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PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to the Mattel, Inc. Fourth Quarter 2017 Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded. I would now like to introduce your host for today's call, Whitney Steininger. Ms. Steininger, you may begin.

Whitney Steininger

Thank you, operator, and good afternoon, everyone. Joining me today are Margo Georgiadis, Mattel's Chief Executive Officer; and Joe Euteneuer, Mattel's Chief Financial Officer.

As you know, this afternoon we reported Mattel's 2017 fourth quarter financial results. We will begin today's call with Margo and Joe providing commentary on our results, and then we will provide extended time for Margo and Joe to take your questions. To help guide our discussion today, we have provided you with a slide presentation. Our discussion and our slide presentation will reference non-GAAP financial measures such as gross sales; adjusted net sales; adjusted gross profit and adjusted gross margin; adjusted other selling and administrative expenses; adjusted operating income or loss; adjusted earnings or loss per share, from which we exclude the impact of a net $457 million noncash charge related to the establishment of a valuation allowance on U.S. deferred tax assets and an estimate of the impact of U.S. tax reform; earnings before interest, depreciation and amortization, or EBITDA; adjusted EBITDA; and constant currency. Our earnings release also includes non-GAAP financial measures. The information required by Regulation G regarding non-GAAP financial measures is included in our earnings release and slide presentation, and both documents are available in the Investors section of our corporate website, corporate.mattel.com.

Before we begin, I'd like to remind you that certain statements made during the call may include forward-looking statements 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 forward-looking statements. We describe some of these uncertainties in the Risk Factors section of our 2016 Annual Report on Form 10-K, our 2017 Quarterly Report on Form 10-Q, our earnings release and the slide presentation accompanying this call, in 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.

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

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

Good afternoon, everyone, and thanks for joining our fourth quarter 2017 earnings call.

Our fourth quarter performance reflects a tough quarter as part of what was a difficult and extraordinary year for Mattel. This year, we faced multiple significant dislocations driven by retail inventory levels, planning misalignments, mixed brand performance and the TRU bankruptcy. Collectively, these contributed to significant top and bottom-line pressures.

Importantly, we used this year to proactively take action to turn around this business and reset our economic model for the future. The results in the quarter reflect a series of decisions to enter 2018 with as clean a slate as possible. We are optimistic the business is on course to stabilize revenue in 2018, and with the benefit of our significant cost reduction program, we expect to improve profit trends in 2018 and to demonstrate momentum towards the medium-term goals we shared at our June Investor Day.

On today's call, I will take you through an overview of our topline performance in the fourth quarter, related drivers and the progress we continue to make in our strategic transformation. We expect a series of green shoots in 2018 that will demonstrate progress against our plan and highlight the value creation potential of our strategy. We will lay out key milestones during today's call, and we'll expand further during our Toy Fair presentation so you can track our progress through the year.

Joe will provide further detail on our fourth quarter financial performance and provide an update on our structural simplification efforts, ongoing strategic investments and our broader capital strategy. Richard will not be joining the call today because he is in Nuremberg at the European toy fair. After Joe, we will open up the call for Q&A.

Let's turn to our top line performance. Our gross sales declined 8% in the fourth quarter and 9% for the year, which was consistent with the most recent outlook we provided in December.

North America gross sales were down 14% for the quarter and continued to reflect challenges associated with tighter retail inventory management, the Toys "R" Us bankruptcy and underperforming brands that we have discussed previously. Internationally, gross sales were up 4% for the quarter, with the strongest performance in LatAm, led by Cars 3, Fisher-Price Core, up 16%, and Barbie, up 14%.

The strongest brands globally in the quarter were Barbie, Cars 3 and Hot Wheels. And we continued to be pleased with the launch of Enchantimals.

Fisher-Price performance in the quarter was stressed, particularly in North America by Toys "R" Us and underperformance of key items versus last year. American Girl remains challenged as we continue the turnaround program. I will address the key momentum drivers for each Power Brand in a moment.

As we have shared throughout 2017, rightsizing retail inventory levels has remained a critical priority. In Q4, we continued our proactive actions to hold the line in shipping and aggressively manage inventory at retail, particularly in the U.S. and Europe. We believe that we have ended the year with retail inventory for our key Power Brands down over 20% across these markets. In the fourth quarter, we saw POS more aligned with shipping for most of our brands and expect to see further alignment going forward with few exceptions. This alignment gives us confidence in setting and achieving our goals in 2018.

A quick note about industry trends. I'm sure you have seen Q4 showed deceleration, although the industry finished up for the full year per NPD data. Franchise brands that deliver immersive and connective experiences and trend-based brands continued to take share as well as companies that are addressing the significant growth differences across international regions. These industry growth drivers fit squarely into our strategy and reinforce our optimism as we reset our business for the future.

Moving on to margins. As expected, we had issues all the way down the P&L in the fourth quarter and full year. We also executed a number of write-downs as part of our action plan to address underperforming areas and to reset profitability. In particular, these items had a significant impact on gross margin, which we would not expect to recur at the same levels in 2018. We do expect smaller charges in 2018 related to ongoing SKU optimization. Joe will walk you through each of these in more detail.

As we look at the full year effect of unwinding the dislocations in our business, the impact on our profitability is significant, and we expect to turn a new page in 2018.

As I shared earlier, our Power Brand performance was mixed, with Barbie and Hot Wheels showing continued momentum. I'll now provide a quick update on each major brand.

Barbie's worldwide gross sales for the fourth quarter were 9% and POS was up similarly in the high single digits. This is the third year in a row this brand has delivered mid- to high single-digit POS growth, demonstrating what our power franchises can achieve with systematic development of 360 physical and digital systems of play. Shipments and POS were in alignment, with strong sell-through at retail in all markets, including strong double-digit wholesale POS in Europe, APAC and Latin America. Barbie remains the world's undisputed leader in dolls, and its continued momentum is allowing us to gain additional market share in dolls and fashion categories, again, per NPD. Barbie had strong momentum heading into 2018 as we continued to lean into empowerment and careers with exciting new 360 systems of play expansions and experiences anchored by compelling content partnerships across short-form television series and documentaries. We are excited to tell you more at Toy Fair.

Hot Wheels Q4 POS grew mid-single digits globally, with gross sales down slightly as we carefully managed retail inventories which are now down over 25% versus last year. This good result reflects our commitment to expanding systems of play. The brand achieved double-digit POS growth in Q4 in both LatAm and Europe and mid-single-digit growth in Asia. The strength of the Hot Wheels brand franchise has allowed it to continue to gain market share even as we work to make Cars 3 a success, per NPD.

In addition, as exemplified by double-digit sales growth of Track Builder sets, we are successfully building beyond the core diecast car line and capturing share of incremental categories, which is part of our systems of play strategy. We believe our success in Construction can be a significant contributor to future growth of the brand.

2018 will be an exciting year for Hot Wheels as we celebrate the 50th anniversary of this iconic brand. We have bold plans for product and marketing to inspire both kids and collectors, including re-releases of original treasured diecast cars and exciting new connected line for younger kids and a next-generation augmented reality offering that fully immerses kids in the Hot Wheels racing experience. We'll share a larger preview of what's coming at Toy Fair.

Turning to Fisher-Price Core, worldwide fourth quarter sales were down 9% and POS was down high single digits. Overall, our fall 2017 product line did not perform as well as our 2016 lineup. In North America, our largest market for Fisher-Price, these issues were exacerbated by the TRU bankruptcy and some online retail issues where competitor price discounting and shipping costs became an obstacle for reordering late in the season on some top items. Where we are fully executing our new strategy across brand, retail and parent engagement, Fisher-Price performed well in 2017, particularly in China and Latin America. China continues to be the leader in our parent engagement program, anchored on our innovative partnership with Babytree, the leading website and app for new moms in China. Over 1 million moms have engaged in our content since our fall launch, and every day thousands are taking our assessment tool, which anchors our customized 24-month age and stage program tailored to the learning and development needs of each child. We look forward to rolling these programs out to additional countries.

We have also brought in a new leader for Fisher-Price, Chuck Scothon, who we are excited to welcome back to the company after a few years away. He is a highly respected, purpose-driven leader and a proven product and marketing innovator who has a track record in driving success at

Fisher-Price. He is deeply passionate about child development and accelerating our ability to help every parent across the world provide their child the Best Possible Start and unlocking the power in Fisher-Price's unrivaled seven decades of learning and development expertise.

As we have discussed in prior quarters, American Girl and Thomas remained under pressure this year. Regarding American Girl, this brand remains one of the most beloved and iconic doll franchises, which we are dedicated to reenergizing. American Girl's a premium experiential brand that needs to be cultivated with the right 360 experiences, premium product and content support. The consumer excitement behind our New York store opening and the very positive reception of overseas partnerships, for example, Dubai, reinforce the true potential of this brand. Our Q4 results showed that we are still deeply in turnaround, with the mass distribution strategy previously put in place not performing and the need to address certain stores that are not meeting our location and brand experience expectation. We are accelerating aggressive plans to refresh this franchise in 2018 with both investment and talent enhancement to revitalize this brand's premium appeal and improve the offline and online experience. We plan to provide more detail in AG's action plan on the Q1 call.

In the case of Thomas, we are excited to reinvigorate this brand in 2018 with new content and expanded retail distribution. The all-new Season 22 of Thomas & Friends takes Thomas on global adventures outside of Sodor for the very first time and introduces exciting new girl characters to expand our already strong broad gender appeal. This new content will launch on many of the #1 kids' preschool networks across global markets, making it available in more than 100 countries worldwide. In Thomas' biggest market, the U.S., we announced last week a major new content and brand activation partnership with Nickelodeon starting in March, which will anchor the transformation of this franchise.

The Toy Box remained under pressure into Q4 as the games from Cars 3, Enchantimals and other properties were overwhelmed by declines in certain underperforming brands, including Monster High, Ever After High and MEGA.

As expected, Cars 3 came within range of our revenue target for the year, led by strength in international markets where the franchise exceeded our expectation. We continue to deepen our close partnership with Disney and believe we will see solid performance into 2018 for Cars 3, particularly across international markets.

Our biggest new own-brand launch this year, Enchantimals, also performed well, especially in Europe where we delivered the broadest retail and content activation program. We will continue to grow this property into 2018.

Looking forward, we continue to focus on the transformation of Toy Box into a more stable and profitable innovation portfolio. We believe that we will complete Toy Box optimization during 2018, focusing on 3 main opportunities.

First, we will continue to invest in our top entertainment partners, including Disney, Warner Bros., Universal, Nickelodeon and WWE. We are bringing them the best of our creativity, 360 play systems capabilities and strong global commercial execution to unlock fan passion for their brand. In 2018, we are excited about year 2 of the Cars 3 franchise, the launch of our Jurassic World line and Sunny Day. We're also leaning into Turning Mecard, which is a breakout franchise in Australia and Korea that we are expanding to multiple markets this year.

Second, we have one of our best ever lineups of own-brand launches, which we will share in depth at Toy Fair. To share a few highlights, Enchantimals is a continued growth opportunity, and we are excited to relaunch Polly Pocket this year, the original surprise brand. We've been testing the brand in Latin America and have taken these learnings to redevelop the product line and content to enable a successful multi-market expansion. We also have a major new UNO-related product launch.

Third, we are committed to retaking our leadership as a top toy innovator in a world where trend-based items are increasingly important in today's digital age. The hallmark of Mattel is connecting deep consumer insight and creative ingenuity. We've created a small dedicated team of expert toy leaders to unleash a much faster, leaner and more nimble business model for hot products. We unveiled the exciting work of this team privately at Hong Kong Toy Fair, and you'll be hearing more about the new products from this group at New York Toy Fair.

Turning to our strategic transformation and the year ahead. We have completed the process of resetting our leadership team and organization, which is a critical underpinning to regaining momentum. We now have regional leaders with consistent responsibility, accountability and operating structures. In addition, the global brand team is now fully focused on creating global brand strategies that allow for the specific developmental needs of individual markets. Our new incentive structure is better aligned with our overall objectives, including a more balanced approach to sales, margins, working capital and EBITDA.

In 2018, we are focusing on stabilizing revenue, enhancing profitability, with staged investments in our growth pillars. We expect improving trends and green shoots to start emerging throughout the year. I'll walk through milestones you can expect as part of our progress.

The cornerstone of our strategy is our 3 key Power Brands: Barbie, Hot Wheels and Fisher-Price. We expect growth across these three Power Brands, driven by more consistent execution across markets and growing our play systems into new areas. Each of these brands has strong brand presence, strong consumer demand and opportunities for differentiation across markets, so the #1 job for us now is high-quality execution to support their continued growth. We also expect to see POS and shipments more closely aligned for our top brands across markets.

We also are committed to our innovation pipeline in The Toy Box, with a focus first on remixing this portfolio to improve revenue sustainability and profitability. Beginning in Q1, we will break out The Toy Box separately from our Power Brands so that you can track how we are progressing across our entertainment partnerships and owned brands. In 2018, our focus is on leaning in to our top entertainment partners, top owned brands and trend-based products, which will be offset by pruning elsewhere. We also will share updates on how top launches such as Jurassic, Sunny Day and Polly Pocket are performing.

We are making fast progress on structural simplification, which is a cornerstone to restoring profitability. We are happy to announce that we expect to achieve a greater proportion of the $650 million savings in calendar year 2018 than originally anticipated. We are also happy to announce a significant reduction of our CapEx spending. Each of these will provide significant lift to margins and cash flow as we move forward. Joe will provide more detail on both shortly.

In addition, we are investing to create the runway for longer-term growth with staged investments against our 5-pillar growth strategy, which we announced at June Investor Day. These investments and milestones should provide you with further confidence that we are on track to delivering the medium-term growth and profitability targets we have shared.

Key milestones you can expect to see in 2018 include breakthrough content partnerships to unlock the value of our IP with a slate of short-form TV series and theatrical content against our top brand franchises. Our new Thomas content and Nickelodeon announcement is the start of this new momentum. As discussed at our June Investor Day, this content strategy is designed to underpin the growth of our brands, unlock increased consumer products opportunities and allow us to better leverage our advertising and promotional spend over time.

On gaming, you recently saw our partnership with NetEase, a leading global gaming company, to create a series of mobile games based on our IP that will unlock meaningful monetization potential from world-class immersive experiences. The first major release, based on our UNO brand, will come out in April and a second will be released in the fall. To enhance our innovation pipeline and economics, you will see us announce more co-production deals. We are on track to unveil multiple co-pro deals with top partners, several of which you will be seeing at Toy Fair.

On connected play systems, we have defined a clear strategy to drive scalable and cost-effective, platform-based innovation led by our new CTO, Sven Gerjets, in partnership with our global brand leaders. In Q4, we made the top decision to clean up some of our connected products that did not meet our new strategy and to redirect or accelerate others. We are prioritizing opportunities in Fisher-Price, Hot Wheels and STEM.

For 2018, you will see us launch exciting connected products such as Hot Wheels AR that deepen our play experience for a digital age and offer extendibility. You also will see us take a careful and staged approach to developing more immersive and adaptive solutions to ensure the highest-quality experiences at accessible price points that our consumers expect from Mattel. You will see an announcement soon about how we are leveraging best-in-class partners with proven software and hardware development capabilities to accelerate progress and capture scale benefits.

In conclusion, while 2017 was a tough year, we took action to work through our main challenges and look forward to our fresh start in 2018. Our 5-pillar strategy remains the foundation for growth and profitability over the medium term. 2018 will be a very different year as we continue to make progress on our strategic transformation. Job one is to return Mattel to a high-performing toy company that delivers the returns you would expect from a toy market leader. In addition, we are making meaningful progress in unlocking the value of our IP and accelerating innovation to create further growth momentum.

We look forward to sharing more exciting updates with you at Toy Fair in a few weeks. And we greatly value your support as we implement our transformation plan to restore growth and profitability and deliver significantly enhanced shareholder returns over the medium term.

I'll now turn the call over to Joe.

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Thank you, Margo, and thank you to everyone for joining the call. While it was a challenging end to a challenging year, we've taken the opportunity to make the tough decisions in 2017 to set the foundation for continued progress on our transformation in 2018.

As mentioned previously, one of the overarching drivers causing dislocation this past year was business planning misalignment, beginning 2017 with a mid- to high-single digit growth expectation for the full year gross sales and ending the year with a high single-digit decline. The cost base of the organization was not able to fully adjust for this swing in the year which negatively impacted our profitability. You will hear in my review of our expense results, the impact this misalignment had on the company.

Since Margo has already addressed our top line performance, I'll start by walking you through the P&L, identifying key drivers and any potential headwinds or tailwinds that we expect to carry-over into 2018.

Starting with sales adjustment, the increase from 10.2% to 11.5% for the full year was primarily driven by the year-over-year sales decline in North America, which resulted in a higher weighting of international sales as a percentage of total sales. Since our international markets have higher sales adjustment rates than North America, our overall sales adjustment rate increased year-over-year due to this weighting. While we would like to reduce sales adjustments over the long term, we expect similar levels to continue in the near term as we continue to stabilize the top line.

Our reported gross margin was 30.7% in the fourth quarter and 37.3% in the full year, which included a $20.6 million asset impairment related to tooling write-offs in the quarter. Our adjusted gross margin decreased significantly from 47% to 32% for the quarter and for the full year, adjusted gross margin declined from 46.8% to 38.3%. The primary drivers of the Q4 and full year decline were actions related to our structural simplification cost-savings initiative, which included write-downs of excess owned inventory and impairment of assets. This made up approximately 40% of the decline for Q4 and 25% of the decline for the full year. We don't expect these costs to recur at these levels in 2018, if at all.

Both the higher sales targets and proliferation of SKUs and brands led to higher level of closeout sales and unfavorable product mix. This made up approximately 20% of the decline for Q4 and 30% of the decline for the full year. As we look to 2018, we will be remixing the business and managing our portfolio of brands and SKUs to improve profitability going forward.

The continued freight and logistics challenges, primarily driven by North America, made up approximately 15% of the decline for both Q4 and the full year. While we started implementing corrective actions in Q4 2017, these challenges may continue to have a negative impact in the first half of 2018.

And finally, increased sales adjustments, as I just previously mentioned, made up approximately 15% of the decline for Q4 and 5% of the decline for the full year.

As we noted in December, advertising was slightly higher in absolute dollars and more so as a percentage of net sales in the full year as sales continued to decline during the year. As part of our structural simplification, we expect to reduce our advertising spend in the coming year without jeopardizing our sales stabilization effort.

Fourth quarter adjusted SG&A was $387 million, up 13% compared to the prior year, driven primarily by an unfavorable year-over-year comparison due to a prior year reversal of incentive compensation as well as increased amortization, unfavorable foreign exchange and bad debt. Our full year adjusted SG&A of $1.4 billion was up 4% versus the prior year and was primarily driven by employee-related expenses, growth investments and bad debt. Full year bad debt as a percentage of net sales was less than 0.5% in both in 2017 and 2016.

In the fourth quarter, our income tax provision was $39.6 million, excluding the impact of U.S. tax reform. As I mentioned on our third quarter earnings call, we booked a onetime noncash charge of $561.9 million to record a valuation allowance for a significant portion of our deferred tax assets. To account for U.S. tax reform, an estimated noncash benefit of $105.3 million was recorded in Q4.

We anticipate finalizing and recording the full impact of tax reform including the liability for the mandatory repatriation tax within a year of its enactment. While we do not have an estimate of the mandatory repatriation tax to share today, the cash tax impact is not expected to be material to our annual cash flows because we will use foreign tax credit and significant deferred tax assets such as loss carryforwards and credits that we have on our balance sheet to offset the cash tax payment. The valuation allowance does not impact Mattel's ability to utilize these deferred tax assets under the applicable tax laws.

Overall, total tax expense for the full year was $548.8 million, inclusive of all noncash charges, current estimated impact from U.S. tax reform and the effects of our operations in 2017. Cash tax payments for 2017 were $117.7 million as compared to $113 million for 2016. Cash tax payments for 2018 should remain relatively constant before taking into account any incremental cash tax liabilities resulting from U.S. tax reform.

The Q4 decline of adjusted operating loss of $434 million, adjusted EBITDA of $418.5 million and adjusted earnings per share of $1.24 were primarily driven by the decline in gross sales and the proactive actions we took in the quarter to set the foundation for our continued turnaround in 2018.

Moving to the balance sheet. We ended the year with a cash balance of $1.1 billion, which reflected the $1 billion of debt issuance, part of which we used to repay all outstanding short-term borrowings as we transitioned to a new capital structure.

In 2017, working capital improved slightly year-over-year in absolute dollars. Key components of working capital included accounts receivable, which was flat year-over-year, with days sales outstanding up primarily as a result of the higher sales in markets with longer payment terms. Our owned inventory balance was $601 million, down slightly versus $614 million in 2016. We increased our obsolescence expense by $96 million this year primarily due to excess owned inventory caused by our Q4 sales decline as well as the discontinuation of certain product lines to simplify our business going forward. As we manage down our excess owned inventory, this may result in gross margin pressure in the first half of the year.

Accounts payable and accrued liabilities were $71 million or 5% higher than 2016. We continue to tightly manage the timing and terms of our payables. As we go through our business transformation, we will continue to emphasize tight management of working capital.

Capital expenditures were $297 million in 2017, reflecting costs associated with our flagship American Girl store in New York and continued investment in automation in our core manufacturing plant. We expect to reduce our CapEx spend by approximately 1/3 in 2018.

We took proactive measures to update our capital structure in Q4, as we said we would on our Q3 call, by replacing Mattel's unsecured revolving credit facility with an asset-based lending facility, which is secured primarily by Mattel's accounts receivable and inventory. In addition, we raised $1 billion of debt to cover the repayment of $250 million in debt coming due in March 2018, along with fortifying our balance sheet.

Looking to 2018, we have engaged in a more comprehensive planning process to ensure clear accountability and alignment on revenue expectations. Additionally, our business leaders have embraced the zero-based budgeting approach to our expenses. Our structural simplification cost savings program is in full force. And we're revising our employee compensation incentive structure to ensure the organization is executing towards a strategy that balances top line, gross margin, EBITDA, working capital and free cash flow.

As we discussed in December, we are working toward revenue stabilization and profit improvement in the year ahead and we'll talk to you more about our expectations for 2018 at Toy Fair in a few weeks.

Last quarter, we announced a structural simplification cost savings program with a plan to eliminate at least $650 million in net cost over the next two years with 1/3 of the savings expected to be achieved in 2018 and the remaining 2/3 exiting 2019. We told you we were going to take action and we did.

We are now on track to exceed our original cost savings expectations for 2018 of 1/3 and are working toward achieving closer to 40% of the total savings beginning with the actions taken in Q4, which included delayering the organization, which eliminated approximately $50 million of run rate payroll exiting 2017; SKU reduction initiatives, which resulted in $20.6 million of tooling write-off; and deploying comprehensive zero-based budgeting to all spend as part of our 2018 budgeting process.

As we entered 2018, we've begun work on the following: pursuing action plans pertaining to indirect procurement to consolidate our vendor base with a focus on reducing the number of small vendors and actions to renegotiate large areas of spend and developing dedicated initiatives to reduce expenses related to product packaging. We continue to expect 2018 cost savings to be achieved primarily through process simplification and the optimization of SG&A, cost of goods sold and advertising while the larger, more structural changes, like our manufacturing footprint and investments in IT, will drive most of the remaining savings in 2019.

Over the next two years, we expect about half of the cost savings to come from cost of goods sold by simplifying the product offering and linking production to demand as well as streamlining our global manufacturing processes. About 45% will come from overhead by streamlining our reporting structure through headcount reduction and reducing the cost of outside services. And 5% will come from the optimizing/right-sizing of our advertising spend.

We remain committed to our strategic investments and are confident that when implemented in conjunction with our structural simplification cost savings program, will lead to improved revenue and profit growth.

As we mentioned on our Q3 earnings call, we expected to spend approximately $30 million on our strategic investments in 2017. The investments made during the year were focused on our China strategic partnerships with Alibaba and Babytree, IT transformation, 360-degree play systems, Hot Wheels connected products and the key external hires we highlighted on the Q3 earnings call.

As we look ahead, our long-term investment plans and areas of business focus have not changed. We still intend to invest $170 million, about half expected to be spent in 2018 and half in 2019, the overall breakdown between operating expense and capital expenditures being approximately 80% to 20%.

Investment areas of focus for 2018 include the execution of our IT transformation, co-production partnerships, China and other emerging markets, connected products, and content to support our brand.

In 2018, we will work toward revenue stabilization, unlocking profitability through structural simplification cost reductions and targeting investments to accelerate our future. We have highly prioritized initiatives against each of our strategic pillars and have an organization in place that is ready and willing to execute against them to transform our business.

Finally, as a management team, we will continue to hold ourselves accountable for the commitments we make to you and can assure you we are taking the necessary steps now to create long-term shareholder value. I look forward to continuing the conversation at Toy Fair in a few weeks.

Thank you. And we'll now open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from the line of Gerrick Johnson with BMO Capital Markets.

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

Two questions. One, if you could just discuss the inventory management efforts a little bit and more granularly I guess, specifically what you're writing down there? And also how did the retailer shift to just-in-time fulfillment affect you guys in the quarter? Did you miss out on sales? Did you build too much and have too much inventory? Did you just get it right? How did that work for you guys?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

I think on the -- on your second question, I think, look, we ended up at the spot where we wanted to on retail inventory. We were down about 20% and that was sort of our target. I think we feel very good about where we are there. When you think about the write-downs and stuff you're talking about, think about that we were going through all of our inventory by SKU. And when you clean out your inventory, some of it, you're using in closeouts. Some of it you're declaring obsolete because you think you're going to be able to sell it at below cost, and so it's a little bit of an accounting issue. But needless to say, we think we cleared the ranks so that we're starting 2018 with the right inventory that we believe is going to help us have a very successful 2018 and, most importantly, focusing on a philosophy of having the demand come and then being able to supply.

Operator

And our next question comes from the line of Linda Bolton-Weiser with D.A. Davidson.

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

I was wondering if you could explain a little bit more about the lower CapEx spending in 2018 that you're projecting? Because I believe your earlier comments were that some investment is needed in the business. So I'm just wondering, should we be worried that you're going to hinder your turnaround because you can't make those investments upfront? And also I think you talked about the investment level and the breakdown between CapEx and income statement. And so will there be some of that strategic investment in the CapEx? And so are you reducing the CapEx net of that investment? And so can you just explain the whole investment side?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Sure, sure. Let me break it out for you. So we're trying to treat capital and the investment buckets separate for you so that we can provide clear transparency on what we're doing. So on the investment side, we said we were going to spend $170 million. We were going to spend it 50-50 in the two years, '18 and '19. So that's -- we did that for you. And from a breakout, we think of the 50-50, 80% would be focused on OpEx and 20% CapEx. So we'll be able to track that for you separately and tell you how we're doing in that regard. In regards to CapEx, we view that as more as the historical stuff that we've done. And remember, this year, we don't have the American Girl store that we built in New York, and we haven't quoted exactly the capital number that we're going to do. But we're just getting back to normal levels of where we're spending and clearly setting ourselves up for the future to finish automation. And part of the reason we're able to do this is we're starting off on a zero-based budget approach, so that we're actually challenging every dollar that we're going to spend, are we going to get the right return and how is it contributing to the overall development of the company going forward? So we will track both separately for you. We'll provide you more color at Toy Fair because we're not through the process yet. But we look forward to seeing you at Toy Fair. And in regards to the capital, I did say that we were going to be down approximately 1/3. So just ballpark numbers, if you said that we were at $300 million and you took 1/3, that's about $100 million. So give or take, $200 million, more or less.

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

So we don't see it as, to answer your other question, Linda, we do not see -- feeling constrained at all in investing in our go-forward strategy, that the ability for us just to right-size our existing CapEx gives us plenty of room to make a meaningful difference there as well as to invest for the future.

Operator

And our next question comes from the line of Michael Ng with Goldman Sachs.

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

I was wondering if you could help parse out the impact of Toys "R" Us in the quarter? And what's your expectation in terms of the impact from the upcoming store closures to Fisher-Price in 2018? And then I have a quick follow-up.

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Sure. So remember, the first impact really happened in the third quarter when we recorded the $43 million reversal of revenue because of the timing of the bankruptcy. What you see in the fourth quarter is just, as you've heard about their performance, it's down from where they thought it would be. And I think they -- from our perspective, we sort of anticipated sort of that in what we were thinking. So we are very cautiously optimistic about where they're going. We're going to continue to work with them. And -- but we haven't cited anything specifically.

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

(inaudible) Are you expecting the store closures to have a meaningful impact to Fisher-Price in '18? Or do you think those distribution points can be absorbed by other retailers?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

(inaudible) We're taking a cautious approach to it to ensure that we're being conservative in our outlook. So that that's baked into the guidance that we'll give you at Toy Fair. And I think just to kind of give you some milepost, if you look at 2017 as a whole, it was a really challenging year for us. Obviously, we ended the year with a 9% sales decline. And so I think the way -- if you want to kind of do mental math, you think about we were only able to recognize our growth in Cars and Enchantimals for the year. And then we had offsetting that, about 50% of the challenge and you think about that sales decline was driven by the retail inventory challenge that we've been talking about in some of the nonrecurring brands. TRU was about 30% to 40% of the growth challenge in the year. And the Power Brand issues like Thomas and AG, which we talked a lot about that, that are in turnaround, were about 20%. So if you -- if we were able, as we now are, just to have the POS takeaway and our shipments in alignment, the year would've looked very different. And so as we think about going forward, we have more time to prepare for the TRU shifts, and we will also have our shipping and POS takeaway in alignment. So that's how I would think about the modeling.

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

Great, that's very helpful. And just a quick housekeeping question. When you talk about revenue stabilization in 2018, what does that mean exactly? Is that flat revenue growth year-on-year? Or is that a revenue decline better than what we saw in 2017?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes. We'll give you the specifics once we get to Toy Fair. We'll give you the whole line out of 2018.

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

And as I said before, stabilizing means in range of flat. And we'll come back with specifics. That's our goal.

Operator

And our next question comes from the line of Arpine Kocharyan with UBS.

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

I was wondering, how much of the SKU rationalization that hits revenue is actually behind Mattel? You had said before that you trimmed around 20% of 2018 launches for this year. And what is going on with Toy Box? It seems like there was a leadership change there recently. Just if you could break down sort of each of those headwinds you expect on top line for this year? And then I have a quick follow-up.

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

For '18?

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

For 2018.

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

(inaudible) For 2018. So as we've talked about -- as we look into 2018, we'll see reduced pressures from the Highs, MEGA and those fragmented launches as you just said. So that clearly was a significant headwind for us this year. In addition, with the inventory issues now behind us, I was just sharing in the previous discussion, now down 20%, more than 20% in several brands. We will then ship what we sell in our cornerstone brands: Barbie, Hot Wheels and Fisher-Price. And that's extremely important to getting ourselves back on track. I mean, just think about it. For Barbie, we were double-digit POS growth for the year. But we were negative 2 in shipments in '17. So it's a very material dislocation in a very important brand. And then we also have had a far stronger portfolio of owned brand and partner launches coming in to the franchise this year, and you'll see a lot more about that in Toy Fair, and I articulated several of those in my previous remarks. I won't repeat that again. So that's how you think about it.

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

Okay, that's very helpful. And then a question for Joe. Could you perhaps talk about the cash situation this year and how much flexibility there is if demand for -- in terms of top line, it doesn't hold up as anticipated? And if Toys "R" Us impact globally is a little bit more than a couple of percentage points on full year basis. How much room there is for Mattel to navigate if it could be another surprisingly tough back half of 2018 in terms of like cash need?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes -- no, we are very confident in our liquidity position going forward in 2018. That was the whole purpose of redoing the capital structure. The $1 billion gives us the initial $250 million to take care of the March maturity and also putting in the asset-backed loan will give us great flexibly going forward. So we feel very, very confident. Even though there's a lot of some potential headwinds that we can manage through the year.

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

That's helpful. And then for a second, going back to the inventory number. I found that number pretty interesting. Margo, you mentioned inventory's down north of 20% at retail. And that's in general a good thing because it sort of allows you to ship in future periods. But if the retailer has adjusted these expectations and now that's a new base whereby it doesn't necessarily mean you could more -- you could ship more in the future, what does that really imply for sort of that underlying base shipment growth for 2018? Because you're absolutely right that there's this huge gap between -- even if it's a wholesale POS but sort of huge gap between wholesale POS and the way you're actually shipping. How do those actually align?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

They're very important in the sense that, this year, we had consumer takeaway. But then we were not realizing the benefits of the incremental shipping because we needed to readjust the inventory levels. So next year, we'll have the positive POS, and we'll have the positive shipping to go with it. And so what you saw in Q4, and Barbie I think was the easiest and best example of that where you had POS and shipping in alignment across all markets. And we made the top decisions to ensure that we were in all markets aligned across our top brands. So therefore going into next year, the POS and the shipping trends will align. So those -- that can all flow together. So when you think about the fact that more than half of our decline this year in revenue was driven by the fact that we had to right-size the retail inventory as well as some of those nonrecurring brands, that will have a very material impact next year. So we can continue to optimize The Toy Box portfolio. So you'll see, as I said, the milestone, as you'll see our key Power Brands as a group growing with positive POS and shipping in alignment and that enables us to remix and improve the profitability of our Toy Box so we have a stable and more profitable base of business on which we can grow going forward. So that's what gives us confidence going in to 2018 to give you targets and hit them.

Operator

And our next question comes from the line of Tim Conder with Wells Fargo Securities.

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

A couple here. Margo, just to clarify, the decline that you mentioned was 20% each for American Girl and Thomas that you referred to earlier?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

No, I was...

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

Or 20% collective?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

I was explaining -- as you try to think about -- since Michael was asking about what happened to sales and how do you think about the sales decline we experienced this year, I was explaining the proportions of what were the drivers behind sales decline to give you the confidence to understand that this was an extraordinary year. But our future performance will not be reflective of what's happened in 2017. So as I explained, the only incremental growth driver this year were really Cars and Enchantimals due to that dislocation between POS and shipments. So when you look at that negative 9% sales decline, think about half of that or a little more coming from the retail inventory reset and some of the nonrecurring brands. But we do not expect that to recur next year. 30% to 40% of it from TRU. We now have advanced understanding of what's happening in their store base versus coming in October so we can plan ahead and ensure that we're having a conservative and thoughtful approach to how we're managing through that in partnership with Toys "R" Us. And then 20% of the decline came from some of those challenges in our Power Brands, American Girl and Thomas. As we announced, Thomas will have new content that's been refreshed. We'll have stronger retail distribution, so we expect that brand to stabilize. And AG is the one brand that we are still in aggressive turnaround plans, and we'll share that with you at the end of Q1.

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

Okay. Okay, thank you. Thank you. And then on the fulfillment issues. How you -- what's your comfort with those being rectified here now as we move forward? Joe, I think you alluded to there could still be some. But by the time we get to the critical back half of the year, how do you feel about that? And then manufacturing. You cited that, that'll benefit still, and that narrative hasn't changed, will benefit more of 2019. But can we get a little bit more color on what your expectations are with that footprint? Any additional color you can give us there?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

Let me take the logistics piece, and then he'll follow up on the manufacturing side. We have a very bold plan that we'll continue to reveal to you. On the logistics side, the issue was not a fulfillment issue as much as it was. We had a cost issue. So we had a third-party contractor that we've made -- [got] a contract on in the fourth quarter of 2016. And that initiative just didn't grow as well as was originally planned. So we now have a focused effort. So it's really a cost overrun for case movement on the shipping. So the reason we feel confident that we can remedy that is that we've now taken back control of that facility, and we are well on track to moving that in the right direction. So we do feel good about the progress that we're making. In addition, as you know, we've been rightsizing retail inventories through the second and third quarter as we recognize the need to want to be much tighter in partnership with our retailers around ensuring them that POS and shipments are in alignment. We now feel that we're in a very good position with our retailers there, so that, going forward, we'll have that cadence far more optimized than we did clearly in this year. So do you want to...?

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

Do you...

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

Sorry.

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

Do you feel that the distribution center on the West -- on the East Coast, excuse me, cost you sales in Q4 as a result of all the logistics issues?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

There's no question that we were not at optimal performance, so we do see that as an opportunity for us.

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

And in regards to the manufacturing -- let me just (inaudible) question in regards to the manufacturing facilities. We've been spending more time on it. We are very, very optimistic about what we have to do. We have to get with the local governments, et cetera, but our plan is very, very aggressive, and we feel very, very good and look forward to giving you the details in the coming months. But we are -- I'm a lot more confident now than when we first started talking about it just because we're into the details and things are accelerating at a great speed for us. So I'm pretty happy about our progress.

Operator

Your next question come from the line of Felicia Hendrix with Barclays.

Felicia Rae Kantor Hendrix - *Barclays PLC, Research Division - MD and Senior Equity Research Analyst*

Can you -- Margo, can you talk a little bit more about the announcement you made recently between Thomas and Nick Jr., just maybe how that benefits you and just some more details there. And then I know you have plans for improvement in American Girl, and you're going to give us more detail in the first quarter, but do you expect that growth to be positive in 2018 or less negative? And finally, I'm wondering if you could just share some thoughts on MEGA. The acquisition really hasn't been additive to the company since it was made. So what are you thinking about that?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

Sure. Let me start -- get all these in turn. On -- let me take American Girl first. On American Girl, this is one of the -- as you know, one of the most beloved and premium brands. What really drove dislocation in American Girl in the fourth quarter was that we had real challenges in the mass distribution strategy that was launched last year. We just were not able to comp that. And as we really moved that franchise to refocus on its premium routes, truly premium experiences, products and a 360 experience which has been the hallmark of that product line since it was originally launched and successful, and I think I've shared that I personally worked on that brand back in the early 2000s, and it's right on trend with what people are looking for today. Amazing, parent-child, grandparent-child, family experiences that are premium and create lifelong memories. So we just need to get back to that root. So I think the best way to think about putting that into your model is the less negative. But what we want to do is the right decision so that we can put the premium back in that franchise and really invest behind it, and that's what you'll be hearing more about in terms of investment, talent, et cetera. At the end of Q1, we just wanted (inaudible) we thought we would just lay out the whole plan for that so you would have that to hand. In the case of Thomas and Nick, we're really excited. The U.S. is the biggest market for Thomas. And while we have some distribution for our content, we weren't getting as much reach through that distribution to as many of the people that love this franchise as we really wanted to. We've also created new content. Thomas is going off of Sodor. He's going to travel the world. He's -- they have great girl characters, which will appeal to the -- broad gender appeal of this iconic brand. And our partnership with Nick we're really excited about is not just content activation on their channel, which is the best kid platform, it also includes a consumer-products activation program so that we can really continue to enhance and surround our fans with a 360 product experience which is world-class. So we -- very excited about working with the Nickelodeon team to expand that franchise. And they obviously are a fantastic partner in doing that. We also have distribution in over 100 markets for existing and new content, and we've received rave reviews about the quality of the content and the excitement behind it. So we feel really good about this being able to reenergize Thomas, which is such a wonderful, wonderful franchise for us. In terms of...

Felicia Rae Kantor Hendrix - *Barclays PLC, Research Division - MD and Senior Equity Research Analyst*

In terms of MEGA, (inaudible) can you talk about the consumer products activation? Just mechanically, how does work between Nick and Mattel?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

We really don't get into those details. But it certainly enables us to take the best of both of our companies and have a very bold and aggressive program that takes the best of both to accelerate that development. So for us, as we shared at the Investor Day, Thomas is one of our iconic brands in terms of its ability to really generate a very strong consumer products franchise. And so this just enables us to continue to extend that best-in-class performance.

Felicia Rae Kantor Hendrix - *Barclays PLC, Research Division - MD and Senior Equity Research Analyst*

Okay. Sorry for interrupting.

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

No that's okay. On MEGA, (inaudible) I wasn't here for the acquisition of the company. It's a wonderful brand that's very powerful in the preschool space. And in that business, I think we've really made some good decisions this year in terms of how to ensure that some of those iconic products like the bag of Bloks, and there's some wonderful all-in-one pull toys that did exceptionally well. We're also very pleased with the performance of our partnership with Pokémon. We have had in some of the other areas that we've shared in previous calls some challenges. There were a lot of new licenses that were developed, and some were really successful like Pokémon, and some were much less successful. And so as we reflect on what's the role of that brand within our franchise, we see a very important role for that franchise in the infant preschool space. The product is fabulous. Kids really love it. And then we're integrating it very successfully and have very strong sales. At American Girl, if you go into the store, you'll find really great construction sets there, and online, they sell really well. It's integrated into our Hot Wheels experience as well as Barbie as part of our construction -- literally, a construction Barbie, which actually gets to build things and do different developmental activities related to it. So we're very excited about that as a brand in its home base and integrated within our other products. And then I think we need to be very selective as we think about expanding into the license arena to make sure that we truly have break-through products as we did in the case of Pokémon, which really just became beloved by fans. And I think that we just need to hold that high bar on inspiration and creativity.

Felicia Rae Kantor Hendrix - *Barclays PLC, Research Division - MD and Senior Equity Research Analyst*

Thanks. And Joe, I know you gave us a number of things to think about on cost and you'll probably have more details at the Investor Day, but our gross margin for 2018, is there going to be a 4 in front of that number or a 3?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

No. Look, we ultimately want to get to where we used to operate, right, so this'll be the first step, and yes, we should be close to the 4s or in the 4s yet.

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

Well in the 4s. We'll give more updates...

Felicia Rae Kantor Hendrix - *Barclays PLC, Research Division - MD and Senior Equity Research Analyst*

Well into the 4s, okay. And then last one, just Joe, so understanding again the spending, can you just give some color on kind of the investing you're doing on systems like your European inventory management, which tend to run significant kind of -- I don't know how you spread it, OpEx or CapEx dollars.

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes. So there's a split between OpEx and CapEx. But yes, we are working on our ERP system and just really trying to get some consolidation of our systems. Sven is doing a marvelous job of doing that. It's not something that's going to happen overnight. But more importantly, it's really about getting everything in the cloud so that we can have easy access to some of this information that is very hard to get to. So we have a very balanced approach to it. I feel very, very good that we're spending at the right levels, and we'll see the results here in the coming months as we go forward.

Operator

Our next question comes from the line of Susan Anderson with B. Riley FBR.

Susan Kay Anderson - *B. Riley FBR, Inc., Research Division - Analyst*

On the $650 million in savings, 1/3 in '18, how should we think about that flowing through? Is it going to be back half weighted or first half? And then just to clarify, did you say some of it came through in fourth quarter?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes. So in the fourth quarter, we recorded just over $40 million of severance which is going to give us a run-rate reduction in payroll going forward of about $50 million. And so when you think about these numbers, the 1/3 and the 2/3, the goal is to get everything out on a run-rate basis as you're exiting the year. And we've gotten started, and I think you're exactly right. Everything will be a little more back-end loaded. But we are seeing some progress made to where we've moved that 1/3 up almost 40% after this year, so for '18. So we will see how it all comes out. But we're going to try to get it out sooner rather than later, and that's why we did the severance here in the fourth quarter to get things moving. We also shut down our Venezuela facility and start looking at facilities that can be shut down.

Susan Kay Anderson - *B. Riley FBR, Inc., Research Division - Analyst*

Great. That's helpful. And then just really quick, a follow-up on Toys "R" Us and inventory. So it sounds like you feel good about inventory at retail. I'm assuming -- does that encompass kind of your view of the Toys "R" Us store closures and how you're going to kind of end out from that and where the inventory is going to go?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes, we feel very good.

Operator

Our next question comes from the line of Greg Badishkanian with Citi.

Fred Wightman

This is actually Fred Wightman on for Greg. If you look at the NPD estimates for the year, I mean, U.S. up around 1%, which is a bit of a step down from the mid-single digit rate that we've seen for the past few years. I mean, I know there's some one-off issues with Toys "R" Us, but what are you guys assuming in the industry growth in the U.S. moving forward?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

So we're optimistic for the industry. The fourth quarter results load, there was clearly less momentum from entertainment properties than we've had in the past. At the same time, we are seeing strong growth in the areas that we're very focused on, which is franchised brands that offer immersive experience. And obviously, you asked about the U.S. But the emerging markets continue to deliver very strong growth. And obviously, trend-based products where we have put in place our new team to really ensure that we're participating in that excitement. So in my view, the plays that are focusing on those things are doing well.

Fred Wightman

Okay, great. And then I think the language you guys used for Cars 3 was that it came in within range of your target. How should we be thinking about the ability to lap that as we head into '18?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

We don't typically give specific guidance. But we do feel good about the property. It was a great partnership with Disney. The product is terrific. And we did come within range of our target, particularly with the strength in international organization. So we're expecting a solid year too, and we'll provide more updates at Toy Fair.

Operator

And our next question come from the line of Steph Wissink with Jefferies.

Stephanie Marie Schiller Wissink - *Jefferies LLC, Research Division - Equity Analyst*

I just want to focus in on the dolls portfolio if we could. I think Barbie looks quite strong. The Other Girls came in a bit below where we would have expected and I think in combination still down kind of mid-single digits in the fourth quarter. So as you look to 2018 and even beyond that, how should we think about the share transfer from Monster High to Barbie? How much more is there for Monster High to donate? And how much of a factor was that in Barbie's growth this year?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

So as I shared earlier, we will have reduced pressure from the Highs, MEGA and the other fragmented launches going into next year. We feel really good about Enchantimals and its performance as well as Barbie. Barbie is a very different franchise. We don't see that as really necessarily taking share from Monster High. That brand's positioned very differently from Barbie. Barbie is about empowerment, career and imaginary play. So it -- we don't view those as really overlapping properties. Just like we don't view Enchantimals as competing with Barbie either.

Stephanie Marie Schiller Wissink - *Jefferies LLC, Research Division - Equity Analyst*

Okay, that's helpful. And then I think what you talked mostly about is your core focus brands. I think you've classified in the past it's about 70% of the revenue. How should we think about the other 30% of the business? What kind of actions are you taking there to maybe streamline some of the portfolio? And how should we think about the capital deployment towards the noncore assets over the next couple of years?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

So Stephanie, the way I -- and we're going to actually change our reporting in Q1 because we think it will be very helpful and more transparent for you. We will be having our Power Brands -- Barbie, Hot Wheels, Fisher-Price, Thomas and American Girl -- reported as the Power Brands. And then we will have The Toy Box separate with entertainment, partner brands and our owned brands so that you'll be able to see those in a much more transparent way, and then we can talk about them as things (inaudible) and you can track them over time. We believe that's important as we move into this strategy. As we think about our investments in the company, we're just as passionate about our Toy Box brands as we are our core brands, and we believe that the investments that we're making in 360 play systems and experiences are equally applicable to both our Power Brands and how we bring the entertainment brands of our franchise partners to life and how we can improve our ability to launch and scale our own brands. So if you think about brands such as Enchantimals, especially in Europe, we had a really full 360 experience with kids and the brand was extremely successful. We had a breakout hit there, and we'll be taking that best practice and expanding it to other markets and so -- the whole concept of how we approach it. As we think about our business, obviously in the near term, our focus in '18 is to really demonstrate consistent growth in our three Power Brands as I shared. That's a critical milestone for us that, that package of brands is growing and that we have POS and our shipping aligned. As we think about The Toy Box, we are focused on remixing that to be a more stable and profitable growth of properties, both within our entertainment partnerships where we think about, not just the A1 licenses that we're really committed to, but also as we think about innovative new co-production arrangements which will have a much more attractive profit profile. As we think about our own brands, obviously, we're focusing on the areas that we know that we have distinctive capabilities and also are very accretive to our franchise as we think about our expertise in dolls and girls properties, our expertise in gaming and games where we've been very successful, which is one of the reasons we're investing in an expansion of our UNO product that you'll see at Toy Fair. So expect to see us continue to lay that out for you. But we're looking at innovation in both. And then 2018 is all about stabilizing revenue, restoring the profitability through structural simplification and portfolio optimization and then have staged investments in our growth -- our 5 pillar growth strategy where we will demonstrate the seeds of opportunity systematically against those so that you can understand that we will have the engine room for growth going forward and profit improvement that you should expect from a market leader.

Stephanie Marie Schiller Wissink - *Jefferies LLC, Research Division - Equity Analyst*

Thanks, Margo. Just a really quick one, Joe, on the tax. There's a lot of information you provided around the tax act. But could you just clarify your comments on the deemed repatriation and some of the potential negative impacts. I just want to make sure we understand how to think about tax rate.

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes, the simple way to think about it for us is that the new tax act is neutral. And then on the repatriation that we will inevitably have will be sort of immaterial. And the real benefit we're getting out of the tax act is really the flexibility on the international cash management.

Operator

Your next question comes from the line of Drew Crum with Stifel.

Andrew E. Crum - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP*

So wondering if you could quantify what e-commerce was as a percentage of gross sales and discuss how it performed during the quarter and if you're seeing any change in the economics with those partners?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

We don't break out e-commerce as a separate channel within our partners. We just break out our top partner. And the share of e-commerce varies significantly across the world. So in Asia, it's half. You got to U.K., that would be sort of the second, about 30-plus percent, maybe 35% this year. And the U.S. is around 23%, 24%. Depending on the category, it varies significantly differently by category. So bigger-ticket items like BabyGear tends to have maybe even up to 40%, 50% penetration. So it's a little bit hard to just give a broad average. We're very committed to being successful online and growing at a proportional share in that business, and that's a very important focus area. One of the reasons that we optimize our organization to really have our brand leaders focus on our global brand footprint and how we develop our brands and marketing and our product line was so that they could specifically ensure that the way we think about our development is very thoughtful and responsive to the needs of that online channel. As things are more and more transparent to the consumer, we have to make sure we provide meaningful merchandise differentiation and consumer excitement in these different channels based on the kind of customers that are going to those sites. We also have to think a lot about our economics of the cube. So what are the shipping costs for our items, and so we have to think about that end-to-end optimization and how that differs by market. And then that enables our commercial leaders now that they're fully focused on the brand activation and having a dedicated management structure to each of our retailers omnichannel or online only. We feel that we have a really strong execution set up now that's consistent across all of our markets. Now clearly -- in China, that's your beachhead of your business so that becomes everyone's business.

Whereas, in Latin America, for example, where online is just a very small penetration, it's a very different focus. It's much more of a marketing focus. Is that helpful?

Andrew E. Crum - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP*

Yes -- no. Appreciate the color. Separately, Margo, could you comment on the outlook for Fisher-Price in China this year? You announced a couple of initiatives last year with Alibaba and Babytree. Are those going to be material to numbers in 2018?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

We continue to feel very good about our Fisher-Price franchise in China. It's the preeminent learning and development brand for parents in the market. And the actions that we've taken with Babytree and Alibaba to create a truly distinctive parenting platform are continuing to enable us to differentiate. We also announced the development of learning and play centers, which we'll launch in 2018 in partnership with Fosun. And so we're very excited to continue that expansion and the differentiation of that franchise in China. We did continue to grow in Fisher-Price some double digit in China and to take share. And we will continue to invest to build that business in the market.

Andrew E. Crum - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP*

Okay. And then just one last question for me and kind of a follow-up to Steph's question, maybe asked differently. On licenses, there's some larger entertainment properties that come up for renewal in the next couple years. Just curious philosophically how you're thinking -- or what the company's appetite is for pursuing these and also your ability to do so given the state of your balance sheet and cash flow?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

So we feel very good about our ability for the A1 licenses to be an exceptionally strong competitor, particularly where they're in our wheelhouse, which obviously is around dolls and action figures. But we're very strong in those markets, and we truly believe we can bring distinctive experience in insights, design, manufacturing and commercial execution that are truly second to none. I think it doesn't take much to compare some of the products that have been taken over and created by others next to our products to understand the enormous difference in quality that we can deliver at the same price point at a very attractive margin. So we feel very strong about our ability to bring not just best-in-class design and insight but also to leverage our capabilities in other areas to ensure that we can provide a differential value proposition.

Operator

Your next question come from the line of Eric Handler with MKM Partners.

Eric Owen Handler - *MKM Partners LLC, Research Division - MD, Sector Head, & Senior Analyst*

Actually 2 questions for Joe. Joe, I wonder if you could sort of give us what the base EBIT is in terms of what you're guiding from for $650 million of cost savings? And then secondly, what are you thinking at this point your interest expense for the year looks like?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

So interest expense will be up on a year-over-year basis just because we put in place the $1 billion at 6.75%, and then during the year, remember, we're going to lose $250 million that's at a much lower interest rate. So interest expense will clearly be up. Look, we talked about at least in December and when I first got here on the third quarter phone call about our aspirations at turning the company around in two years and getting back to the levels of margins and stuff that we've seen historically. It's not all going to get done in one fell swoop. So it's going to take a 2-step process. '18 is that sort of reestablishing process. So when you hear things like being flat on the top line and trying to become self-sustainable, that's sort of the initial goal. And then once you can get that under control, you can sort of grow from there. But that is taking into account the added new interest expense. It's taking into account the fact that we think we have a good capital program. But it also takes into account that we're going to continue to invest concurrently with the turnaround so that we can build future revenue streams and profitability for the company going forward.

Eric Owen Handler - *MKM Partners LLC, Research Division - MD, Sector Head, & Senior Analyst*

Okay. And then one for Margo. Margo, I'm curious that you talked for a while that the company, for a long time, it's had a revenue issue. And with all the changes that have occurred at the company, do you feel like there's enough creative talent to facilitate that turnaround?

Mary Margaret Hastings Georgiadis - *Mattel, Inc. - CEO & Director*

So I definitely do. What inspired me from the first day was the people that I met. Their incredible passion and insight into kids and decades of proven ability to create and sustain some of the most beloved franchises that were ever created in this industry. So that passion in this company is still there. As we talked about a couple of years ago when we lost the Disney Princess franchise and then our Monster High franchise started to go through a natural cycle -- evolutionary cycle that you see with entertainment-led properties, we had a choice. Do we right-size the company to a new base business, or do we try to outrun those losses. And the decision that was made -- and I really wasn't here so I can reflect on it, all I can see is the aftermath of that. The decision was made to outrun them then with a very aggressive set of launches and promotion programs over a couple of years. And as we've talked openly about, that decision inadvertently led to the issues that we've had in 2017 where you sort of got the trifecta of issues, right. You had the combination of inventory misalignment with a planning misalignment. We started the year with a high single-digit growth, which was a little bit too aggressive. We had too-high aspirations for the year to -- a number of these new launches, so that led to dislocations in a long lead cycle business. And then we added to that the TRU bankruptcy. And some usually quite manageable issues that you can have from time to time with some of your brands as they go through different life cycle transitions. So we just had all of those at once in 1 year, which is why we keep talking about how 2017 was just an extraordinary year but does not reflect what these brand franchises are capable of. And that's why we've continued throughout the entire year to focus the discussion on the real consumer takeaway that's happening against these brands. The fact that Barbie is delivering the third year of high -- mid- to high single-digit growth and it's driven by consumer passion for that franchise. It's following in social media. It's excitement on YouTube and the willingness of kids to fall in love with this content on Netflix, and we're only continuing to expand those initiatives. Hot Wheels continuing to grow in the face of a very successful launch of Cars 3 because we've really differentiated them. They're 2 very different properties that serve at different passion points for kids and families. And that's why the Hot Wheels franchise continues to be very successful because it's a fantastic play pattern. And the combination of diecast cars, play sets and the opportunity now to expand into construction and younger kids offers us a really strong growth opportunity in that franchise. And I could go on with each one of our franchises. So the reason why we're optimistic about the future is we know and have a very strong strategy for how we want to grow this company in a profitable way that's truly differentiated, anchored on Power Brand franchises and capabilities, and then our ability to take that capability set and use it to activate innovation in our Toy Box, whether it's with our wonderful entertainment partners or creating next-generation launches in spaces where existing brands aren't competing. And we feel that we're starting the year in '18 in a much better position in terms of retail inventory. So our sales will fully reflect the consumer takeaway. Our economic models now reset with the tough decisions that we made to take the write-downs that we needed to do and our structural simplification program, which is well underway, and that will restore our profitability. And this year, it's our plan. We're going to set realistic revenue expectations, and we're going to align our operating costs all the way down to P&L. If you heard from Joe, we have issues all the way down the P&L because of the very high plan we started with and where we ended. That will not happen this year. And we have a fully new leadership team and a much stronger organization structure and the incentives to get the job done. So that's how I view where we are, and we hope that our investors will be able to keep it in perspective and appreciate that we're making the tough decisions to reinvigorate this incredible franchise, and we hope you'll be at Toy Fair and can see how magical the product is and how wonderful the creative team.

Operator

Your next question come from the line of William Reuter with Bank of America.

William Michael Reuter - *BofA Merrill Lynch, Research Division - MD*

I've got a couple. The first one is for Joe. I just want to make sure I understand the 15% decline in gross margins. I think when you were breaking down the different percentages, you said that 40% of it was due to the write-down of inventory. I guess one, did I hear that correctly, which will be about 6%? And two, would that be kind of one-time-ish in nature in your opinion?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes, I mean, look, we -- on that one, we clearly went and tried to clean up as much as we can. Will we never have another inventory write-off in the future? Probably not. We probably will have some. But we tried to get the majority out now and shouldn't have any of these large repeating items like we have now. It's all about better management on a going-forward basis and making sure that we're setting up our inventory to match demand out there rather than building ahead of it.

William Michael Reuter - *BofA Merrill Lynch, Research Division - MD*

Okay. And just to make sure I understand. You did not add that back to your adjusted EBITDA number, that write-down of inventory, did you?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

No. No.

William Michael Reuter - *BofA Merrill Lynch, Research Division - MD*

Just my second question is with the 40% of the $650 million of cost savings you think you can achieve this year, I know you're going to be reinvesting $170 million over the next two years in some technology. But other than that, should we assume that the remainder of those cost savings will flow through to the bottom line?

Joseph J. Euteneuer - *Mattel, Inc. - CFO*

Yes. Remember where we said that the $650 million would be net. But remember, we also talked about $200 million of implementation, of which $40 million came here in the fourth quarter with the severance plan that we put in place. Still have about another $160 million of implementation that will be onetime to touch certain areas over the two years.

Operator

Ladies and gentlemen, that concludes today's question-and-answer session. I would now like to turn the call back over to Whitney Steininger for any closing remarks.

Whitney Steininger

There will be a replay of this call available via webcast and audio beginning at 8 p.m. Eastern today. The webcast link can be found on our investor page. Or for an audio replay, please dial (404) 537-3406. The pass code is 84841057. Thank you for participating in today's call.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes the program, and you may now disconnect. Have a great day, everyone.