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MAT - Q4 2014 Mattel Inc Earnings Call

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OVERVIEW:

Co. reported 4Q14 EPS of $0.44.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to Mattel's fourth-quarter 2014 earnings conference call. (Operator Instructions) As a reminder, this conference is being recorded.

I will now turn the call over to your host, Drew Vollero, Senior Vice President of Corporate Strategy and Investor Relations. Please go ahead.

Drew Vollero - ***Mattel, Inc. - SVP Corporate Strategy & IR***

Thanks, Stephanie. As you know, this morning we reported Mattel's 2014 fourth-quarter and fiscal year-end results. We've provided you with a slide presentation to help guide our discussion today. The slide presentation and the information required by Relation G regarding non-GAAP financial measures is available on the investors and media section of our corporate website, corporate. Mattel.com.

In a few minutes, Chris Sinclair, Mattel's Chairman and Interim CEO, and Kevin Farr, Mattel's CFO, will provide comments on the results and the call be open for your questions.

Certain statements made during the call may include forward-looking statement relating to the future performance of our overall business, brands, and product lines. These statements are based on currently available information that are subject to a number of significant risks and uncertainties which could cause our actual results to differ materially from those projected in the forward-looking statements.

We describe some of these uncertainties in the risk factors section of our 2013 annual report on Form 10-K and our 2014 quarterly reports on Form 10-Q and other filings we make with the SEC from time to time, as well as in other public statements. Mattel does not update forward-looking statements and expressly disclaims any obligation to do so.

Now I would like to turn the call over to Chris.

Chris Sinclair - ***Mattel, Inc. - Chairman & Interim CEO***

Thanks, Drew, and good morning, everyone. I want to thank you for joining us today.

It has been a busy week for all of us here at Mattel. By now you've had a chance to review our preliminary fourth-quarter and fiscal-year 2014 earnings results as well as the full earnings release that we issued this morning.

Before I get into the results, I would like to take a moment to describe why the Board decided to make the leadership change that we announced on Monday. After that, I will quickly recap our performance for the fourth quarter and the full year. I will talk about what I am focused on as we work to drive improved profitability at Mattel. Kevin is then going to take you through our results in more detail and we will be happy to take your questions.

Now let me start by saying that Mattel has a unique leadership position in the toy industry, given our unmatched portfolio of brands, our global scale and infrastructure, and our strong balance sheet. We also have a strong management team along with our many talented employees around the world.

We appreciate Brian's efforts and contributions over the years, but the Board determined that it is time for new leadership to change the trajectory of the business to maximize our potential going forward and certainly to take advantage of our many assets. I am honored that the Board selected me to serve as Chairman and interim CEO, and I assure you that I am committed to delivering improved performance.

Now having served as a member of Mattel's Board of Directors since 1996 and as the Independent Lead Director since 2011, I know the Company well and I have tremendous confidence in our ability to revitalize this business as we work to identify the right leader for Mattel's next phase of growth and value creation.

Now let me shift gears and turn to our fourth quarter and to our full-year 2014 results. Quite simply, our results were not acceptable. So what happened?

Well, our performance was impacted by a number of factors; some of which are out of our control, but most of which are not. As evidenced by the declining POS momentum in the fourth quarter, the Company did not execute well during the holiday season. Specifically we fell short in three areas.

First, our brand propositions were simply not compelling enough to consumers. This was particularly true across our Barbie and Fisher-Price brands. Our product innovation was inconsistent as some brands performed well, but many did not. In addition, the success of our marketing activities was mixed as our spending did not generate a lift to brand sales beyond the specific products that we were promoting.

Now these results make it clear that we need to do a better job of creating compelling brands and products for our consumers. At the same time we must maintain our brand engagement throughout the year instead of waiting until just the holiday season. Now this is important to help sustain a more consistent consumer mind share each month with advertisements peaking at the holiday season.

Second, we were impacted by the most dynamic and challenging environment in the doll category that we've seen in many years. Our doll brands account for approximately 40% of our business and Mattel owns or licenses the top five fashion doll properties. However, the white-hot success of Disney's Frozen, particularly during the holiday season, did not drive significant overall growth in the doll category. And as a result, Barbie lost ground.

On American Girl, while we saw growth in its Girl of the Year product line, we did see declines in its other brands. Again, we think this was a function of intensified competition. Beyond this, we were also not successful in delivering captivating products in our Monster High brand, where we became much too dependent on line extensions.

Finally, our global retail execution also fell short, especially here in North America. For the year, our results were clearly hampered by the inventory overhang from 2013 and in the fourth quarter the retail environment was far more competitive and challenging that it had been in the past.

Against this backdrop, we exacerbated the challenging environment through poor execution in store, which was not offset by our efforts online. We saw a decline in retail ad lifts and shelf space productivity, all of this as we worked with retailers to move through much of the channel inventory.

Bottom line is that our global marketing programs and go-to-market strategy did not effectively break through in a highly competitive environment. Clearly, we must do a better job to reignite momentum.

I have spent this week working closely with the leadership team and immersing myself in the details of the business and over the next few months we will evaluate all aspects of it. We do not anticipate a fundamental shift in strategy at this time, but we clearly need to act with urgency to make the necessary changes around how we execute and how we support and build our brands and drive new innovation.

At a high level, we will be focused on actions designed to improve performance across our key brands in the doll category; to develop and implement a rigorous sales plan both in-store and online to improve our customer performance; to accelerate our efforts to better position Fisher-Price as a child development brand. And we are also going to concentrate our efforts around capitalizing on the most significant international market opportunities.

Once we have had a chance to more thoroughly evaluate the business, I will look forward to providing you with a lot more specifics on our Q1 call about the actions we intend to take. Beyond our focus on execution and driving the top line, I also want to mention that we will continue to pursue our Funding our Future program to reduce costs and to reinvest savings to support growth.

Now while we have a lot of work to do, I think it is also important to note that we are making good progress in terms of new innovations, product developments, and partnerships. You will hear more from us on this at Toy Fair in a couple of weeks and we look forward to seeing many of you there.

Finally, while I am not going to speculate on the timing, I will also be working with the Board to evaluate internal and external candidates to identify a permanent leadership for the Company as we go forward.

Now let me wrap up by saying that the Board and I believe very strongly in Mattel. We believe in its brands, its financial strength, and most of all, its people. And I look forward to engaging with all of you, as well as with the entire Mattel community, as we work to revitalize this business and to deepen our connections with children and parents around the world.

With that, let me turn it over to Kevin.

Kevin Farr ***- Mattel, Inc. - CFO***

Thank you, Chris, and good morning, everyone. Given all the changes this week, I will not be going through my typical review of our earnings slide deck, but instead will focus on providing additional color on our operating results and free up some more time for Q&A. And with Chris being in his CEO position on an interim basis for just five days, we will not be making any specific comments on our 2015 outlook at this time.

As Chris said, over the next few months our management team will evaluate all aspects of the business. During our first-quarter investor conference call in mid-April, we plan to update you on the specific actions we plan to take to build and support our brands and drive new innovation in order to change the revenue trajectory of our business and deliver improved profitability.

Let me start by echoing Chris's comment that our fourth-quarter and full-year results are unacceptable. At a high level our international business did okay from a top-line perspective, but our domestic business really struggled in the quarter. Neither business met our expectations with respect to revenues and profitability.

As we previously said, our objectives in 2014 were to exit the year with improved POS momentum and lower retail and Mattel-owned inventory levels. We did see POS continue to outpace shipping in the quarter, but our overall POS momentum in the fourth quarter decelerated. International POS was flat, while domestic POS declined high single digits, resulting in global POS being down mid single digits in the quarter.

For the year, global POS was down slightly with domestic POS down mid single digits, partially offset by international, which was up low single digits led by growth in emerging markets including Russia and China. Clearly, our issue is that POS exiting 2014 is not where we need it to be. As Chris said, our brand propositions were simply not compelling enough to consumers, particularly across our Barbie and Fisher-Price brands, and our marketing activities did not generate the lift that we expected. And our global retail execution in store also fell short, especially in North America.

That said we did make some progress on retail inventories as we partnered well with retailers to move through much of the channel inventory on a global basis, although pockets remain in some markets and for some brands. Domestic retail inventories are down significantly and retail inventories are down in most international markets as well.

That said, given our current POS trends, retail inventories may still not be where they need to be in certain markets. Similarly, our Mattel-owned inventories are lower versus last year but higher than our historical averages.

Looking at our POS results by brand, overall our Girls portfolio ended the year with positive POS, but that was driven by the success of Frozen. Barbie experienced steeper declines in the very competitive holiday period, ending the year with POS down single digits -- high single digits. Monster High POS coming off of record sales last year was down high teens for the year, pretty consistent with where it has been in the last two quarters.

Global POS for total Fisher-Price brands remained challenged on an overall basis, which was down mid single digits for the year, but we did see some pockets of strength in two areas. First, Fisher-Price international POS grew mid single digits for the year. This is good to see as the brand is starting to gain traction in emerging markets, including China and Russia.

And second, we saw positive global POS for the year in our infant business, which includes BabyGear and Laugh & Learn product lines where we had some really good innovation. Finally, for the US overall Fisher-Price POS was down low double digits for the fourth quarter and the full year.

Of our remaining core brands, we had solid POS gains for Hot Wheels and Thomas in the quarter and throughout the year, and saw very positive results in our international markets for these two brands.

Now turning to revenues, gross sales were down 3% in the quarter and down 6% for the year. Chris briefly touched on our Girls portfolio and the key reasons why it did not grow in the quarter, so I will focus my comments on the performance of our other core brands.

Worldwide sales of Hot Wheels were positive in the quarter. Hot Wheels continues to do particularly well in international markets with the basic car and track segments which highlight the brand's core play pattern.

Worldwide sales of total Fisher-Price brands were down double digits in the quarter, driven by declines in key Fisher-Price core brands like Little People and Imaginext, as well as tough comparisons related to Fisher-Price Friends licensed entertainment properties. Thomas shipping was positive internationally, which was a strategic priority with the HIT acquisition.

And finally, we worked hard to successfully integrate MEGA Brands in 2014. While our sales for the partial year have been impacted by things such as international distributor transitions, they were consistent with our expectations. Looking to 2015, we now have the opportunity to sell MEGA Brands products globally by utilizing Mattel's global infrastructure, which is an important growth opportunity going forward.

From a regional perspective, our North American business was down 2% in the quarter and we had mixed results in our international business, which was down 5% including the impact of foreign exchange. Not surprisingly, the strengthening of the US dollar significantly impacted reported revenues in the fourth quarter. Our 3% decline in worldwide sales included 4 percentage point unfavorable impact due to foreign exchange, and the 5% decline in our international revenues included an 8 percentage point unfavorable impact due to foreign exchange.

With respect to international markets in the fourth quarter, sales in our European region were down 6%, which included a negative 9 percentage point impact of foreign exchange, driven by continued strong growth in Russia despite the challenging macroeconomic environment. Sales in our Latin America region were down 8%, which included a negative 7 percentage point impact of foreign exchange as we continued to weather macroeconomic challenges as well as work through retail inventory overhang from 2013.

Sales in our Asia-Pacific region were up 12%, which included a negative 5 percentage point impact of foreign exchange, driven by continued strong growth in China. We expect that the headwinds related to the strengthening of the US dollar will continue in the near term.

With respect to projecting the impact of foreign exchange in our financial performance in the future, our general rule of thumb remains that a 1% change in the US dollar index should impact annual EPS by about $0.01 to $0.02 and revenues by 0.5 percentage point.

Moving beyond the top line, I will touch on the key drivers of the P&L.

For the fourth quarter gross margin was 50.4%, down 410 basis points versus last year's 54.5%. Gross margins continued to decline relative to record highs achieved in 2013, reflecting the cost of trade programs to drive holiday POS as well as the impact of our MEGA Brands acquisition.

The gross margin of 50.4% included a 160 basis point negative impact from MEGA Brands in the quarter. Excluding MEGA Brands, a little over three-quarters of the remaining 250 basis point decline was related to trade programs to improve POS during the holiday season, and the balance was split between the loss of manufacturing scale and mix related to lower sales of our Girls portfolio products. Finally, pricing actions and net savings from OE 3.0 initiatives roughly offset increases in product costs.

For the full year, gross margin was 49.8%, down 380 basis points versus 53.6% in 2013. This included a 150 basis point impact from MEGA Brands. Excluding MEGA Brands, more than half of the remaining 230 basis point decline was related to efforts to clean up inventories and trade programs to improve POS both during the holiday season and throughout the year.

And the balance was split between the loss of manufacturing scale and mixed related to lower sales of our Girls portfolio of products. Finally, pricing actions and net savings from OE 3.0 initiatives roughly offset increases in product costs.

Looking forward on gross margins, we continue to manage the business for the long term and believe our long-term gross margin objective of about 50% is reasonable. Looking forward to 2015, we should see some tailwinds with favorable commodity trends, cost savings from our Funding our Future initiatives, and the absence of MEGA Brands' fair value inventory adjustments.

And we also expect headwinds like the ongoing impact to MEGA Brands, potential product mix related to the performance of our Girls portfolio, investments in improving core brand POS through retail execution, foreign exchange, and higher input costs including direct or labor.

Despite the revenue shortfall and the gross margin challenges, we continued to manage the middle of the P&L. We made excellent progress against our OE 3.0 cost-saving initiatives, exceeding expectations and delivering $119 million of gross savings in 2014. As a result, we have delivered cumulative gross savings of $179 million over the two-year program. Combined with our first two programs, GCL and OE 2.0, we have delivered almost $600 million in gross savings to date.

Advertising on an absolute dollar basis was lower for the full year, reflecting lower overall sales volume. However, advertising was up substantially in the fourth quarter in both absolute dollars and as a percentage of net sales, reflecting the shift in spending to align with consumer purchase patterns. Our marketing activities and promotional programs did not generate the POS lift that we expected, which made it clear that we need to create more compelling product for consumers and we must maintain our brand engagement throughout the year.

Total SG&A spending was up for the quarter and up slightly for the year. If you exclude incentive and equity compensation and the impact of MEGA Brands, SG&A spending was roughly flat in the fourth quarter and the full year compared to 2013. The fourth quarter and full-year results include $22 million and $53 million, respectively, of MEGA-related acquisition, integration, and amortization expenses.

Our incentive and equity compensation was lower on a full-year basis given that we are a pay-for-performance company and our results were well below our financial objectives. Our bonus pool was $25 million, which was down about 60% versus last year. Our most senior executives will not receive an annual bonus and there was no equity compensation accrued related to long-term incentive plan this year because we did not hit our performance targets. But our incentive accrual reflects a small discretionary bonus paid to the rest of our employees.

Severance charges were also higher in the quarter, primarily related to integration charges for MEGA. Looking forward to 2015, we see tailwinds in SG&A from lower MEGA acquisition and integration expenses and lower amortization of acquired MEGA intangible assets, gross savings from our Funding our Future program, and the impact of foreign exchange. We will also likely see headwinds related to severance investments in our Funding our Future initiatives.

Overall, operating income was $653.7 million versus $1.17 billion in 2013. Excluding some discrete tax benefits, Mattel's tax rate for the year was 22% and we expect our tax rate to be 22% to 23% going forward, assuming no changes to current tax laws.

EPS for the quarter was $0.44, which included $0.05 of MEGA Brands' integration cost and a negative tax impact of $0.03 per share. Full-year EPS was $1.45 including $0.16 of MEGA Brands' acquisition and integration costs and a tax benefit of $0.13 per share.

Now turning to the balance sheet and cash flow, we improved our Mattel-owned inventory position as we exited 2014 but it is still higher than our historical averages. Excluding the impact of MEGA Brands, our owned inventory was down about $40 million versus 2013.

Despite the very challenging year driven by a decline in top-line revenue and gross margin, we generated almost $889 million in cash flow from operations versus $698 million in 2013. The increase in cash flow of $191 million from operations was primarily driven by reductions in net working capital, partially offset by lower net income.

And we ended the year with about $970 million of cash in our balance sheet. This puts us at a higher end of our $800 million to $1 billion target in our capital and investment framework. Our 2014 results also reflect our ongoing commitment to disciplined and balanced capital deployment, which included $260 million of capital expenditures, $515 million allocated to the dividend, $423 million dedicated to acquire MEGA Brands, and $177 million to share repurchases including $49 million in the fourth quarter.

After reinvesting in our business, dividends remain our first priority and the Company declared a first-quarter dividend of $0.38 per share, which is flat compared to the first quarter of 2014. As we have historically done, we will evaluate capital deployment priorities as the year progresses, consistent with business performance as well as our capital investment framework which balances many factors. These include cash generation potential of the business, potential deployment opportunities, and our overall financial flexibility.

In closing, we are clear eyed about the challenges that lie ahead of us, and I am excited about working with Chris and the Mattel management team as we take on these challenges with an even greater sense of urgency. As we do, we continue to be confident in our ability to win over the long term.

The toy industry continues to grow and accelerate with new innovation. The depth and breadth of Mattel's brands continue to be unmatched. Our global scale and infrastructure is a key differentiator. And we will continue to be financially disciplined as we expect to generate significant cash, which can fund further growth and be used to reward our shareholders.

We look forward to seeing most of you at Toy Fair next month as we show you some exciting product and marketing innovation. Stephanie, I would now like to open up the call for questions.

QUESTION AND ANSWER

Operator

(Operator Instructions) Sean McGowan, Needham & Company.

Sean McGowan *- Needham & Company - Analyst*

First question, where is the decline in the entertainment category coming from? What is really driving that decline?

Kevin Farr *- Mattel, Inc. - CFO*

I think the decline in the entertainment category is Planes and Cars were part of the decline as well as Superman and games.

Sean McGowan *- Needham & Company - Analyst*

Okay. And of the MEGA Brands -- it looks like MEGA Brands was up nicely in the quarter. What drove that?

Kevin Farr *- Mattel, Inc. - CFO*

Again, I think it has had momentum this year with respect to I think it's Halo and Call of Duty, as well as the basic products. And that is the biggest drivers.

Sean McGowan *- Needham & Company - Analyst*

Okay. Then last question for now; it's hard to see in the P&L all the $600 million in savings that you outlined over those three programs with the SG&A at a kind of record high in percentage of sales. I know that that is driven partly by sales decline, but just in gross dollars where has all that savings gone?

Kevin Farr *- Mattel, Inc. - CFO*

Well, as you know, this program was really focused on the supply chain initiatives like packaging, design for manufacturing, and so the majority, I think 60% of the savings are in cost of goods sold. And you can see that in gross margins.

However, as you know, this year, with respect to gross margins, there was a lot of moving pieces in the year. Our gross margins were impacted with the acquisition of MEGA Brands, our efforts to clean up inventory, the loss of manufacturing scale and mix related to lower sales of the Girls portfolio of products, but we did see good savings with respect to gross margins from our OE 3.0 activities.

Sean McGowan *- Needham & Company - Analyst*

Thank you.

Operator

Gerrick Johnson, BMO Capital Markets.

Gerrick Johnson *- BMO Capital Markets - Analyst*

Good morning. Just wondering about the flow of goods. Did you bring goods in early to avert port issues and did this cause any problems down the road?

And secondarily, on your promotional activities, you saw a nice big increase in the ratio of promotions to gross sales. Can you talk about the progression of those promotions? Did you take more prior to the holiday relative to last year? Was it more after the holiday? How did that work out? Thank you.

Kevin Farr *- Mattel, Inc. - CFO*

Okay, so with respect to the port, I think we did have some delays but we didn't bring back -- bring in product much earlier than we planned to, so that wasn't a big issue in the quarter. I think with regard to the promotions this year, I think from a perspective of our promotional aspects it really was -- as we saw two changes with respect to our spending mix model. We really looked at the research and analytics and applied the spending mix model.

First, we spent more media on digital versus TV and, second, we spent more on our advertising in the fourth quarter and it was spent later in the fourth quarter. So I think we feel good about the shift to digital, where we had good success, although the success of our marketing was mixed as our spending didn't generate the lift we expected it to. So as Chris said earlier, we think we need to continue to engage our brand connections earlier throughout the year to sustain more consistent mind share each month with advertising peaking at the end of the year.

Then we work with customers, particularly as consumers came out later, to move the inventory and those occurred later in the fourth quarter.

Operator

Tim Conder, Wells Fargo.

Tim Conder *- Wells Fargo Securities - Analyst*

Thank you. A couple here. I guess on a fundamental basis -- and, Chris, I understand that you may not -- this is just being very informative here.

How do you see the ability or opportunity to change Mattel's fundamental innovation process? Basically, so you can take consumer feedback earlier in the process and either kill or proceed with an idea so that the ideas that you do get out there have a higher batting average I guess is the root of the question.

And then, Kevin, any geographic and brand color on the inventory where you are still, say, some of the highest areas globally? And then finally, pricing. You took some price in 2014. I guess on a go-forward basis, given let's just call it global deflation and then the POS issues that you have, how do you feel about pricing in 2015? Thank you.

Chris Sinclair - ***Mattel, Inc. - Chairman & Interim CEO***

It's Chris here. Let me take your first question, then I'm going to let Kevin pick up the balance.

One of the things that is clear -- and we have been looking at this I guess for the last six to nine months -- is we had some work to do on the talent front and certainly a lot of work to do on the culture front to spur innovation and creativity. I think we were all sort of focused on bringing Richard Dickson in to kind of spearhead this. I think he has done a great job and you will see some of this as we get to Toy Fair; kind of igniting the creative talent from the organization.

And part of it is also broadening our outreach for innovation. There's a lot of people and inventors in the marketplace that we have had to rekindle our relationships with. We are starting to work with some of the digital partners out there that can bring us a lot of innovation.

And, importantly, I think using research is something you alluded to. We've brought in a lot of talent there to help us get better analytics, better focus on our consumer and understanding them, and upgrading our testing capabilities. I think you will see us start to move quicker to get some research going on some of our ideas, catch it early. Clearly, not everything works; you want to know that and make adjustments. All of that is in stride.

But I come back to talent and culture and I think we are feeling actually very good about what Richard is doing with his team. Don't forget we have had -- despite the grim news, we have had some very good successes in the last year. Ever After High, BOOMco, things like that have actually been good wins for us. So it's a matter of doing more of that, making sure we are doing it with bigger bets, and in the right areas.

And I think stay tuned. I think this will get better and it's something that we are laser focused on. A lot of the issues we deal with come right back to the top line and it comes back to our branding and our innovation. We've got to get that right as a first priority.

Kevin Farr - ***Mattel, Inc. - CFO***

Following up on your question on inventories, this was a key objective for us and we worked hard at it and saw some improvement. If you look at our owned inventories, they are lower than last year, as I said, but they are higher than historical averages. So we've got work to do with customers to move through that product.

Retail inventories are down around the world, led by the US. Down almost a third at our top six and down high single digits in key international markets. We made progress in most countries, but we have pockets of retail inventory remaining in certain countries and regions, particularly core Europe and there is some in Latin America. So we are in a better position I think as we enter 2015 than we left 2014; we have made some progress here.

With respect to pricing, we do a lot of research to try to understand the strength of our brands and products. And as we price our items we consider many factors, one of them is our POS momentum of our brands; other is product innovation and brand strength. Right now we are not feeling that we need to do more work around that.

Retail dynamics and competitive assessments. So when we look at our overall product line, we are going to price appropriately. And given the recent volatility around input costs and currencies, we are still in the midst of talking to our customers about the price for our 2015 product lines.

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

Okay, great. Thank you, gentlemen.

Operator

Taposh Bari, Goldman Sachs.

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

Good morning, everyone. I was hoping to get an update on where you stand regarding your dividend, specifically which metrics are you most focused on going forward as you consider sustainability.

Kevin Farr *- Mattel, Inc. - CFO*

As I said in my remarks, consistent with our capital investment framework, dividends remain our first priority after investing in our business. The Company did declare a first-quarter dividend of $0.38 per share, which is flat with the prior year.

As we have done historically, we will evaluate capital deployment priorities as the year progresses consistent with business performance, marketplace opportunities, and our capital investment framework. As we look at it right now, we are okay and we will continue to evaluate capital deployment priorities as the year progresses.

Taposh Bari *- Goldman Sachs - Analyst*

Great. And maybe if I could just follow up on that point, on the point of financial flexibility that you mentioned in your script, Kevin. How committed are you to an investment-grade credit rating? And do you have any clauses in any of your license deals that require you to maintain that kind of credit rating?

Kevin Farr *- Mattel, Inc. - CFO*

First I will answer the second: we don't have any clauses in our license deals. I think what we do know about this business is it is working capital intensive, not capital intensive, and the most efficient way to finance this business is through access to the commercial paper market.

So our credit rating is very important. We are committed to our credit rating to be investment grade and we do target single-A metrics. So as we look at financial flexibility, we look at that in terms of our single-A metrics as well as with respect to -- we also have a backup revolver of $1.6 billion that is out there till March. So we have got plenty of liquidity as a Company, but we are focused on those credit metrics.

Taposh Bari *- Goldman Sachs - Analyst*

Great, thank you.

Operator

Felicia Hendrix, Barclays.

Felicia Hendrix *- Barclays Capital - Analyst*

Thank you for taking my questions. Mr. Sinclair, you said at the beginning regarding the CEO search you weren't going to talk about timing, but you did say you were looking internally and externally. Just wondering if you could talk a little bit more about the type of person you are looking for, perhaps what kind of industries you would prefer that they came from. Any kind of color on this search would be helpful, thank you.

Chris Sinclair *- Mattel, Inc. - Chairman & Interim CEO*

Felicia, let me just say at the outset, we don't have a search going right now and I wouldn't prejudge where that's going. Clearly, as we are focused right now on revitalizing the business and sort of energizing and focusing this management team, the things we are going to be keeping an eye out for is clearly leadership. You want proven leadership in an individual that's going to direct the Company.

Certainly experience in innovation and creativity in building brands, global brands. I think, first and foremost, it would be that; a track record of success and decisiveness. That could be inside. It could be outside.

I think we and the Board will work on that in due course. Our priority right now is to get the business righted and back in good shape.

Felicia Hendrix *- Barclays Capital - Analyst*

Thank you. Kevin, you all talked in the prepared remarks about the competitive doll category in the quarter and some specifics around Barbie and Monster High and why those might have underperformed. But I'm just curious; you had the doll in the quarter with Frozen, or dolls. We have 200 of them in my house.

Just wondering competitively, if you don't want to talk specifically about who or what you were competing with, maybe just generically so that we can understand what else was out there. Because between Frozen, Monster High, Barbie, I can think of a few others from competitors, but really when you say competitive what exactly are you speaking of?

Kevin Farr *- Mattel, Inc. - CFO*

Really we're talking about Frozen. It was white-hot property as you know this fall; I think you've seen it in your home, so that is principally what we are talking about.

It up-aged -- the brand up-aged and it's also sitting sort of in between Barbie and Monster High. So we saw that be competitive and also we saw it being competitive we think against American Girl.

Felicia Hendrix *- Barclays Capital - Analyst*

Okay, so you are speaking mostly about more cannibalization versus growing the whole category for you. Okay, so now I understand that.

Then just finally, Kevin, getting back to this dividend question and I think you've been very clear about your commitment to keeping the investment-grade rating and how you are going to evaluate things as the year goes on. I'm just wondering what is the commitment here to the dividend. Has there been any thought about perhaps using some of that cash to reinvest in the business, particularly as you are going through this transition now?

Kevin Farr *- Mattel, Inc. - CFO*

I think, as we said before, I think we are okay right now and I think we're going to look forward through the year and evaluate our capital deployment priorities as the year progresses. What's the best use of cash at the time we generate it.

Chris Sinclair *- Mattel, Inc. - Chairman & Interim CEO*

Felicia, that is an ongoing process at the Board. This is not new to where we are today. We typically evaluate things on a regularized basis. Clearly, we are committed to dividends as a major component of our capital deployment. And I think Kevin has got it right; right now we feel fine, but obviously we are evaluating a lot of things.

Felicia Hendrix *- Barclays Capital - Analyst*

Okay, thank you very much.

Operator

Linda Weiser, B. Riley.

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

Just to go back again to the issue of the retail inventory, I believe you said that POS in the US was down high single digit in the fourth quarter, and yet your North American sales were down 2%. And that would include American Girl, which was actually a little bit worse. So it seems to me that POS was actually worse than your shipments in.

So how does that really function to reduce inventory at retail? It seems to me that might have actually worsened the situation, so maybe you could explain that.

Then my second question is on Fisher-Price. It seems that -- I've heard comments from MGA that their Little Tikes brand is just really doing well. It's actually growing and I would assume this is in the preschool area. So are there any lessons you can take from whoever is doing well in the category and what they are doing right and kind of try to come up with something on Fisher-Price?

It seemed Richard Dickson had some ideas on Barbie and Monster High, but it seemed he was further behind in analyzing the Fisher-Price situation. So maybe you could just -- am I accurate on that? Will we hear more from him at Toy Fair about Fisher-Price or --? Maybe you could comment on that. Thank you.

Chris Sinclair - ***Mattel, Inc. - Chairman & Interim CEO***

Linda, I will take your last question then I will let Kevin go back on the inventory.

But Fisher-Price has probably been a tougher nut to crack for a while because it is so fragmented in terms of the segments it competes in and the brands that are underneath it. But we do actually have a pretty good focus right now on that preschool segment. I think you will see some things from Richard. I think he and his team are definitely catching up there.

A lot of it has to do with branding and innovation work, but also we have got to get price value and things like that right in select markets. So it's kind of a holistic approach. But I think -- stay tuned, I think we'll have more to talk about on Fisher-Price.

Kevin Farr - ***Mattel, Inc. - CFO***

And I think with your question with regard to retail inventories, I think as you look at the full year our sales were down high single digits and obviously our -- basically our retail inventories were down a third.

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

Okay. Then just one follow-up on the financials. In terms of cash flow for 2015, I know it's hard to project that because it's hard to project earnings, but on the working capital front I would expect there wouldn't be as much cash thrown off from working capital reduction. Is that an accurate assumption?

Do you think working capital will be a positive source, though, Kevin? Do you have any idea about that? Thanks.

Kevin Farr - ***Mattel, Inc. - CFO***

Again, we are not going to give guidance on it. I think what we would say, though, is we will continue to manage our working capital tightly. We will look at realistic revenue assumptions and again manage it tightly like we did this year.

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

Great. Thanks a lot.

Operator

Drew Crum, Stifel.

Drew Crum - ***Stifel Nicolaus - Analyst***

Thanks. Good morning, everyone. Kevin, I wonder if you could address MEGA Brands and specifically the 100 basis point headwind that you are expecting for gross margin. Absent the inventory adjustments that you had in 2014, what are the drivers for the headwind?

And I guess more generally, are you abandoning the guidance you had provided a couple quarters ago that MEGA Brands should be accretive to numbers in 2015?

Kevin Farr - ***Mattel, Inc. - CFO***

I think with respect to MEGA Brands, as we did the acquisition and we looked at it strategically, MEGA Brands on a standalone basis had margins of about 30%. When we looked at the category, it's a great category. Obviously a competitor is a strong player in that category, but it has great margin profile, much like our doll portfolio.

So what we see is near term that it's actually going to be dilutive to our gross margins because it's lower margin. I think consistent with what we said as we acquired it is we think it's going to have about 100 basis point ongoing negative effect to our gross margins because of the mix to our margins.

That said, we think there's plenty of opportunities to improve the margins I think with regard to some of the properties that we have, with regard to new properties like SpongeBob and Despicable Me Minions, that those are good margin products. And then again, I think our synergies in running the manufacturing operations and getting scale in sales should allow us to improve margins over time.

With respect to talking about whether MEGA Brands is accretive next year, I think it was accretive if you take out restructuring, integration, and amortization charges this year. It's too early to really talk about 2015 because we haven't made decisions, as we are using this as a great platform for growth in 2015, how much we're going to put behind the brand on a global basis as we use our sales affiliates and our global infrastructure around the world to build the brand through investments in things like advertising.

So we are excited about the progress we made in 2014. We did integrate it effective January 1 for most places around the world. We are going to be selling it through our existing subsidiaries, including North America. We've got a good platform for growth and I think we are still trying to determine how much advertising dollars we should put behind it to drive that growth. So more to come on that later.

Drew Crum - ***Stifel Nicolaus - Analyst***

Thanks, Kevin. Then Brazil is one of your biggest markets. I think in the slide deck you noted that you are seeing some improvement there. If you could expound upon what's working or where you are seeing improving trends in that market.

Kevin Farr - ***Mattel, Inc. - CFO***

Yes, I think we've got a strong -- our brands are probably the strongest in the world in Brazil. Obviously there has been macroeconomic issues in Brazil and also we did have some inventory issues, but things like Fisher-Price is doing well. And other brands like Barbie and Hot Wheels are doing well down there.

Drew Crum - ***Stifel Nicolaus - Analyst***

Thanks, guys.

Operator

Jaime Katz, Morningstar.

Jaime Katz - ***Morningstar - Analyst***

Good morning, thanks for taking my questions. So piggybacking on that MEGA question, can you just talk about how the reception has been with international retailers and the ease of getting the distribution through the Mattel channel?

And then, as far as share repurchases are concerned, I know the slides say they are still an important piece of the capital investment framework, but can we assume that that will be at a much slower pace, at least in the first half of the year, until things are sort of back in order over there? Thanks.

Kevin Farr *- Mattel, Inc. - CFO*

Yes, I would say on their international business with regard to MEGA we were in transition in 2014. We were getting out of distributors, so 70% of our business was in the US this year, about 30% outside.

Really we were getting ready for launching in international markets. We think it's a big opportunity because they are only 30% outside the US, and I think really we will see much better distribution as our affiliates pick it up and manage that business in 2015.

With respect to share repurchases, as we said before, dividend is our first priority after investing in the business. And as always, we will be opportunistic on share repurchases based upon our cash flow situation. But, again, that's going to be based upon our business performance and it would be consistent with our capital investment framework. But I think it's safe to say in the near term we're not going to be doing any share repurchases.

Jaime Katz *- Morningstar - Analyst*

Thanks.

Operator

Mike Swartz, SunTrust.

Mike Swartz *- SunTrust Robinson Humphrey - Analyst*

Good morning. I just wanted to kind of circle back to the opening remarks that Chris was making about some of the areas where maybe you fell short in the fourth quarter. And just kind of digging down, when you think of those three items that you mentioned, how many of those are actually -- do you perceive as being in your control versus maybe being dictated by the externals?

Chris Sinclair *- Mattel, Inc. - Chairman & Interim CEO*

Mostly in our control, Mike. Clearly, the market was more competitive than historically and particularly in dolls, which Frozen led that charge. But having said that, we created our own problems with inventory proliferation of line items that weren't particularly impactful. We kind of missed consistency on our branding, particularly on Barbie and Monster High.

A lot of those things are to me eminently fixable. Execution in the marketplace, obviously we can do a much better job with that on the retail front. It all kind of comes back to driving strong brands, which makes everything else work, but we missed the mark on lining up a lot of our execution at retail with some of our key brand programs and so forth.

These are fixes that we can make. We are obviously making progress on innovation and we will get some of these other things sorted, I assure you. The competitive environment is always going to be there; this stuff we need to be doing a better job at.

Kevin Farr *- Mattel, Inc. - CFO*

I think the organizational change where we have appointed Richard last year as head of all brands and then we have Tim Kilpin being the commercial officer, I think that alignment will help us execute on bigger and better ideas in 2015 across the globe. So I think that's also going to help us.

Mike Swartz *- SunTrust Robinson Humphrey - Analyst*

Then, Kevin, just switching over to currency, I know you've put out kind of -- or put the rule of thumb in the slide deck, but help us understand does that currency impact include the impact of any hedging? And maybe remind us what your hedging policy is on currency.

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Kevin Farr *- Mattel, Inc. - CFO*

It does include hedging to a certain extent with respect to -- as we look forward, the rule of thumb is a high-level calculation. And when we look at our hedging strategy, we usually hedge 12 to 18 months looking forward and our goal is really to take volatility out of the P&L with respect to hedging, because we don't know whether foreign currency is going to strengthen or go down. So our target over that 12- to 18-month period is about 50%.

And really the key -- some of the key currencies that you need to really focus in is on euro, on the peso, and the Brazilian real.

Mike Swartz *- SunTrust Robinson Humphrey - Analyst*

Okay, great. Thanks a lot.

Operator

Stephanie Wissink, Piper Jaffray.

Maria Vizuete *- Piper Jaffray & Co. - Analyst*

Thanks for taking our question. This is actually Maria Vizuete on for Stephanie. We just have a couple quick questions. Just wondering if you could talk a little bit about the strategy of utilizing trade programs versus the impact on margins, both in the quarter and the strategy longer term.

Kevin Farr *- Mattel, Inc. - CFO*

With respect to trade programs, again as we looked and planned for 2014 we were facing some issues with losing shelf space. Basically in the second half of the year we are really focused in on in-aisle displays and promotional ads and promotional programs. Then when we see we didn't have the POS momentum that we needed, we really used additional trade programs to sell-in and try to sell-through our product in the holiday season, where people were in store looking for toys.

So with regard to the trade programs, as Chris said, it wasn't as effective as we wanted it to be, but again as we look at 2015 we are going to look at what worked and basically try to do more of what worked in 2015.

Maria Vizuete *- Piper Jaffray & Co. - Analyst*

Thank you, that's very helpful. Then just looking at the American Girl performance, can you just talk a little bit about what the declines were tied to?

Chris Sinclair *- Mattel, Inc. - Chairman & Interim CEO*

Could you repeat that, Maria, please, on American Girl?

Maria Vizuete *- Piper Jaffray & Co. - Analyst*

Yes, just looking at American Girl, the declines there, could you talk about what maybe the underperformance was tied to?

Kevin Farr *- Mattel, Inc. - CFO*

With American Girl I think, as we said, I think Frozen impacted our doll portfolio in total and we also think it impacted American Girl. There were two principal drivers of AG's decline in the last two quarters.

First, it was very competitive in the doll environment, as I said, and that primarily impacted the My AG product line. Second we did have a new BeForever launch. It is promising, but it came out late.

What are we doing about it? We had a great Girl of the Year. Our stores are good and what we need to do is really reassert American Girl's strong point of differentiation, particularly in the My AG product line.

And also then we are building off of the continued success of Girl of the Year product lines. Our new doll is off to a good start in 2015. And we continue to work on our retail expansion, particularly outside the US and Canada. We do have a new partnership in Mexico.

So you are going to see a lot of innovation and also some differentiation for My American Girl at New York Toy Fair in a couple of weeks.

Maria Vizuete *- Piper Jaffray & Co. - Analyst*

Great, thank you so much and best of luck.

Operator

Greg Badishkanian, Citigroup.

Greg Badishkanian *- Citigroup - Analyst*

Great, thanks. If you look at -- just from a very high level you mentioned some issues that impacted you for the fourth quarter and for the full year. Is it one or two things that you could have done differently, or is it just a lot of smaller execution issues across the board that was the problem?

Chris Sinclair *- Mattel, Inc. - Chairman & Interim CEO*

Greg, I don't want to prejudge it completely at this point, but I do think it was a host of issues starting with the brand innovation and branding programs we had on our major items. But we also had a lot of alignment and execution issues that went along with that.

So we are focused, I think as I said at the beginning, on a number of priorities to reignite things, but largely it is hitting some bigger things and getting those right than it is a lot of small execution issues.

Greg Badishkanian *- Citigroup - Analyst*

Okay. Second question, just with retail inventory; I just want to make sure I understand it properly. So retail inventories seem like you have reduced those pretty significantly. Maybe you have a little bit in Europe and LatAm that you have to -- there is some pockets that are higher than you would like.

When we look at the first half of 2015 compared to 2014, the fact that you had to reduce inventories so significantly last year, is that going to be a tailwind for you this year because you won't have to reduce it as much as you did last year?

Kevin Farr *- Mattel, Inc. - CFO*

Again, I think we're in a better position coming into 2015. Again, our POS trajectory isn't where we would like it to be and then, finally, I think are owned inventories are a little bit higher than desired. But we are better than last year.

Greg Badishkanian *- Citigroup - Analyst*

Okay. And you're not -- you don't want to quantify the tailwind, do you?

Kevin Farr *- Mattel, Inc. - CFO*

No.

Greg Badishkanian *- Citigroup - Analyst*

Okay, all right.

Chris Sinclair *- Mattel, Inc. - Chairman & Interim CEO*

That's good, right?

Greg Badishkanian *- Citigroup - Analyst*

Yes, thanks.

Operator

Eric Handler, MKM Partners.

Eric Handler *- MKM Partners - Analyst*

Yes, thanks for taking my question. I actually got two questions for you. First, quickly on your cash. What percentage of your cash is onshore versus overseas?

And then secondly, just digging into Fisher-Price. Fisher-Price revenue is down 25% from its peak in 2007 and that's even after you layer in the HIT Entertainment acquisition in 2012. And I just wondered, given how fragmented Fisher-Price is, does it make sense to be in all those segments that it's in? Might you be better off and get higher returns on capital if you sold off pieces of Fisher-Price that have just been in perpetual decline for the last five to seven years?

And along those lines when you look at HIT Entertainment is Thomas a growing brand? And when you look at the other brands within the HIT Entertainment portfolio, they had a pretty deep portfolio when you acquired them. It seems like you've been under utilizing some of those brands. Might it be better to sell off to an entertainment company some of those brands as well?

Kevin Farr *- Mattel, Inc. - CFO*

Okay, so with respect to Fisher-Price, I think we do have certain segments that we play in and I think we like all of the segments. And we have been making progress with this child development angle and approach and focus. And with regard to our Baby business, which accounts for almost half of the sales, we have seen positive POS.

With respect to where the issue is, it's really in the preschool area, where we struggled in 2014 and prior with regard to playsets like Little People and Imaginext. We do like that category. It is probably -- from a global perspective preschool is the biggest category in infant, preschool. We have historically been strong there. I think we just need to strengthen our brands, as Chris has said, and also create more innovative product in that space.

Then Fisher-Price Friends, again, is great with respect to when we have good license properties and they're strong. There is sort of a cycle that you go through from time to time and this year it wasn't as strong as we would like it to be. But we do like partnering with companies like Disney and Nickelodeon to really drive toys with their great intellectual property.

Then, finally, Thomas is a great preschool property. We think we have got a lot of opportunities with regard to Thomas, with regard to building that brand, creating more compelling product around that brand.

It is doing well on a global basis, particularly in international. When we looked at international and we looked at the fact that the business for Thomas was about 75% in the US, 20%, 25% outside the US, principally in five markets around the globe, all in English-speaking countries, we think there is a huge opportunity for us to grow Thomas globally. And we were very pleased this year to see us start to gain traction after building awareness for a couple of years.

We continue to look at other things in the HIT portfolio. Next up I think is Bob the Builder. We are working on content for that. We are looking to launch that later in 2015 or early 2016, and we are looking at rebuilding that brand. Many years ago Bob the Builder was actually bigger than Thomas, so we think that is a great opportunity for us.

With regard to cash offshore, I don't have it at my fingertips. We do have cash in the US as well as cash offshore. I would just have to say that we can get at the cash when we need it, where we need it. That isn't a problem from the perspective of our liquidity and also our ability to pay dividends or do share repurchases or do acquisitions.

Eric Handler *- MKM Partners - Analyst*

Great, thank you very much.

Operator

Jim Chartier, Monness, Crespi & Hardt.

Jim Chartier *- Monnes, Crespi, Hardt & Co. - Analyst*

Good morning. You talked about believing that your long-term gross margin goal of 50% remains reasonable. You did not comment on your near-term goal, which I think as recently as the October investor day you thought was the low to mid 50% range.

Can you just give us an update there? If that has changed, just talk about the puts and takes behind that. Thank you.

Kevin Farr *- Mattel, Inc. - CFO*

Again, I think -- you know we don't give guidance but we do continue to believe our long-term gross margin objective of about 50% is reasonable. With respect to commenting on the near term, as Chris mentioned, over the next two months we are going to evaluate all aspects of the business. So, again, I'm not going to comment on near-term with regard to gross margins.

Jim Chartier *- Monnes, Crespi, Hardt & Co. - Analyst*

Okay. Then is it fair to say that the Funding our Future initiative is primarily an SG&A-related opportunity versus gross margin?

Kevin Farr *- Mattel, Inc. - CFO*

Well, I think as we talked about it last October, we really said there's a couple of parts on it. It's more focused than OE 3.0 was on SG&A, so we said with regard to we've got a goal of $250 million to $300 million of savings under this new program over the next two years. We said about $100 million of that would relate to global supply chain, which is principally going to improve our gross margins, and then the other $150 million to $200 million is again with regard to SG&A.

Jim Chartier *- Monnes, Crespi, Hardt & Co. - Analyst*

Great, thank you.

Drew Vollero *- Mattel, Inc. - SVP Corporate Strategy & IR*

Operator, we have time for one more question.

Operator

John Taylor, Arcadia Investments.

John Taylor - ***Arcadia Investment Corporation - Analyst***

Good morning. Thanks for taking my question. I have two I guess.

One, Kevin, so we went through a period of rising oil prices there for a long time, which put pressure on gross margin. I wonder if you could talk about what the outlook for the next year or two might be if we stabilize somewhere in here. That's the first question.

Then I wonder, in talking about the doll portfolio -- so we are looking at the sunset of your Disney Princess license at the end of next year and I'm wondering how you are likely to manage the flow or the cadence of that as you approach the end of that particular thing. And I guess the third question is I think a lot of us would -- it would be nice to have a sense of how big that Princess business might have been in 2014 so we can start to think about what kind of gap there might be down the road, thank you.

Kevin Farr - ***Mattel, Inc. - CFO***

I think with regard to our costs, there's a basket of costs and I think as we look forward oil is certainly a tailwind, but we also have currency being a headwind. So, overall, we continue to look at this volatility in commodity prices and look at what our pricing is going to be for 2015, and we are working with retailers due to that recent volatility.

With regard to Disney Princess, I think we've talked about that before, J.T., and that has roughly been a $300 million business over the last several years. It's more than that in 2014 due to the strength of Frozen and we are really going to be opportunistic to maximize that opportunity in 2015. As we look at 2016, we know girls and we are working quite hard on strategies to launch new doll segments to fill that gap.

John Taylor - ***Arcadia Investment Corporation - Analyst***

Great, thank you.

Drew Vollero - ***Mattel, Inc. - SVP Corporate Strategy & IR***

Thank you. There will be a replay of this call available beginning at 11:30 AM Eastern Time today. The number to call for the replay is 404-537-3406 and the passcode is 61570566. Thank you for participating in today's call.

Operator

Thank you, ladies and gentlemen, that does conclude today's conference. You may all disconnect and, everyone, have a great day.