Mattel, Inc. - Goldman Sachs 2024 Communacopia Conference Fireside Chat

Stephen Laszczyk: Thanks, everyone, for joining us this morning. I'd like to welcome Ynon Kreiz and Anthony DiSilvestro, the CEO and CFO of Mattel. Thank you for being back at the Communacopia & Technology Conference again this year. Very excited to have a conversation with you both.

Ynon Kreiz: Thank you for inviting us. It's great to be here, always.

Stephen Laszczyk: Absolutely. So, great. I wanted to start off high level, Ynon. Mattel's made some significant progress. On the many goals that you set out when you really started at the company six years ago as CEO, you've had success with content in the Barbie movie last year. You've taken significant costs in capex out of the P&L. The balance sheet is back to investment grade. Could you maybe start by talking about where Mattel is in the arc of its long-term strategy, and how your vision from here evolves and how it creates shareholder value?

Ynon Kreiz: Thank you. Yes, it has been a journey, where we've achieved significant progress across all aspects of the enterprise. We did take significant costs out of the business, as you mentioned, more than $1.3 billion dollars of cost savings. We reduced the workforce by about 35%, existed five factories and on our way to exit another one. Became much more capital light. And with that, significantly improved our results.

If you look at some of the key metrics of the company, we grew sales by over $0.5 billion. We improved gross margin by almost a thousand basis points. We improved our EPS from a negative $1.20 to a positive $1.23. Our cash, cash flow, went from a negative $325 million to more than $700 million last year.

And of course, in the process, we've lowered our leverage ratio from 25 times debt to EBITDA to about 2.4, and we're now investment grade, and already in the thick of share repurchase.

So financially, operationally, it's been a transformative period for the company, and in the process, of course, we strengthened our supply chain dramatically. It is now a competitive advantage. We continue to gain share. Last year, in fact, was the year where we had the highest share gain in our history in the US. And so you see the performance playing across not just the – how we operate, but seeing the results in the company's continued evolution and growth.

We are now entering, in some ways, a new chapter, post the Barbie movie, which was an important juncture in our strategy. When we set out to transform Mattel from a toy manufacturing company to an IP company that is managing franchises, the vision was to continue to grow our toy business and expand our entertainment offering and capture full value from our intellectual properties.

At the core, Mattel is an IP company, driven by innovation. And we believe that our brands can create significant value, both in toys as well as outside of the toy aisle. And we're very much on our way to achieve that. As I said, the Barbie movie's success was a juncture in terms of highlighting and encapsulating this strategy, and really reflecting the potential about brands and the strength of our IP that we're in success, monetizing our brands can create significant transformative value for shareholders. It's important to mention that it's not just about Barbie, and not just about movies. It's about capturing full value from our intellectual properties.

And the last point I would make is that the toy side of the company represents significant upside. You know, we're not looking to get out of the toy business – it's a great business when it works. It's highly cash generative. In success, it scales, and it's very profitable.

Our opportunity is to grow in addition to that, so continue to grow within the toy business, and then expand and start participating in other highly accretive business verticals that are driven by big brands. And in some cases, those verticals are bigger than the toy industry, and that's the opportunity that we see in front of us to capture value on top of what we do on the toy side of the company.

Stephen Laszczyk: Let's talk a little bit more about what you're seeing in the toy industry today. On your second quarter earnings, you spoke about some of the better-than-expected trends you saw in the first half of the year out of the industry. You raised your guidance for the full year for 2024, to be down only modestly. Could you maybe talk a little bit more about what's driving your optimistic outlook for the back half, where 70%-plus of industry revenue is still to come?

Ynon Kreiz: Sure. So, just a bit of perspective. The toy industry grew by 25% between 2019 and 2021. '21 was a record high for the industry. '22 was a flat year, another record number for the industry in spite of inventory issues that affected the broader economy, not just the toy industry, which really spoke to the resilience and strength of the toy category.

'23, we saw decline – again, off record high, and still – but still well above 2019 pre-pandemic. And we still expect a decline in 2024, although less than we thought at the start of the year.

The trends that impacted the industry in '23 was a shift of consumers from products and goods into experiences and services. We're seeing that, returning back to historical patterns. And we're seeing the toy industry performing well. It was comparable – the first half was comparable to last year. And we see demand coming back. We see people prioritize quality product, especially when it comes to trusted brands, quality trusted brands. And retailers are leaning in.

The toy industry has very strong fundamentals. The toy industry caters to a fundamental human behavior of play. Parents will always prioritize spending money on their children, especially when it comes to quality product and trusted brands. Retailers also lean into the category – it's a strategic vertical for them. It's experiential. It drives foot traffic, it brings people in, and it's very sticky. The items are affordable, especially when you have a relatively broad price range that caters for all types of demographics and income levels.

So as a whole, the toy industry is a good, resilient, growing industry, and we expect that it will continue to improve – we continue to see improving trends, and that the toy industry will return to growth and continue to grow over the long term.

Stephen Laszczyk: There's been a lot made about the consumer backdrop. Heading into the back half of the year, we've seen some macro unevenness. There's been a lot made of the timing of the election and the shorter holiday season. I'm curious, what are you hearing from your retail partners as we head into the holiday shipping season? And then, how should investors think, perhaps, about the pacing of revenue and PLS as we look for that to trend into the back half of the year?

Anthony DiSilvestro: Great. Steve, first, thanks for having us. Great to be here.

I think, starting at a macro level, we're seeing what most people are seeing, right? Continued economic growth, inflation subsiding, the increasing likelihood of interest rate declines in the near future on a macro level.

From a consumer perspective, we are seeing some improvement in consumer sentiment overall, and the consumer spending levels are fairly resilient, and our expectation is for a little bit of growth in consumer spending overall for the back half of the year.

But what we are seeing is some value seeking consumer behavior, particularly around lower income cohorts. So that's going on out there, and I know that retailers are adjusting their plans to accommodate for that.

This is where Mattel thrives. You know, well-known, trusted brands. We bring innovation to the market. We have high quality products at a value, and Ynon touched on the breadth of our portfolio, everything from a single diecast Hot Wheel to a Barbie Dreamhouse, so we can meet the demands of those various consumers, whatever they're shopping for.

As we do our own internal research, it suggests that more consumers are going to buy toys this holiday season than before, so that clearly bodes well for our outlook. And our outlook for the second half is for our toy business to grow as we move into the holiday season, and we have robust plans developed with our retail partners. We have more innovation coming. We have more advertising and promotion, and we have more and new content that will support that. So, we feel good about where we are, and our position heading into the back half.

Stephen Laszczyk: And I think maybe just to clarify, you mentioned that you feel better than before. Is that before, relative to last year, or perhaps before, relative to your expectations going into the middle part of this year?

Anthony DiSilvestro: Yes, so our expectations haven't changed. We can reiterate our guidance today in terms of full year and net sales to be comparable to last year in constant currency. But again, I think it's hard – we are confident in our outlook. The programming and demand creation we have in the marketplace to drive sales in the second half.

Stephen Laszczyk: That's great. Ynon, as you mentioned, some of the innovation that you have coming down the pipeline. Could you perhaps talk a little bit more about product and innovation going into this holiday season, and perhaps as you look across some of your brands, where do you think there's the most opportunity to innovate going forward?

Ynon Kreiz: Yes. We have done a lot of work to continue to strengthen our innovation and design capabilities in line with supply chain and commercial execution. As you know, we are organizing by six categories, three of which we are a global leader, and in three we are a challenger. If you look at our leader categories – Dolls, Vehicles and Infant Toddler Preschool, we have very strong drivers in each of them.

Within the Dolls categories, Barbie is launching two new segments and celebrating her 65th anniversary this year. And we have exciting innovation coming in and around the Barbie line.

Monster High is launching new content and collector – collect the dolls that look just incredibly exciting and strong.

American Girl is also in the midst of its turnaround, and we're seeing very good indications of performance. It's up for two consecutive quarters already, and some of the comparable same-store data are very positive, which is another good thing.

And we also have two new movies that are coming, joining our portfolio – Moana 2, and Wicked later this year. That will also amplify our offering in Adults category.

Vehicles is doing incredibly well. Hot Wheels is on track to achieve its seventh consecutive record year, with more innovation, extended product offering, new lines of business, more content on Netflix, and it just – on a very strong trajectory.

Infant Toddler Preschool is a category that has been declining for Mattel, but as you know, we recently announced our new strategy. Last quarter, Fisher-Price was up double digit, 11%. And we're seeing the turnaround starting to play. It's still early – we're not celebrating success just yet, but early indications are a positive.

The Wood line is doing very well, it's growing well. Little People is also expanding. And we continue to innovate with new product, while at the same time, we exit the loss-making, underperforming parts of the business, which offset within the category some of the performance. But Fisher-Price Core, which is the main part of the category, is growing and doing very well. And we expect that we continue to play going forward.

Within the challenger categories, we've also been doing much work on innovation, and the one to highlight is Uno, which is an incredibly strong brand, doing really well. We continue to offer new product. Uno is the number one card game in the industry, the number one game as well, and we are very excited to see that progress.

So, across the portfolio, we remain very committed to innovation, to creativity, and do it while we improve productivity. So this is not just about great product, but also designing product that is cost efficient, and continue to improve supply chain and drive more execution at the – on the commercial side.

Mattel sells product in about 500,000 stores globally. This is where our products are put on the shelf. And that relationship with all the major retailers around the world is a foundational strength for the company that we continue to build upon, and we believe will be another competitive advantage for us, in addition to strong design and innovation and a competitive supply chain at global scale that can help us achieve the best pricing for the best product.

Stephen Laszczyk: That's great. Maybe just zooming in on two of your power brands a little bit more – Barbie and Hot Wheels. Barbie just came off this historic year with the movie. What are your plans to build momentum off of the success last year, and return that brand back to growth in 2025 and beyond? And similarly, on Hot Wheels, we've sort of seen this historic run over the last five, six years in the Hot Wheels brand. What keeps that going? And then, there's – with the upcoming – any updates on when we could expect timing and then storyline around that?

Ynon Kreiz: Yes, the strength of Barbie and Hot Wheels is a story in and of itself. The Barbie movie was a showcase, a focal point of what the brand can do and can achieve. But as I said, it goes much beyond the movie.

Those two brands are cultural. They have societal relevance. And maybe represent in the best way our playbook, where we bring together brand purpose, consumer-centric innovation, cultural relevance, and franchise mindset.

We believe that both brands are still at the early stage of how far they can go in terms of becoming form factors. And both are so much more than toys. Barbie's not a toy. Barbie is a pop culture icon. And Hot Wheels in itself is a whole domain, representing Vehicles, or wheels, if you want to call it that way.

And we're seeing how both brands continue to expand product offering, reach more demographics, especially attracting adult demos and collectors. We sell Barbies that in

some cases, retailing for $500 for collectors. And Hot Wheels range from $1.10 all the way to collector items that are hard to get, and you have to wait in line for a presale, an online presale.

And so we're seeing brands that – those two brands resonate in culture, and have important societal value.

There is the success of the Barbie movie – it was unique because it – we were not even targeting the Toy demo. It was really looking to excite and delight and attract adults and men and people that normally would not have consumed the Barbie doll in its old incarnation. But today, both brands are complete domains, and we believe it can play out, not just in toys and not just in movies, but also in television, theme parks, digital games, consumer product merchandise, and different experiences.

There is also, as you know, as it relates to Hot Wheels, a movie that we are working on with J.J. Abrams at Warner Bros. to create the Hot Wheels movie, and we could not be more excited about that potential. And when it comes to Barbie, without commenting on a sequel, and because I know it's a question out there, just more broadly, we've always said that our goal is to create film franchises, where – that play over time and across multiple executions. Again, I'm not talking specifically about Barbie, but the opportunity for us is to do – to build franchises across our entire portfolio.

Stephen Laszczyk: That's great. You mentioned this a little bit earlier, but the film side's picking up quite nicely for you. Over the next six months, you have two Disney Princess films, and Moana and Snow White, the film release of Wicked. Ynon, could you maybe talk a little bit more high level about the path and trajectory of your partner IP strategy, where it stands today, and any thoughts on where you'd like to take that over the next three to five years? And then, Anthony, just since it's been a little while since we've seen a normalized box office, could you perhaps remind investors what they should expect out of a release of like Moana or a Snow White, the financial impact it could potentially have on your business?

Ynon Kreiz: Sure. I'll start by saying that we have done a lot of work to position Mattel as a partner of choice for the major entertainment company, where we partner and collaborate with important global brands. In other words, the way we see it, if you are an owner of a big, important brand, we would like to offer you the best capabilities in terms of design and development, supply chain, and commercial execution, at a global scale.

And given our capacity and how today the company is designed with a flexible model that can operate at scale, we believe we can achieve the best results for our partners. We've been very selective who we'll work with, but when we collaborate and partner with major IP owners, we treat their brands as if – is our own. And of course, we bring in domain experience in Dolls, in Vehicles, in Infant Toddler Preschool, Action Figures, Games, and Building Sets.

In those capabilities, we have the best – some of the best people in the industry, that run those categories, can apply their capabilities and expertise and our scale into partners' product and execute at the best level. So we see that as another growth driver for Mattel. There's no tradeoff. It's not – it doesn't cannibalize our own execution, but it allows us to manage our portfolio at scale, where a rising tide lifts our boats, and we can develop a very effective strategy to grow our partner brands. And that's – you're going to see more of that playing out, in addition to growing our own product, based on our own IP, rather. Product based on our own IP.

Anthony DiSilvestro: From a financial perspective, we don't disclose the actual individual numbers, but it is fair to say that a successful toyetic film has a significant impact on our financial results, whether it's a Disney film, whether it's something like Toy Story or Jurassic World.

Jurassic World is a great example, and I think highlights Mattel's capabilities in terms of design and development. So when we do the movie year, I think where we really excel is post-movie year, we can turn an event into an evergreen property. So Jurassic World in our product line is synonymous with dinosaur play, so not only do we capture the movie year, we capture the post-movie years as well.

Stephen Laszczyk: That's helpful. Ynon, one of your goals has been leveraging your IP to create content of your [inaudible] with Barbie last year, you've spoken a lot about working with studios across various of your IP properties to create a more regular cadence of content. Could you maybe update us on the progress you made there, the entertainment strategy as a whole, and what investors could expect at the pace of content production, to be like out of Mattel over the next couple of years?

Ynon Kreiz: Mattel is the owner of one of the strongest portfolios for children and family entertainment franchises in the world. And when you look around at the broader media and entertainment landscape, it's all about big brands that move the market. Not just major acquisitions, but every investment, every important move is driven by big IP, big brands, big franchises. This is what the game is about. And as the owner of so many strong, iconic societal heritage brands, we have a very unique opportunity to participate in large verticals, including content, but not just.

When we say content, this is film and television, and what we are seeing is that our brands are in demand. We attract and collaborate with some of the most prolific creators of our generation on the movie side, and also on the television side. And the reason it matters is because a strong brand gives you a very strong jump point – jumping off point to start the journey.

No matter who you are, if you are the best creator in the world, if you start a new project from scratch, it's hard. It's hard to get the awareness, hard to get the attention, it's more expensive, more competitive. It's harder.

When you start the journey with a built-in fan base, where people are engaged, excited and aware of what you do, you have a much better shot. And in our mind, an asymmetric opportunity for Mattel, given the strength of our brands.

And again, going back to the Barbie showcase, in a very competitive industry, in a particularly tough time for the industry, what you saw is a movie that became a cultural phenomenon. It was much more than a movie. It was a cultural phenomenon. And we believe a big part of it is the brand. Of course, the movie was great, and we could not be more proud of how the movie – what the movie created and how it came about, and of course, the talent that was attached to the movie. But if you take the same movie, or the same script, the same cast, the same budget, the same marketing, but it's after a doll named Susie and not Barbie, might probably not have been the same result.

Of course, it has to be still a great movie and a great cast and a great director and creator to achieve the success, but the foundation of the journey is a strong brand. And by the way, without the brand, you couldn't have attracted probably the best talent out there, because they would not have been excited to do something unless it's based on a strong brand that has cultural resonance.

So we believe that strong brands are not the only way to achieve success, but an important accelerator and dramatically increase the likelihood of success, which is why

we're able to attract incredible creators that are excited and also proud to collaborate with us based on brands that they look up to, that they admire, that they've been following and engaging with since they were children, and partner with people who then interpret the brands and create the running execution of which we are supporting, and continue to put out the great content.

Now, our goal with Mattel Films is to collaborate with leading filmmakers to create standout quality movies based on our iconic brands that will resonate in culture and appeal to global audiences. And the operative word here is to partner with leading creators. We are looking to attract and create the biggest playground for them, to imagine and interpret our brands. And then, we look to amplify and support and empower them, to achieve the best they can.

And it is very much about a creative collaboration, creative partnership, where the mandate is to create quality content that people want to watch. And the theme of what we're looking to create in terms of the Mattel cinematic universe is brand purpose and cultural relevance. And while you might not see the same characters in a play within different movies, the common theme – the DNA of what we're looking to put out is about brand purpose and cultural relevance.

You saw that in the Barbie movie, and you will see that in every one of our executions and our productions and content going forward.

Stephen Laszczyk: Great. Let's talk about another form of content, which is digital gaming. Mattel's leaned a lot more into digital gaming over the last year with its partnership with NetEase. Can you talk a little more about your ambitions in the digital gaming industry, and what you believe the right business model looks like for Mattel at the moment, whether it's licensing or self-publishing model that you think works best for you at this moment?

Ynon Kreiz: We have a very good balance and mix of different commercial models that we are deploying. We have a traditional licensing model where we get a royalty, based on our own – again, based on our IP. We have Mattel163, where we are a co-owner, the 50/50 JV with NetEase that is doing extremely well, already at more than $200 million revenue at very, very high profit margin.

And drawing from that experience, where we see how our brands play, the success of just three games, we were able – you know, with the JV was able to generate so much success. We're not looking to enter the self-publishing side of the business. And what is interesting is that we've seen, over the last few years, the mobile gaming side of the industry, on one level, became more competitive and very advanced with a lot of games being put out there. But at the same time, costs – development costs coming down, and importance of brands going up. The brands are much more important today than ever, especially given the amount of product that is being put out there.

So as the owner of some of the most iconic brands in the industry, we believe we have an asymmetric opportunity in terms of risk/reward, to enter the – to do our own self-publishing. And you're looking at a relatively capital-light investment into developing mobile games, where you can stage-gate the investment – in other words, you don't put the entire budget, and only at the end you see the result, but you can actually test and fine-tune the product along the way, so you can actually moderate the investment.

And the marketing and user acquisition is all performance-based, where you get the result on the impact of your marketing activity in real time. And that is also tied to success. In other words, unlike the movie business, where you spend – you could spend $100 million, $200 million movie until the product is finished, and put all the marketing up

front and then see the result of the opening weekend. Here you can actually stage-gate the – both the investment in the development of the product, as well as in marketing.

And given the importance of big brands, we believe that we have a real opportunity with multiple [inaudible] goal, low capital risk to have several experiences that in success, can have a very asymmetric return for Mattel in an industry that is driven and so dependent on big IP. And so, we've been gearing up to execute on that strategy, and we'll have more to share in the coming weeks and months.

Stephen Laszczyk: That's great. I want to pivot quickly and touch on margins. Anthony, you're targeting gross margins of 48.5% to 49% for this year, which is about 100 to 150 basis points – better than what you achieved last year on essentially flat revenue. Could you talk a little bit more about the puts and takes, the margin story this year, and then maybe longer term, how you're thinking about the sources of operating leverage in the model?

Anthony DiSilvestro: Sure, Stephen. As you said, we're guiding to 48.5% to 49%, so nice improvement versus the prior year. And there are a few puts and takes. First, the positive side is cost savings. You know, as Ynon touched on, we have a long track record of successfully identifying and delivering against cost savings programs. In the beginning of this year, we announced the new $200 million program by 2026, and we're off to a good start. So that's on the positive side.

Also on the positive side is improved fixed cost absorption. What I mean by that, in the prior year, we had to curtail our production levels to address some – our own inventory situation. And we brought our own inventory down by over $300 million last year – over 3%. And that was one of the contributors to the $700 million-plus free cash flow. This year, we resumed normal production levels, so year on year, we have a nice benefit.

We also have lower costs around what we call inventory management costs. These are closeout sales and obsolescence this year compared to last year, where we were also dealing with some of the inventory situations.

Now going the other way is the Barbie movie wrap. As you know, we generated over $150 million of revenue from the movie, the movie-related toy sales, and consumer products with a 60% operating margin. So we're wrapping that this year. Most of that wrap is going to occur in the third quarter.

So those are the puts and takes. We're off to a really good start. In the first half, our gross margin on an adjusted basis is up 600 basis points, so we're seeing cost savings come through. We have a full year target of $60 million. We did $37 million in the first half, so we're on track to achieve or exceed our $60 million target against the program.

Looking longer term, we continue to see opportunities to expand our gross margin coming from several drivers. First is continuing our cost savings efforts. As I said, this is – this idea of cost saving and productivity and efficiency is part of our DNA, and it will continue to be going forward.

The second is scale, and we've talked about growing both our top and bottom line in 2025. And we have a scalable platform. As we put more through it, there's an opportunity to expand margin.

And the third is the benefit from our entertainment strategy. These verticals, whether it's consumer products or digital gaming or films, all have significantly higher margins, and that will be a really nice mixed business in the portfolio.

So good progress this year, line of sight to continue to expand our margin going forward.

Stephen Laszczyk: That's great. And maybe with a minute or so remaining, just to touch on capital allocation. You mention the stock repurchase – the last two quarters, $100 million. Ynon, in the past, you've said M&A has been a priority of yours, using the balance sheet as a lever of growth, perhaps, in that fashion. Could you maybe just talk a little bit more about what that M&A pipeline looks like today, if you've seen anything that perhaps fits your strategy? And if not, what we would need to see to – to maybe see share repurchases ramp back, ramp up further.

Ynon Kreiz: Yes, we have four priorities in our capital allocation strategy. Organic growth is the first and foremost. Then we're looking to maintain our leverage ratio and investment grade rating. Then we talk about M&A and share repurchase.

Now, this is dynamic, and of course, we continue to look and evaluate opportunities and where we stand in the market and what opportunities are out there. The fact is that share repurchase has taken priority over M&A. We haven't seen anything out there that we believe would be accretive and that we should acquire. And what you have seen is that over the last 12 months, we've been – we acquired $400 million of shares, $200 million in the first two quarters of this year.

We still have $800 million remaining on our current authorization, and given what the share price is today, we did say that we expect to continue to do share repurchase, because we believe the stock today is very undervalued.

Now, it – we have to continue to look and evaluate market conditions, of course, relative to what the share is trading at the given point, what opportunities are out there. But the key message is that we are being very strategic, very thoughtful, very disciplined in how we evaluate opportunities, including M&A. We're very cognizant about – of the risk, and the challenges of doing the wrong acquisitions, as well as the opportunities when you do the right acquisition. But as of now, the priority has been share repurchases, given where the share is trading today relative to where we believe the company – how the company is doing today, but more importantly, the future potential of Mattel and the opportunity for us to create long-term shareholder value.

Stephen Laszczyk: That's great. We'll have to leave it there. Ynon, Anthony, thank you so much for taking the time today.

Anthony DiSilvestro: Thank you.

Ynon Kreiz: Thank you – thank you.