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EDITED TRANSCRIPT

MAT - Q1 2016 Mattel Inc Earnings Call

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OVERVIEW:

MAT reported 1Q16 reported EPS of negative \$0.21. Expects 2016 net sales to be relatively flat in constant currency. Expects 2Q16 gross sales to be relatively flat in constant currency.



CORPORATE PARTICIPANTS

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Mattel Inc. first-quarter 2016 earnings conference call. (Operator Instructions)

As a reminder, this call is being recorded.

I would now like to turn the conference over to Martin Gilkes, Vice President, Investor Relations. Please go ahead.

Martin Gilkes - Mattel, Inc. - VP, Corporate Strategy and IR

Thank you, Sabrina. Good afternoon, everyone. Joining me today are Chris Sinclair, Mattel's Chairman and Chief Executive Officer; Richard Dickson, Mattel's President and Chief Operating Officer; and Kevin Farr, Mattel's Chief Financial Officer.

As you know, this afternoon we reported Mattel's 2016 first-quarter financial results. We will begin today's call with Chris, Richard and Kevin providing commentary on our results, and then we'll take your questions.

To help guide our discussion today, we have provided you with a slide presentation. Both our earnings release and slide presentation include non-GAAP financial measures. The information required by Regulation G regarding non-GAAP financial measures is included in these materials, and both documents are available on the investors section of our corporate website, corporate. Mattel.com.

Before we begin, I'd like to remind you that certain statements made during the call may include forward-looking statements related to the future performance of our overall business, brands and product lines. These statements are based on currently available information, and they are subject to a number of significant risks and uncertainties that could cause our actual results to differ materially from those projected in the forward-looking statements.

We describe some of these uncertainties in the risk factors section of our 2015 annual report on Form 10-K, our 2015 quarterly reports on Form 10-Q and other filings we make with the SEC from time to time as well as in other public statements.



Mattel does not update forward-looking statements and expressly disclaims any obligation to do so.

Now I'd like to turn the call over to Chris.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

Thanks, Martin, and welcome, everyone. I'd like to thank you for joining us. Today, I'm going to lead things off with a brief perspective on both the quarter and the full year, and then Richard and Kevin will each provide some additional details. And, as usual, we'll open things up at the end for any questions you might have.

Let me begin by saying that, overall, we are very encouraged by the start of the year and particularly with our ability to hold the top line as we offset the loss of Disney Princess. We also made some good progress against our cost reduction goals, both in cost of goods and in SG&A.

The offsetting negative, of course, continues to be significant headwinds in foreign exchange, both in translation and transaction, which depressed our gross margins in the quarter.

We also recorded a \$26 million charge in other income to recognize adjustments from Venezuela's currency devaluation, which I think most of you know has severely impacted most corporations with operations in that country.

Putting aside foreign exchange, the net message is that we continue to make good progress on our strategic priorities. And we also remain on track to execute well and to deliver on our outlook for this year. And we're certainly setting up well to restore real growth in 2017 and beyond.

Our shipments and POS were closely aligned in this quarter, with POS positive and shipments off slightly in constant currency. We were also encouraged by solid POS trends on key core brands like Barbie, Fisher-Price and Hot Wheels, and by a number of our key brands within the Toy Box.

Importantly, our retail space also stabilized versus last year. And shelf productivity has remained strong, which we expect will support some expansion opportunities on shelf space this fall.

We also continued to execute well broadly across much of our customer base. To this latter point, while North America remains a good leading indicator of our progress, with positive shipping in the quarter, we are also seeing some fairly broad-based strength across most regions, particularly in our emerging markets.

As for the middle of the P&L, we also made some good progress, and we do remain on track with our cost targets, the performance of which was largely masked, at least in gross margin, by the impact of currencies.

Here, it is important to point out that on a constant currency basis gross margin was actually relatively stable. Looking ahead, we expect the cost savings to accelerate through the balance of the year. We also expect the seasonal impacts from foreign exchange and from the loss of Disney Princess to begin to mitigate. Net, we are still tracking to our expectations.

Finally, I'd note that our balance sheet remains strong. We're continuing to invest in the business and to maintain our dividend.

To summarize, we are encouraged, and we remain cautiously optimistic about the way the year is setting up. It's early, and we still have a lot of work ahead. But we are executing well. Our entertainment drivers and most of our important brands are performing. We're expanding rapidly in key emerging markets. And we are getting out the costs that we expected to.

A little help from foreign exchange would be nice as well, but we do think that we have this accounted for as we move through the year.

What this all means is that we continue to see things taking shape, much as we communicated to you in February at Toy Fair. Our outlook for 2016 is largely unchanged, and we're tracking well for strong performance next year.

With that as a setup, let me turn things over to Richard to highlight some of our top-line progress and our core initiatives. He'll be followed by Kevin, who will give you a lot more color on our performance and on our outlook. Richard?

Richard Dickson - Mattel, Inc. - President and COO



Thank you, Chris. As Chris said, we are making progress on many fronts, with lots of positive indicators of our success, not the least of which is the attention Mattel's transformation is receiving worldwide. Consumers and the media are once again focused on our brands and our products rather than our challenges.

And while much of the attention we've been receiving has revolved around key strategic priorities, we attribute our success largely to quarter after quarter of solid execution. And our first-quarter execution demonstrates that we are off to a good start with consumer takeaway and shipping, giving us even more confidence that we can achieve our 2016 goal to hold the top line relatively flat in constant currency.

Let's review some specifics. We were pleased to see continued positive global POS, up 2%, normalizing for the Easter holiday with considerable POS strength in international markets. One of the most encouraging stats this quarter is that we almost completely offset the loss of the Disney Princess license, which represented about \$100 million, or 10%, of last year's sales. This was accomplished through great execution across the entire organization. And when the impact of Disney Princess is excluded, Mattel's positive POS performance improved significantly to the mid-single digits, with shipping up high single digits.

It wasn't that long ago that we began to transform the Company's culture and reset our approach to brand management with the creation of our core brand teams and the Toy Box organization. While recognizing we have more work to do, the first-quarter results continued to demonstrate our conviction to fundamentally change our approach to the business. These trends also continue to validate our strategic initiatives: ongoing revitalization of our core brands, the rebuilding of relationships with strategic license partners, accelerated growth in emerging markets, and a much more effective presence at retail.

Let's take a closer look at the results. Overall, our strong holiday season led to reduced retail inventories on key brands. We were encouraged by retailer confidence in our business as they look to restock their shelves with Mattel products in the first quarter. Excluding the impact of forex, we saw strong shipping numbers on many of our brands including Barbie, Fisher-Price, Hot Wheels, Thomas and MEGA Brands. And we saw strong consumer and retail support for our new DC Comics executions.

We continue to be pleased with Barbie's performance coming off such a strong holiday season, with global POS and shipping closely aligned in the first quarter. As you know, last year we were essentially relaunching Barbie and saw tremendous results, particularly in the US, where POS was up double digits. And from that new base, we continue to see positive POS here in the US. And, with shipping up 11%. We are also beginning to see this momentum broaden, with positive Barbie POS in Europe and Asia.

Now, we have more work to do, but we will continue to build on the brand's resurgence in North America and the very strong response we are seeing with our Barbie marketing strategy and new breadth of product.

We will also be increasing our successful marketing to moms to drive brand preference. Looking forward, expect us to build on these successes through many exciting innovations, including those you saw recently at Toy Fair. We are confident that Barbie will only become more engaging and relevant to girls and moms as we move forward toward holiday 2016.

But remember, Mattel is not just a Barbie story. Fisher-Price results for the quarter reflect positive POS trends with very strong shipping. We were pleased to see our biggest segment, baby, have particularly solid POS and shipping in the quarter, notably in international markets.

We are seeking to accelerate this momentum as we continue to emphasize early childhood development, the most important demand driver in the category today. We've already seen a tremendous response to our new Think and Learn line, with the widely anticipated Codeapillar product set to launch later this year.

In addition, earlier this month we were excited to formally announce the appointment of one of today's most popular designers, Jonathan Adler, as Creative Director for the Fisher-Price brand. You will begin to see his influence this fall, and we are hard at work leveraging his unique understanding of lifestyle aesthetics for today's families with more sophisticated Fisher-Price style, fashion and function for 2017.

Thomas and Hot Wheels each continue to see solid POS and shipping trends, particularly in the international markets. Both brands have exciting new content and products this year to support the strong momentum we're seeing on these brands.

Now, as we said in February, American Girl results will be challenging in the first half of this year as the major new initiatives to generate positive brand momentum will be coming online in the third and fourth quarters. We continue to take meaningful steps to energize this brand. And as I mentioned in our last update, there are some specific price value issues that we are addressing as well as improved distribution and expanded consumer engagement. I'll be sharing more on these as the year progresses.



Monster High has yet to stabilize. Despite some success with our new offerings, the decline in POS and competitive product launches have impacted its shelf space and overall performance. Consumer engagement continues to build with this brand, with over 2 million subscribers on Facebook, over 800,000 monthly visits to the website and significant growth in views on YouTube. Our focus remains on how to connect this great brand energy with more toy sales.

As you know, we are effectively relaunching the brand in the second half of this year with a new look, new content, a refocus on popular core characters, more features and enhanced play value. We remain cautiously optimistic, but realistically hope to see improving POS trends in the second half of the year, which will be a leading indicator that the brand is stabilizing as we exit 2016.

Turning now to Toy Box, we've been very encouraged by early consumer demand for our new DC Super Hero Girls line, even though some of its content just went live late in Q1. While currently an exclusive launch at Target, its retail presence will go broader in June.

On a related note, we are very pleased with the initial response to our DC superheroes Batman versus Superman product, with the blockbuster film premiering the last week of the quarter. We are excited to watch how this franchise builds as we continue to support the extensive upcoming DC movie slate.

And lastly, I'd like to highlight the solid performance of MEGA Brands' construction globally. We continue to see very strong results with MEGA's preschool executions, our own brand overlays of Monster High and American Girl, as well as the initial popularity of the Teenage Mutant Ninja Turtles product line ahead of the June movie release.

Overall, I am pleased with the Company's performance. I'm proud of the continuing progress on resetting Mattel's culture to be more innovative, more competitive and more efficient. We have both significant opportunities and significant challenges to face this year, and I'm encouraged by our execution to date and look forward to reporting more progress to you throughout the year.

As Chris said, our progress to date has generated strong momentum to build on, and we are increasingly well-positioned for growth and greater profitability in 2017 and beyond.

And now I'd like to turn the call over to Kevin Farr. Kevin?

Kevin Farr - Mattel, Inc. - CFO

Thank you, Richard, and good afternoon, everyone. As Chris said, foreign exchange continues to negatively impact our financial results in the first quarter. Overall, our results were in line with our expectations. Specifically, we are encouraged by our top-line performance as growth in our revenues of our core brands and Toy Box almost fully offset the loss of the Disney Princess license.

We also made significant progress on executing our cost savings programs, which resulted in roughly flat year-over-year operating margin on a reported basis.

Before going into detail, I want to remind everyone that unless otherwise noted I will be referring to sales in constant currency and adjusted financial results that exclude certain items related to our acquisitions of MEGA, Fuhu, and Sproutling, as well as severance expense.

Highlighting the top-line trends, gross sales were down just 1% in constant currency, or 6% as reported. This included growth in North America and Europe despite the loss of the Disney Princess license business. We continue to see double-digit growth in China, but our Asia-Pacific region declined modestly, primarily due to Australia.

Latin America also declined as Mexico continues to deliver solid growth, but our business in Brazil has been impacted by macroeconomic weakness, pricing challenges and inventory overhang.

And, of course, the underlying trends look much more favorable when we exclude Disney Princess, with overall gross sales up high single digits for the quarter. This included broad-based growth across all regions except Latin America, where sales were flat. Overall, very solid top-line performance on an underlying basis.

These early reads are very encouraging, as continued strong growth in our core brands and Toy Box revenues are the key for us to achieve our goal of relatively flat sales for the full year.

Moving to the rest of the P&L, sales adjustments were roughly flat versus the prior year as a percentage of net sales, where we continue to invest in retail promotions to drive POS and shipping for the first quarter and full year.



As Chris said, our gross margin was relatively flat year over year in constant currency, but 44.7% as reported.

As we said in our 2016 outlook, we expected foreign exchange would be a headwind for the full year. We expected that particularly in the first half on a gross margin rate basis due to the seasonally smaller quarters and tougher year-over-year comparisons. And we saw this in the first quarter, with around 340 of the 410-basis-point decline in gross margins attributable to unfavorable foreign exchange.

Almost half the negative impact from foreign exchange can be explained by less favorable euro hedging rates in 2016 versus 2015. Another driver is the fact that we are selling inventory that was produced last year at less favorable rates, when the dollar significantly strengthened against key currencies.

In the first quarter, we also saw strong trends in growth in countries with more volatile currencies like Mexico and Russia versus 2015. Looking forward, we expect this to balance out, particularly in the second half of the year, with higher seasonal revenues.

The other key driver of the decline in gross margin rate in the quarter was related to a mix shift from our higher-margin doll business, given the loss of Disney Princess to lower-margin product lines like MEGA and Fisher-Price.

And, finally, as it relates to our overall gross margin, what is encouraging is that our cost-savings initiatives more than offset inflation while continuing to improve our price value propositions.

Moving beyond gross margin, advertising was lower as we began to move somewhat closer to the 12% for the full year, coupled with the benefit of foreign exchange.

On a positive note, adjusted SG&A was down \$25 million, or 7% year over year, as cost savings and favorable foreign exchange more than offset labor-related inflation. In total, we delivered gross cost savings of \$46 million in the quarter, roughly evenly split between gross margin and SG&A.

Finally, adjusted EPS was a negative \$0.13 per share, or a negative \$0.21 as reported. As some of you may know, in February the Venezuelan government changed its official exchange rate, which prompted a devaluation this quarter. As a result, reported EPS included a \$0.06 negative impact from the remeasurement of our bolivar denominated assets, primarily cash in Venezuela which we excluded from adjusted EPS.

As it relates to our balance sheet cash flow, we ended the quarter with around \$600 million in cash, a similar quarter-over-quarter change to where we ended the fourth quarter of 2015. This is in line with our expectations and reflects solid performance, especially when you consider the roughly \$30 million cash outlay for the acquisition of Fuhu and Sproutling, and roughly \$20 million reduction in cash due to the Venezuelan devaluation.

Not surprisingly, owned inventory on our balance sheet was up year over year as we positioned the business to support our new licensed entertainment launches throughout the year in addition to the continued positive POS trends on a global basis, including great momentum and new launches for MEGA.

Receivables were also up due to later timing of the customer shipments, as well as the impact of longer terms for some of our emerging market customers.

We did see a benefit this quarter from our efforts around extending key vendor terms to match industry norms over the last two years, with the latest extension implemented in May of 2015. This favorability should moderate going forward based on the timing of when we implemented these changes in 2015. However, we will continue to emphasize even greater overall discipline in accounts payable management going forward.

And we continue to reward our shareholders by deploying capital in a disciplined manner and maintaining the dividend. As we have said, dividends remain our first priority after reinvesting in the business. And the Board declared a second-quarter dividend of \$0.38 per share, which is flat compared to the second quarter of 2015.

As we look ahead to our second-quarter and full-year 2016 outlook, we are targeting gross sales in the second quarter to reflect similar year-over-year trends to what we achieved in the first quarter, or relatively flat on a constant currency basis. Although Disney Princess comparisons get easier, we believe there was some benefit in the first quarter from initial retail restocking of Mattel products due to low beginning inventory levels on shelves.

Offsetting this is early results from key incremental revenue drivers, which look promising, and this momentum should continue in the second quarter and beyond.

As it relates to gross margin, we believe the second-quarter gross margin rate will be roughly flat to the first quarter, with supply chains efficiencies and cost savings partially offsetting foreign-exchange headwinds.



And we believe we will continue to see year-over-year savings in adjusted SG&A in the second quarter, driven by continued efficiencies and cost-savings initiatives. However, the year-over-year improvement will be less than what we saw in Q1, in part due to the full-quarter addition of Fuhu SG&A. As such, we expect second-quarter adjusted SG&A spending to be modestly down versus the first-quarter run rate in dollars.

Finally, despite the significant first-half headwinds, our full-year P&L outlook for 2016 remains unchanged. I'll briefly focus on the key drivers.

We're still looking to deliver relatively flat net sales in constant currency. On gross margin, we continue to target about 50% for the full year, similar to what we achieved in 2015. Specifically, there are two key drivers of first-half headwinds that should moderate in the second half.

The first is foreign exchange; assuming current spot rates and our current hedge position. For reference, foreign exchange had roughly a positive 100-basis-points impact on gross margin rate in the first half of 2015, versus roughly a negative 200-basis-point impact to gross margin rate in the second half.

For the second half of the year, we expect the impact of foreign exchange will moderate, as seasonal revenues are significantly higher in the second half. The hedge euro rate differential for the second half is closer to the hedge rate for 2015. Country mix should balance out. We offset some of the foreign exchange with price increases on the fall line and easier year-over-year gross margin rate comparisons.

The second factor is mix. As we look to the second half, we expect that the negative impact of Disney Princess mix will lessen since it is smaller relative to our overall revenues. And we should see the benefit from expected growth in our doll business, including Barbie, the global launch of DC superheroes and strong initiatives on American Girl. And, importantly, as we ramp up production in the second quarter and work towards peak production, we expect structural supply chain savings to accelerate, which will be positive to gross margin for the second half.

Lastly, we continue to target adjusted SG&A to be down \$55 million to \$65 million year over year. Our previous outlook excluded SG&A from Fuhu and Sproutling, which we had recently acquired. However, we will look to absorb the bulk of the overhead from Fuhu/Sproutling acquisitions by aggressively pursuing additional cost-savings opportunities.

Finally, looking beyond this year of transition, as Chris said, we see a path to approaching our 15% to 20% operating margin target in 2017, as we have a tailwind on top-line revenues from the Cars 3 movie and continued traction in China, Russia and emerging markets.

Beyond the key drivers we've already discussed, Fuhu and Sproutling will help offset the earnings impact related to their increased SG&A in 2016. But we expect sales to ramp up in 2017 as we leverage their technology platform across our portfolio and expand our market opportunities.

In closing, we don't want to get ahead of ourselves in the seasonally small quarter, but the turnaround continues to track to our expectations. Our global POS remains positive, which is driving further shelf space stabilization for key core brands and a shipping recovery across most of our regions when you exclude Disney Princess. If these trends continue, it should set a solid foundation for growth and improved profitability in 2017.

We look forward to updating you on our progress throughout the year. And we'll now open the call up to questions. Operator?

QUESTION AND ANSWER

Operator

(Operator Instructions) Jaime Katz, Morningstar.

Jaime Katz - Morningstar - Analyst

I'm curious if you guys would be willing to talk about the contribution from the DC Comics relationship. Obviously, entertainment has been pretty lucrative for Hasbro, and I'm curious how the read-through has been for you guys so far.

Chris Sinclair - Mattel, Inc. - Chairman and CEO



As I mentioned, we are really pleased with the early reads right now of the DC Super Hero Girls collection. Exclusive at Target currently, but we'll have a broader rollout in June. And we anticipate continued momentum through the year and potentially a much longer franchise as they continue to introduce new characters into the mix.

In addition, as we also mentioned, we're coming off of the blockbuster hit at this point with Batman versus Superman. The toy business is reacting really terrific. We continue to see momentum behind that segment. And, as you know, we have a really robust lineup over the next several years with Warner Bros. and DC. So we are looking forward to continuing to grow that franchise overall and currently really pleased with the initial readings.

Jaime Katz - Morningstar - Analyst

Okay. And then can you -- I don't know if you guys have gone this deed, but can you talk about how you're thinking about integrating some of the digital ideas from either Fuhu or Sproutling into the product lines, and what sort of prototypes you might see coming out of those acquisitions?

Chris Sinclair - Mattel, Inc. - Chairman and CEO

Jamie, I'll take that. I think we've got a very active team working on integrating it at this point. A lot of work being done to sort of integrate both Fuhu and Sproutling with some of the Fisher-Price lines. I think we'll probably be rolling some things out in the fourth quarter this year, principally in China as the lead market. But all designed to go after early childhood development; sort of a nursery of the future, if you will. Getting a lot of excitement and interest on that front.

Additionally, we are doing a lot of things with the Fuhu learning platform that we'll start to roll out a little bit more this fall on their tablet business. But we think actually have some great applications with some partners we're working on, again, starting in Asia.

But the early read on both is very exciting -- I think are integral, actually, to the whole childhood development platform we're going after on Fisher-Price principally.

There's another benefit that I would highlight is that we're going to have these toys with sort of connected homes and the nurseries, which obviously will give us a great pipeline of data that we can help them manage and mine for consumer marketing. So, another sort of key benefit to these acquisitions.

Jaime Katz - Morningstar - Analyst

Okay. And then lastly, Kevin, I think there's a note coming due later this year. And in light of the fact that debt-to-cap is around 45%, I think, are you guys thinking about refinancing, letting that mature? How do you see capital allocation?

Kevin Farr - Mattel, Inc. - CFO

I think we've got a strong balance sheet and adequate liquidity. So as we look at the full year, our plan is to refinance that in the back half.

Jaime Katz - Morningstar - Analyst

Okay. Thank you.

Operator

Eric Handler, MKM Partners.

Eric Handler - MKM Partners - Analyst

Kevin, I know you gave a little bit of color regarding gross margin. And I wonder if you could just talk a little bit again about the back half of the year. It seems like you are implying a 52%, 53% gross margin in the third and fourth quarters. It's been a long time since we've seen gross margins that high. Is it just the fact that you're going to see more girls' doll business, or are there other factors involved in that?



Kevin Farr - Mattel, Inc. - CFO

Okay. I'd be happy to answer that. We are still targeting gross margins of 50% for the year, as I said, similar to the amount that we achieved last year. And that means a moderate year-over-year improvement in our second-half gross margin rate versus last year, where we achieved gross margins of about 50%.

And based upon a current spot rates and hedge rates, we believe it's achievable and well within our three- to five-year historical averages. But how we achieve it in 2016 will be a little bit different than how we achieved it in our historical averages, which relied more on pricing and better mix.

As we look at the second half of the year, we are going to really achieve it through acceleration of cost of goods sold through supply chain structural changes, which don't impact our price value propositions.

So it is going to be more about accelerating cost savings on structural supply chain in the second half of the year.

Eric Handler - MKM Partners - Analyst

Okay. That's helpful.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

There will be some positive mix shifts versus the first half of the year which start to come into effect. And I think he also pointed out we do expect forex to moderate as we move into the back half, though. When you ladder those things, I think we're comfortable getting somewhere close to that 50% target.

Eric Handler - MKM Partners - Analyst

Okay. That's very helpful. And as a follow-up, you pointed to contributions from Toy Box as being a key driver this year. And can you just go through again what have been some of those successes from Toy Box that have got you excited?

Richard Dickson - Mattel, Inc. - President and COO

Sure, Eric. And you know, Toy Box is a myriad of brands, as you know. Certainly our license partnership brands are in there as well as a variety of other brands and properties within Mattel.

Specifically, we've had some great POS traction on our games business. Uno continues to grow and is a legacy brand in our portfolio. And the team there is doing an incredible job of keeping that brand relevant and driving newness. MEGA continues to be outstanding for us overall; had a great quarter internationally, specifically, as well as the US. And we continue to get traction both in the preschool segment as well as leveraging our own properties -- American Girl, Monster High. And, of course, as we anticipate the launch of the Teenage Mutant Ninja Turtles movie, we think that we are going to have a great hit there.

Brands like Minecraft also continue to be really terrific, and the team is doing an excellent job maintaining the relevance of that brand. And brands like Dinotrux with our partnerships with DreamWorks; Blaze also with Nickelodeon is doing terrific. There's a lot of great brands within Toy Box that are continuing to be nurtured and developed and are, frankly, chipping away at our gap but ultimately driving some great growth in their own right.

As we continue to develop the strategic partnership profile, not only will we do a continued job driving our existing, but we continue to seek new relationships as well as renew existing relationships. So, going forward, Cars 3 of course, which we've talked about, lining up even 2018 with Toy Story and others will be revealed shortly.

Eric Handler - MKM Partners - Analyst

Very helpful. Thank you.



Operator

(inaudible)

Unidentified Participant

Could you talk a little bit about POS for the quarter? The global POS improvement you talked about, is that adjusted for Disney? Is it possible to give us at least US Disney adjusted and Easter adjusted in terms of POS?

Richard Dickson - Mattel, Inc. - President and COO

This is Richard. What we can tell you is ex Disney [**Clarification:** Disney Princess], as I mentioned in my opening remarks, has performed very well. Up single-digit increases worldwide. It's commensurate with our shipping numbers as well. Across our core brand portfolio, we've seen more positives than not. In fact, in cases like Hot Wheels, across the board we've seen both shipping and POS really strong results. I mentioned Fisher-Price had a really strong quarter both in shipping and POS. Brands like Barbie, of course, turning the corner and gaining more and more momentum.

US was a strong performer. Europe is now reflecting positive POS as well as Asia. And we continue to work on Latin America. Ex the Disney Princess business, we are performing quite nicely.

Unidentified Participant

Thank you very much.

Operator

Tim Conder, Wells Fargo.

Tim Conder - Wells Fargo Securities, LLC - Analyst

Richard, I'll just stay on that a little bit here. Any breakdown there on Fisher-Price between US and international? And then maybe the infant portion -- you seemed to call out that that was remaining very strong -- the infant versus the non-infant portion of Fisher-Price at POS.

Richard Dickson - Mattel, Inc. - President and COO

Sure. I think, as I mentioned, across the board, particularly in international, we were really pleased with the Fisher-Price brand overall. Baby, which as we mentioned, is our biggest and, frankly, most strategic piece of the business. Had positive POS across all regions. So we were really pleased with the response that our child development messaging certainly has been having. And also, product and pricing has played a great impact in the continuation of the trend with Fisher-Price.

Generally speaking, as we sort of look ahead, we continue to leverage the momentum that we currently have, especially in international markets. The strength across the baby business will continue. There's some amplified marketing as we continue with our Best Possible Start campaign that's gotten great traction. The continued brand evolution tied to child development is really rich with content and connectivity, as we said, particularly in emerging markets like China.

And even as we reenter the preschool learning category more aggressively with our Think and Learn line, the Codeapillar, which I mentioned, is a key item for us, is getting an lot of attention and traction. We anticipate that that will be just one of many early childhood development items that Fisher-Price becomes well-known for.

Not to belabor the point of Jonathan Adler's appointment, but I think the aesthetic piece of what he'll bring to the overall brand will be important as we move and develop the line with a bit more fashion sensibility. And, of course, as we mentioned, new content, new partnerships with 9 Story, DHX all fuel that particular segment of the brand.



So we're confident in our strategic path going forward, and certainly early reads are suggesting we're heading in the right direction.

Tim Conder - *Wells Fargo Securities, LLC - Analyst*

So it would be fair to say that Fisher-Price is going to be more of an early childhood development versus -- and maybe the preschool part will be somewhat deemphasized on a relative historical basis?

Chris Sinclair - *Mattel, Inc. - Chairman and CEO*

I wouldn't characterize it quite like that. I would say that we are going to put a lot more emphasis on the early child development and the nursery of the future. But, clearly, the rest of the line will continue to get plenty of focus.

Tim Conder - *Wells Fargo Securities, LLC - Analyst*

Okay. And one maybe housekeeping item here -- the currency impact from Venezuela, was that in or not in the gross margin? I know you called it out on the EPS side and on the adjusted basis. But on a gross margin basis, was that included in your gross margin number?

Chris Sinclair - *Mattel, Inc. - Chairman and CEO*

No. That was in other nonoperating losses.

Tim Conder - *Wells Fargo Securities, LLC - Analyst*

Okay. And then from an inventory perspective, you called out Monster High, your plan to hopefully exit the year with that sort of stabilized. That was still a little bit challenged. And then Latin America as a whole. Any pockets of inventory, I guess, brand-wise, geographic-wise? You exited the third quarter of last year, you felt good on a global basis, and that really showed up in Q4. And then -- so how is that now here sort of in the off-season, so to speak?

Chris Sinclair - *Mattel, Inc. - Chairman and CEO*

I think we made progress in the only place that we had overhang in the fourth quarter, which was Brazil. We made good progress in the first quarter. There's still a bit left, but we will be through that by the time we get to the all-important second half of the year.

Kevin Farr - *Mattel, Inc. - CFO*

We're actually, I think, in very good shape, Tim, on inventory at this point.

Tim Conder - *Wells Fargo Securities, LLC - Analyst*

And American Girl, gentlemen, do you feel good where that is? I know you've got a lot of new stuff coming in the back half of the year.

Richard Dickson - *Mattel, Inc. - President and COO*

Yes, I think, as we mentioned, we've isolated the brand with a diagnosis that we've now started to execute against. First half, we anticipated would be challenging as we do some pricing strategy, evaluate distribution and reengage with some new content, all of which will be executed and revealed in the back half.

We're excited about the programs that we have. I think our partnership that we've announced with Amazon is going to bring new content connectivity to the consumer and to reach a broader-based consumer. And I think some of the work that the team is doing there will show up on the scoreboard, of course, in the second half. So we are confident with our plans there.



Kevin Farr - Mattel, Inc. - CFO

And just adding to the retail inventory answer, I think what Chris indicated is we're in much better shape. I think on a year-over-year basis that's particularly true in Europe.

Tim Conder - Wells Fargo Securities, LLC - Analyst

Okay. And then lastly, Kevin, just a clarification on the hedging. You guys had called out the various favorable hedging that you had in 2015. How is the cadence of that? Should we think about -- you said that FX a bit more favorable in the back half of the year just from where the rates are. But where did you have the best hedges on? I guess what creates the most difficult comparison in 2015?

Kevin Farr - Mattel, Inc. - CFO

I think that was really in the first half of the year. As I said, in the first half of the year the year-over-year gross margin rate was favorably impacted by 100 basis points. Where in the second half of the year, it was unfavorable by 200 basis points.

Tim Conder - Wells Fargo Securities, LLC - Analyst

200? Okay. You did mention it. My apologies there.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

Tim, most of that was in the euro, by the way.

Tim Conder - Wells Fargo Securities, LLC - Analyst

Okay.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

It had a step down this year.

Tim Conder - Wells Fargo Securities, LLC - Analyst

Great. Thank you, gentlemen.

Operator

Jim Chartier, Monness, Crespi, Hardt.

Jim Chartier - Monness, Crespi, Hardt & Co. - Analyst

Just wanted to circle back on the gross margin, Kevin. Looking at the full-year outlook -- \$125 million to \$135 million of cost savings and \$46 million realized in the first quarter. It looks like the rest of the year, the cost saving would have a smaller impact as a percentage of sales on margins. So is there more than just the funding or future cost savings embedded in the improvement in second half-gross margins? You talked about some structural changes there.



Kevin Farr - Mattel, Inc. - CFO

Yes. I think, as we said, our funding our future is part of what we're doing. We're going to target to deliver at the high end of the range. But we have incremental programs around structural cost savings related to cost of goods sold as well as SG&A that will be in excess of what Funding our Future is.

So as we look at the cadence of the year, the inventory that we're selling in the first quarter, we produced last year. As I said in the call earlier, that as we ramp up our seasonal production in the second quarter and get peak production in the third quarter, we should see more flow-through from these structural savings in the second half of the year. And that will help us, as I said, to improve our year-over-year gross margins in the second half of the year, along with better mix and less impact of foreign exchange in the second half of the year.

Jim Chartier - Monness, Crespi, Hardt & Co. - Analyst

Okay. And I just wanted to clarify, Fuhu and Sproutling acquisitions -- will they be neutral to EPS this year and then accretive next year? Is that the plan?

Kevin Farr - Mattel, Inc. - CFO

Yes. Overall, we should be adding top-line revenues for the year. And we are adding SG&A. But from a perspective of looking at those operations, we expect them to be breakeven for this year and then hopefully accretive next year.

Jim Chartier - Monness, Crespi, Hardt & Co. - Analyst

Great. Thanks, and best of luck.

Operator

Gerrick Johnson, BMO.

Gerrick Johnson - BMO Capital Markets - Analyst

Can we talk about Barbie for a second? The disconnect between US up 11%, international down 7% -- local. And we haven't have a positive quarter in Barbie internationally since 2013. So what's the difference? Why is it doing well here and not out there?

Richard Dickson - Mattel, Inc. - President and COO

I think we've always watched, and so we have enough history with this brand. North America tends to lead the brand's narrative both in messaging and in product connectivity as well as retail execution. It tends to be part of the history of the brand. And as we see North America really starts to get traction and connectivity, both at retail execution and with consumers, those programs take shape sort of as the tail, if you will, in the international market a bit later.

And, you know, when you digest or at least dissect the international market, there is developing markets, there's developed markets -- there's a variety of different things that go into the play of the brand. But overall, what we're seeing now is Europe getting traction on POS with Barbie. Asia also getting traction on POS Barbie. Latin America is still catching up. We have some work to do in Latin America.

But overall, we're seeing great connectivity. Frankly, the successful campaign that we ran here, the You Can Be Anything campaign that was widely acclaimed, didn't get executed throughout international. So that's still new in some cases and rolling out as we speak. Some of the new product that we launched here in the US is also being executed later in certain markets. Our DVD calendar in terms of distribution and marketing is also slightly different in international markets.

So I think overall, I would take a look at the domino of the business being North America as a lead indicator of where the brand should be going and could be going. And so far, the indications here are very good, and the tail in the context of international is catching up.



Gerrick Johnson - BMO Capital Markets - Analyst

Okay. So, in what markets were the new Fashionista Barbie dolls launched? Was it US? And what other markets are those dolls currently in?

Richard Dickson - Mattel, Inc. - President and COO

They are currently rolling out now. In fact, they are just hitting shelves in Europe more significantly than other markets. As you look at the Barbie brand, we have segmentation strategies. So there's a variety of different segments to the brand. There's an I Can Be segment. There's a fairy segment. There's entertainment segment. There's Fashionistas. There's key items. And as we execute against the brand around the world, different countries dial up or down different segments.

So it's difficult to have a peanut-butter approach to the answer. But what I would tell you is that the Fashionista collection is rolling out more aggressively in Europe. It will hit Asia shortly in certain markets in Asia, and Latin America probably in the second half of the year.

Gerrick Johnson - BMO Capital Markets - Analyst

Okay. And one more on dolls. The DC Super Hero Girls -- are those in any markets internationally, or are they only in Target here in the US?

Richard Dickson - Mattel, Inc. - President and COO

Only in Target here in the US, and those will also be rolling out in the back half.

Gerrick Johnson - BMO Capital Markets - Analyst

Okay. Great. Thank you.

Operator

Taposh Bari, Goldman Sachs.

Taposh Bari - Goldman Sachs - Analyst

I wanted to ask a question on sales in the quarter versus your expectations. It sounds like you were pretty pleased with the underlying sales momentum despite the fact that you lost the Disney piece and the fact that that impact was proportionately large in the quarter. So can you give us a sense for how POS and/or shipments kind of realized versus your expectations and if Easter has any effect on the reported numbers?

Chris Sinclair - Mattel, Inc. - Chairman and CEO

Yes, Taposh, how are you? Look, we actually normalized Easter. So, it's important to understand we took out any of that effect. And so the numbers you're seeing, I think, are fairly pure as you would look at it.

I would say overall we're actually very enthused by the outcome of the first quarter. I think we actually probably exceeded a little bit what we had hoped to do, and I think it was very broad-based, which was encouraging. And not just the core brands, but the Toy Box kicked in in a lot of meaningful ways.

So I think, as we tried to indicate, we felt we are well-positioned for what we've been guiding for the full year, and I think this is just a good early start. But, again, broad-based -- and both shipping and POS.

Taposh Bari - Goldman Sachs - Analyst



Great. And just a follow-up on both the entertainment and the construction segment line. You had some big increases there presumably due to some of these licensed properties that you're taking on this year. Trying to get a better sense for if there was anything unique to the first quarter, given that you are probably filling the channel for some of these product lines. In other words, should we expect to see continued robust growth rates in those segments throughout the year, especially as you roll out the DC superheroes line and also enter the Ninja Turtles theatrical window?

Chris Sinclair - *Mattel, Inc. - Chairman and CEO*

Go ahead, Richard.

Richard Dickson - *Mattel, Inc. - President and COO*

Well, I think specifically for MEGA, as I mentioned, we introduced some of our brands into the construction category. American Girl has been a resounding success out of the gate. Monster High also connecting very well in construction. And, of course, Teenage Mutant Ninja Turtles is launching and the movie hasn't started, and we're relatively pleased with that progress.

And as you know, the preschool segment of MEGA is robust and doing well.

So we anticipate that that will get better and better as we execute against those properties and introduce others as time moves on. You know -- so I think overall, in general, we're really pleased with where we're moving, and I think it's just going to continue momentum.

Chris Sinclair - *Mattel, Inc. - Chairman and CEO*

Yes, the other thing I would add on MEGA is a lot of that growth also came internationally. So it's not structurally tied to either an entertainment property or one of our own brands per se. We're expanding; we're getting new distribution; we're getting better execution against it.

Taposh Bari - *Goldman Sachs - Analyst*

And one last one -- last year 2015 was a year where you were really increasing spending in terms of supporting the trade. As you think about 2016, it looks like advertising was down. Your sales adjustments were flat year over year even though you were guiding for it to be up. Help us better understand how you're thinking about supporting the trade in 2016. Thanks.

Kevin Farr - *Mattel, Inc. - CFO*

I'll just talk about it from a financial perspective, and then Richard can talk about it from more of an execution. But I think as we did our 2016 outlook, we really said we reinstated our sales adjustments from a planning perspective to be at the higher rate that we experienced in 2014 so we would make sure that we would drive POS this year. Whether we spend that or not will depend upon how our POS performs in the second half of the year. But that's the way we put the financial plan together.

Richard Dickson - *Mattel, Inc. - President and COO*

And speaking specifically on behalf of the retail execution, we continued to have those reserves and be ready to drive very different forms of execution to ensure retail success whether or not those applications are used or not.

And then on an overall advertising side, we continue to get much more intelligent in the context of what works and what doesn't in our media spend. And that will continue to evolve. So, much of our advertising moves around and gets redeployed based on what we believe is going to have better connectivity. And as you know, that's a moving target as our consumer constantly changes and new forms of connectivity are introduced constantly. So we are very much on top of that as well.

Kevin Farr - *Mattel, Inc. - CFO*



Yes, and I think -- going back to our planning, too, we also planned advertising to be less, getting closer to the midpoint of our 11% to 13% range. But also, we need to drive POS. Then we will invest what's necessary in advertising to do that.

Taposh Bari - Goldman Sachs - Analyst

Thanks. All the best.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

Okay.

Taposh Bari - Goldman Sachs - Analyst

Sorry -- were you going to say something, Chris?

Chris Sinclair - Mattel, Inc. - Chairman and CEO

No. I was just going to say the one thing to keep in mind on advertising, most of the scale-back is in what we would call nonworking. So, the actual impact of advertising going against the consumer is not being reduced. It's more effectively deployed, but it's the nonworking production stuff that we've been shaving.

Taposh Bari - Goldman Sachs - Analyst

Thanks a lot.

Operator

Linda Bolton Weiser, B. Riley.

Linda Bolton Weiser - B. Riley & Co. - Analyst

Just to circle back once more on Barbie; again, on that international decline in the Barbie shipments in constant currency. When Richard was talking about it, he said that Barbie was -- I think he'd use the word gaining traction or something in Europe and Asia. So does that mean improving-but-still-down POS? And that down POS correlates to be down shipments? Or do we still have some kind of inventory problem in the channel? In other words, POS is actually kind of growing but you still have inventory too high in certain markets. Can you just explain a little bit more?

Richard Dickson - Mattel, Inc. - President and COO

Sure, Linda. Let me be more specific. The POS momentum in Barbie is real in the international marketplace, specifically in Europe and in Asia. Now, it varies by country, but overall we're seeing great positive traction on POS, some in the lower single digits and some in the higher. But generally speaking, gaining more and more momentum.

We continue to look at Latin America as, to some extent, sort of catching up. There's some programs that we're launching there and some various different challenges that we've had in that marketplace, but it is moving along. It's a smaller percentage as a total. But, in general, we're seeing more green shoots with Barbie across the world.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

And final point -- there is no inventory issue, if that was your other question, Linda.



Linda Bolton Weiser - B. Riley & Co. - Analyst

Okay. So then we should start to see that shipment pattern improve for the international piece of Barbie, it sounds like.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

We would expect so.

Linda Bolton Weiser - B. Riley & Co. - Analyst

Okay. And then can you just clarify how much of the Batman versus Superman products shipped in the first quarter? Is it a significant bigger shipment in the second quarter?

Richard Dickson - Mattel, Inc. - President and COO

No. I don't think it's significantly bigger. I think there will be -- no, because we sort of build the shelves up in the first, and then we are continuing to restock in the second and introduce some new items. So it -- we think it will be significantly bigger now.

Linda Bolton Weiser - B. Riley & Co. - Analyst

Okay. And then finally, Kevin, on the cash flow performance in the quarter, you mentioned that working capital used more cash than last year. What are your thoughts on that for the full year? Are you thinking working capital could be a modest source or use of cash?

Kevin Farr - Mattel, Inc. - CFO

Look, I think what we've said when we did the outlook is that in a challenging year we delivered strong cash flow in 2015, and we expect cash flow to be a little bit better in 2016. And we're still focused on tightly managing working capital. I think there's an opportunity for us to -- as we exit the year to tightly manage inventories. They are a little bit higher than our historical rates. And I think through better information technology, better planning process and trying to shorten lead times, we think there's an opportunity to exit the year with working capital being positive.

Linda Bolton Weiser - B. Riley & Co. - Analyst

Okay. That's it for me. Thank you.

Martin Gilkes - Mattel, Inc. - VP, Corporate Strategy and IR

Operator, I think we have time for one final question.

Operator

Gregory Badishkanian, Citigroup.

Gregory Badishkanian - Citigroup - Analyst

With the expected second-half acceleration in sales, what do you think that biggest driver will be? Or is it just going to be across multiple brands?



Richard Dickson - Mattel, Inc. - President and COO

Greg, we've described our plan as without a silver bullet. So the collection of core brand momentum, I think, will contribute to the momentum. And we've been pleasantly surprised, as I mentioned, with a lot of the Toy Box initiatives. Some of these smaller brands are really showing up on the scoreboard and incrementing our expectations.

But, as we've said, Hot Wheels, Barbie, Fisher-Price, Thomas, specifically, are continuing to deliver and certainly will have a strong back half as planned. And then as we drive some of our entertainment relationships that are incremental, like Warner Bros., that will drive momentum.

MEGA continues to gain traction. And I think as you look at our brands in the construction space, it's all very new business for us. And we're excited with that continuing to build. And the construction category, which, as you know, is a successful growing category in the industry.

And then there's a variety of other new things that we're excited to introduce. Mixie Q's is a new brand for us that's going to be launching through the Toy Box. And innovative items like the Thing Maker, which we introduced at Toy Fair, is getting a lot of traction and interest, and symbolizes the innovation and invention aspect that we are driving as part of our new culture.

So we've really got all our ducks in a row. And now, as I mentioned, it's really about the execution of it mattering more.

Gregory Badishkanian - Citigroup - Analyst

Great. And would you -- so you would expect, let's say, maybe the third quarter to start seeing positive year-over-year growth, if I were to put words in your mouth? Or do you think it will be the fourth quarter?

Chris Sinclair - Mattel, Inc. - Chairman and CEO

I don't think, Greg, we've given any guidance. We've sort of told you where we think we'll be for the year, which is fairly flat on constant currency. So that would be a good model for you to work with.

Gregory Badishkanian - Citigroup - Analyst

All right. Good. Thank you. Appreciate it.

Chris Sinclair - Mattel, Inc. - Chairman and CEO

Good try.

Richard Dickson - Mattel, Inc. - President and COO

Thank you, Greg.

Martin Gilkes - Mattel, Inc. - VP, Corporate Strategy and IR

All right, guys. Thanks, everyone. There will be a replay of this call available getting at 8 PM Eastern time today. The number to call for the replay is 404-537-3406, and the pass code is 74326242. Thanks for participating in today's call.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This does conclude the program. You may all disconnect. Everyone have a great day.



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