent and a benefit of 37.5 percent, respectively, compared with a U.S. federal statutory rate of 35.0 percent.

The difference between the effective tax rate and the U.S. federal statutory tax rate for the three months ended March 31, 2011 was primarily attributed to net decreases in tax liabilities associated with uncertain tax positions due to the expiration of the statute of limitations on certain liabilities in various foreign jurisdictions, which resulted in a tax benefit of approximately \$1,200.

The differences between the effective tax rate and the federal statutory tax rate for the three months ended March 31, 2010 were primarily attributed to:

- decreases in tax liabilities associated with uncertain tax positions due to the expiration of the statute of limitations on certain liabilities in various foreign jurisdictions, which resulted in a tax benefit of \$1,361,
- foreign subsidiary net losses for which no tax benefit was being recognized, and
- the foreign exchange gain related to the implementation of highly-inflationary accounting for Venezuela recognized for financial reporting purposes, but not for income tax purposes.

As of March 31, 2011, the Company had accrued \$14,886 (net of \$5,687 of other assets related to competent authority and royalty benefits) related to unrecognized tax positions compared with \$15,679 (net of \$5,687 of other assets related to competent authority and royalty benefits) as of December 31, 2010. This net decrease was primarily attributed to the expiration of the statute of limitations on certain liabilities in various foreign jurisdictions.

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The Company's U.S. federal income tax returns for 2003 through 2009 are open to examination for federal tax purposes. The Company has several foreign tax jurisdictions which have open tax years from 2000 through 2009. The Internal Revenue Service (IRS) is currently conducting an audit of the Company's U.S. federal income tax returns for the 2006 through 2008 tax years.

In October 2009, the IRS issued an examination report formally proposing adjustments with respect to the 2003 through 2005 taxable years, which primarily relate to the prices that were charged in intra-group transfers of property and the disallowance of related deductions. The Company has commenced administrative proceedings with the Office of Appeals of the Internal Revenue Service challenging the proposed adjustments. Management believes that the Company has appropriately reserved for these matters at an amount which it believes will ultimately be due upon resolution of the administrative proceedings, and such amounts reflect management's estimates based upon available evidence resulting from discussions with the IRS Office of Appeals. These estimates are based upon a more-likely-than-not recognition threshold. The Company is currently unable to determine the outcome of these discussions and their related impact, if any, on the Company's financial condition, results of operations, or cash flows.

Although the Company believes its estimates are reasonable, the Company can make no assurance that the final tax outcome of these matters will not be different from that which it has reflected in its historical income tax provisions and accruals. Such difference could have a material impact on the Company's income tax provision and operating results in the period in which the Company makes such determination.

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(11) **Commitments and Contingencies**

Legal Proceedings

The Company is party to various legal proceedings, including those noted below. Management cannot predict the ultimate outcome of these proceedings, individually or in the aggregate, or their resulting effect on the Company's business, financial position, results of operations or cash flows as litigation and related matters are subject to inherent uncertainties, and unfavorable rulings could occur. Were an unfavorable outcome to occur, there exists the possibility of a material adverse impact on the business, financial position, results of operations, or cash flows for the period in which the ruling occurs and/or future periods. The Company maintains directors' and officers' liability, product liability, general liability and excess liability insurance coverage. However, no assurances can be given that such insurance will continue to be available at an acceptable cost to the Company, that such coverage will be sufficient to cover one or more large claims, or that the insurers will not successfully disclaim coverage as to a pending or future claim.

NutriPlus LLC Arbitration

On July 12, 2010, the Company submitted a demand for arbitration to the American Arbitration Association (the "AAA") naming NutriPlus LLC ("NutriPlus") as respondent. The Company seeks a declaration of its rights and obligations, including with respect to royalty payments, and the calculation thereof, arising out of an Asset Purchase Agreement and subsequent Settlement Agreement entered into by the Company and NutriPlus in 1999 and 2000, respectively (together the "Purchase Agreement").

On July 20, 2010, NutriPlus submitted its own demand for arbitration to the AAA naming the Company as respondent. NutriPlus alleges that the Company underpaid NutriPlus for royalties arising out of the Purchase Agreement. In arbitration, NutriPlus seeks damages related to the alleged underpayment and a declaratory judgment with respect to the method the Company must use in determining the amount of royalties to pay NutriPlus in the future.

The arbitration demands have been consolidated into a single proceeding, the hearing for which is currently scheduled for July 2011. The Company cannot predict the outcome at this time. The Company has been accruing a liability for unpaid royalties to NutriPlus in an amount equal to the royalties that would have been paid under the calculation method previously applied by the Company, which method the Company now contends was in error, for which it is seeking relief. This accrual may be in excess of the actual liability or insufficient, depending on the outcome of the arbitration, which the Company cannot predict at this time.

Other Litigation

The Company is party to various other legal proceedings in several foreign jurisdictions related to VAT assessments and other civil litigation. Although there is a reasonable possibility that a material loss may be incurred, the Company cannot at this time estimate the loss, if any. Therefore, no provision for losses has been provided. The Company believes future payments related to these matters could range from \$0 to approximately \$1,500.

Non-income Tax Contingencies

The Company has reserved for certain state sales and use tax and foreign non-income tax contingencies based on the likelihood of an obligation in accordance with accounting guidance for probable loss contingencies. Loss contingency provisions are recorded for probable losses at management's best estimate of a loss, or when a best estimate cannot be made, a minimum loss contingency amount is recorded. The Company provides provisions for potential payments of tax to various tax authorities for contingencies related to non-income tax matters, including value added taxes and sales tax. The Company provides provisions for U.S. state sales taxes in each of the states where the Company has nexus. As of March 31, 2011 and December 31, 2010, accrued liabilities include \$9,461 and \$10,235, respectively, related to non-income tax contingencies. While management believes that the assumptions and estimates used to determine this liability are reasonable, the ultimate outcome of those matters cannot presently be determined. The Company is not able at this time to predict the ultimate outcomes of those matters or to estimate the effect the ultimate outcomes, if greater than the amounts accrued, would have on the financial condition, results of operations or cash flows of the Company.

Government Regulations

The Company is subject to governmental regulations pertaining to product formulation, labeling and packaging, product claims and advertising, and to the Company's direct selling system. The Company is also subject to the jurisdiction of numerous foreign tax and customs authorities. Any assertions or determinations that either the Company or the Company's Distributors are not in compliance with existing statutes, laws, rules or regulations could potentially have a material adverse effect on the Company's operations. In addition, in any country or jurisdiction, the adoption of new statutes, laws, rules or regulations, or changes in the interpretation of existing statutes, laws, rules or regulations could have a material adverse effect on the Company and its operations.

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Although management believes that the Company is in compliance, in all material respects, with the statutes, laws, rules and regulations of every jurisdiction in which it operates, no assurance can be given that the Company's compliance with applicable statutes, laws, rules and regulations will not be challenged by foreign authorities or that such challenges will not have a material adverse effect on the Company's financial position, results of operations or cash flows.

(12) Fair Value Measurements

The fair value of a financial instrument is the amount that could be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Financial assets are marked to bid prices and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs. A fair value hierarchy is used to prioritize the quality and reliability of the information used to determine fair values of each financial instrument. Categorization within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The fair value hierarchy is defined into the following three categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data

The following table presents the Company's hierarchy for its asset measured at fair value on a recurring basis as of March 31, 2011:

| | Level 1 Quoted Prices in Active Markets for Identical Assets | Level 2 Significant Other Observable Inputs | Level 3 Significant Unobservable Inputs | Total |
|----------------------------------------------------------|--------------------------------------------------------------------------|---------------------------------------------------------|--------------------------------------------------|----------|
| Investments available for sale | | | | |
| Municipal obligations | \$ | | \$ 1,738 | \$ 1,738 |
| U.S. government security funds | 970 | | | 970 |
| Short-term deposits | | 2,663 | | 2,663 |
| Equity securities | 417 | | | 417 |
| Investment securities | 1,770 | | | 1,770 |
| Total assets measured at fair value on a recurring basis | \$ 3,157 | \$ 4,401 | \$ | \$ 7,558 |

The following table presents the Company's hierarchy for its asset measured at fair value on a recurring basis as of December 31, 2010:

| | Level 1 Quoted Prices in Active Markets for | Level 2 Significant Other Observable | Level 3 Significant Unobservable Inputs | Total |
|--|------------------------------------------------------|-----------------------------------------------|--------------------------------------------------|-------|
|--|------------------------------------------------------|-----------------------------------------------|--------------------------------------------------|-------|

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| | Identical Assets | | Inputs | | |
|----------------------------------------------------------|------------------|-------|--------|-------|----------|
| Investments available for sale | | | | | |
| Municipal obligations | \$ | | \$ | 1,960 | \$ 1,960 |
| U.S. government security funds | | 974 | | | 974 |
| Short-term deposits | | | | 3,148 | 3,148 |
| Equity securities | | 388 | | | 388 |
| Investment securities | | 1,778 | | | 1,778 |
| Total assets measured at fair value on a recurring basis | \$ | 3,140 | \$ | 5,108 | \$ 8,248 |

Investments available for sale The majority of the Company's investment portfolio consists of various fixed income securities such as U.S. government funds, state and municipal bonds, mutual funds, short-term deposits and equity securities. The Level 1 securities are valued using quoted prices for identical assets in active markets including equity securities, U.S. government treasuries, and various mutual funds. The Level 2 securities include investments in state and municipal bonds whereby all significant inputs are observable or can be derived from or corroborated by observable market data for substantially the full term of the asset.

Investment securities The majority of the Company's trading portfolio consists of various marketable securities that are using quoted prices in active markets.

For the three months ended March 31, 2011 and December 31, 2010, there were no fair value measurements using the significant unobservable inputs (Level 3).

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The carrying amounts reflected on the consolidated balance sheet for cash and cash equivalents, accounts and notes receivable, and accounts payable approximate fair value due to their short-term nature. During the three months ended March 31, 2011, the Company did not have any write-offs related to the re-measurement of non-financial assets at fair value on a nonrecurring basis subsequent to their initial recognition.

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

The following Management's Discussion and Analysis should be read in conjunction with the unaudited consolidated financial statements and notes thereto included in this report, as well as the consolidated financial statements, the notes thereto, and management's discussion and analysis included in our Annual Report on Form 10-K for the year ended December 31, 2010, and our Reports on Form 8-K, that have been filed with the SEC since then through the date of this report.

Throughout this report, we refer to Nature's Sunshine Products, Inc., together with its subsidiaries, as *we*, *us*, *our* Company or *the Company*.

OVERVIEW

Nature's Sunshine Products, Inc. and its subsidiaries are primarily engaged in the manufacturing and marketing of nutritional, herbal, weight management, energy and other complementary products. Nature's Sunshine Products, Inc. is a Utah corporation with its principal place of business in Provo, Utah. We sell our products to a sales force of independent Distributors and Managers who use the products themselves or resell them to other Distributors or consumers. The formulation, manufacturing, packaging, labeling, advertising, distribution and sale of each of our major product groups are subject to regulation by one or more governmental agencies. We also sell our products through a separate division and operating business segment, Synergy Worldwide. Synergy Worldwide offers products with formulations sufficiently different from those of the Nature's Sunshine Products offerings to warrant its treatment as a separately reportable business segment. In addition, Synergy Worldwide's marketing and Distributor compensation plans are sufficiently different from those of Nature's Sunshine Products to warrant accounting for these operations as a separate business segment.

We market our products in Australia, Austria, Belarus, Canada, the Czech Republic, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Germany, Guatemala, Honduras, Hong Kong, Indonesia, Ireland, Israel, Japan, Kazakhstan, Latvia, Lithuania, Malaysia, Mexico, Mongolia, the Netherlands, Nicaragua, Norway, Panama, Peru, the Philippines, Poland, Russia, Singapore, South Korea, Sweden, Taiwan, Thailand, Ukraine, the United Kingdom, the United States, Venezuela and Vietnam. We export our products to several other countries, including Argentina, Australia, Chile, New Zealand and Norway.

During the first quarter of 2011, we experienced an increase in our consolidated net sales of 7.0 percent. Our Synergy Worldwide business segment (Synergy Worldwide) experienced an increase in net sales revenue of approximately 48.1 percent (or 42.8 percent in local currencies excluding the positive impact of foreign currency fluctuations). Our Nature's Sunshine Products International business segment (NSP International) experienced an increase in net sales of approximately 1.0 percent compared to the same period in 2010, and a decrease in local currency net sales of 0.3 percent (excluding the positive impact of foreign currency fluctuations), while our domestic business segment (NSP United States) net sales decreased approximately 2.8 percent. We saw improvements in certain foreign markets due to strengthening demand as a result of current economic conditions, and growth from expansion into new or existing markets. The most significant positive impact on sales revenue was from our European, Russian, Korean and United States (Synergy) markets during the first quarter of 2011. Gains in these markets were offset by decreases in our Dominican Republic, Japan and Mexico markets.

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Over the same period, our selling, general and administrative costs as a percentage of net sales revenue have decreased from 41.2 percent in the prior year to 34.9 percent as a result of our revenue growth (primarily in Synergy), and concerted efforts to reduce our operating costs in all of our operating segments. We continue to implement cost reduction measures within all of our operating segments.

As a result of our overall growth in net sales revenue and reductions in operating expenses, our operating income increased from 0.7 percent in the prior year to 8.2 percent of net sales revenue.

We distribute our products to consumers through an independent sales force comprised of Managers and Distributors. A person who joins our independent sales force begins as a Distributor. A Distributor interested in earning additional income by committing more time and effort to selling our products may earn Manager status. Manager status is contingent upon attaining certain purchase volume levels, recruiting additional Distributors, and demonstrating leadership abilities. Active Managers worldwide slightly increased and totaled approximately 30,300 and 29,900 at March 31, 2011 and 2010, respectively. Active Distributors worldwide slightly increased and totaled approximately 696,400 and 693,200 at March 31, 2011 and 2010, respectively.

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The following table summarizes our unaudited consolidated operating results in U.S. dollars and as a percentage of net sales revenue for the three months ended March 31, 2011 and 2010 (dollar amounts in thousands).

| | 2011 | | 2010 | | Change from 2011 to 2010 | |
|----------------------------------------------------|---------------|----------------------|---------------|----------------------|--------------------------|------------|
| | Total dollars | Percent of net sales | Total dollars | Percent of net sales | Dollar | Percentage |
| Net sales revenue | \$ 92,844 | 100.0% | \$ 86,790 | 100.0% | \$ 6,054 | 7.0% |
| Costs and expenses: | | | | | | |
| Cost of goods sold | 18,552 | 20.0 | 17,917 | 20.6 | 635 | 3.5 |
| Volume incentives | 34,298 | 36.9 | 32,551 | 37.5 | 1,747 | 5.4 |
| SG&A expenses | 32,373 | 34.9 | 35,752 | 41.2 | (3,379) | (9.5) |
| Total operating expenses | 85,223 | 91.8 | 86,220 | 99.3 | (997) | (1.2) |
| Operating income | 7,621 | 8.2 | 570 | 0.7 | 7,051 | 1,237.0 |
| Other income, net | 265 | 0.3 | 2,901 | 3.3 | (2,636) | (90.9) |
| Income before provision (benefit) for income taxes | 7,886 | 8.5 | 3,471 | 4.0 | 4,415 | 127.2 |
| Provision (benefit) for income taxes | 1,264 | 1.4 | (1,300) | (1.5) | 2,564 | 197.2 |
| Net income from continuing operations | 6,622 | 7.1 | 4,771 | 5.5 | 1,851 | 38.8 |
| Loss from discontinued operations | | | (618) | (0.7) | 618 | 100.0 |
| Net income | \$ 6,622 | 7.1% | \$ 4,153 | 4.8% | \$ 2,469 | 59.5% |

Net Sales Revenue

Consolidated net sales revenue for the three months ended March 31, 2011 was \$92.8 million compared to \$86.8 million in 2010, an increase of approximately 7.0 percent. The increase in net sales revenue for the three months ended March 31, 2011 compared to the same period in 2010, is primarily due to improvements in our Synergy Worldwide segment, and was partially offset by a decline in our NSP United States segment.

NSP United States Segment

Net sales revenue for our NSP United States segment for the three months ended March 31, 2011 was \$35.6 million compared to \$36.7 million for the same period in 2010, or a decrease of 2.8 percent in 2011 compared to 2010. Shifting the timing of our national convention from the fall of 2010 to the spring of 2011 negatively affected Manager retention and Distributor recruiting efforts during the prior year, which has continued to adversely affect our sales during the current year. The prior year quarter also included heavy Manager and Distributor purchases in advance of price increases the following quarter. Net sales revenue also decreased compared to the same period in the prior year due to changes to some of our promotional programs.

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The NSP United States segment includes both English and Spanish language sales divisions, of which the English language division is approximately 80 percent of segment net sales revenue. English language division net sales revenue decreased \$0.6 million for the three months ended March 31, 2011, or 2.2 percent, compared to the same period in 2010. Our Spanish language division net sales revenue decreased \$0.5 million, or 5.1 percent, for the three months ended March 31, 2011, compared to the same period in 2010. While both the English and Spanish language divisions were significantly affected by shifting the timing of the national convention from 2010 to 2011 and the corresponding effect on Manager and Distributor retention, the change to some of our promotional programs had a more significant impact on our Spanish language division.

During our National Convention held in March 2011, we launched the Brilliant Body, Brilliant Business program and the response from the field was positive. This significant initiative aims to expand our Manager and Distributor base by emphasizing daily consumption of our products and providing an easier and more standardized approach for recruiting and retaining new members. This program is in its early development stage and it is our intention to build the program over the next few years.

Active Managers within NSP United States totaled approximately 6,500 and 7,200 at March 31, 2011 and 2010, respectively. The decrease in the number of active managers was caused by the discontinuance of a program that allowed Distributors to attain

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Manager status by meeting low performance criteria and the lingering effect of shifting the timing of our national convention. Active Distributors within NSP United States totaled approximately 205,000 and 231,000 at March 31, 2011 and 2010, respectively.

NSP International Segment

Our NSP International segment reported net sales revenue for the three months ended March 31, 2011 of \$36.5 million, compared to \$36.2 million for the same period in 2010, an increase of approximately 1.0 percent. In local currencies, net sales decreased 0.3 percent, compared to the same period in 2010. Fluctuation in foreign exchange rates had a \$0.5 million favorable impact on net sales for the three months ended March 31, 2011. The decrease in sales is due to lower local currency sales in our Dominican Republic, Japan and Mexico markets, offset by higher sales in our Russian markets and positive currency fluctuations.

We had the following significant results within the markets of our NSP International segment:

In our Russian markets (Russia, Ukraine and several other Eastern European nations), net sales revenues increased approximately \$1.0 million, or 6.7 percent, for the three months ended March 31, 2011, compared to the same period in 2010. Our Russian markets continue to build on the momentum gained in the prior year as a result of improved Manager and Distributor recruiting efforts and strengthening economies in the region.

In the Dominican Republic, our net sales revenues decreased approximately \$0.5 million, or 41.7 percent, for the three months ended March 31, 2011, compared to the same period in 2010. The decrease in sales is due the elimination of promotional programs and events which historically had promoted sales growth, but did not produce profitable results.

In Japan, our net sales revenues decreased approximately \$0.2 million, or 10.0 percent, for the three months ended March 31, 2011, compared to the same period in 2010. In local currency, net sales decreased 20.0 percent, compared to the same period in 2010. Fluctuations in foreign exchange rates had a \$0.2 million favorable impact on net sales for the three months ended March 31, 2011. The decrease in local currency sales is partially due to the recent earthquake, tsunami and subsequent nuclear disasters, which has suppressed consumer confidence and spending and has made it difficult to ship ordered products, as well as retain active Distributors. Our future sales may be negatively affected while Japan begins to rebuild and recover from these recent disasters.

In Mexico, our net sales revenues decreased approximately \$0.3 million, or 8.3 percent, for the three months ended March 31, 2011, compared to the same period in 2010. In local currency, net sales decreased 14.3 percent, compared to the same period in 2010. Fluctuations in foreign exchange rates had a \$0.2 million favorable impact on net sales for the three months ended March 31, 2011. The decrease in local currency net sales is due to a tax law interpretation by the Mexican taxing authority requiring the collection of value-added tax on all of our products sold in Mexico.

Active Managers within NSP International totaled approximately 21,200 and 21,000 at March 31, 2011 and 2010, respectively. Active Distributors within NSP International totaled approximately 409,800 and 387,500 at March 31, 2011 and 2010 respectively.

Synergy Worldwide Segment

Synergy Worldwide reported net sales revenue for the three months ended March 31, 2011 of \$20.7 million, compared to \$13.9 million in 2010, an increase of approximately 48.1 percent. In local currencies, net sales increased 42.8 percent for the three months ended March 31, 2011, compared to the same period in 2010. Fluctuations in foreign exchange rates had a \$0.7 million favorable impact on net sales for the three months ended March 31, 2011 compared to the same period in 2010. The increase in net sales was primarily due to growth in our United States, Korean and European markets, and the opening of our Vietnam market, offset by sales declines in our Japan market.

We had the following significant results within the markets of our Synergy Worldwide segment:

In the United States, our net sales revenues increased approximately \$2.5 million, or 96.2 percent, for the three months ended March 31, 2011, compared to the same period in 2010. Our growth within the United States is due to effective Company and Manager sales and marketing efforts of a well-accepted product offering, which has resulted in the growth of our U.S. Distributor base.

In Europe, our net sales revenues increased approximately \$2.2 million, or 88.0 percent, for the three months ended March 31, 2011, compared to the same period in 2010. In local currency, our net sales increased 83.1 percent, compared to the same period in 2010. Fluctuations in foreign exchange rates had a \$0.1 million favorable impact on net sales for the three months ended March 31, 2011 compared to the same period in 2010. Our growth in Europe is due to increased market penetration primarily within Austria, Norway and Sweden.

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In Korea, our net sales revenues increased approximately \$1.4 million, or 70.0 percent, for the three months ended March 31, 2011, compared to the same period in 2010. In local currency, our net sales increased 60.3 percent, compared to the same period in 2010. Fluctuations in foreign exchange rates had a \$0.1 million favorable impact on net sales for the three months ended March 31, 2011, compared to the same period in 2010. Our growth in Korea is due to strong and productive Company and Manager development of sales groups and a broader product line that is well accepted in the market.

In Japan, our net sales revenues decreased approximately \$0.1 million, or 2.5 percent, for the three months ended March 31, 2011, compared to the same period in 2010. In local currency, net sales decreased 13.6 percent compared to the same period in 2010. Fluctuations in foreign exchange rates had a \$0.4 million favorable impact on net sales for the three months ended March 31, 2011, compared to the same period in 2010. Recent signs of strengthening of the business in Japan were stalled by the recent earthquake, tsunami and subsequent nuclear disaster. Our future sales may be negatively affected while Japan begins to rebuild and recover from these recent disasters.

Active Managers within Synergy Worldwide totaled approximately 2,600 and 1,700 at March 31, 2011 and 2010, respectively. Active Distributors within Synergy Worldwide totaled approximately 81,600 and 74,700 at March 31, 2011 and 2010, respectively.

Further information related to NSP United States, NSP International and Synergy Worldwide business segments is set forth in Note 9 to the Unaudited Condensed Consolidated Financial Statements in Part 1, Item 1 of this report.

Cost of Goods Sold

Cost of goods sold as a percent of net sales revenue decreased to 20.0 percent in 2011 compared to 20.6 percent in 2010. This decrease is primarily due to the write-off of finished products in some of our foreign markets during the prior year, offset by increased importation fees related to higher transfer prices within some of our foreign markets during the current quarter and changes in product mix between markets.

Volume Incentives

Volume incentives are a significant part of our direct sales marketing program and represent commission payments made to our independent Distributors and Managers. These payments are designed to provide incentives for reaching higher sales levels and for recruiting additional Distributors. Volume incentives vary slightly, on a percentage basis, by product due to our pricing policies and commission plans in place in our various operations. Volume incentives as a percent of net sales revenue decreased to 36.9 percent in 2011, compared to 37.5 percent in 2010. The decrease is primarily due to reductions in volume incentive payment rates due to our lower Manager and Distributor base within the NSP United States segment and an increase in product purchases with a lower volume incentive in Synergy Worldwide.

Selling, General and Administrative

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Selling, general and administrative expenses decreased to 34.9 percent of net sales revenue for the three months ended March 31, 2011, compared to 41.2 percent in 2010, or by approximately \$3.4 million to \$32.4 million in the first quarter of 2011.

Significant increases to selling, general and administrative expenses during the three months ended March 31, 2011, compared to the same period in 2010 included:

- increased variable costs of \$0.7 million related to the sales growth of Synergy Worldwide in Europe, Korea, the United States and Vietnam as well as NSP International in the Russian markets;
- approximately \$0.5 million of unfavorable currency fluctuations, which may be recurring depending upon changes in future exchange rates relative to the U.S. dollar; and
- approximately \$0.4 million in professional fees related to litigation costs.

Significant decreases to selling, general and administrative expenses during the three months ended March 31, 2011, compared to the same period in 2010 included:

- decreased administrative costs of \$1.5 million in U.S. convention related costs due to the differences in event qualification periods between years;
- decreased U.S. compensation and other benefit related costs of \$1.0 million;
- cost reductions in many of our foreign markets totaling approximately \$1.0 million;
- a \$0.4 million decrease in foreign value-added tax reserves between periods;

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- a \$0.4 million decrease in U.S. sales tax reserves between periods; and
- a decrease of \$0.4 million related to our U.S. healthcare costs during 2011.

We continue to implement cost reduction measures within all of our operating segments.

Operating Income

Consolidated operating income increased approximately \$7.1 million during the three months ended March 31, 2011, compared to the same period in 2010, from \$0.6 million to \$7.6 million.

Operating income for NSP United States increased \$3.3 million for the three months ended March 31, 2011, compared to the same period in 2010, from \$0.5 million to \$3.8 million. The increase in operating income is primarily the result of significant cost reductions in our selling, general and administrative expenses described above.

Operating income for NSP International increased approximately \$1.2 million for the three months ended March 31, 2011, compared to the same period in 2010, from \$0.8 million to \$2.1 million, primarily as the result cost reductions within our foreign markets and positive change in foreign VAT reserves, offset in part by increased costs related to growth in our Russian markets.

Operating income for Synergy Worldwide increased \$2.5 million for the three months ended March 31, 2011, compared to the same period in 2010, from an operating loss of \$0.7 million to operating income of \$1.8 million. This was primarily due to improvements in sales within its European, U.S. and Korean subsidiaries.

Other Income, Net

Other income, net for the three months ended March 31, 2011 decreased \$2.6 million, compared to the same period in 2010. The decrease is primarily due to prior year foreign exchange gains of \$3.7 million in Venezuela as a result of the devaluation of the bolivar and the change to a highly inflationary economy that were non-recurring, offset by net foreign exchange gains and losses in certain of our other markets based on changes in exchange rates.

Income Taxes

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Interim income taxes are based on an estimated annualized effective tax rate applied to the respective quarterly periods, adjusted for discrete tax items in the period in which they occur. For the three months ended March 31, 2011 and 2010, the Company's provision (benefit) for income taxes, as a percentage of income before income taxes (benefit), was a tax provision of 16.0 percent and a benefit of 37.5 percent, respectively, compared with a U.S. federal statutory rate of 35.0 percent.

The difference between the effective tax rate and the U.S. federal statutory tax rate for the three months ended March 31, 2011 was primarily attributed to net decreases in tax liabilities associated with uncertain tax positions due to the expiration of the statute of limitations on certain liabilities in various foreign jurisdictions, which resulted in a tax benefit of approximately \$1.2 million.

The differences between the effective tax rate and the federal statutory tax rate for the three months ended March 31, 2010 were primarily attributed to:

- decreases in tax liabilities associated with uncertain tax positions due to the expiration of the statute of limitations on certain liabilities in various foreign jurisdictions, which resulted in a tax benefit of \$1.4 million,
- foreign subsidiary net losses for which no tax benefit was being recognized, and
- the foreign exchange gain related to the implementation of highly-inflationary accounting for Venezuela recognized for financial reporting purposes, but not for income tax purposes.

The Company's U.S. federal income tax returns for 2003 through 2009 are open to examination for federal tax purposes. The Company has several foreign tax jurisdictions which have open tax years from 2000 through 2009. The Internal Revenue Service (IRS) is currently conducting an audit of the Company's U.S. federal income tax returns for the 2006 through 2008 tax years.

In October 2009, the IRS issued an examination report formally proposing adjustments with respect to the 2003 through 2005 taxable years, which primarily relate to the prices that were charged in intra-group transfers of property and the disallowance of related deductions. The Company has commenced administrative proceedings with the Office of Appeals of the Internal Revenue Service challenging the proposed adjustments. Management believes that the Company has appropriately reserved for these matters at an amount which it believes will ultimately be due upon resolution of the administrative proceedings, and such amounts reflect

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management's estimates based upon available evidence resulting from discussions with the IRS Office of Appeals. These estimates are based upon a more-likely-than-not recognition threshold. The Company is currently unable to determine the outcome of these discussions and their related impact, if any, on the Company's financial condition, results of operations, or cash flows.

Although the Company believes its estimates are reasonable, the Company can make no assurance that the final tax outcome of these matters will not be different from that which it has reflected in its historical income tax provisions and accruals. Such difference could have a material impact on the Company's income tax provision and operating results in the period in which the Company makes such determination.

Discontinued Operations

During 2010, we ceased our operations in Brazil as a result of increased import regulations and declining sales. As a result, we reclassified the Brazil subsidiary's operations to discontinued operations. During 2011, there were no significant costs related to this market. This market represented less than 0.3 percent of our consolidated net sales for 2010.

LIQUIDITY AND CAPITAL RESOURCES

Our principal use of cash is to pay for operating expenses, including volume incentives, inventory and raw material purchases, capital assets and funding of international expansion. As of March 31, 2011, working capital was \$48.7 million, compared to \$41.4 million as of December 31, 2010. At March 31, 2011, we had \$55.4 million in cash and cash equivalents, of which \$43.9 million was held in our foreign markets and may be subject to various withholding taxes and other restrictions related to repatriation, and \$5.8 million in unrestricted short-term investments, which were available to be used along with our normal cash flows from operations to fund any unanticipated shortfalls in future cash flows.

Our net consolidated cash inflows (outflows) are as follows (in thousands):

| | Three Months Ended March 31, | |
|----------------------|-------------------------------------|-------------|
| | 2011 | 2010 |
| Operating activities | 7,253 | \$ 3,512 |
| Investing activities | 477 | (704) |
| Financing activities | | |

For the three months ended March 31, 2011, we generated cash from operating activities of \$7.3 million compared to \$3.5 million for the same period in 2010. Operating cash flow improved due to growth in our operating income, the timing of payments for accrued volume incentives and income taxes payable, and was offset by the timing of payments and receipts for accounts receivable and accrued liabilities.

Capital expenditures related to the purchase of equipment, computer systems and software for the three months ended March 31, 2011 and 2010 were \$0.2 million and \$0.7 million, respectively.

During the three months ended March 31, 2011, we had cash proceeds of \$0.7 million from the sale of available-for-sale investments.

We do not currently maintain a long-term credit facility or any other external sources of long-term funding; however, we are exploring the possibility of establishing a long-term credit facility. We believe that our working capital requirements can be met for the foreseeable future with the cash generated from our operating activities and our available cash and cash equivalents. However, among other things, a prolonged economic downturn, a decrease in demand for our products, an unfavorable settlement of our unrecognized tax positions or non-income tax contingencies could adversely affect our long-term liquidity. Therefore, we believe it is prudent to explore the possibility of establishing a long-term credit facility and that such funding can be established with competitive terms.

We have the ability to borrow up to approximately 80 percent of the fair value of our municipal obligations within our available-for-sale investments.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our unaudited consolidated financial statements have been prepared in accordance with U.S. GAAP and form the basis for the following discussion and analysis on critical accounting policies and estimates. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related

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disclosure of contingent assets and liabilities. On a regular basis we evaluate our estimates and assumptions. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates and those differences could have a material effect on our financial position and results of operations. Management has discussed the development, selection and disclosure of these estimates with the Board of Directors and its Audit Committee.

A summary of our significant accounting policies is provided in Note 1 of the Notes to Consolidated Financial Statements in Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2010. We believe the critical accounting policies and estimates described below reflect our more significant estimates and assumptions used in the preparation of our consolidated financial statements. The impact and any associated risks on our business that are related to these policies are also discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations where such policies affect reported and expected financial results.

Revenue Recognition

Net sales revenue and related volume incentive expenses are recorded when persuasive evidence of an arrangement exists, collectability is reasonably assured, the amount is fixed and determinable, and title and risk of loss have passed, generally when the merchandise has been delivered. The amount of the volume incentive is determined based upon the amount of qualifying purchases in a given month. It is necessary for us to make estimates about the timing of when merchandise has been delivered. These estimates are based upon our historical experience related to time in transit, and timing of when shipments occurred and shipping volumes. Amounts received for undelivered merchandise are recorded as deferred revenue. From time to time, our U.S. operations extend short-term credit associated with product promotions. In addition for certain of our international operations, we offer credit terms consistent with industry standards within the country of operation. Payments to Distributors and Managers for sales incentives or rebates are recorded as a reduction of revenue. Payments for sales incentives and rebates are calculated monthly based upon qualifying sales. Membership fees are deferred and amortized as revenue over the life of the membership, primarily one year. Prepaid event registration fees are deferred and recognized as revenues when the related event is held.

A reserve for product returns is recorded based upon historical experience. We allow Distributors or Managers to return the unused portion of products within ninety days of purchase if they are not satisfied with the product. In some of our markets, the requirements to return product are more restrictive.

Investments

Our available-for-sale investment portfolio is recorded at fair value and consists of various fixed income securities such as U.S. government and state and municipal bonds, mutual funds, depository certificates and equity securities. These investments are valued using (a) quoted prices for identical assets in active markets or (b) from significant inputs that are observable or can be derived from or corroborated by observable market data for substantially the full term of the asset. Our trading portfolio is recorded at fair value and consists of various marketable securities that are valued using quoted prices in active markets.

For available-for-sale debt securities with unrealized losses, we perform an analysis to assess whether it intends to sell or whether it would be more likely than not required to sell the security before the expected recovery of the amortized cost basis. Where we intend to sell a security, or

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may be required to do so, the security's decline in fair value is deemed to be other-than-temporary and the full amount of the unrealized loss is recorded within earnings as an impairment loss.

For all other debt securities that experience a decline in fair value that is determined to be other-than-temporary and not related to credit loss, we record a loss, net of any tax, in accumulated other comprehensive income (loss). The credit loss is recorded within earnings as an impairment loss when sold. Management judgment is involved in evaluating whether a decline in an investment's fair value is other-than-temporary.

Regardless of our intent to sell a security, we perform additional analysis on all securities with unrealized losses to evaluate losses associated with the creditworthiness of the security. Credit losses are identified where we do not expect to receive cash flows sufficient to recover the amortized cost basis of a security.

For equity securities, when assessing whether a decline in fair value below our cost basis is other-than-temporary, we consider the fair market value of the security, the length of time and extent to which market value has been less than cost, the financial condition and near-term prospects of the issuer as well as specific events or circumstances that may influence the operations of the issuer, and our intent and ability to hold the investment for a sufficient time in order to enable recovery of our cost. New information and the passage of time can change these judgments. Where we have determined that we lack the intent and ability to hold an equity

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security to its expected recovery, the security's decline in fair value is deemed to be other-than-temporary and is recorded within earnings as an impairment loss.

Inventories

Inventories are stated at the lower-of-cost-or-market, using the first-in, first-out method. The components of inventory cost include raw materials, labor and overhead. To estimate any necessary lower-of-cost-or-market adjustments, various assumptions are made in regard to excess or slow-moving inventories, non-conforming inventories, expiration dates, current and future product demand, production planning and market conditions.

Self-Insurance Liabilities

Similar to other manufacturers and distributors of products that are ingested, we face an inherent risk of exposure to product liability claims in the event that, among other things, the use of our products results in injury to consumers due to tampering by unauthorized third parties or product contamination. We have historically had a very limited number of product claims or reports from individuals who have asserted that they have suffered adverse consequences as a result of using our products. These matters have historically been settled to our satisfaction and have not resulted in material payments. We have established a wholly owned captive insurance company to provide us with product liability insurance coverage and have accrued a reserve that we believe is sufficient to cover probable and reasonable estimable liabilities related to product liability claims based upon our history. However, there can be no assurance that these estimates will prove to be sufficient, nor can there be any assurance that the ultimate outcome of any litigation for product liability will not have a material negative impact on our business prospects, financial position, results of operations or cash flows.

We self-insure for certain employee medical benefits. The recorded liabilities for self-insured risks are calculated using actuarial methods and are not discounted. The liabilities include amounts for actual claims and claims incurred but not reported. Actual experience, including claim frequency and severity as well as health care inflation, could result in actual liabilities being more or less than the amounts currently recorded.

Incentive Trip Accrual

We accrue expenses for incentive trips associated with our direct sales marketing program, which rewards independent Distributors and Managers with paid attendance at our conventions and meetings. Expenses associated with incentive trips are accrued over qualification periods as they are earned. We specifically analyze incentive trip accruals based on historical and current sales trends as well as contractual obligations when evaluating the adequacy of the incentive trip accrual. Actual results could generate liabilities more or less than the amounts recorded.

Impairment of Long-Lived Assets

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We review our long-lived assets, such as property, plant and equipment and intangible assets for impairment when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. We use an estimate of future undiscounted net cash flows of the related assets or groups of assets over their remaining lives in measuring whether the assets are recoverable. An impairment loss is calculated by determining the difference between the carrying values and the fair values of these assets. As of March 31, 2011 and December 31, 2010, we did not consider any of our long-lived assets to be impaired.

Contingencies

We are involved in certain legal proceedings. When a loss is considered probable in connection with litigation or non-income tax contingencies and when such loss can be reasonably estimated with a range, we record our best estimate within the range related to the contingency. If there is no best estimate, we record the minimum of the range. As additional information becomes available, we assess the potential liability related to the contingency and revise the estimates. Revision in estimates of the potential liabilities could materially affect our results of operations in the period of adjustment. Our contingencies are discussed in further detail in Note 11, *Commitments and Contingencies*, to the Notes of our Condensed Consolidated Financial Statements, of Item 1, Part 1 of this report.

Income Taxes

Our income tax expense, deferred tax assets and liabilities and contingent reserves reflect management's best assessment of estimated future taxes to be paid. We are subject to income taxes in both the United States and numerous foreign jurisdictions. Significant judgments and estimates are required in determining the Company's consolidated income tax expense.

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Deferred income taxes arise from temporary differences between the tax and financial statement recognition of revenue and expense. In evaluating our ability to recover our deferred tax assets, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. In projecting future taxable income, we develop assumptions including the amount of future state, federal and foreign pretax operating income, the reversal of temporary differences, and the implementation of feasible and prudent tax planning strategies. These assumptions require significant judgment about the forecasts of future taxable income and are consistent with the plans and estimates that we are using to manage the underlying businesses. Valuation allowances are recorded as reserves against net deferred tax assets by the Company when it is determined that net deferred tax assets are not likely to be realized in the foreseeable future.

Changes in tax laws and rates could also affect recorded deferred tax assets and liabilities in the future. Management is not aware of any such changes that would have a material effect on the Company's results of operations, cash flows or financial position.

The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax laws and regulations in a multitude of jurisdictions across our global operations. Income tax positions must meet a more-likely-than-not recognition threshold to be recognized.

Share-Based Compensation

We recognize all share-based payments to employees, including grants of employee stock options, to be recognized in the statement of operations based on their grant-date fair values. We record compensation expense, net of an estimated forfeiture rate, over the vesting period of the stock options based on the fair value of the stock options on the date of grant. We estimate the forfeiture rate based upon historical experience.

RECENT ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1 to the Unaudited Condensed Consolidated Financial Statements in Part 1, Item 1 of this report for information regarding recently issued accounting pronouncements.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

The Management's Discussion and Analysis of Financial Condition and Results of Operations and other sections of this report may contain forward-looking statements. Such forward-looking statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities and Exchange Act. All statements other than statements of historical fact are forward-looking statements. Forward-looking statements may include, but are not limited to, statements relating to our objectives, plans and strategies. All statements (other than statements of historical fact) that address activities, events or developments that we intend, expect, project, believe or anticipate will or may occur in the future are forward-looking statements. These statements are often characterized by terminology such as believe, hope, may, anticipate, should, intend, plan, will, expect, estimate, project, positioned, strategy and similar terms, based on assumptions and assessments made by management in light of their experience and their perception of historical trends, current

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conditions, expected future developments and other factors they believe to be appropriate. Forward-looking statements are not guarantees of future performance and are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified. Future events and actual results could differ materially from those set forth in, contemplated by, or underlying the forward-looking statements.

Important factors that could cause our actual results, performance and achievements, or industry results to differ materially from estimates or projections contained in our forward-looking statements includes, among others, the following:

- our relationship with and our ability to influence the actions of our independent Distributors and Managers;
- our ability to attract and retain a sufficient number of independent Distributors and Managers;
- changes in laws and regulations regarding network marketing that may prohibit or restrict our ability to sell our products in new or existing markets;
- determinations regarding tax liabilities and required tax obligations in U.S. and foreign jurisdictions;
- our products and manufacturing activities are subject to extensive government regulations and restrictions;
- general economic conditions;

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- an economic slowdown in the markets in which we do business could reduce consumer demand for our products;
- currency and exchange rate fluctuations could lower our revenue and net income;
- some of the markets in which we operate may become highly inflationary;
- some of the markets in which we operate have currency controls in place which restrict our ability to repatriate funds to the United States;
- the availability and integrity of raw materials could be compromised;
- significant legal disputes and adverse settlements;
- geopolitical issues and conflicts could adversely affect our business;
- our business is subject to the effects of adverse publicity and negative public perception;
- changes in taxation and transfer pricing could affect our operations;
- our business is subject to intellectual property risks;
- product and liability claims;
- changing consumer preferences and demands;

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- inventory obsolescence due to finite shelf lives and changing product demand;
- product concentration;
- system failures;
- changes in key management personnel; and
- the competitive nature of our business.

Additional factors that could cause actual results to differ materially from our forward-looking statements are set forth in this report and our Annual Report on Form 10-K for the fiscal year ended December 31, 2010 under the heading Risk Factors.

Forward-looking statements in this report speak only as of the date hereof, and forward-looking statements in documents attached that are incorporated by reference speak only as of the date of those documents. We do not undertake any obligation to update or release any revisions to any forward-looking statement or to report any events or circumstances after the date hereof or to reflect the occurrence of unanticipated events, except as required by law.

Item 3. *QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK*

We conduct business in several countries and intend to continue to grow our international operations. Net sales revenue, operating income and net income are affected by fluctuations in currency exchange rates, interest rates and other uncertainties inherent in doing business and selling product in more than one currency. In addition, our operations are exposed to risks associated with changes in social, political and economic conditions inherent in international operations, including changes in the laws and policies that govern international investment in countries where we have operations, as well as, to a lesser extent, changes in United States laws and regulations relating to international trade and investment.

Foreign Currency Risk

During the three months ended March 31, 2011, approximately 56.1 percent of our net sales revenue and approximately 55.6 percent of our operating expenses were realized outside of the United States. Inventory purchases are transacted primarily in U.S. dollars from vendors located in the United States. The local currency of each international subsidiary is generally the functional currency, while certain regions, including Russia and the Ukraine, are served by a U.S. subsidiary through third party entities, for which all business is conducted in U.S. dollars. We conduct business in twenty-three different currencies with exchange rates that are not on a one-to-one relationship with the U.S. dollar. All revenues and expenses are translated at average exchange rates for the

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periods reported. Therefore, our operating results will be positively or negatively affected by a weakening or strengthening of the U.S. dollar in relation to another fluctuating currency. Given the uncertainty and diversity of exchange rate fluctuations, we cannot estimate the effect of these fluctuations on our future business, product pricing, results of operations, or financial condition, but we have provided consolidated sensitivity analyses below of functional currency/reporting currency exchange rate risks. Changes in various currency exchange rates affect the relative prices at which we sell our products. We regularly monitor our foreign currency risks and periodically take measures to reduce the risk of foreign exchange rate fluctuations on our operating results. We do not use derivative instruments for hedging, trading or speculating on foreign exchange rate fluctuations. Additional discussion of the impact on the effect of currency fluctuations has been included in our management's discussion and analysis included in Part I, Item 2 of this report.

The following table sets forth a composite sensitivity analysis of our net sales revenue, costs and expenses and operating income in connection with strengthening of the U.S. dollar (our reporting currency) by 10%, 15% and 25% against every other fluctuating functional currency in which we conduct business. We note that our individual net sales revenue, cost and expense components and our operating income were equally sensitive to increases in the strength of the U.S. dollar against every other fluctuating currency in which we conduct business.

Exchange rate sensitivity for the three months ended March 31, 2011 (dollar amounts in thousands)

| | | With Strengthening of U.S. Dollar by: | | | | | |
|-------------------------------------|-----------|---------------------------------------|--------|------------|--------|------------|--------|
| | | 10% | | 15% | | 25% | |
| | | (\$) | (%) | (\$) | (%) | (\$) | (%) |
| Net sales revenue | \$ 92,844 | \$ (2,939) | (3.2)% | \$ (4,216) | (4.5)% | \$ (6,465) | (7.0)% |
| Cost and expenses | | | | | | | |
| Cost of goods sold | 18,552 | (545) | (2.9)% | (782) | (4.2)% | (1,198) | (6.5)% |
| Volume incentives | 34,298 | (1,107) | (3.2)% | (1,588) | (4.6)% | (2,435) | (7.1)% |
| Selling, general and administrative | 32,373 | (1,039) | (3.2)% | (1,490) | (4.6)% | \$ (2,285) | (7.1)% |
| Operating income | \$ 7,621 | \$ (248) | (3.3)% | \$ (356) | (4.7)% | \$ (547) | (7.2)% |

As noted above, certain of our operations, including Russia and the Ukraine, are served by a U.S. subsidiary through third-party entities, for which all business is conducted in U.S. dollars. Although changes in exchange rates between the U.S. dollar and the Russian ruble or the Ukrainian hryvnia do not result in currency fluctuations within our financial statements, a weakening or strengthening of the U.S. dollar in relation to these other currencies can significantly affect the prices of our products and the purchasing power of our independent Managers and Distributors within these markets.

The following table sets forth a composite sensitivity analysis of our financial instruments by those balance sheet line items that are subject to exchange rate risk, together with the total gain or loss from the strengthening of the U.S. dollar in relation to our various fluctuating functional currencies. The sensitivity of our assets and liabilities, taken by balance sheet line items, is somewhat less than the sensitivity of our operating income to increases in the strength of the U.S. dollar in relation to other fluctuating currencies in which we conduct business.

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Exchange rate sensitivity of Balance Sheet as of March 31, 2011 (dollar amounts in thousands)

| | With Strengthening of U.S. Dollar by: | | | | | | |
|----------------------------------------------------------------------|---------------------------------------|------------|--------|------------|---------|------------|---------|
| | 10% | | 15% | | 25% | | |
| | (\$) | (%) | (\$) | (%) | (\$) | (%) | |
| Financial Instruments | | | | | | | |
| Included in Current Assets | | | | | | | |
| Subject to Exchange Rate Risk | | | | | | | |
| Cash and cash equivalents | \$ 55,418 | \$ (3,848) | (6.9)% | \$ (5,521) | (10.0)% | \$ (8,465) | (15.3)% |
| Available-for-sale investments | 5,788 | (242) | (4.2)% | (347) | (6.0)% | (532) | (9.2)% |
| Accounts receivable, net | 10,671 | (392) | (3.7)% | (563) | (5.3)% | (863) | (8.1)% |
| Financial Instruments | | | | | | | |
| Included in Current Liabilities Subject to Exchange Rate Risk | | | | | | | |
| Accounts payable | 4,485 | (80) | (1.8)% | (115) | (2.6)% | (176) | (3.9)% |
| Net Financial Instruments Subject to Exchange Rate Risk | | | | | | | |
| | | (4,402) | | (6,316) | | (9,684) | |

The following table sets forth the local currencies other than the U.S. dollar in which our assets that are subject to exchange rate risk were denominated as of March 31, 2011, and exceeded \$1 million upon translation into U.S. dollars. None of our liabilities that are denominated in a local currency other than the U.S. dollar and that are subject to exchange rate risk exceeded \$1 million upon translation into U.S. dollars. We use the spot exchange rate for translating balance sheet items from local currencies into our reporting currency. The respective spot exchange rate for each such local currency meeting the foregoing thresholds is provided in the table as well.

Translation of Balance Sheet Amounts Denominated in Local Currency as of March 31, 2011 (dollar amounts in thousands)

| | Translated into U.S. Dollars | At Spot Exchange Rate per One U.S. Dollar as of March 31, 2011 |
|-----------------------------------------------------|------------------------------|----------------------------------------------------------------|
| Cash and Cash Equivalents | | |
| Japan (Yen) | \$ 7,691 | 82.9 |
| European Markets (Euro) | 4,033 | 0.7 |
| Canada (Dollar) | 4,005 | 1.0 |
| Mexico (Peso) | 2,388 | 11.9 |
| Colombia (Peso) | 1,963 | 1,894.6 |
| South Korea (Won) | 1,540 | 1,105.8 |
| Honduras (Lempira) | 1,423 | 7.8 |
| Indonesia (Rupiah) | 1,179 | 8,748.9 |
| Venezuela (Bolivar) | 1,215 | 5.3 |
| Other | 7,073 | Varies |
| Total foreign denominated cash and cash equivalents | 32,510 | |

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| | | | |
|--------------------------------------------------------------|----|--------|--------|
| U.S. dollars held by foreign subsidiaries | | 11,346 | |
| Total cash and cash equivalents held by foreign subsidiaries | \$ | 43,856 | |
| Accounts Receivable | | | |
| Japan (Yen) | \$ | 1,172 | 82.9 |
| Other | | 3,145 | Varies |
| Total | \$ | 4,317 | |

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Finally, the following table sets forth the annual weighted average of fluctuating currency exchange rates of each of the local currencies per one U.S. dollar for each of the local currencies in which sales revenue exceeded \$10.0 million during any of the two periods presented. We use the annual average exchange rate for translating items from the statement of operations from local currencies into our reporting currency.

| Three months ended March 31, | 2011 | 2010 |
|-------------------------------------|----------------|-------------|
| Canada (Dollar) | 1.0 | 1.1 |
| Japan (Yen) | 81.6 | 90.7 |
| Korea (Won) | 1,122.3 | 1,149.6 |
| Mexico (Peso) | 12.0 | 12.8 |
| Venezuela (Bolivar) | 5.3 | 4.3 |

The local currency of the foreign subsidiaries is used as the functional currency, except for subsidiaries operating in highly inflationary economies or where the Company's operations are served by a U.S. based subsidiary (for example Russia and Ukraine). The financial statements of foreign subsidiaries, where the local currency is the functional currency, are translated into U.S. dollars using exchange rates in effect at year-end for assets and liabilities and average exchange rates during each year for the results of operations. Adjustments resulting from translation of financial statements are reflected in accumulated other comprehensive loss, net of income taxes. Foreign currency transaction gains and losses are included in other income (expense) in the consolidated statements of operations.

The functional currency in highly inflationary economies is the U.S. dollar and transactions denominated in the local currency are re-measured as if the functional currency were the U.S. dollar. The re-measurement of local currencies into U.S. dollars creates translation adjustments, which are included in the consolidated statements of operations. A country is considered to have a highly inflationary economy if it has a cumulative inflation rate of approximately 100 percent or more over a three-year period as well as other qualitative factors including historical inflation rate trends (increasing and decreasing), the capital intensiveness of the operation and other pertinent economic factors. During the three months ended March 31, 2011 and 2010, Venezuela was considered to be highly inflationary. With the exception of Venezuela, there were no other countries considered to have a highly inflationary economy during the three months ended March 31, 2011 and 2010.

As of January 1, 2010, Venezuela was designated as a highly inflationary economy. Accordingly, the U.S. dollar became the functional currency for the Company's subsidiary in Venezuela. All gains and losses resulting from the re-measurement of its financial statements are determined using official rates. On January 8, 2010, the Venezuelan government announced the devaluation of the bolivar against the U.S. dollar.

Currency restrictions enacted by the government of Venezuela require approval from the government's currency control agency organization in order for the Company's subsidiary in Venezuela to obtain U.S. dollars at the official exchange rate to pay for imported products or to repatriate dividends back to the Company. Prior to January 1, 2010 the market rate, which is substantially lower than the official rate, was available to obtain U.S. dollars or other currencies without approval of the government's currency control organization. In 2010, the government of Venezuela enacted additional currency restrictions, which effectively replaced the market rate with the System for Foreign Currency Denominated Securities (SITME), which is administered by the Venezuela Central Bank. Under SITME, entities domiciled in Venezuela can obtain U.S. dollar denominated securities in limited quantities each month through banking institutions approved by the government.

At this time, the Company is not able to estimate reasonably the future state of exchange controls in Venezuela and its availability of U.S. dollars at the official exchange rate or at the SITME rate. However, the Company has been successful repatriating funds from Venezuela for imported products using the SITME rate. The Company re-measures its results in Venezuela at the SITME rate, which was approximately 5.30 bolivars per U.S. dollar as of March 31, 2011.

As a result of the events described in the preceding paragraphs, the Company recorded a gain of \$3.7 million in the first quarter of 2010 in connection with the re-measurement of its balance sheet to reflect the highly inflationary designation and the devaluation due to the negative position of the Company's Venezuelan subsidiary's net monetary assets, which is recorded in foreign exchange gains or losses, a part of other income. The success of future operations will be affected by several factors, including the Company's ability to take actions to mitigate the effect of devaluation, further actions of the Venezuelan government and economic conditions in Venezuela, such as inflation and consumer spending.

During the three months ended March 31, 2011 and 2010, the Company's Venezuelan subsidiary's net sales revenue represented approximately 1.4 percent and 1.7 percent of consolidated net sales revenue, respectively. The Company's Venezuelan subsidiary held total assets of 8.1 million and \$8.0 million (which includes an intercompany receivables denominated in U.S. dollars

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of \$2.0 million and \$2.0 million) and net assets of \$5.2 million and \$4.2 million at March 31, 2011 and December 31, 2010, respectively.

Interest Rate Risk

The primary objectives of our investment activities are to preserve principal while maximizing yields without significantly increasing risk. These objectives are accomplished by purchasing investment grade securities. On March 31, 2011, we had investments of \$5.8 million of which \$1.7 million were municipal obligations, which carry an average fixed interest rate of 5.1 percent and mature over a 5-year period. A hypothetical 1.0 percent change in interest rates would not have had a material effect on our liquidity, financial position or results of operations.

Item 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) are designed to provide reasonable assurance that the information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in rules and forms adopted by the SEC, and that such information is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, to allow timely decisions regarding required disclosures. Our management, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2011. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of March 31, 2011, at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the fiscal quarter ended March 31, 2011, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

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Please refer to Note 11 to the Unaudited Condensed Consolidated Financial Statements in Part 1, Item 1 of this report, as well as our recent SEC filings, including our Annual Report on Form 10-K for the year ended December 31, 2010, for information regarding the status of certain legal proceedings that have been previously reported.

Item 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the risks discussed under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2010, which could materially affect our business or our consolidated financial statements, results of operations, and cash flows. Additional risks not currently known to us, or risks that we currently believe are not material, may also impair our business operations. There have been no material changes to our risk factors since the filing of our Annual Report on Form 10-K for the year ended December 31, 2010.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. REMOVED AND RESERVED

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Item 5. OTHER INFORMATION

None.

Item 6. EXHIBITS

a) Index to Exhibits

| Item No. | Exhibit |
|-----------------|-----------------------------------------------------------------------------------------------------------------------------------|
| 31.1(1) | Certification of Chief Executive Officer under SEC Rule 13a 14(a)/15d 14(a) promulgated under the Securities Exchange Act of 1934 |
| 31.2(1) | Certificate of Chief Financial Officer under SEC Rule 13a 14(a)/15d 14(a) promulgated under the Securities Exchange Act of 1934 |
| 32.1(1) | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 |
| 32.2(1) | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 |

(1) Filed currently herewith.

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SIGNATURES

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

NATURE S SUNSHINE PRODUCTS, INC.

Date: May 6, 2011

/s/ Michael D. Dean
Michael D. Dean, President and Chief Executive Officer

Date: May 6, 2011

/s/ Stephen M. Bunker
Stephen M. Bunker, Executive Vice President, Chief Financial Officer
and Treasurer