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MAT.OQ - Q1 2022 Mattel Inc Earnings Call

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OVERVIEW:

Co. reported 1Q22 net sales of $1.041b, adjusted operating income of $90m and adjusted EPS of $0.08. Expects 2022 net sales growth, in constant currency, to be 8-10% and adjusted EPS to be $1.42-1.48.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Mattel, Inc. First Quarter 2022 Earnings Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded. (Operator Instructions)

I would now like to hand the conference over to your speaker, Mr. David Zbojniewicz, Head of Investor Relations.

David Zbojniewicz - *Mattel, Inc. - Vice-President IR*

Thank you, operator, and good afternoon, everyone. Joining me today are Ynon Kreiz, Mattel's Chairman and Chief Executive Officer; Richard Dickson, Mattel's President and Chief Operating Officer; and Anthony DiSilvestro, Mattel's Chief Financial Officer.

As you know, this afternoon, we reported Mattel's 2022 first quarter financial results. We will begin today's call with Ynon and Anthony providing commentary on our results, after which, we will provide some time for Ynon, Richard and Anthony to take your questions.

To help supplement our discussion today, we have provided you with a slide presentation. Our discussion, slide presentation and earnings release may reference non-GAAP financial measures, including adjusted gross profit and adjusted gross margin; adjusted other selling and administrative expenses; adjusted operating income and adjusted operating income margin; adjusted earnings or loss per share; adjusted tax rate; earnings before interest, taxes, depreciation and amortization, or EBITDA; adjusted EBITDA; free cash flow; free cash flow conversion; leverage ratio; and constant currency.

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In addition, we present changes in gross billings, a key performance indicator. Please note that we may refer to gross billings as billings in our presentation and that gross billings figures referenced on this call will be stated in constant currency unless stated otherwise. Our accompanying slide presentation can be viewed in sync with today's call when you access it through the Investors section of our corporate website, corporate.mattel.com.

The information required by Regulation G regarding non-GAAP financial measures as well as information regarding our key performance indicator is included in our earnings release and slide presentation and both documents are also available in the Investors section of our corporate website.

In the second quarter of 2021, we elected to revise prior periods for certain immaterial out-of-period adjustments that do not require us to amend previous filings. These adjustments are reflected in our first quarter earnings release and slide presentation and will be reflected in our 2022 first quarter Form 10-Q. These adjustments will also be subsequently updated on the financial history section of our Investor Relations website at a later date.

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 business, brands, categories and product lines. These statements are based on currently available information and assumptions, and they are subject to a number of significant risks and uncertainties that could cause our actual results to differ from those projected in the forward-looking statements, including risks and uncertainties associated with the COVID-19 pandemic and the Russian-Ukraine war.

We described some of these uncertainties in the Risk Factors section of our 2021 annual report on Form 10-K, our earnings release and the presentation accompanying this call 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, except as required by law.

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

Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

Thank you for joining Mattel's first quarter 2022 earnings call. Mattel achieved its highest first quarter results we have on record for net sales, operating income and EBITDA. Having completed our turnaround in 2021, we are firmly in growth mode and are operating as an IP-driven, high-performing toy company. The full year outlook is strong. We expect to grow market share, and we are reiterating our 2022 guidance and 2023 goals.

Looking at first quarter financial highlights versus prior year. Net sales were up 19% and exceeded $1 billion, a remarkable performance on top of a 47% increase in 2021. Adjusted operating income nearly tripled. Adjusted earnings per share improved from a negative $0.10 to a positive $0.08 and adjusted EBITDA increased by 65%.

Our performance was comprehensive, with growth in gross billings in constant currency in all regions and up double digits in North America, EMEA and Latin America. We also grew in 6 of 7 categories where we operate with double-digit growth in our 3 power brands, Barbie, Hot Wheels and Fisher-Price and Thomas & Friends.

We expect the strong performance to continue with growth in the second quarter amplified by sales tied to the theatrical releases of Universal's Jurassic World: Dominion as well as Disney and Pixar's Lightyear. We believe we are well positioned with owned and retail inventories to meet consumer demand for our products.

First quarter benefited from increased points of distribution as well as retailers restocking low inventories following the strong holiday season, and gearing up to support product launches tied to the upcoming theatrical releases.

POS declined high-single digits, reflecting promotional and spring reset timing, retailers restocking low inventories following the strong holiday season and the Easter shift to the second quarter. As we begin the second quarter, April POS has increased more than 25%, bringing year-to-date POS in line with expectations.

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While first quarter gross margin was down due to significant inflation, favorable foreign exchange, pricing, scale and cost savings helped mitigate the inflation impact. With the added benefit of strong top line growth, we achieved significant gains in operating income and EBITDA with adjusted EPS turning positive. We continue to anticipate higher inflation in 2022 versus last year, but expect it to moderate in 2023.

Per The NPD Group, Mattel was the #1 toy company in the U.S. and the #1 globally in our leader categories, Dolls, Vehicles and Infant, Toddler and Preschool. Barbie, Hot Wheels and Fisher-Price were each the #1 property in their respective categories.

Mattel's supply chain is playing a key role in our success. All of our factories are fully operational, and we are working with our retail partners to ensure product is available on shelves to meet consumer demand. While we are monitoring macro level factors affecting supply chain and the broader economy, we are confident in our growth trajectory.

Looking at gross billings by category versus the prior year. Our strong performance continued, and our products resonated with consumers and families. Dolls grew 8%, led by Barbie and Polly Pocket. Barbie was up 12% and continued its multiyear momentum. American Girl declined $10 million compared to a very strong first quarter last year. We expect American Girl to grow for the full year.

Vehicles increased 36% with growth across all product lines, Hot Wheels, Matchbox and Disney's Pixar Cars. Hot Wheels grew 36% with retailers restocking our top-selling diecast cars. Infant, Toddler and Preschool increased 15%, driven primarily by Fisher-Price Core with growth in Imaginext, newborn, infant and Little People as well as Thomas & Friends.

Challenger categories together grew 44%, led by exceptional growth in action figures and building sets. Action Figures were up a strong 75%, driven by Jurassic World, Lightyear and Masters of the Universe.

The first quarter results are in line with our strategy to grow Mattel's IP-driven toy business. As we scale our portfolio, we also expanded to 494,000 brick-and-mortar stores where our product is sold. We strengthened our position as a partner of choice for the major entertainment companies with the recently announced multiyear global licensing agreement with Universal for DreamWorks Animation's Trolls.

Mattel will have the licensing rights to develop a full line of this toyetic franchise, which is expected to launch at retailers in line with the new theatrical release in fall of 2023. We recently expanded our DTC offerings to customers across several major EMEA countries. We are building a strong and engaged collector base with our Mattel Creations platform.

We further optimized our operations with the recent consolidation of our manufacturing in Mexico. The state-of-the-art facility will help to diversify Mattel's supply chain footprint and optimize nearshoring of production. In line with our Capital Light approach, we are making targeted strategic investments to increase manufacturing capacity, improve productivity and leverage technological capabilities while reducing costs and enhancing operational efficiencies.

We also made progress on our strategy to expand our entertainment offering, as we look to capture the full value of our intellectual properties in highly accretive business verticals, which are directly adjacent to the toy industry. This includes content, consumer products and digital experiences.

We have just announced that JJ Abrams' Bad Robot will produce the Hot Wheels movie, which we are developing with Warner Brothers. The Barbie movie is in principal photography in London, and we could not be more excited about Greta Gerwig's vision and creative execution for what is shaping up to be an iconic cultural event.

Will Ferrell and Issa Rae have recently joined the all-star cast led by Academy Award nominees, Margot Robbie and Ryan Gosling as well as, Simu Liu, America Ferrera, Kate McKinnon, Michael Cera and Hari Nef, among many other top-tier talents. As announced yesterday by Warner Brothers, the film will be released theatrically worldwide on July 21, 2023.

In addition to the growing portfolio of Mattel 163 mobile games, this week, we launched the He-Man Human and Masters of the Universe digital game on Roblox. Mattel also launched new NFT sets for Hot Wheels and Barbie and Balmain, which sold out instantly. We are looking to further leverage our iconic brands in the fast-growing world of digital art collection with several more launches planned in 2022.

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We take our role as a responsible corporate citizen very seriously and aim to contribute to a more diverse, equitable, inclusive and sustainable future. This week, we are publishing Mattel's 2021 Citizenship Report. It provides a progress update on environmental, social and governance strategy and goals including a new goal to reduce plastic packaging by 25% per product by 2030. This is in addition to other previously announced sustainable product and packaging goals including to achieve 100% recycled, recyclable or bio-based plastic materials in our products and packaging by 2030.

We are committed to Mattel's purpose to empower the next generation to explore the wonder of childhood and reach their full potential, and to our mission to create innovative products and experiences that inspire, entertain and develop children through play.

On behalf of the entire Mattel team, I would like to express our sadness and dismay, at the devastating impact of the war in Ukraine on innocent children and families. We stand with the Ukrainian people and have launched programs to support organizations on the front lines, aiding refugee children and families. We hope for a peaceful resolution and our thoughts are with all those who are suffering.

And now Anthony will cover the financial performance in more detail.

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Thanks, Ynon. We started 2022 with a very strong first quarter. We generated net sales of $1,041 million, an increase of 19%. Excluding the negative impact of currency translation, we grew 22% with growth across all regions and all of our reported categories.

Adjusted gross margin declined by 70 basis points with significant cost inflation mostly offset by the favorable impact of foreign exchange transactions, pricing, scale and cost savings. Adjusted operating income was $90 million, up 190% as we scale the business, while adjusted operating income margin increased by 520 basis points to 8.7%.

Adjusted EPS was a positive $0.08 compared to a negative $0.10 in the prior year period. The adjusted EPS improvement was primarily driven by operating income growth and lower interest expense. Adjusted EBITDA increased by $60 million or 65%, driven primarily by top line growth.

Turning to gross billings in constant currency. Total company gross billings increased 23% and benefited from increased points of distribution, retailers restocking low inventories following the strong holiday season, and gearing up to support product launches tied to the upcoming theatrical releases. Quarter end retail inventory was up in both dollars and weeks of supply as we work with retailers to meet strong second quarter consumer demand.

Looking at gross billings by region. North America was up 25%, driven by growth across key categories and all power brands. POS declined due to the Easter shift and promotional timing. EMEA was the fastest-growing region with a 29% increase, driven by growth across all markets with positive POS.

Latin America also had a very strong quarter increasing by 28%, driven by growth across all markets and categories with positive POS. Asia Pacific increased by 1% with strong growth in Australia and Japan, mostly offset by declines in China, which was impacted by COVID-related retail closures. POS declined in the region.

At the end of the quarter, retail stores were fully opened in North America and Latin America, while Europe had less than 1% of stores closed due to the war in Ukraine. In Asia Pacific, approximately 6% of stores were closed due to restrictions in China, which accounted for 11% of sales.

Adjusted gross margin declined 70 basis points to 46.6%. As anticipated, cost inflation had a significant 550 basis point impact, primarily due to increases in materials and ocean freight costs. The impact of cost inflation was mostly offset by several factors. Foreign exchange transactions had a favorable impact of 160 basis points. Pricing, primarily the carryover benefit of our second half 2021 actions, contributed 120 basis points.

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Strong top line growth generated a fixed cost absorption benefit of 100 basis points and savings from optimizing for growth added 90 basis points, completing the bridge to 46.6%. Given the anticipated level of cost inflation, as previously discussed, we are implementing pricing actions in 2022 that are factored into our guidance.

Moving down to P&L. Advertising expenses were about flat at $74 million. Adjusted SG&A expenses were $322 million, an increase of 4% due to employee-related expenses as well as higher bad debt expense related to the Russia-Ukraine war, partly offset by incremental Optimizing for Growth savings.

Bottom line performance was very strong across key metrics. Adjusted operating income increased by 190% or $59 million to $90 million. The increase was primarily driven by the flow-through benefit of top line growth, favorable FX, pricing and cost savings, partly offset by inflation and cost of goods sold. Adjusted operating income margin increased from 3.5% to 8.7%, an improvement of 520 basis points. Adjusted EBITDA increased by 65% or $60 million to $152 million.

Cash from operations was a use of $144 million, reflecting the seasonality of the business compared to $36 million in the prior year. The increased use of cash was due to higher working capital requirements. As a result, free cash flow was negative $180 million compared to $72 million in the prior year, with capital expenditures comparable to the prior year at $36 million.

On a trailing 12-month basis, we generated $226 million of free cash flow compared to $305 million in the prior year. Free cash flow was negatively impacted by the growth in inventories as we are prebuilding earlier in the season to support growth. Free cash flow conversion for the trailing 12-month period was 21% compared to 36% in the prior year period. Looking ahead to the full year, we expect to improve free cash flow and conversion rate.

Taking a look at the balance sheet. Cash balance was $537 million compared to $615 million in the prior year. Total debt was $2,572 million, down from $2,838 million in line with our strategy of using free cash flow to repay debt. Accounts receivable increased by $182 million to $862 million, driven primarily by the first quarter sales growth.

Inventory was $969 million compared to $626 million last year due to the earlier timing of our regional inventory build as well as the impact of inflation. Leverage ratio continues to improve. We finished the first quarter with a debt to adjusted EBITDA ratio of 2.4x compared to 3.3x in the prior year and expect it to continue to further improve. This is driven by the growth in adjusted EBITDA and debt reductions.

Savings from the Optimizing for Growth Program were $17 million in the quarter. Looking ahead, we continue to expect the program to achieve incremental savings of $80 million to $90 million in 2022 and total savings of $250 million by 2023.

As Ynon mentioned, we are reiterating our full year guidance for 2022, reflecting our momentum and the expectation for another strong growth year for Mattel. With respect to the impact of the Russia and Ukraine war, our business in these countries represented less than 3% of total gross billings in 2021. We now expect our business in these 2 countries to decline in 2022. However, this negative impact is expected to be offset by improvements in other geographies.

We expect to grow net sales in 2022 by 8% to 10% in constant currency. This will be driven by growth in our leader categories, led by our Power Brands and American Girl as well as our Challenger categories together, driven primarily by Action Figures.

Full year adjusted gross margin is expected to decline from 48.2% in 2021 to approximately 47% in 2022. Cost inflation, primarily in raw materials and ocean freight, is expected to be more significant in 2022 than in 2021 before moderating in 2023.

We expect the negative gross margin impact of inflation will be mostly offset by the benefits from pricing, including the incremental 2022 actions, fixed cost scale benefit from top line growth and anticipated savings from the Optimizing for Growth program.

2022 adjusted EBITDA is expected to increase to a range of $1.1 billion to $1.125 billion, representing growth of 9% to 12%. As a percent of net sales, SG&A is expected to continue to decline, while Advertising remains relatively stable.

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From our 2021 base of $1.30, adjusted EPS is expected to increase to a range of $1.42 to $1.48 per share. Adjusted EPS is benefiting from lower interest expense as we reduce debt in the near term, partly offset by an expected increase in the adjusted tax rate.

We are now providing a forecast for adjusted tax rate which excludes the impact of non-GAAP items. For 2022, we are forecasting an adjusted tax rate of 26% to 28% compared to 25% in 2021. Our year-to-go EPS performance will be more significantly impacted by the timing of tax expense compared to the prior year period. Capital expenditures are forecast to be in the range of $175 million to $200 million, an increase from prior year as we strategically invest to increase manufacturing capacity in our owned Dolls and Vehicles facilities. This investment is in line with our Capital Light strategy to support anticipated growth and where we have a significant competitive cost advantage.

Looking ahead, we expect to achieve strong growth in the second quarter and are confident in meeting our full year guidance. The guidance takes into account the anticipated market and supply chain disruptions that we are aware of today, but is subject to any unexpected supply chain disruption, market volatility and other macroeconomic risks and uncertainties.

Looking ahead to 2023, we are reiterating our 2023 goals to achieve high single-digit net sales growth in constant currency, and an adjusted operating income margin of approximately 16% to 17% of net sales. Our 2023 EPS goal is to exceed adjusted EPS of $1.90, driven by top line growth, margin expansion and the benefit of improved free cash flow.

In closing, Mattel executed another outstanding quarter, and we are very pleased with our start to the year.

Thanks for your time today, and I will now turn it over to the operator for Q&A.

Operator

Before we begin our Q&A session, I would like to turn the call back over to David Zbojniewicz for a few remarks.

David Zbojniewicz - *Mattel, Inc. - Vice-President IR*

Thank you. Before we begin the Q&A, I would like to state that per our company policy, we will not be commenting on press reports and speculation that have come out over the past 24 hours. We are focused on executing our strategy to grow Mattel's IP-driven toy business and expand our entertainment offering.

And with that, we are happy to answer your questions. Operator, back to you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will come from Eric Handler with MKM Partners.

Eric Owen Handler - *MKM Partners LLC, Research Division - MD*

Anthony, I'll start with you. In prior quarters, you've done a very good job of framing what the retail environment looks like with, I believe, average weekly inventory on hand. I wonder if you could sort of update how things ended in the first quarter and what you're seeing into 2Q?

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Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Sure. I can certainly address that question. I think what you see is a differential between gross billings and POS. And gross billings, as we said, benefited from a number of factors, increased points of distribution, retailers restocking, low inventory on shelves following a very strong holiday season and gearing up to support product launches tied to the upcoming theatrical releases.

So quarter-end retail inventory was up in both dollars and weeks of supply, which positions us very well to support second quarter growth expectations. I'll also say that retail inventory is very healthy, and we feel are in a great position and have reiterated our guidance for strong top line growth of 8% to 10%.

Eric Owen Handler - *MKM Partners LLC, Research Division - MD*

Great. And then as a follow-up, I guess, for Ynon. I did think it was interesting yesterday to see the launch of the He-Man Masters of the Universe game on Roblox. Just curious with all of your IP that you have, how are you thinking about Mattel's position in the metaverse?

Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

Yes. The -- we know we have one of the strongest catalogs of children and family entertainment franchises in the world. And that applies to content, consumer product and the digital experiences. And as it relates to the metaverse, specifically, and NFT as a subset, these areas are driven by collectability and communities. And in both cases, our brands and franchises are positioned perfectly to win in the area.

We launched 5 NFT campaigns in less than a year, all of which have been sold out instantly. They were not at commercial scale, they were more experimental and market testing, but we could not be more encouraged and happy with the results. So we know we are well positioned, and we see that as a real tangible opportunity over time.

Operator

Our next question will come from Linda Bolton-Weiser with D.A. Davidson.

Linda Ann Bolton-Weiser - *D.A. Davidson & Co., Research Division - Senior Research Analyst*

Yes. I was just curious; your results were so strong in the first quarter and your revenue beat the Street by quite a bit. What were your thoughts about potentially increasing the guidance for the year? I guess what held you back in doing so, even if you could have gone to like 9% to 11% growth, for example? Can you just kind of go through your thoughts about how your outlook is changing for the rest of the year?

Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

Yes, Linda. This is still early in the year. We have 3 more quarters to go. Very happy with our performance in the first quarter and focus on continue to executing our strategy. We did say we expect to grow in the second quarter. We're reiterating guidance, both top line and bottom line and continue to execute what we set out to do.

Linda Ann Bolton-Weiser - *D.A. Davidson & Co., Research Division - Senior Research Analyst*

Okay. And then as a follow-up, could I just ask you on the cost inflation front, can you give us a little more color on how things are changing? A couple of companies have said and some data we look at indicate that, for example, container freight rates have peaked and are actually kind of trending down. Are you seeing that? And what can you say about some of the other cost inputs?

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Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Sure, I can address that. We are seeing some decline in spot rates from the recent peak. Although, certainly against prior year and historically, they continue to be quite elevated. Given that we procure ocean freight through a combination of contracts and spot purchases, that impact is fairly modest and really it doesn't change our outlook for the full year.

As we've said before, we are impacted by materials, particularly resins and zinc as well as ocean freight. We're seeing some inflation and wages in some of our supply chain markets. So our full year outlook for inflation has not changed. We continue to expect it to be more significant in 2022 than 2021.

And I would add, in response to that, we did take pricing in '21, which is having a carryover benefit into 2022, and we are implementing additional pricing actions in 2022, that will improve the back half, and we've factored those into our guidance. As we look ahead on the inflation front to 2023, we do expect it to moderate.

Operator

Our next question will come from Arpine Kocharyan with UBS Investment Bank.

Arpine Kocharyan - *UBS Investment Bank, Research Division - Director and Analyst*

This is Arpine. I was wondering, how much did your distribution grow year-over-year? Because it's surprising as a lot of people perhaps think of your distribution as saturated, you're already shipping to everywhere you could be shipping. So what channels drove that growth?

And then you mentioned extended direct-to-consumer offering outside of North America. Could you detail exactly what those were? And then I have a quick follow-up.

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes. On the first part of the question, in terms of distribution, I think this goes to our performance over the last couple of years, the fact that we've gained market share 2 years in a row, we have good momentum. We have actually gained shelf space, and that's what we're seeing come through in terms of points of distribution.

Arpine Kocharyan - *UBS Investment Bank, Research Division - Director and Analyst*

Okay. And then direct-to-customer offering outside of North America?

Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

Yes. And I can add on that. The -- and in addition to shelf space, just to confirm, we also increased the actual number of doors, brick-and-mortar stores where we sell our product from around 485,000 to now at around 494,000 stores where our product is sold. We haven't provided breakdown how this is split, but we are looking to continue to grow the retail footprint where our product is sold and offer consumer choices.

The brick-and-mortar business represented less than 70% of our business in 2021. Online retail and e-commerce continues to grow and represents -- in 2021, represented 31% of all POS. DTC is a growing part of our strategy, as you know. This is part of -- a key part of our strategy. It's divided between Mattel Creations, which is more of the high touch, highly curated part of the business. We have the Mattel Shopper and of course, the American Girl DTC business.

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All in all, we have an omnichannel retail strategy. We aim to be wherever consumers are and continue to expand and grow the number of places where people can shop and buy our product.

Arpine Kocharyan - *UBS Investment Bank, Research Division - Director and Analyst*

That's super helpful. Pricing helped your margin by 150 basis points, I think, in Q4, but about 120 basis points this quarter. Could you give us a sense of what that looks like for the rest of the year? And I know you said you've taken -- you intend to take more pricing. There is a lot of concern from investors about sort of state of the consumer and inflationary pressures. As you reiterate your guidance here, is there some kind of price elasticity work that you've done to assess the impact of pricing on demand for your brands that you could share?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes, I can talk a little bit about the pricing. And as you noted, pricing had a 120 basis point positive impact on Q1. Most of that is the carryover impact of the pricing action from last year. And as we noted on our last call, we were contemplating additional pricing actions this year. The inflationary environment continues to be very significant and have an impact on us. So we are implementing pricing actions in 2022, which will go into effect in the second half. I mean, obviously, we factored those into our guidance, particularly for gross margin.

As you know, we're guiding gross margin down a little bit to 47% with a significant impact on inflation. And what we feel good about is that we're able to offset most of that through a combination of the pricing actions that we've taken, the cost savings from our Optimizing for Growth program, as well as the scale benefit from our top line growth.

And as we've said before, longer term, we would expect the impact of pricing and cost savings over time to more than offset the impact of cost inflation and contribute to margin expansion.

Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

And with respect to the second part of the question, we haven't seen any negative impact on demand with pricing. And important to say that when we take pricing action, we are being very thoughtful and are committed to maintaining the right balance between the high quality and value for consumers and are being very smart and strategic about it. So we have not seen any impact in the first pricing action we took last year, and we are not -- we don't expect to see an impact this year.

Operator

Our next question will come from Drew Crum with Stifel.

Andrew Edward Crum - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

Action figures up 75%, if I heard correctly, and the lift appears to be shipping movie properties during 1Q. How does that compare to your expectations for 2Q? And your commentary was you expect to achieve strong growth in the quarter. But in addition to the movie properties, are there any other key drivers you'd highlight? And then I have a follow-up.

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

So our Action Figures business has been incredibly strong. As you know, driven by Jurassic World, Disney and Pixar's Lightyear, and of course, Masters of the Universe. We're expecting continued growth for the rest of the year with these incredible theatrical releases. And specifically, the momentum is continuing on Masters of the Universe.

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Our portfolio also includes further growth with Minecraft and WWE as evergreen properties. We don't provide the financial projections by property, but specifically, these 2 blockbuster theatricals are the drivers of the category, and then, of course, our evergreen brands, MOTU, Minecraft, WWE, all with innovation and great marketing going forward.

So a very, very strong category performance and expect it to be strong for the year.

Andrew Edward Crum - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

Got it. And then my follow-up pertains to Europe. It looks like the gross billings and EMEA they're pretty good in 1Q. If you break out Europe only, what's been your read on retailer and consumer demand? And any notable changes you've observed in April as the wars dragged on?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes. With respect to our performance in EMEA, as we noted in our remarks, it's very, very strong. It's our fastest growing region and really comprehensive growth across all markets, positive POS, a 29% increase in gross billings and it's just a continuation of the great performance we've seen in the region over the last couple of years.

And with respect to the start to the second quarter, not isolating EMEA in particular, but our POS for the April month to date has exceeded 25%. So we're off to a good start to the second quarter.

Operator

Our next question will come from Stephanie Wissink with Jefferies.

Matthew Catton - *Jefferies LLC - Equity Research Associate*

It's Matt Catton from Jefferies filling in for Steph Wissink here today. Very strong results in the first quarter. I was hoping that you could help us think, further think through current trade level inventories. Have you achieved desired trade level inventory to support anticipated demand trends? Or is there still some channel to fill in Q2.

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes. We feel -- in terms of retailer inventory, we feel like we're in a very good position. We saw some restocking during the quarter. The inventories are healthy, well positioned to support future growth and as Richard just noted, the theatrical tie-ins that are coming midyear. So we feel like we're in a really good position as we look ahead.

Matthew Catton - *Jefferies LLC - Equity Research Associate*

Awesome. And then in terms of owned inventory with quarterly inventory being up 59% year-over-year, can you just provide a little more insight into the level and composition, please?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Sure. So on our balance sheet, our inventory ended at $969 million. It is up from $626 million last year and really reflects mostly our decision, right, to prebuild earlier in the season to support growth. And about 1/4 of that increase is actually the impact of cost inflation. But again, a proactive

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step on our part to build ahead, spread out manufacturing through the season more so that we make sure we have product availability for retailers and consumers throughout the year.

Operator

Our next question will come from Gerrick Johnson with BMO Capital Markets.

Gerrick Luke Johnson - *BMO Capital Markets Equity Research - Senior Toys and Leisure Analyst*

In addition to building inventory earlier, are retailers bringing product in earlier and maybe moving forward set dates for movies and back-to-school?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Not aware of any shift in timing, Gerrick.

Operator

Our next question will come from Megan Alexander with JPMorgan.

Megan Christine Alexander - *JPMorgan Chase & Co, Research Division - Research Analyst*

Just back to the gross margin follow-up. In 1Q -- in the first half, you talked about significant pressure. 1Q was only down 70 basis points. So you're still expecting gross margin down 110 for the year. So can you just help us, how we should be thinking about gross margin for 2Q and then the second half? What's changing in the remainder of the year such that the decline gets worse? You have another price increase coming and then we'll start to lap some of the more significant freight and input cost increases in the back half. So is it that raw material costs are higher than you expected? Or is there something else that you saw in 1Q that maybe doesn't continue?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes. Good question. So I can comment on that. As you noted, we're down 70 basis points in the first quarter. Our full year guidance implies about 120 basis points of decline. And what you see is because of the seasonality of the business, the first quarter is small, so when you get that outsized top line growth, you get a greater fixed cost absorption benefit in the first quarter than you will in the balance of the year.

And secondly, our savings from Optimizing for Growth tend to be more fixed cost. So they have a bit of an outsized impact on Q1 relative to the balance of the year as well. But again, as we look at the full year, some downward pressure, but we feel good about the fact that our pricing and cost savings are going to offset most of the expected inflation.

Megan Christine Alexander - *JPMorgan Chase & Co, Research Division - Research Analyst*

That's helpful. And then a quick follow-up. There have been some reports about Amazon Prime Day moving into July from June. If that were the case, would that impact the shipments timing? Or would most of the shipments still happen in 2Q?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

That wouldn't have a material impact on our timing of our shipments.

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Operator

Our next question will come from Fred Wightman with Wolfe Research.

Frederick Charles Wightman - *Wolfe Research, LLC - Research Analyst*

If we just look at the COGS bridge that you gave, it looks like sequentially, it was -- the cost inflation was a little bit better, down 550 this quarter. I think that was 600 last quarter. Do you think that, that inflationary number has peaked and should continue to come down from here?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

No, I would expect, as we said, our outlook for inflation hasn't materially changed. We still expect to have a more significant impact in 2022 than the 400 basis points in 2021. And I would say that the first quarter is in line with that. That being said, probably a little more weighted to the first half than the second half given the escalation that happened in the back half of 2021.

Frederick Charles Wightman - *Wolfe Research, LLC - Research Analyst*

Makes sense. And then are you guys still expecting all power brands to grow for the year?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes, we are.

Operator

Our next question will come from Mike Ng with Goldman Sachs.

Michael Ng - *Goldman Sachs Group, Inc., Research Division - Research Analyst*

I was just wondering if you could talk a little bit about the point-of-sale trends. I think you had said it was in line with expectations through April. I was just wondering if you had a number that you could share with us for the company? And then any specific commentary around Barbie or Dolls would be great?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

Yes. So as we stated, we feel really good about April. April month-to-date POS is up more than 25% on a total company basis. And as we also stated in our prepared remarks, POS was down high single digits in the first quarter. But EMEA was up. Latin America was up. North America was down. Asia Pacific was down.

And one point I'd like to make with respect to the POS data, we do provide a significant level of disclosure and detail about our performance. And POS is a directional tool and impacted by different variables that may not provide an accurate view of underlying trends in the short term. So what we're saying is going forward, we're going to provide POS at a macro level for the portfolio or on a regional basis and in specific situations where it's relevant for the long-term trajectory of the business. So we're not going to be providing it at the category level and Barbie in particular on a regular basis.

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

Michael, I'll expand upon the Barbie question. Barbie had an incredible quarter. We were up 12% and that's on top of an 86% growth last year. So clearly, the brand is continuing its multiyear momentum. We were the #1 overall Dolls property every week in the U.S. and the #1 global Dolls property. The strength continues. We've got some incredible innovative products that are in the marketplace like Barbie Extra, and we recently launched a new innovative entry called Cutie Reveal. This was just launched in March, and Cutie Reveal hit the Doll category industry top 10. That's a big feat in its first month, and it actually outpaced the launch of our largely successful Color Reveal line.

So we continue to drive momentum and cultural relevance. We had an incredible sellout overnight sensation with our Barbie Queen Elizabeth collector doll. You'll continue to see more culturally relevant collector product in the marketplace. And we're looking forward to the momentum continuing not only for Barbie, but the entire dolls category.

Operator

Our next question will come from Jim Chartier with Monness, Crespi, Hardt.

James Andrew Chartier - *Monness, Crespi, Hardt & Co., Inc., Research Division - Security Analyst*

You guys have a strong movie release calendar this year, but a car series launching on Disney+. I'm curious, given the strength of other streaming series, how impactful that could be this year?

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

Our vehicles category has been extraordinarily strong. I mean the whole category itself has been growing. We grew 36% on top of 15% last year. And that's growth across all product lines. Hot Wheels' Matchbox and as you've asked, Disney Pixar cars. The line is incredibly strong, great innovation. We continue to work incredibly close with our partners at Disney, innovating and extending the incredible characters in the car series in new and different ways. But ultimately, these results demonstrate our successful execution of a category structure that we're applying across our entire portfolio, but in particular, the vehicles category has incredible momentum, including Disney Pixar Cars, Matchbox, Hot Wheels and much more to come.

James Andrew Chartier - *Monness, Crespi, Hardt & Co., Inc., Research Division - Security Analyst*

Great. And then on American Girl, what gives you the confidence the business will grow this year despite the first quarter decline? What are you seeing within the stores, are tourists and traffic coming back to the stores?

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

Yes. Thank you for that question. We are expecting full year growth in American Girl. We've got incredibly strong plans in place. And as we progress through our turnaround, we're very confident. The product launches and marketing plans for American Girl are primarily focused on the second half of the year. The decline that we saw in the first quarter was primarily due to later Easter and as well closure of 2 stores.

You know we've shared; we've continued to evaluate our retail footprint. At the same time, we've been investing in our flagship stores. So as you mentioned, New York City has been really on a great turnaround. Traffic is up. Our business is actually up in that store. I encourage anyone for that matter, who visits or lives in New York, to visit our flagship store and really see the revitalization both in merchandising, event, and customer service at an entirely new level of excitement.

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So all in all, again, I think from a marketing, merchandising, DTC, store experience perspective, we are very much on track with our American Girl plans, and I think you'll start to see a lot of excitement and scoreboard growth in the back half.

Operator

Our next question will come from Jaime Katz with Morningstar.

Jaime M. Katz - *Morningstar Inc., Research Division - Senior Equity Analyst*

Games have become a pretty important component of one of your competitors plan. And I know Roblox was mentioned. So I'd be interested to hear how you guys are sizing that opportunity for yourself and maybe how you think about that contributing to the profit profile going forward?

Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

Jaime, digital gaming is a strategic priority and part of our mid- to long-term strategy to capture the full value of our IP. Clearly, it's a large market, and we see a significant opportunity to grow our business there and leverage the strength and engagement and communities that our franchises have.

We have a 3-part strategy for gaming. One is Mattel163, it's our own mobile game publisher and partnership as part of a JV with NetEase. So far, we launched 2 games, UNO and Phase 10 in full fledge and recently launched the third game, Skip-Bo. we already shared that last year, this JV exceeded $100 million of revenue -- so based on 2 games only.

So this is growing fast. It's -- we don't consolidate the number given that we don't control the JV, but it's a fast-growing part of our business. We also have licensed partnerships. This is where we work with third parties. This is also a nice business that is growing. It's not as big, but it's still early, and we're having a lot of momentum there.

And the third piece, self-publishing. This is where we launch games on kids-targeted platforms such as Roblox. We have already the Hot Wheels game on that platform. We recently or this week launched the Masters of the Universe game on Roblox. So we are building scale, building momentum, still early. But given the strength of our catalog, we believe we have a real opportunity to have a scaled business in this area.

Jaime M. Katz - *Morningstar Inc., Research Division - Senior Equity Analyst*

Okay. And then just as a follow-up, would you help us understand whether or not the retailers' you guys are working with are having any different expectations this year for things like sales allowances or any different demands that they are putting on you guys given supply chain issues?

Anthony P. DiSilvestro - *Mattel, Inc. - CFO*

No, we don't see any material change in sales adjustments for us.

Operator

I'm showing no further questions in the queue at this time. I would now like to turn the call over to Mattel's Chairman and CEO, Mr. Ynon Kreiz.

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Ynon Kreiz - *Mattel, Inc. - Executive Chairman & CEO*

Thank you, operator, and thank you all for your questions. In summary, this was an outstanding start of the year for Mattel. Our momentum continued across the business. We started the second quarter with strong consumer demand. The full year outlook is also strong, and we expect to grow market share. We are firmly in growth mode and are operating as an IP-driven, high-performing toy company.

As always, we appreciate you following our journey and your interest in the company. Thank you, and I will now turn the call over to Dave.

David Zbojniewicz - *Mattel, Inc. - Vice-President IR*

Thank you, Ynon, and thank you, everyone, for joining the call. The replay of this call will be available via webcast in audio beginning at 8:30 p.m. Eastern Time today. The webcast link can be found on our Investor page or for an audio replay, please dial 1 (404) 537-3406. The passcode is 3845555. Thank you for participating in today's call.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.

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