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Siena Market Line
4th week of November 2015

Mattel Inc.
MAT

Analyst: Kyle Ritchie
Sector: Consumer Discretionary

BUY on MAT

Price Target: $30.71

Key Statistics as of 11/21/15

Market Price:	$24.54
Industry:	Toy Manufacturing
Market Cap:	$8.3 B
52-Week Range:	$19.45 - $31.91
5 Year Beta:	.94

Thesis Points:

- Ability to sustain leading market share
- Historically proven to create shareholder value
- Improving margins

Company Description:

Mattel Inc. is an American multinational toy manufacturing company that designs, manufactures and markets a range of toy products worldwide. Mattel is well-known for offering toys along with board games and puzzles under some of the most iconic brands in the toy industry. These brands include Fisher-Price, Barbie, Hot Wheels, Matchbox, Max Steel, Disney Planes, CARS, WWE Wrestling and Toy Story. The company operates in three segments: North America, International and American Girl. Mattel Inc. sells its products directly to consumers via its catalog, Website, and proprietary retail stores as well as direct retailers which include stand-alone toy stores, chain stores, department stores and various retail outlets. The company was founded in 1945 by Harold "Matt" Matson, Ruth and Elliot Handler and is now headquarter in El Segundo, California.

Thesis

Mattel Inc. is a world-class innovator and leading competitor in the toy industry. The company has over 70 years of experience in this industry which comes with a timely understanding of the ever-changing consumer trends. What has had the largest impact on this company in recent years is the major transition from the "physical play to the digital play." Despite the impact from this transition, Mattel has historically proven its ability to innovate and satisfy its customers. The company launched a cost-savings program in late 2008 that has generated over $550 million in gross savings. Prior to 2014, the result of this program is demonstrated in the company's Gross Profit, EBITDA and Net Income margins which had been consistently improving year over year since the recession in 2008. Mattel Inc. is certain to have a tremendous rebound from these "digital play" pressures. The current low price of this company's stock along with the upcoming holiday season poses an opportune time to BUY for investors.

Industry Outlook

According to the NPD group, a credible market research company, global toy sales are up 7% for the first nine months of the year. The upcoming holiday season also accounts for a major portion of toy manufacturers annual retail sales. Specifically for Mattel, seasonal sales historically represented roughly 50% of the company's retail sales. In regards to 2016 and 2017, growth in the toy industry is expected to steadily increase. The impact of the "digital play" is a major factor of the toy industry growth. 3D printing has also become an important factor for the toy industry. Mattel recently announced an exclusive partnership with Autodesk, the world leader in 3D design software. While US sales data from 2015 has not been released yet, the popular traditional toy categories that have seen notable growth from 2013 into 2014 include: Action Figure/Accessories at 10%, Building Sets at 13%, Games/Puzzles at 10% and Youth Electronics at 10%. Due to Mattel's international presence the impact of the strong dollar has hurt the company's revenues and profits. Mattel's popular products that are selling well in the US include Hot Wheels and Minecraft toys.

Porter's Five Forces

Bargaining power of suppliers: **LOW**

Toy companies are constantly purchasing a wide range of raw materials that are inputs in manufacturing toys. There are various sources of these raw materials and the fact that toy manufacturers are purchasing quantities on such a large scale gives their supplier very little bargaining power.

Bargaining power of customers: **HIGH**

Mattel's customers include not only its consumers at various points of sale but also and more importantly the number of retailers that shelve its products. These retailers require lead time and reasonable prices to ensure sales.

Threat of substitutes: **MEDIUM**

There will always be alternatives to purchasing toys for children. The other obvious forms of entertainment include video games and books.

Existing rivalry: **HIGH**

The toy industry revolves around constant innovation. The primary obstacle that competitors in this industry are faced with is producing the most popular toy at a low cost. Customers can also substitute a new toy that may have high expectations for an older toy that is already known to be popular.

Barriers to Entry: **LOW**

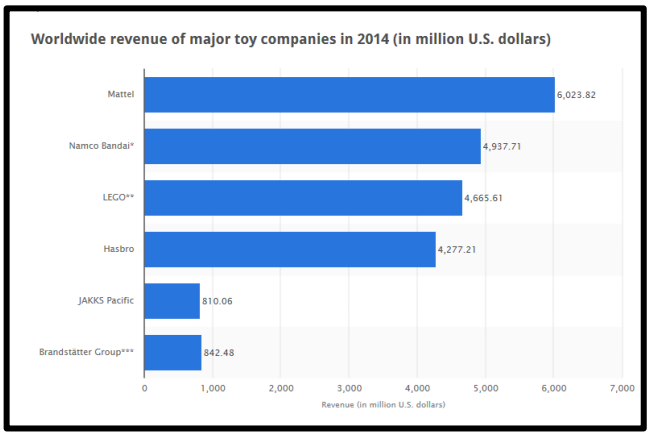
There are no significant barriers to entry in the toy industry. As previously mentioned, competition is based primarily upon the ability to design and develop new toys. A popular idea requires a license and/or trademark to enter the market and become successful.

Leading Market Share

Mattel's direct competitors include Namco Bandai, LEGO, Hasbro, JAKKS Pacific and Brandstatter Group. To emphasize Mattel's position in this

market, the following chart illustrates the company's

performance in comparison to its closest competitors (the aforementioned companies respectively) in 2014.



Mattel Inc. is and has been the leader in the toy industry for several years maintaining an estimated 28% market share. The drivers behind Mattel's success is their ability to consistently innovate, utilize/expand its iconic brand names and improve its internal operations. Due to this transition from the "physical play to the digital play," Mattel and other large toy manufacturers are having to realign their product development to online games. Mattel recently announced an exclusive partnership with Autodesk, the world leader in 3D design software. 3D printing has become a major part in the toy industry which will allow Mattel to decrease their operating costs for years to come. Mattel also announced another exclusive partnership with Quirky, an invention platform that connects inventors with companies that specialize in a specific product category. This partnership will certainly drive innovation for the company.

Consistent Value Creation

An important indicator of a company's performance is their ROIC/WACC ratio. What this ratio demonstrates is how strategically a company chooses to invest its capital. If a company's return on invested capital exceeds its weighted average cost of capital, they are ultimately creating shareholder value. The company is expanding its business by investing in profitable ventures and receiving a higher yield than its cost of capital. Mattel has been wisely investing its capital for many years. As you can see in the

following table, the five-year average ROIC/WACC ratio for Mattel is 1.98.

	2010	2011	2012	2013	2014	
ROIC	13.4%	13.2%	14.0%	14.4%	9.7%	
WACC	6.9%	6.3%	6.0%	6.8%	7.0%	5-Year Average
ROIC/WACC	1.96	2.11	2.32	2.13	1.40	1.98

Improving Margins

Mattel launched its cost-savings program in late 2008 which has generated over $550 million in gross savings. The table below illustrates from 2008-2013 how this program has influenced the company's Gross Profit, EBITDA and Net Income margins.

Gross Profit, Adj	2,684.4	2,714.7	2,955.0	3,145.8	3,409.2	3,478.9
Margin %	45.4	50.0	50.5	50.2	53.1	53.6
EBITDA, Adj	713.9	964.9	1,085.5	1,217.3	1,357.1	1,383.5
Margin %	12.1	17.8	18.5	19.4	21.1	21.3
Net Income, Adj	379.6	541.3	696.4	769.3	871.4	908.0
Margin %	6.4	10.0	11.9	12.3	13.6	14.0

The cost savings program has allowed Mattel to notably expand its margins which demonstrates management's ability to improve its operations. Unfortunately, when comparing 2014 to 2013 the Gross Profit, EBITDA and Net Income margins fell 4%, 6% and 6% respectively. The company's disappointing performance in 2014 was due to inconsistent product development and global retail execution. Also, the downward pressures from the "digital play" is requiring a more technical product development which Mattel is currently making adjustments for (mentioned in the section Leading Market Share). When analyzing these margins the major takeaway is that this company has proven its ability to improve its operations. One disappointing year does not offset this company's decades of experience and ability to expand.

Valuation

The valuation of Mattel Inc. is based on a valuation computed by a pro forma using a discounted cash flow method with a main focus on return on invested capital. Attached is an overview of the inputs, assumptions and results used in valuing this company. When valuing Mattel given its current state, a conservative approach has been applied. Given the fact that this company will most likely be expanding its product line due to the drastic trend, a 10-year period to convergence has been used. Analysts are split 40%-60% between HOLD and BUY. The average target price among the analysts who consider Mattel a promising buy is $31. The financial metrics

of the company were made to converge to the industry. A 6% market risk premium was used in this valuation given the stability of the industry along with an average decay in revenue growth for its reversion to the continuing period. The pro forma calculated a lower-bound intrinsic value of $30.55 with a 1-year target of $30.71

Conclusion

After a thorough analysis, it is clear that Mattel is undervalued. This company has proven to create value to its shareholders and has dominated the toy industry for decades. Coupled with its iconic brand names and world-class innovation, it will not be long before this company's stock reverts back to its true value. The company certainly took a hit over the past year but this only poses an opportune time to BUY for investors.

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Mattel, Inc.	MAT	Analyst	Current Price	Intrinsic Value	Target Value	Divident	1-y Return: 31.32%	BULLISH
		rPig (1/2 man, 1/2 bear,	$24.54	$30.55	$30.71	6%		

General Info	
Sector	Consumer Discretionary
Industry	Leisure Products
Last Guidance	October 15, 2015
Next earnings date	January 26, 2016

Market Data	
Enterprise value	$10,239.06
Market Capitalization	$4,449.48
Daily volume	0.22
Shares outstanding	339.35
Diluted shares outstanding	339.55
% shares held by institution:	26.01%
% shares held by insiders	0.30%
Short interest	21.23%
Days to cover short interes	12.84
52 week high	$31.69
52-week low	$19.45
5y Beta	0.94
6-month volatility	30.88%

Peers	Market Cap.
Hasbro Inc.	$9,407.83
JAKKS Pacific, Inc.	$146.23
Brunswick Corporation	$4,376.54
LeapFrog Enterprises Inc.	$45.43
Polaris Industries Inc.	$6,914.51

Current Capital Structure	
Total debt/Common Equity (LTM)	0.48
Cost of Borrowing (LTM)	3.83%
Estimated Cost of new Borrowing	5.53%
Altman's Z	3.56
Estimated Debt Rating	BB
Current levered Beta	0.75
LTM WACC	5.87%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Sinclair, Christopher	Chairman, Chief Executive Officer, Mer	$306,486	$305,758	$316,248
Dickson, Richard	President and Chief Operating Officer	$0	$0	$4,139,118
Farr, Kevin	Chief Financial Officer	$6,910,059	$3,305,565	$3,973,447
Normile, Robert	Chief Legal Officer, Executive Vice Pre	$4,736,913	$2,145,606	$2,754,395
Vollero, Drew	Senior Vice President of Investor Relat	$0	$0	$0
Gros, Richard	Chief Human Resources Officer and Ex	$0	$0	$0

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS	Standard Error of "Surprise"
Last Quarter	-5.10%	-13.09%	-11.25%	2.42%
Last Quarter-1	-0.37%	5.85%	NM	3.11%
Last Quarter -2	2.37%	-61.20%	NM	31.79%
Last Quarter -3	0.21%	-9.26%	-20.00%	5.84%
Last Quarter -4	-7.13%	-3.98%	-3.92%	1.06%
Standard error	1.8%	11.7%	4.6%	4.70%
Standard Error of Revenues prediction	1.8%			
Imputed Standard Error of Op. Cost predicti	11.5%			
Imputed Standard Error of Non Op. Cost pre	NM			

Industry Outlook (Porter's Five Forces)

Bargaining Power of Suppliers (100th Percentile), Bargaining Power of Customers (100th Percentile), Intensity of Existing Rivalry (100th Percentile), Threat of Substitutes (100th Percentile), Threat of New Competition (100th

Proforma Assumptions

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All base year ratios linearly converge towards the Industry ratios over an explicit period of 10 years

General Assumptions	
Money market rate (as of today)	0.37%
Risk-Free rate (long term estimate)	2.93%
Annual increase (decrease) in interest rates	0.1%
Marginal Tax Rate	37.5%
Country Risk Premium	6.0%

Forecast Year	Revenue Growth Forecast	Revenue ($) Forecast
LTM		$5,636.84
FY2015	-1.0%	$5,646.47
FY2016	1.0%	$5,716.47
FY2017	8.0%	$6,186.31
FY2018	7.2%	$6,637.34
FY2019	6.5%	$7,073.28
FY2020	5.3%	$7,495.32
FY2021	5.3%	$7,900.70
FY2022	4.7%	$8,286.66
FY2023	4.2%	$8,651.14
FY2024	3.6%	$8,992.88
Continuing Period	3.0%	$9,315.21

Items' Forecast Assumptions

	Base year (LTM)	Convergence period (Industry)	djustment per yea
Operating Cash/Rev.	0.00%	0.00%	0.0%
NWV/Rev.	28.31%	16.59%	-1.2%
NPPE/Rev.	12.66%	11.10%	-0.2%
Dpr/NPPE	31.72%	28.53%	-0.3%
NOPAT MARGIN	11.06%	8.17%	-0.3%
Op. Exp./Rev.	82.00%	82.00%	0.0%
SBC/Rev.	0.93%	0.71%	0.0%
Rent Exp./Rev.	2.12%	0.00%	-0.2%
R&D/Rev.	3.86%	2.82%	-0.1%
E&D/Rev.	0.00%	0.00%	0.0%
SG&A/Rev.	30.00%	20.93%	-0.3%
ROIC	9%	19.64%	1.02%
EV/Rev.	1.57x	1.26x	-0.03x
EV/EBITA	10.43x	9.66x	-0.08x
Debt/Equity	48%	58%	1.0%
Unlevered beta	0.57	0.80	0.02
Dividends/REV	9%	3%	-0.6%

Other Assumptions

Tobin's Q	80%
Excess cash reinvestment	Cost of capital
Other claims on the firm's asse	$0.00

Capitalization

100% of all rent expenses are capitalized and amortized 'straightline' over 10 years
100% of all R&D expenses are capitalized and amortized 'straightline' over 10 years
E&P expenses are not capitalized
75% of all SG&A expenses are capitalized and amortized 'straightline' over 2 years

Valuation Focus

DCF Valuation	100%
Relative valuation	0%
Distress Valuation	0%

Monte Carlo Simulation Assumptions

Revenue Growth deviation	Normal (0%, 1%)
Operating expense deviation	Normal (0%, 1%)
Continuing Period growth	Triangular (5.82%, 6%, 6.18%)
Country risk premium	Triangular (2.91%, 3%, 3.09%)
Intrinsic value σ(ε)	$0.09
1-year target price σ(ε)	$0.10

Valuation

Forecast Year	ROIC	WACC	Invested Capital	Implied Enterprise Value	Claims on Assets and Dilution	Shares Outstandin	Price per Share
LTM	9.5%	5.9%	$7,280.32	$14,153.20	$3,403.26	339.35	$30.53
FY2015	9.2%	6.1%	$6,958.29	$14,020.91	$3,097.03	339.35	$30.69
FY2016	9.5%	5.7%	$6,706.30	$13,901.93	$2,976.97	339.35	$30.81
FY2017	10.6%	5.8%	$6,843.94	$14,138.00	$2,982.75	339.35	$31.06
FY2018	11.0%	6.0%	$6,964.81	$14,353.48	$2,946.42	339.35	$31.38
FY2019	11.5%	6.2%	$7,069.48	$14,554.53	$2,863.38	339.35	$31.83
FY2020	11.9%	6.5%	$7,161.97	$14,743.75	$2,746.23	339.35	$32.39
FY2021	12.3%	6.7%	$7,242.57	$14,944.83	$2,575.64	339.35	$33.14
FY2022	12.6%	7.0%	$7,312.99	$15,147.43	$2,348.99	339.35	$34.10
FY2023	13.0%	7.3%	$7,375.99	$15,366.87	$2,064.73	339.35	$35.29
FY2024	13.3%	7.6%	$7,435.05	$15,614.03	$1,722.04	339.35	$37.17
Continuing Period	13.6%	8.5%	$3,873.77				

Monte Carlo Simulation Results

The 3σ(ε)-adjusted intrinsic value is $30.55; the 3σ(ε)-adjusted target price is $30.71; and the analysts' median target price is $26.64

Sensitivity Analysis

Revenue growth variations account for 95.9% of total varianc
Risk premium's variations account for 2.5% of total variance
Operating expenses' variations account for 1.4% of total varia
Continuing period growth variations account for 0.2% of tota