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# EDITED TRANSCRIPT

## MAT - Q3 2015 Mattel Inc Earnings Call

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**OVERVIEW:**

MAT reported 3Q15 adjusted operating profit of $322m and adjusted EPS of $0.71.

## CORPORATE PARTICIPANTS

**Martin Gilkes** *Mattel Inc - VP of IR*

**Chris Sinclair** *Mattel Inc - Chairman & CEO*

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

**Kevin Farr** *Mattel Inc - CFO*

## CONFERENCE CALL PARTICIPANTS

**Sean McGowan** *Oppenheimer & Co. - Analyst*

**Stephanie Wissink** *Piper Jaffray & Co. - Analyst*

**Lee Giordano** *Sterrne Agee CRT - Analyst*

**Greg Badishkanian** *Citigroup - Analyst*

**Taposh Bari** *Goldman Sachs - Analyst*

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

## PRESENTATION

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**Operator**

Good day, ladies and gentlemen and welcome to the Mattel third quarter 2015 earnings conference call.

(Operator Instructions)

As a reminder, today's conference is being recorded. I would now like to introduce your host for today's conference, Mr. Martin Gilkes, Vice President Investor Relations. Sir, please begin.

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**Martin Gilkes** - ***Mattel Inc - VP of IR***

Thank you, Liz and 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 third quarter 2015 financial results. We will begin today's call with Chris, Richard and Kevin providing commentary on our results and then we will 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 in the Investor 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 relating 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 sections of our 2014 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 our other public statements. Mattel does not update forward-looking statements and expressly disclaims any obligation to do so. I'd now like to turn the call over to Chris.

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**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Thank you, Martin and good afternoon, everyone. I'd like to thank you for joining us today. In a few minutes, Richard and Kevin will provide a lot more detail on the quarter and our outlook.

I wanted to start things off today by giving you some perspective on how we're progressing broadly on our turnaround at Mattel. And then in that context, how we view the quarter and the balance of the year.

So briefly to the quarter. Clearly the results were somewhat mixed and certainly we would have liked to have had a little bit more on the top line. But absent the major impacts of weakening foreign currencies, the results are just about where we expected to be. As most of you know, foreign exchange continued to be a huge headwind as currencies in many of our key markets weakened even further and depressed our overall quarterly gross sales by close to 8%.

It also had a significant impact on gross margin and on operating income. Separating this out, our progress was more balanced. Further, we're very encouraged by the progress we're making on our turnaround, our cultural transformation and on our strategic priorities.

Since my first call with you in January, we have been digging deep as I said we would. We've begun to make some significant progress in transforming and strengthening ourselves. Today, I can quite confidently say that we're a radically different and stronger Company than we were just nine months ago. We've continued to reshape our culture to emphasize creativity, innovation, speed and more personal accountability. And we've substantially transformed our leadership team to help lead this change.

In fact, since January, we've changed out over two-thirds of our key senior leaders. We've also attracted some extremely talented new executives to help lead us in important areas like Human Resources, Core Brands, Content and Brand and Commercial Finance. We're continuing to streamline further to reduce bureaucracy. We're also driving stronger performance management systems to build more accountability and to help us drive change.

We've also begun to execute strongly against our six key priorities where our core brand positionings and platforms are much improved, our pricing and price value is much more competitive, and where we're getting some very good content deals in the works, including the recently announced Barbie movie with Sony. We've also continued to build our Toy Box initiative with a full court effort under way on the licensing front with all of our major studio and network partners.

At the same time, we have some other creative deals underway like the recently announced 9 Story venture for brands like Barney and Angelina. We're continuing to drive the invention and innovation pipeline with ventures like our deals with Google and View-Master and with ToyTalk and Hello Barbie.

Retail execution and focus has also improved significantly. And we've begun to strengthen our top to top relationships across all of our major retail and e-commerce customers. We've also been building a much more robust holiday strategy and we've increased our ad and display support in most of our key accounts.

Similarly, we've executed well on many of our major cost initiatives and we've begun to bend the curve on cost of goods and SG&A. We continue to see hitting at the high end of our cost reduction target of $250 million to $300 million by the end of next year. And we're already getting a pretty good sight line on moving well beyond that range.

This strong focus on cost has allowed us to step up investments in advertising and trade promotion, in retail expansion for American Girl, and to accelerate our emerging markets business in key countries like China, a market that continues to perform extremely well. Frankly, we should begin to see more flow-through on these cost initiatives and reinvestments over the balance of this year and into 2016.

Turning back more specifically to the quarter and to the full year. My take-aways are as follows. First, some real positives. We're building strength in our leadership team and improving our culture. Equally importantly, retail POS is growing across most of our core brands, with notable strength in Fisher-Price and Hot Wheels and stability now with Barbie. We're also executing better with our customers and we're setting up for improvements in space and merchandising. We're getting costs out at an accelerating rate and we're managing the middle of the P&L much better. Finally, we're getting some very good traction in core emerging markets like China and Russia.

All of this said, we are clear eyed about the challenges we face. ForEx will certainly continue to be a headwind across many key markets. We're also moving aggressively to offset significant declines in important entertainment properties like Disney Princess and to reverse continued softness with Monster High.

We're acutely focused on addressing the challenges caused by space losses over the past 12 months and some of the recent customer shifts on inventory timing. While our work is by no means done, I am pleased with the way that our team is responding and I'm confident in our direction.





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As we look ahead, we expect the fourth quarter to be another very competitive and aggressive one across all categories. But overall, we do expect improvements with a stabilizing of space and inventory impacts, stronger trade promotion and merchandising support, continued core brand growth, and improved flow-through on our cost initiatives. Net, with some appropriate caution, we continue to believe that the full-year 2015 outlook that we provided after the first quarter is largely on track.

Further, as we continue to build momentum around implementing our core strategic priorities, we remain committed to continuing our current dividend payout which the Board just reaffirmed. So with that, let me now turn it over to Richard who will give you a lot more specifics.

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

Thanks, Chris. As Chris just alluded to, there were three things that weighed down our third quarter financial results; a continuation of strong foreign exchange headwinds, declines in Monster High and softness in some licensed entertainment properties. Although we look at our business quarterly, we also need to look beyond the financial headline to assess the business and when we do that, we see a lot of progress towards our turnaround and lots of reasons to believe in Mattel's long-term success.

Long-term success starts with having the right people in the right places and this past quarter, we were pleased to announce four exceptional new members to our leadership team. They join Mattel with clear mandates to strengthen and build four critical opportunity areas; Core Brands, Content and Digital, Brand and Commercial Finance, and Culture. Each of these leaders is a recognized innovator and already on the job contributing to Mattel's transformation.

Many of the signs of a turnaround at Mattel are just below the surface. So as I take you through some of the specifics of our Q3 results, I'll go a little deeper to give you the opportunity to see what I'm seeing, which is great progress to date and a belief that our turnaround efforts are in line with our expectations.

Today, with regard to performance, I will focus on POS to show how our brand management and retail execution efforts are driving consumer demand and strengthening Mattel's retail customer base. Then I'll quickly pivot to talk about what our turnaround progress means for the upcoming holiday season and for 2016.

Global POS, arguably the leading indicator of our progress, remains positive for the year, although down slightly in Q3. Not surprising, the decline in the quarter was mainly driven by Monster High and Disney Princess. But when we look at the numbers excluding Disney Princess, global POS was actually up about 3% and in fact, accelerated relative to the first half of this year. Most importantly, POS continues to outpace shipping which means with better alignment there is a real opportunity to increase sales going forward. Almost all of our core brands have POS outpacing shipping as we enter the holiday season with a significant opportunity to better align Barbie and Fisher-Price shipping to POS trends.

Core brands are the leading indicators of our success. So let me take a minute to provide a little bit more detail on the three brands that you are likely to be most interested in, Fisher-Price, Barbie and Monster High. On Fisher-Price, we continue to see positive and improving POS this year despite some POS headwinds related to licensed properties within Fisher-Price Friends. And for the first time in a very long time, global Fisher-Price POS is up mid-single digits year-to-date and up high single-digits in the third quarter. With Q3 POS significantly outpacing shipping, which was up only slightly in the quarter, we have a great opportunity to close the gap and increase sales.

In our Baby business, which represents about half of our total Fisher-Price business, our efforts to connect and convert with innovative product and messaging are gaining traction. We are seeing real solid results as we build the brand into a relationship with millennial parents, one that provides the guidance, gear and toys parents need to help their children get the best possible start in life.

There is great enthusiasm and a renewed focus on brand management at Fisher-Price that's showing in consumer programming and our Fisher-Price Best Possible Start campaign is a great example of this. We still have work to do in our preschool line and we will have more positive news about our Friends licensed entertainment business soon. But as we move out of the third quarter, we see a great opportunity to leverage our progress to date and begin to close the gap between POS and shipping.

Moving on to Barbie. Now earlier this year, I mentioned that we expected 2015 to be the most competitive doll market in recent memory and we really saw that in Q3 as significant doll competitors hit the shelves with advertising to support the launches. So given that, we're pleased to see Barbie POS continue to hold its own this quarter with global POS up slightly year-to-date and Q3 POS flat.

We continue to see positive results in the US where our brand-new marketing messages and strategies got an earlier start and we are very happy to see improving POS trends internationally, as we cleaned up older inventory and now move into the holiday season with a clean slate and the opportunity to really drive sales. Relevance never rests and the Barbie brand's renewed commitment to connect to pop culture is really starting to show in POS trends and growing buzz for the brand, both with girls and moms.

On the digital front, we saw significant increase in app views this past quarter and our YouTube video views nearly doubled. From our milestone globally diverse Fashionistas line to the recent New York Times magazine cover story featuring our innovative Hello Barbie doll, we are very pleased to see Barbie leading the cultural conversation again. We are continuing to expand our efforts to spread the word about Barbie in that vein. Just last week we launched a ground-breaking new advertising campaign titled Imagine the Possibilities that reinforces and goes to the heart of Barbie's message.

Like Fisher-Price, Barbie brand shipping is lagging POS trends, partly due to older inventory that was on the shelf in some international markets and a reduction in shelf space globally. But now with shelf space productivity up and currently clean inventory on shelf, there is a great opportunity to close the POS to shipping gap and improve sales momentum going forward.

International shipping has already started to respond. In Q3, we saw sequential improvement and we see a great opportunity in North America where Barbie POS is significantly outpacing shipping, with POS up high single-digits and shipping down 8%. From exciting new product to focused, more relevant marketing and a renewed sense of purpose, Barbie's strategically returning to strength despite a very tough marketplace.

So on balance, I see a lot of very positive momentum coming out of our two biggest brands. Momentum that we haven't seen for a while. Moving brands like Barbie and Fisher-Price takes time but I am increasingly convinced about the work that we're doing and I am pleased to see that the strategies we've put in place are working. These brands are getting stronger and the work we've done this year will only continue to build into 2016.

Moving on, let's take a look at our greatest challenge in core brands, Monster High. As you know, the brand has struggled in its evolution from the global sensation it was at launch to an evergreen brand. Yet, it remains very relevant as a top five global doll property and arguably, the Monster High message is more relevant than ever in today's pop culture.

In Q3, while we saw declines in the base business persist globally, we were encouraged to see that the additional new product lines introducing new scales and new form factors performed well. Girls continue to tune in. Website traffic remains robust and this quarter, we saw app views increase along with YouTube video views.

IP for this brand is incredibly powerful as the metrics show. So as we fix the toy side of the business, we are also thinking bigger by finding ways to monetize the brand as global IP. The brand's recent partnership with High School Story, the number one game for female tweens in the US, is a great example. And this month, Monster High will be the star of the game.

The brand's refreshed, purpose-driven message means it can command marquee partners and placements. And we couldn't be more thrilled about our collaboration with Lady Gaga's Born This Way Foundation, a leading voice for inclusivity and tolerance worldwide. Lady Gaga is one of the most distinctive and famous music artists in the world today and she is fiercely dedicated to her Foundation's mission, which dovetails nicely with Monster High's brand purpose. This is a partnership that will unite and mobilize both fan bases to multiply a shared message through original content, social media and eventually, product. It's a perfect pairing.

To be sure, the journey to date for Monster High has been bumpy but I can tell you I like where this brand is going with strong new work just starting to hit the market now and much more to come in 2016. Despite my optimism, I'm sure the question remains with Disney Princess and Monster High declining, what are the implications for Q4 and for 2016? Clearly, we have our work cut out for us but there are several positive catalysts for Q4 including our continued revitalization of core brands, which gives us the opportunity to increase sales momentum by closing the current POS and shipping gap, particularly with Barbie and Fisher-Price as we've discussed.

We should see continued momentum from Hot Wheels and Thomas & Friends which are performing well both from a POS and shipping perspective. I'm particularly excited about View-Master, since it's getting placement in different parts of the store which will hopefully lead to expanded cross-generational appeal.

MEGA brands, which is gaining some traction in international markets will have exciting new products timed to the release of Halo 5: Guardians as well as the new Call of Duty: Black Ops video game. MEGA will also have great holiday products for its expanded licensed properties, Minions and SpongeBob.

We will see continued sales momentum with our new license entertainment properties Minecraft and Nickelodeon's Blaze and the Monster Machines and we are building on momentum from our investments in emerging markets, particularly China, where sales are accelerating.

While there's been a lot of product news and activity this year and this quarter, traction is also due in part to substantially better execution at retail. Going forward, in addition to benefiting from some timing shifts, we will be supported by increased advertising and stronger trade promotion and merchandising support. This year, we have made significant progress aligning our brands and commercial organization to execute at retail including, for holiday 2015, doubling our presence on many of the retailer Top Toy lists like Walmart and Toys R Us.

And we have a much bigger presence in many of their toy catalogs. This year unlike last year, we will have meaningful statements in store during Black Friday and Cyber Monday events with a number of key products and you will see several out-of-aisle product placements throughout the holiday period. These catalysts give us confidence that we can achieve the 2015 outlook we shared with you earlier this year and Kevin will walk you through more of the details on that in a moment.

Looking ahead to 2016, it's clear we will continue to have significant challenges with the loss of Disney Princess and the current trend of Monster High. We have been aggressively developing plans to offset the Disney Princess revenue gap and we have confidence in the new team managing Monster High. We're focusing our efforts to build core brand momentum and building on new partnerships.

And as we are just beginning to share our 2016 plans with retailers, here's some insight. We expect partnerships will make up a big chunk of the gap including incremental in 2016 in partnership with Warner Bros. we will be supporting brand new entertainment properties from their DC Comic world.

For starters, we're tapping into the rich DC Comic vault and focusing on the growing hyper relevant DC superhero girl franchise with content launching this fall. In addition, Warner Bros. is kicking off a completely new multi-film, multi-year theatrical franchise in 2016 with the release of Batman v Superman: Dawn of Justice. Also incremental to 2016, MEGA Brands will be launching a new innovative line of toys supporting the incredibly popular property Teenage Mutant Ninja Turtles and it's 2016 theatrical release.

We will also continue to build on our efforts to date and improve the momentum on all of our core brands. We will look to Toy Box, Mattel's energetic hub of innovation and new technology to provide the scores of the incredible ideas and partnerships that are setting a new pace for the industry. We will continue to invest and expand in emerging markets like China with all of our brands. And of course, we will continue to align our brand and commercial organizations and focus on supporting our retail partners around the world. Beyond these efforts, we continue to build a robust pipeline for the licensed entertainment component of our business and I look to sharing more news with you on this in the upcoming months.

The net is this. While we are just entering the holiday season, which represents more than 50% of retail sales for the year, and have recently begun to preview fall 2016 lines with customers, we are increasingly confident that we should be able to cover a significant portion of the Disney Princess revenue gap as we build momentum throughout the year and into 2017.

The current year, now three quarters in, has not been without its challenges. But taken as a whole, we believe we are meeting these head on, making solid progress against our strategic priorities and positioning ourselves competitively for the future.

As we enter this critical holiday period and look toward next year, Mattel is structurally a much stronger organization. We have focused ourselves whole heartedly to the creativity, innovation and speed that made Mattel great. When I speak with partners, licensors, licensees, press and our own people, there is unmistakable energy and enthusiasm for what we're doing and evidence that we're on the right path.

Transformation is hard work and we're making great progress. So my continued thanks to the people at Mattel who I know are today more committed than ever to accelerating our turnaround. I look forward to sharing much more with you in the coming months and now I'd like to turn the call over to Kevin.

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**Kevin Farr** ***- Mattel Inc - CFO***

Thank you, Richard and good afternoon, everyone. As Chris said, while our overall third quarter results were about where we expected them to be, our reported sales were slightly below expectations for the quarter due to the strengthening of the US dollar versus our plan, specifically in late August and early September, which negatively impacted sales by an incremental $50 million. The retailers bought our product later as they reduced their mix of direct import purchases which likely shifted $30 million to $40 million of sales to the fourth quarter.

Looking beyond the top line, gross margins was also significantly impacted by currency but we did make progress with our cost saving initiatives which are helping to fund investments in the turnaround, and a key reason that we believe we can deliver gross margins of about 50% for full-year 2015 despite the currency headwinds.

With foreign exchange having a significant impact on the quarter and year-to-date, I'll provide some additional color on the currency dynamics before moving into the brand and P&L discussion.

In aggregate, currency reduced reported net revenues by $150 million in the quarter, and almost $300 million year-to-date. As many of you know, we have market leading positions in Mexico and Brazil where the peso and real depreciated about 20% and around 40% year-over-year in the quarter. These markets represent two of our largest countries outside the US and currency volatility had a meaningfully negative impact on our reported results.

We also saw the Russian ruble weaken by around 40% year-over-year in the third quarter. We expect revenues will continue to be negatively impacted by foreign exchange but we believe the impact in the fourth quarter will be less pronounced since the US dollar began to strengthen in the fourth quarter of 2014.

Adjusted gross margin was another key P&L driver that was significantly impacted by currency accounting for 200 basis points of the year-over-year decline. As we noted on our last earnings call, the transaction impact on gross margin is more pronounced in the second half due to seasonality, coupled with the timing of inventory movements and hedging at less favorable rates in 2015 versus 2014. We expect this trend to continue in the fourth quarter but similar to the sales line, it should be less of a headwind than in the third quarter.

As we move into detailed sales and P&L discussion, I want to remind everyone that I'll be discussing our results in constant currency and referring to adjusted financial measures that exclude certain items related to our acquisition of MEGA as well as severance expense, unless otherwise noted, to provide better visibility into the underlying business performance as we execute the turnaround.

In constant currency, worldwide gross sales for the quarter were down 3%, down 11% as reported. Year-to-date, worldwide gross sales were flat in constant currency, or down 8% as reported.

From a brand perspective, worldwide sales for Mattel girls and boys brands were down 5% in the quarter and down 3% year-to-date. Monster High shipping continues to be our biggest headwind in the quarter and year-to-date followed by softer shipping of licensed entertainment properties. This was partially offset by continued strength in Hot Wheels and our Minecraft license.

Barbie sales were down 4% in the quarter, moving from down 8% year-to-date. Notably, Barbie international shipments improved to down 2% year-over-year in constant currency after declining 9% in the first half. As you know, about two-thirds of Barbie sales are from international markets so this is an important element at getting the brand on an improving trend globally.

Worldwide sales for Fisher-Price brands were up 1% in the quarter and up 3% year-to-date. With good strength in our BabyCo business which accounts for about half of the total as well as Thomas and Imaginext which were offset to a large degree by declines in a number of Fisher-Price brands licensed properties.

American Girl was down 2% in the quarter and down 1% year-to-date. Our BeForever historical line continues to be the bright spot with its recent brand relaunch and strong new character introductions which were offset by Truly Me and Girl of the Year.

We're very encouraged by the performance of our shop-in-shops in Canada and Mexico which continue to meet expectations. MEGA shipping was up 2% in the quarter despite declines in the Arts and Craft business where we're deemphasizing nonstrategic lower margin product lines.

Importantly, the performance in the Construction business continues to be in line with our expectations. We're particularly pleased with its growth internationally which was up 40% in the quarter in constant currency. International expansion was a big focus for this acquisition and these trends reinforce the potential.

Looking at regional sales, we had mixed results on the surface but I'll highlight a few key themes. Asia-Pacific was very strong in the quarter and year-to-date led by China where investments are paying off with accelerated sales. We also continue to see strong growth in Russia, another market where we've been investing, but this had been offset by softness in Western Europe. Mexico was posting solid growth but our overall sales in Latin America are being impacted by a slowing economy in Brazil. Furthermore, while there are nuances by market, brands like Hot Wheels, Fisher-Price Core and Thomas are doing well around the world.

Finally, we worked hard in the quarter to successfully clean up remaining retail inventory overhang in international markets, particularly Europe, and we are entering the holiday season relatively clean around the world which has enabled us to effectively activate all the great retail promotional programs you heard about earlier.

Before discussing the rest of the P&L, I want to briefly reiterate Richard's commentary on POS versus shipping trends. Excluding Disney Princess, global POS was up low single-digits in the quarter compared to declines in gross sales in constant currency which presents an opportunity to improve shipping through better alignment.

We believe the combination of cleaner inventories, incremental in aisle displays to mitigate shelf space losses and better shelf productivity should help us narrow this gap especially for key brands like Barbie and Fisher-Price. As always, global Fisher-Price **[Correction: Mr. Farr was referring to global POS]** should be considered directional and reflects our internal figures which are based on wholesale sales and reflect more comprehensive coverage of our diverse product offerings and extensive global reach.

Looking beyond the top line to our other key P&L drivers. Our adjusted gross margin remains solid at 49.1% in the quarter, but down 170 basis points versus 50.8% in 2014, primarily due to the negative impact of foreign exchange which was about 200 basis points. As I said, we believe the impact to gross margin from ForEx should be less in the fourth quarter.

As it relates to other key drivers of gross margin in the quarter and year-to-date, our cost savings initiatives and our price increases more than offset changes in product related cost, higher royalties and mix. And finally, our overall basket of product related costs were roughly consistent with our forecast assumptions for the year as we exited peak production.

As planned, our advertising rate remained higher including additional spending in emerging markets. SG&A was down versus the prior year in absolute dollars on both a reported and adjusted basis. We continue to aggressively reduce overhead costs, coupled with synergies from our MEGA Brands acquisition and balanced with strategic investments in growth.

As it relates to our funding our future program, we delivered $45 million in overall gross savings in the quarter and $93 million year-to-date, putting us ahead of our run rate for 2015. As a result, we'll exceed our 2015 objectives of $125 million en route to delivering at the high end of the $250 million to $300 million range for the program by the end of 2016. For 2015, we now expect to deliver gross cost savings of $140 million to $145 million. We expect half of the 2015 gross savings will impact gross margin and the balance will reduce SG&A and advertising.

In the quarter, our adjusted operating profit was $322 million versus $435 million in the prior year, and currency was an $80 million headwind in the quarter. Adjusted EPS for the quarter was $0.71 and $0.63 per share year-to-date, compared to $0.98 and $1.06 respectively in 2014. Currency had a negative impact of $0.20 per share in the quarter and $0.23 per share year-to-date, explaining the majority of the year-over-year decline in the quarter and more than half of the decline year-to-date.

Turning to the balance sheet and cash flow. Consistent with our expectations, we ended the quarter about $290 million of cash in our balance sheet as we continue to invest in our business and tightly manage our seasonal working capital needs over the first nine months.

Our third quarter results also reflect our ongoing commitment to disciplined capital deployment. As we said, dividends remain our first priority after reinvesting in the business and the Board declared a fourth quarter dividend of $0.38 per share which is flat compared to the fourth quarter of 2014. Overall, we remain confident in our progress to date, as does the Board, and we have sufficient flexibility within our capital deployment framework to execute the turnaround in 2016. We're also committed to growing back into a reasonable dividend payout ratio and yield with our turnaround efforts.

Clarifying our 2015 outlook, based on our year-to-date financial results, we continue to believe the 2015 outlook that we provided in the first quarter of investor call remains achievable including stabilizing net sales for the full-year versus 2014 on a constant currency basis. Based on year-to-date trends and assuming current spot rates for the fourth quarter, foreign exchange is now expected to be a 5% to 7% headwind to revenues for the full-year versus our previous estimate of 4% to 6% impact. And the negative impact adjusted EPS is expected to be 32% to 37% **[Clarification: $0.32 to $0.37]** versus [$0.30 to $0.35] previously communicated. Based on current spot rates we expect ForEx translation headwinds to be about 6% for the fourth quarter which is slightly less than the negative year-to-date impact.

We also believe that fourth quarter revenues will be higher than the third quarter this holiday season. As Richard already said, as part of our turnaround efforts we have worked hard to improve our retail execution this holiday season. While the last two holiday seasons do not reflect this, we historically ship more in the fourth quarter than the third quarter.

With respect to other P&L metrics, we continue to target gross margins of about 50% for the year where we expect stronger gross margins in the fourth quarter, relative to the third quarter. Advertising at the high end of the 11% to 13% range and adjusted SG&A for full-year 2015 that will be down in absolute dollars compared to 2014 by $80 million to $95 million.

In closing, we recognize that risks remain and we'll continue to monitor the currency markets and macroeconomic outlook closely. But as you heard from both Chris and Richard, we see several clear catalysts to deliver solid performance in the fourth quarter. There's always puts and takes in the early stages of a turnaround but overall, we're pleased with our progress to date. In particular, we've been encouraged by our ability to improve POS for core brands through product and marketing and retail execution with increased shelf space productivity which gives us greater confidence about the levers under our control as we prepare to execute in the holiday season and beyond. With that, we'll now open the call for questions. Operator?

## QUESTION AND ANSWER

**Operator**

(Operator Instructions)

Our first question comes from the line of Sean McGowan with Oppenheimer & Company. Your line is now open.







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**Sean McGowan** - ***Oppenheimer & Co. - Analyst***

Thank you. Lot of information there. It's all very helpful. It's all very helpful. We appreciate the color.

I wanted to start with a question on how you guys describe -- as you guys describe closing the gap between POS and shipment. I assume at some point closing the gap means positive shipments, otherwise that would be a weird relationship. So do you think there's a possibility that at least Barbie and Fisher-Price could actually see increased shipments in local currencies in the fourth quarter?

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Sean, it's Chris. Let me take a stab at that. Actually, we are looking at the fourth quarter as probably when the inflection point starts to happen. Clearly, we've been chasing lost space which has been part of the gap creator. I think that was in Kevin's remarks.

Some of it was this direct import inventory shifts that also affected the quarter. As we start to move through the fourth quarter, we think both will start to mitigate, so I don't know if it will be completely in balance at that point but certainly we'd expect it to start to close the gap.

**Sean McGowan** - ***Oppenheimer & Co. - Analyst***

Okay. On that direct import shift, do you have a high degree of confidence that that business will be recaptured in the fourth quarter, that it's simply a question of timing?

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Yes, we do. Look, we go through this on a constant, regular basis, we keep testing it. So far, barring anything unforeseen happening on open orders or whatever, we think we've got a pretty good sight line on the fourth quarter and it does look like we'd be offsetting most of that.

**Sean McGowan** - ***Oppenheimer & Co. - Analyst***

Okay. And my other question, and I know you never like to comment on particular customers, but Walmart did sort of spook the world recently with their comments on expectations. What do you think that says about the pricing environment that you're facing this holiday season and is it more a case of them losing business to other retailers where Mattel could be picking up some of that business that Walmart appears to be concerned about losing? Thank you.

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Walmart's been an excellent performer for us this year and a very strong customer, Sean, so we're benefiting from their efforts to get more aggressive and particularly in some of our sectors. We expect that to continue in the fourth quarter. I think what they're trying to do in-store makes sense and obviously we're hoping to partner with them in doing it. So we're quite optimistic on what Walmart's doing at this point, at least from our business standpoint.

**Sean McGowan** - ***Oppenheimer & Co. - Analyst***

Okay. The last housekeeping question I have is when you say Disney Princess, are you including Frozen in that? I don't know if they've officially made that move yet.

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Yes, we are.

**Sean McGowan** - ***Oppenheimer & Co. - Analyst***

Okay. Just wanted to clarify that. Thank you very much.

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**Operator**

Our next question comes from the line of Stephanie Wissink with Piper Jaffray. Your line is now open.

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**Stephanie Wissink** *- Piper Jaffray & Co. - Analyst*

Thank you. Good afternoon everyone. I want to follow up on Sean's question regarding closing the gap between POS and shipment. I think Richard, you talked a little bit about the space losses and rising competition. Can you give any more detail on your ability to fully close that gap if you are facing some intense competition for that space?

And then secondly, just related to the A&P spend, it does remain elevated versus historic levels. How have your discussions been going around 2016 with your retail partners and what's the expectation to maintain that level of support? Thank you.

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

It's Richard. So Stephanie, we're pretty confident that obviously with the continued results of POS that shipping inevitably will follow. And just speaking in the context of clean inventories and good POS, we're looking pretty good at this point to close that gap. Statistically speaking we'll obviously deliver those results at the end of the year, but there's a lot of confidence that those numbers will come our way.

We are increasing our advertising in the fourth quarter. There's a variety of different promotional efforts along with new allocations in media, some increases in digital as well as some reallocations in terms of traditional TV advertising. Overall, I think we're confident in the context of our percentage that we're spending in advertising and we continue to invest significantly more in our core brands and key license partners.

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**Chris Sinclair** *- Mattel Inc - Chairman & CEO*

Do you want to touch on next year? I think she also asked that. I think your question was also, Steph, if I heard you right, do you expect us to continue next year in terms of heavy spending, is that fair?

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**Stephanie Wissink** *- Piper Jaffray & Co. - Analyst*

Yes, what's expected of you by some of your partners in terms of that elevated spending?

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**Chris Sinclair** *- Mattel Inc - Chairman & CEO*

I think we've been pretty clear that we're continuing to stay price competitive. You'll probably expect to see us promoting like we have been and our advertising rates I think we've flagged would be also in the same vicinity of where we are this year.

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**Kevin Farr** *- Mattel Inc - CFO*

I think as we plan 2016, we want to make sure that we're focused in on generating top line revenues and get the momentum continuing POS and aligning shipping. So at this point subject to review after the holidays, we're planning on keeping those elevated levels in 2016.

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**Stephanie Wissink** *- Piper Jaffray & Co. - Analyst*

Thanks, guys. Very helpful.

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Steph, the last point I would make on your question on space, remember that as we did the fall resets, that was another punch-through on space loss for us. So when you're talking about inventory and shipping adjusting, we should be stable on space now going through the fourth quarter and beyond. So logically it would start to come back in balance.

**Kevin Farr** - ***Mattel Inc - CFO***

One of the things that's going to help us to close that gap in POS versus shipping is also the space that we do have is more productive and that should drive more sales.

**Stephanie Wissink** - ***Piper Jaffray & Co. - Analyst***

Thanks, guys. Kevin, just one follow-up with respect to the loss of Disney and the replacement of that business potentially in part with the DC business. Is there any comparability we should think about in terms of the margin structure of the incoming and the outgoing businesses? Thank you guys.

**Kevin Farr** - ***Mattel Inc - CFO***

I think with regard to that, look, the Disney Princess business is a great business both from a top line and bottom line perspective. And as we look forward to 2016, we think we've closed, as Richard said, a significant amount of that gap. So that's from a revenue side.

I think from a margin side, we are confident as we continue to work on the cost side that we can deliver strong margins of 50%. And look, we've got a tailwind with respect to our cost savings initiatives and that we're going to be at the high end of the range of $250 million to $300 million. And as Chris said earlier, we also have a sight line beyond that that's well beyond that range. So I think all that together should help us offset Disney Princesses from a profit perspective too.

**Stephanie Wissink** - ***Piper Jaffray & Co. - Analyst***

Thanks, guys. Appreciate it.

**Operator**

Our next question comes from the line of Lee Giordano with Sterne Agee CRT. Your line is now open.

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Lee.

**Operator**

Your line may be muted.

**Lee Giordano** - ***Sterrne Agee CRT - Analyst***

Can you hear me?

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

We do now.

**Lee Giordano** - ***Sterrne Agee CRT - Analyst***

Sorry, guys. My question's on emerging markets. Just wondering your thoughts about the recent volatility we've seen in China and Russia? It sounds like you're doing pretty well overseas these days. Any changes to your plans? It sounds like you're doing well but just wondering long-term how you view those markets considering what we've seen lately? Thank you.

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Actually, Lee, I frankly just got back from China a couple weeks ago and had a pretty good review on that business. And I would tell you, while we've seen a little bit of impact at retail from some of this latest turmoil, we've got so many good things going there in terms of driving the brands, driving e-commerce, driving new distribution, that we haven't seen a beat missed in that market and continue to be very optimistic with the plans.

Russia, we went through a little bit of a wobble like everybody else did when things cratered earlier in the year and we thought we were going to see a fairly big pullback. If anything, that's actually showing a lot of strength recently. So we're kind of in a more forward leaning posture if you will. But we think the emerging market businesses for us are a huge upside in the coming months.

**Lee Giordano** - ***Sterrne Agee CRT - Analyst***

Great. Thank you.

**Operator**

Our next question comes from the line of Greg Badishkanian with Citi. Your line is now open.

**Greg Badishkanian** - ***Citigroup - Analyst***

Great. Thanks. So just if you think about losing Disney Princess in 2016, you have core growth of your brands. What's going to be the biggest driver do you think to bridge the gap?

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

Like I mentioned, we have a lot of great new volume and incremental volume coming from new partners. The Warner Bros. piece of our business is going to be significant. Obviously as I mentioned, we're looking forward to the new girls launch, rich IP value, great trend product, and a great activation program including content which will be pretty robust. In addition to that, as I mentioned, there's a multi-year, multi-theatrical lineup with Warner Bros. that we are partnered with them on.

In addition to that as well, with the current trajectory of our core brand revitalization as you can see, of interest, Barbie and Fisher-Price being the two largest, starting to deliver POS growth ultimately with the strength that we're building on 2016 should be another good, strong POS year. With the adjustments in cleaner inventory and adjusted space, we should start to see real give back in the context of filling that gap.

We're also really excited about some of the initiatives from the Toy Box. There's some great new items that we're obviously launching this fall with View-Master for one but there's a series of lineups that are going to be announced subsequently later on for Toy Fair we'll show and share with you. Some really powerful new properties and some great new products lined up for 2016.

All in all, I would say core brand, continued growth. Hot Wheels as you can see, I've mentioned it time and time again that is to some extent the sleeper in the portfolio, delivering great POS. And also MEGA, with a great platform for us in the Construction category and of course, Teenage Mutant Ninja Turtles which is the theatrical release will commence right there and that will be great new volume for us.

**Greg Badishkanian** - ***Citigroup - Analyst***

Great, makes a lot of sense. Then just in terms of Star Wars and your Hot Wheels business, little bit of color there? And then just if you could remind us, how much Star Wars business did you have during the last movie?

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

So the Star Wars -- first of all, I'm really excited to have a piece of the Star Wars business and in particular, I think what it does is it proves the extension possibilities that we have with Hot Wheels. To imagine a Star Wars vehicle integrating Star Wars into vehicle play was pretty extraordinary and the results of which we're really pleased with and encourages us to extend further partnerships using Hot Wheels as the leverage to do so. Star Wars is going to be a great business for us this year and we anticipate subsequent years to follow. And we'll share more with the results at the end of the year.

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**Greg Badishkanian** - ***Citigroup - Analyst***

All right. Thank you very much.

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**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Thanks, Greg.

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**Operator**

Our next question comes from the line of Taposh Bari with Goldman Sachs. Your line is now open.

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**Taposh Bari** - ***Goldman Sachs - Analyst***

Hey, guys. Good afternoon. A couple questions on net sales and constant currency. So you've given us a bunch of pieces, but can you tell us if that line should grow or decline in the fourth quarter?

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**Kevin Farr** - ***Mattel Inc - CFO***

I think what we said versus the third quarter, we expect the fourth quarter to be bigger.

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**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

So yes, it will grow.

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**Kevin Farr** - ***Mattel Inc - CFO***

Right.

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**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

In the fourth quarter.

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**Taposh Bari** - ***Goldman Sachs - Analyst***

How about year-over-year versus the fourth quarter of last year?

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

Well, we're sitting here deciding how much we can give you color on this. I'd say pretty close is probably a good answer.

**Taposh Bari** - ***Goldman Sachs - Analyst***

Okay. And then as we think about next year, you've given us a bunch of different pieces, including a lot of licenses and opportunities in the works. Is there a possibility that, again, constant currency net sales can increase next year or is that pretty unlikely in light of the hole that you face and the challenges that you're facing with Monster High?

**Chris Sinclair** - ***Mattel Inc - Chairman & CEO***

I'm not sure we want to get into quite that level of detail today, to be honest with you. But I think what we're trying to signal is we're working pretty hard at closing that gap and trying to keep stability at the top line and I think that's probably where we've been.

**Taposh Bari** - ***Goldman Sachs - Analyst***

Great. And the last one is just on input costs. Kevin, it seems like you called out input costs as a headwind to gross margins year-to-date. Clearly the outlook shows a different trajectory. So can you remind us I guess first how much of your COGS are comprised by resin and how we should think about kind of the magnitude of input cost relief going forward?

**Kevin Farr** - ***Mattel Inc - CFO***

Raw material costs with regard to resin are about 15% and the headwinds traditionally over the last few years have really been in direct labor which has been growing at a double-digit rate. But again, as we've talked about, we're trying to bend the cost curve here and as we look at a line of sight beyond our current range we're really trying to bend that -- continue to bend that cost curve in 2016.

**Taposh Bari** - ***Goldman Sachs - Analyst***

Great. And Richard, can I ask one more for you on DC superhero girls? I guess it's a new type of toy. It's not a doll. It's not an action figure. Where do you expect it to be sold in the toy aisle and what do you think it replaces?

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

Well, we positioned it as actually action figures for girls and arguably, one could debate whether action figures are dolls and dolls are action figures. But ultimately, there's some features, articulation, scale that basically positioning as well that we're driving to capture girls attentions in the action figure aisle.

We have a great amount of research and insight that suggest there are girls actually shopping in the action figure aisle. We hope that retailers acknowledge and put the brand and double expose the brand in a variety of different places. That will be obviously determined by retailers. But everybody collectively is pretty excited about the category and certainly, that we are providing in fact a play pattern for girls that's been missing with obviously iconic product, really driven by girls themselves. The insights and design application has been really hand in hand with girl insight.

**Taposh Bari** - ***Goldman Sachs - Analyst***

Great. Thank you. Best of luck this holiday.

**Martin Gilkes** - ***Mattel Inc - VP of IR***

Operator, I believe we have time for one last question.

**Operator**

Our last question comes from the line of Linda Bolton Weiser with B. Riley. Your line is now open.

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

Hi. Just on Monster High, I know you've talked about it a lot but can you just kind of explain once again why it is taking so long to get a turnaround strategy for that one? You've really made great progress on a lot of the other brands and this one just seems to be still problematic. Is it a matter of prioritizing versus the other brands or what? And then can you just remind us is Monster High similar in margin profitability to Barbie? Thanks.

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

Sure, Linda. Look, Monster High was a lightning rod, an unbelievable brand that frankly, proved Mattel's savviness in the context of marketing and content and digital. The reality of how the brand has progressed is it's going through a maturity curve that we likely, frankly accelerated by moving too quickly away from the core messaging, not necessarily investing enough in product innovation and frankly, exploited the characters a little too far without enough content to describe who these characters were.

Frankly, the insights and research and certainly the response that we get from our consumers in their relationship with the brand and the stories, continue to suggest that we have something pretty powerful. And we believe with the right management and investment we're going to find the sustainable foundation and then start to build upon it.

I think some of the work that the team has done is pretty outstanding in the context of the speed of which we brought new product, new scales to market. We've been doing some tests that we've gotten some great reactions on. We reestablished our creative messaging. I think for 2016, you'll see a whole variety of changes from product to packaging to content.

And I think examples like this partnership we're announcing with Lady Gaga, is pretty remarkable and I think that it validates the longevity of what Monster High could be. Clearly, we'd like the turnaround to be faster. But I as mentioned, I'm really excited about some of the work that's going to be coming out for 2016 and we anticipate the brand will stabilize and then ultimately we'll grow upon that stability.

**Chris Sinclair** *- Mattel Inc - Chairman & CEO*

Your second question on the profitability, the profitability is very similar to Barbie. It is a very profitable brand.

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

Great. Thanks a lot.

**Chris Sinclair** *- Mattel Inc - Chairman & CEO*

Okay, Linda.

**Martin Gilkes** *- Mattel Inc - VP of IR*

There will be a replay of this call available beginning at 8:00 PM Eastern time today. The number to call for the replay is 404-537-3406, and the pass code is 39720076. Thank you for participating in today's call.

**Operator**

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







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