

Spin Master Corp.

Second Quarter 2024 Results Conference Call

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CORPORATE PARTICIPANTS

Sophia Bisoukis

Spin Master Corp. — Investor Relations

Max Rangel

Spin Master Corp. — Global President and Chief Executive Officer

Mark Segal

Spin Master Corp. — Chief Financial Officer

CONFERENCE CALL PARTICIPANTS

Martin Landry

Stifel — Analyst

Luke Hannan

Canaccord Genuity — Analyst

Drew Reynolds

RBC — Analyst

Brian Morrison

TD Cowen — Analyst

Adam Shine

National Bank — Analyst

David McFadgen

Cormark Securities — Analyst

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Spin Master Corp. Second Quarter 2024 Results Conference Call.

At this time, all lines are in a listen-only mode. Following the presentation we will conduct a question-and-answer session. If at any time during the call you require immediate assistance, please press star, zero for the Operator. This call is being recorded on Wednesday, July 31, 2024.

I would now like to turn the conference over to Sophia Bisoukis, please go ahead.

Sophia Bisoukis — Investor Relations Spin Master Corp.

Thank you, Joelle, and good morning. Welcome to Spin Master's Financial Results Conference Call for the Second Quarter 2024.

I'm joined this morning by Max Rangel, Spin Master's Global President and CEO, and Mark Segal, Spin Master's Chief Financial Officer.

For your convenience, the press release, MD&A and interim consolidated financial statements are available on the Investor Relations section of our website at spinmaster.com and on SEDAR+.

Before we begin, please note that remarks on this conference call may contain forward-looking statements about Spin Master's current and future plans, expectations, intentions, results, level of

activity, performance goals or achievements and any other future events or developments. Forward-looking statements are based on information currently available to Management and on estimates and assumptions made based on factors that Management believes are appropriate and reasonable in the circumstances. However, there can be no assurance that certain estimates or assumptions will prove to be correct.

Many factors could cause actual results to differ materially from those expected or implied by the forward-looking statements. As a result, Spin Master cannot guarantee that any forward-looking statements will materialize, and you are cautioned not to place undue reliance on these forward-looking statements. Except as may be required by law, Spin Master has no obligation to update or revise any forward-looking statements, whether because of new information, future events or otherwise. For additional info on these assumptions and risks, please consult our cautionary statements regarding forward-looking information in our earnings release dated July 30, 2024. Please note that Spin Master reports in U.S. dollars and all other amounts to lead today are expressed in U.S. currency unless otherwise noted.

I would like to turn the call over to Max.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Good morning, and thank you, Sophia. Thanks for joining us today.

We are pleased to report that our second quarter financial results were within our expectations, and we are maintaining our full year guidance. As expected, our Q2 revenue declined 2.1 percent to \$412

million due to continued pressure on consumer spending, which impacted Toy gross product sales and in-game purchases within Digital Games. Toy gross product sales were down to \$384.7 million, a decrease of 1.4 percent versus 2023. Sales were lower for two primary reasons. First, due to shipments moving from Q2 to Q3. Second, as a result of us lapping the initial shipments in Q2 last year related to the launch of the second PAW Patrol movie.

Melissa & Doug had a strong quarter with revenue of \$43.3 million as we invested in in-store programs and marketing support. We're pleased with the pace of our integration efforts and are realizing cost synergy opportunities across many different areas. Our commercial teams continue to collaborate to help drive penetration of Melissa & Doug products at retail, primarily in Mexico, Canada and Europe, where the brand is significantly underrepresented.

Consumer spending across discretionary categories remains challenged. According to Circana, G11 POS was down 4.7 percent in Q2 while Spin Master was down 8.1 percent, and Spin Master combined with Melissa & Doug in 2024, was up 11.9 percent. We maintained our position as the fourth largest manufacturer globally in Q2. Our retail inventory, excluding Melissa & Doug is down just over 5 percent.

The average selling price of our U.S. retail inventory is down 8 percent compared to 2023 as we have increased the mix of lower priced items. More of this inventory is in our key brands with strong POS as well as new brands. All-in-all, U.S. inventory is in much healthier state than last year. In Europe, retail inventory is down nearly 7 percent and in an equally healthy position. Melissa & Doug retail inventory in the U.S. is down double digits versus 2023. All these bodes well for toy sales in the back half of 2024.

Let me review performance by category. Beginning with Infant, Toddler and Preschool, we finished Q2 as a number two corporate manufacturer in the G11 per Circana, up from number three previously, and owing to the inclusion of Melissa & Doug. We had 2 of the top 10 items for Q2 and year-to-date per Circana. The lower price point items within our line are performing the best, reflecting current consumer shopping trends.

Our PAW Patrol jungle pops vehicle line was the number one new item in the Infant/Toddler/Preschool Super category for second quarter 2024. Spin Master was the number one corporate manufacturer and property in the Preschool Toys segment year-to-year in Q2 and year-to-date. PAW Patrol is the number one preschool toy property in the G11 for the 14 straight quarter dating back to the first quarter in '21.

We anticipated some softness in PAW this year following the second movie and are making incremental investments in retail programs and marketing in Q3 and Q4. We are also continuing our efforts to grow viewing minutes across traditional and non-traditional platforms to further drive Toy demand. We are seeing strong international growth for Gabby's Dollhouse. DreamWorks has a number of experiential events planned in the U.S., combined with more content releases on Netflix in advance of the Gabby Movie launch on September of 2025.

Melissa & Doug had a strong quarter in shipments, and saw improved POS performance. Low retail inventory levels at major U.S. retailers are helping to drive replenishment orders for M&D earlier in the cycle, which bodes well for the back half of 2024. Melissa & Doug gained market share in the Arts & Crafts

category in G11 in the second quarter and year-to-date, driven by the Sticker Wow launch, and Melissa & Doug also grew share in puzzles in the U.S.

After the quarter, Melissa & Doug had a strong organic sales growth over last year during Amazon Prime Day with U.S. POS up 40 percent. This performance was driven by a focus on lower price point items in the range which resonated well in the current environment. M&D is launching Blockables in the fall, an exciting new line of wood-based construction toys that allows multisensory play and which fits well into the growth of the construction and building sets category.

Finally, Melissa & Doug will have two items within our total Ms. Rachel assortment, which has just started shipping for this fall. Speaking of Ms. Rachel, we continue to strengthen our presence in early childhood toys with the launch of the new Spin Master, and as I just said, Melissa & Doug toy line set to launch in October. This is one of the most anticipated toy launches of the fall with pent-up demand for the property continuing to grow as evidenced by the strong early performance of the Ms. Rachel book presale and initial Pajama launch earlier in the year.

With our huge YouTube viewership, Ms. Rachel has captivated and connected with children and parents. Our toy collection is inspired by the learning approach loved by parents in her show. We are thrilled with the line, and retailers have responded very positively. In dolls and interactive, we have a host of new introductions leading into the fall. We released our teaser for our latest innovation in Hatchimals. Something magical is coming on Hatchimals Day, which is October 4, when we will have the full reveal of our reimagined Hatchimals with new features and expanded interactions for a new generation of kids. Since first launching Hatchimals in 2016, over 14 million of the big eggs have been sold.

The Unicorn Academy toy line hit shelves in June, timed with the new content of Netflix and early POS reads show very encouraging performance. We have gained share in the youth electronics category with continued popularity of Bitzee and the introduction of two new iterations, Bitzee Magicals and Disney Bitzee. Adding to our growth is Punirunes, the squishy digital pet from Japan in partnership with Takara Tomy. While these items just started to sell in June, they are off to a very strong start.

We increased our market share in Arts & Crafts in the second quarter and year-to-date. According to Circana, Kinetic Sand grew POS 6.6 percent in the second quarter compared to a 12 percent decline in the Arts & Crafts super category. Kinetic Sand was a number two brand, up from number three in 2023.

Monster Jam continues to have an excellent year, and our POS grew over 33 percent in the second quarter and over 32 percent year-to-date per Circana. Monster Jam was the number one license in the second quarter and year-to-date in the super category and overall was the number two property year-to-date in the vehicles super category. With families prioritizing experiences, the Monster Jam live shows are creating a core of loyal fans. This fall, a new line of monster trucks from Marvel, featuring popular superheroes, including Spiderman and a new RC vehicles collection and playsets will launch, and this will help the brand tap into an expanded fan base and encourage them to grow their collection.

Our Entertainment Creative Center had another solid quarter with revenue increasing by over 7 percent. We released Chapter 2 of Unicorn Academy Season 1 on Netflix globally. It quickly shot to the top spot for kids and families in over 90 countries. In addition to the content on Netflix and off-platform on YouTube and TikTok, our team is also rolling out licensed consumer products for the franchise, which now has over 35 licensed partners across lifestyle goods, publishing and accessories, with many more to

be announced this fall. I am very pleased to announce that we just completed our deal with Netflix for further 16 episodes, which will give us two more seasons in 2026.

PAW Patrol continues to rein as a top preschool show. Total gross view in minutes for the PAW Universe were up 24.5 percent in the quarter. In May, we launched a PAW Patrol short-form content series on YouTube as part of our strategic alliance with Moomba to capture additional viewing minutes and deepen engagement with preschoolers. This August, we have several exciting premieres planned for the PAW Universe, including a special episode of Rubble & Crew with Aaron Judge, as well as PAW Patrol Rubble & Crew crossover event. In addition to short-form content the team is in production of Season 11.

For 2025, the team is producing several TV specials, including a holiday special, which will give families a chance to co-view during the season with their favourite pops, leading to the reimagined third movie in the fall of 2026.

Within our Digital Games Creative Center, mobile gaming spending slowed at the industry level in Q2 and in-app purchases within Toca Life World experienced, a similar decline. Overall, Q2 Digital Games revenue declined by just over 14 percent. Piknik subscriptions grew in the quarter, driving higher subscription revenue validating that our model of bundling together multiple apps in an appealing offering for parents is working. PAW Patrol Academy will become part of the Piknik subscriptions bundle in Q1 of next year, which should help grow further Piknik subscriptions as well as expand the user base.

Now, despite a decline in in-app purchases in the Toca Life World brand, engagement remains near our all-time high. Monthly active users were at 61 million at the end of Q2, up 3 percent, and fans are responding positively to content drops, including our first ever artist collaboration with global superstar

Conan Grey, which launched in June. If you recall, last year, we released Spongebob, and we saw a halo effect throughout the summer. We are seeing similar trends with these strategic collaboration.

Rubik's Match, our new Match 3 game, leveraging the brand awareness of the Rubik's cube, continues to roll out in select markets, leading up to the full global release in September. The game is now available for preorder on both the App Store and Google Play.

Toca Days, our multiplayer mobile game continues to roll out on a targeted country-by-country basis, and we are gathering the learnings and feedback from players to enhance and fine-tune the experience, as we ramp up to a global release. This pace of engaged players provides us with real time KPIs and learnings to help us refine the game and maximize results when we launch on a global scale.

In closing, the quarter met our expectations from a revenue perspective, and we're confident that our innovation across toys, entertainment Digital Games has positioned us well for the second half. We are encouraged that consumer sentiment appears to be improving and that families intend to prioritize purchases that bring both joy and value for their family in toys. Even though the consumer continues to face many financial headwinds, particularly in the U.S., there are reasons to believe that the back half of the year will be positive for the toy category. Our innovations and the introduction of new licensed brands, such as Ms. Rachel, will positively impact volume in the fall.

Beyond this year, we have a strong growth potential in 2025 with new licensed properties with a full year of Ms. Rachel and the reintroduction of Dora the Explorer, the new theatrical toy lines planned for 2025, including Superman, Dragons and Gabby's Dollhouse, as well as disruptive innovation in our toy line, together with expanding Digital Games experiences to attract new players. We are in a strong

financial position, and combined with our diversified portfolio and leadership in the children's entertainment industry, we will deliver our long-term strategic and financial goals.

Before I turn over, we announced that Mark Segal, our Chief Financial Officer, has made the decision to retire in the first half of 2025. Mark originally joined Spin Master in 2001 and spent 10 years as CFO. This was an unprecedented time of expansion for Spin Master. During that time, Mark helped to build the infrastructure to enable Spin Master to continue to grow profitably through international expansion, acquisitions, partnerships and innovation. Mark left for a while, but he could not stay away and rejoined Spin Master in 2015 to lead our IPO, and help build Spin Master's internal and external capabilities as a Public Company.

Mark has steadfastly guided us forward by applying his exceptional financial leadership to preserve a strong balance sheet and generate cash flow, which in turn has helped the Company to provide a platform for our future growth ambitions. He has been invaluable advisor to me during my time at the Company, consistently demonstrating his integrity, financial discipline and commitment to our strategic goals, while also establishing a strong finance team. We are fortunate to have Mark with us as CFO into the first half of 2025. Following the transition to a new CFO, I look forward to working with Mark as a Strategic Advisor to Spin Master.

On behalf of Ronnen, Anton, Ben and the entire team, I want to thank Mark for his incredible contributions that further our leadership within the children's entertainment industry.

Now with that, I will turn it over to Mark.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Thank you, Max, and good morning.

Spin Master is a truly remarkable Canadian and global success story, and it's really been my privilege to have been part of its evolution and growth journey. As Max mentioned, I will remain as CFO throughout the 2024 yearend and help onboard a new CFO in the first half of 2025, and then look forward to continuing to contribute to Spin Master as a Strategic Advisor.

Let me now review our consolidated and creative center results with you briefly. We delivered \$412 million in revenue in Q2 across all three creative centers, including just over \$43 million from Melissa & Doug. As expected, Q2 revenue declined 2.1 percent in comparison to 2023. Adjusted EBITDA was \$53.6 million, an expected decline from last year. Adjusted EBITDA margin was 13 percent compared to 21 percent due to the increased proportion of revenue from the Toy's creative center and margin dilution from M&D where profitability is fully weighed to H2.

Our Q2 gross profit decreased by \$31.4 million to \$199.6 million and gross margin declined to 48.4 percent from 54.9 percent, primarily due to the impact of the Melissa & Doug inventory fair market value adjustment. As we explained in Q1, as part of the acquisition of Melissa & Doug, we acquired just under \$180 million of inventory, of which approximately \$66 million relates to the required fair market value step-up adjustment, representing the difference between inventory cost and net realizable value.

As this inventory is sold, a fair market value increment is then recognized in cost of sales. In Q2, this inventory fair market value adjustments included in Toy cost sales was \$24.2 million and \$44 million

year-to-date. At the end of Q2, \$21.5 million of stepped-up inventory remains on hand, which we expect to sell through in Q3.

Adjusted gross profit, which removes the impact of the M&D inventory fair market value increment, decreased by \$7.2 million to \$223.8 million. Adjusted gross margin was 54.3 percent, down 60 basis points from 54.9 percent, mainly due to product mix in the Toy creative center, partially offset by an increase in distribution revenue from the PAW Patrol movies and series in Entertainment.

Let's review each creative center's performance in a little more detail. Toy gross product sales in Q2 were down 1.4 percent, including Melissa & Doug, and down 14.6 percent excluding Melissa & Doug. As Max described, Toy gross product sales, excluding M&D, were lower than Q2 '23 for two primary reasons. Firstly, approximately \$30 million of customer orders shifted from Q2 into early Q3, most of which has already shipped. In addition, Q2 '23 included approximately \$35 million of initial shipments from the launch of the second Paw Patrol movie.

Melissa & Doug performed well in Q2, delivering Toy gross product sales of \$51.7 million, a double-digit growth rate over the same quarter in 2023. Preschool, Infant & Toddler and Plush gross product sales were flat, with a positive impact of including Melissa & Doug offset by the shift of customer orders into Q3 and the impact of lapping the \$35 million of PAW Patrol movie shipments from Q2 last year.

Activities, Games & Puzzles and Dolls and Interactive grew \$19.6 million or 17.9 percent led by Unicorn Academy, Bitzee and Kinetic Sand. Wheels & Action declined to \$25.4 million or 25 percent due to the declines in Bakugan, DC and Techtik (phon) partially offset by Monster Jam. Outdoor was up 2.8 percent to \$14.7 million.

Sales allowances in Q2 were 11.9 percent of Toy gross product sales, slightly elevated compared to 11.2 percent as we invested in M&D retail trade promotions and marketing. Excluding Melissa & Doug, sales allowances were 11.7 percent, flat to 2023.

Adjusted EBITDA in Q2 for Toys was \$20.9 million or 6.1 percent margin compared to 13.8 percent. The decrease in Adjusted EBITDA margin was driven by the inclusion of Melissa & Doug, a high proportion of administrative and marketing spend in relation to Toy revenue and lower gross margins, partially offset by lower selling expenses. In Q2, Entertainment revenue increased by \$2.5 million or 7.4 percent. We continue to see higher revenue from the distribution of the PAW Patrol movies and series. Offsetting this was a decline in production revenue from fewer content deliveries, as we were lapping the delivery of Unicorn Academy and Vida the Vet in 2023.

Adjusted operating income increased by \$3.7 million or 22.7 percent and adjusted operating margin increased to 54.9 percent from 48.1 percent. The improved margin was due to higher movie distribution revenue and fewer lower margin content deliveries this year.

Digital Games revenue declined by \$5.8 million or 14.3 percent to \$34.7 million, primarily due to lower in-game purchases in Toca Life World, partially offset by higher subscription revenue for the Piknik bundle and PAW Patrol Academy. As Max mentioned, industry-level mobile gaming spending has slowed, which has led to lower spending from monthly active user in our business. Engagement remains very high, and the number of monthly active users for Toca Life World was approximately \$61 million, a 3 percent increase sequentially and up 6 percent compared to 2023. Our focus is to both increase in-app revenue

conversion levels in Toca Life World and increase monthly recurring revenue from our active subscriber base.

On this point, subscription monthly recurring revenue, or MRR, it's a new high in June. Since we launched Piknik, we focused on getting customers to choose the bundle over individual apps. Currently, 90 percent of new activations are for the bundle, and these subscribers are staying longer, which is a big driver of the MRR increase. We are now starting to focus on getting more customers to choose annual plans over monthly plans. Our medium-term goal is to get 40 percent of our subscribers on annual plans, up from 15 percent currently.

Digital Games adjusted operating margin was 17 percent compared to 31.6 percent last year driven by the decline in revenue and higher user acquisition costs for PAW Patrol Academy and Piknik. We have seen a pickup in Digital Games revenue in July in what is typically the seasonally strongest engagement period when kids are on summer holidays.

Turning back to consolidated results, adjusted SG&A increased by \$24 million or 14.7 percent to \$187.5 million. As a percentage of revenue, adjusted SG&A increased to 45.5 percent from 38.9 percent, primarily from the inclusion of Melissa & Doug. This has resulted in deleveraging in Q2, due to the seasonality of Melissa & Doug's revenue profile, which is heavily weighted to the second half. Excluding Melissa & Doug, adjusted SG&A as a percentage of revenue was 42.6 percent compared to just under 39 percent.

Consolidated Adjusted EBITDA for Q2 was \$53.6 million compared to \$88.4 million. Adjusted EBITDA margin was 13 percent compared to 21 percent. The decrease in Adjusted EBITDA was primarily

from the Toy and digital game segments. Adjusted EBITDA, excluding Melissa & Doug, was \$60.6 million compared to \$88.4 million, a decline of \$27.8 million. Adjusted EBITDA margin, excluding Melissa & Doug, was 16.4 percent compared to 21 percent.

Adjusted net income was \$9.6 million or \$0.09 per share compared to adjusted net income of \$48.8 million, \$0.47 per share.

Looking at our balance sheet, we continue to improve our inventory position. Inventory excluding Melissa & Doug was \$145 million, down \$7 million compared to 2023. We are continuing to reduce overall inventory levels and flush the inventory subject to the fair market value step-up adjustment through the P&L.

Free cash flow in Q2 was negative \$3.6 million compared to negative \$5.9 million last year. Free cash flow increased due to higher cash generated from working capital, partially offset by higher interest paid and lower adjusted operating income. We ended Q2 with \$154.6 million in cash. Our plan to create shareholder value remains consistent. In Q2, we maintained our strong cash flow and executed our planned capital allocation initiatives. A higher dividend was implemented and our share buyback program continued, reflecting our commitment to returning value to shareholders. At the end of Q2, we had repurchased over 1.1 million shares for approximately \$25.9 million. After the quarter, we repurchased a further 318,200 shares for \$6.9 million. Please note that these dollar values for the NCIB I just discussed are in U.S. dollars, but the Canadian dollar equivalent is in the press release.

We repaid \$15 million of debt in Q2, and on a year-to-date basis, we have reduced our borrowings by \$65 million to \$460 million.

Turning now to our outlook, we are maintaining our full year guidance. We expect Toy gross product sales for 2024, excluding Melissa & Doug, to be in line with 2023. As a result of the order shift I referred to earlier, we expect Q3 to represent approximately 40 percent of full year gross product sales compared to 38 percent in 2023. As a reminder, at this point in the year, we typically have a significant portion of our Q3 orders locked in. The outlook for 2024 reflects our view that Spin Master retail inventories are in good shape, and we have a strong, innovative, deep and value-focused line. Of course, tempered by the reality that consumer behaviour is likely to continue to be volatile with five fewer shopping days leading into Christmas 2024.

We continue to expect sales allowances to be approximately 13 percent of gross product sales. Total revenue, excluding Melissa & Doug, is also expected to be in line with 2023, with lower revenue from entertainment offset by higher Digital Games revenue for 2024. In Digital Games, we have a large amount of fresh content in Toca Life World planned for the second half of 2024, a growing recurring revenue base in our subscriptions business and the full introduction of Rubik's Match in September. Note that Rubik's Match will require upfront marketing investment spend and amortization of the capitalized development costs will dilute Digital Games EBIT margin until they are fully recouped.

From a cost perspective, we are seeing some inflationary pressures on certain lines of ocean freight due to the Red Sea and a pull forward in shipments in certain industrial sectors in advance of planned U.S. tariffs on China. However, we are managing our cost base very tightly and we continue to expect Adjusted EBITDA margin excluding Melissa & Doug, to be in line with 2023.

In connection with Melissa & Doug, for 2024, we continue to expect gross product sales of between \$420 million and \$430 million, with revenue of \$370 million to \$375 million. Melissa & Doug retail inventory is in a very healthy position. From a seasonality perspective, second half revenue for Melissa & Doug will be split roughly equally between Q3 and Q4. For 2024, we continue to expect Melissa & Doug's Adjusted EBITDA margin to be approximately 19.5 percent.

The integration activities with Melissa & Doug are progressing well. We are successfully identifying cost synergies with \$1.4 million in net cost synergies realized year-to-date. We continue to expect \$6 million of net cost synergies to be generated in 2024.

A few specific outlook call outs for 2024: marketing will remain between 9 percent and 10 percent of revenue; cash interest rate paid will be around \$25 million; our consolidated effective tax rate estimate remains at approximately 26 percent; CapEx is expected to be just under 6 percent of revenue; depreciation and amortization, excluding Melissa & Doug, is expected to be approximately \$105 million, of which \$65 million will hit COGS; Melissa & Doug depreciation and amortization is expected to be approximately \$27 million.

In conclusion, we will continue to focus our capital allocation strategy on innovation, entertainment content, Digital Games and M&A. We will then return cash to shareholders through both share buybacks and dividends and we'll continue to pay down debt with residual cash. We expect to end 2024 with a net debt-to-Adjusted EBITDA ratio of approximately 0.8 times.

Overall, we remain on track to achieve our financial targets for 2024 and are confident in our ability to manage our capital effectively. We remain well-positioned strategically, financially and operationally

and are fully committed to continue to execute our strategy for long-term growth and shareholder value creation.

That concludes our prepared remarks. We will now be pleased to take questions. Operator, please open the line.

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. If you have a question, please press star, followed by the one on your touchtone phone. You will hear a three-toned prompt acknowledging your request and your questions will be polled in the order they are received. Should you wish to decline from the polling process, please press star, followed by two. If you are using a speaker phone please lift the handset before pressing any keys. One moment please for your first question.

Your first question comes from Martin Landry with Stifel. Your line is now open.

Martin Landry — Analyst, Stifel

Hi, good morning guys.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Good morning.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Good morning, Martin.

Martin Landry — Analyst, Stifel

There's a lot of noise in your results with the shipments going into Q3 with the Melissa & Doug acquisition as well. I was wondering if maybe we can take a step back and look at things a bit more higher level. Max, in your opening remarks, you're talking about your capabilities in Toys, Entertainment and Digital Games that it will allow you to deliver on your long-term financial goals. I was wondering if you could expand a little bit on what are the Company's long-term financial goals.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Martin, good morning. First of all, before we get to the financial goals for the future, we are very committed and confident to deliver this year's guidance. Okay, so let me start with that, and have started Q3 with a really positive tone. That's the start of my answer. The second thing is, we want to continue to basically grow our Toy business and beat industry growth rates. That's what we've been doing, and that's what we will continue to do. We will lean into innovation, building brands and our great and expanding license portfolio that we continue to gain from key licensors.

When it comes to Entertainment, we have now created two new IPs, and we will continue to basically bring new IPs to the Company while nurturing the IPs we just launched and let's not forget, having PAW Patrol forever.

When it turns into our Digital Games, we are very, very committed and have great confidence in continuing to build both our Toca Boca property into a very large franchise, including multiplayer game

and including novel concepts for children that come in to a digital ecosystem as social broadcasting and our subscription business, which is accelerating its subscribers from just over 300,000 about a year ago, now closing on \$0.5 million and on our way to \$1 million by next year.

We're very confident that we have all the tools in place, and let's not forget, we've brought a beautiful brand like Melissa & Doug, which has responded very well to marketing and in-store programming. We have already started Q3 with a very, very, very positive foot forward. Prime Day was a great, great example of supporting the brand fully and it has responded beautifully. We have a bright future, and I hope that helps answer the question.

Martin Landry — Analyst, Stifel

Yes. Well, maybe just a follow up on that. In the past, I believe the Company communicated that the charge for organic growth was aspirationally to grow in the mid-single digit range, and to complement that with M&A, so to bring your revenue growth in the high single digits. Also for your EBITDA margin to expand annually as Digital Games would become a larger point revenues. Is that still achievable? Is that still aspirationally your goals?

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Nothing has changed versus what you stated. I will have Mark expand, but that is what we're planning against.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Yes. Martin, as you described, if you actually look since our IPO, our gross product sales CAGR has been around 8 percent. As we said at the IPO and have continued to say, we expect our organic gross product sales growth to be in the mid-single digits range. We'll supplement that with acquisitions over time. Obviously, there will be some years of higher growth and some years of more modest growth.

The other point that we've said publicly which we continue to drive towards is that we want 20 percent of our total revenue to come from the Digital Games area as well. That's a big part of our margin goals. Our gross margin goal is to be north of 50 percent on gross margin and to be north of 20 percent on Adjusted EBITDA margins.

Martin Landry — Analyst, Stifel

Okay. That's helpful. You alluded to Q3 a little bit. Then maybe I was wondering if you could share some colour. You talked about Amazon Prime being strong for Melissa & Doug. But is there any other colour you can talk about in terms of shelf space heading into Q3 point of sale for July? Any tidbits you could share would be helpful.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Yes, absolutely. We started Q3, obviously, with well over double-digit GPS growth versus a year ago. A lot of that, obviously, part of the shipments moving forward. But importantly, when you think about Q2 POS into June, July, the Q2 POS industry down five was down eight. When you look at it sequentially. May was better than April and June was better than May. In fact, in June, we were in line with the industry

and in Europe, we were well ahead of the industry. We actually grew 3.2 percent, industry was down 2.7 percent. Into July, that trend continues, and we feel very confident.

Mark Segal — Chief Financial Officer, Spin Master Corp.

I just want to add, Martin, to your point. As we called out in the guidance, we expect our Q3 to represent a bigger proportion of sales this year than we saw in Q3 last year. That's also good news in the sense that it actually puts less pressure on Q4 for us because a lot of the shipments come in earlier, it gives us more opportunity to get replenishment orders. We feel good about that.

Martin Landry — Analyst, Stifel

Okay, thank you. Mark, congrats on your accomplishments and good luck in your future endeavors.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Thanks, Martin.

Operator

Your next question comes from Luke Hannan with Canaccord Genuity. Your line is now open.

Luke Hannan — Analyst, Canaccord Genuity

Great, thanks. Good morning, and I'll echo that congratulations as well, Mark. Towards the end of your prepared remarks, you talked about the pull forward of some orders as it relates to tariffs it sounds like. Folks in the industry want to get ahead of some tariff implementations. If I call it correctly, that is

something a similar experience that we had witnessed about four, five years ago. Can you just give us a sense, maybe a high-level overview of one, if that is the case, if it is a similar setup to around this time five years ago. If so how much better prepared are you for that sort of scenario compared to back then?

Mark Segal — Chief Financial Officer, Spin Master Corp.

Thanks, Luke. I'm glad you asked the question, because my reference to tariffs actually has nothing to do with the toy industry. There is no impact on tariffs for the Toy industry. The reference was to the tariffs that the U.S. government put on electronic components and solar panels that impacted various technology industries in the U.S., I think, effective August 1. As a result of that, those industries were pulling forward orders into the U.S. and a lot of containers were actually on their way to the U.S. and not where they needed to be in China.

As a result of that, that caused a little bit of volatility in the ocean freight pricing market and that actually caused some of our retail customers to delay some of their deliveries from Q2 into Q3 with the expectation that the rates would then decline again when things settle down. I just want to be clear, that had nothing to do whatsoever with tariffs on Toys, but simply was an industry-wide issue that affected ocean freight rates in general for the market. I hope that's clear now.

Luke Hannan — Analyst, Canaccord Genuity

It is. That's very helpful. If we can maybe switch just to Digital Games, I'm curious to know when it comes to specifically Toca Days and Rubik's Match, how are you doing so far in the markets where these properties are deployed? How are you doing as far as KPIs go across acquisition, engagement and

monetization, notwithstanding the fact that as you called out earlier, the macro seems to be affecting the monetization element? Thanks.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Good morning, Luke. Let's start with our Rubik's Match. We are achieving good soft launch KPIs and strong app stability. Specifically on the KPIs, day one, day two retention are quite healthy. Our store conversion is also very healthy, and we're getting closer to our final monetization soft launch KPIs. We feel good about that. We're basically still scheduled to launch in September broadly. That's basically the sequence on Rubik's Match.

When you get to Toca Days, actually very positive as well. We have short term engagement, which is performing to our expectations of day one (phon) retention for some user experience. The session lens is outstanding. Then we're now basically into the long-term retention and app stability and monetization. I'll just give you some things that are very encouraging from where we sit.

One of the most impressive stats is, and I'm happy to share with you our MAU in Toca Days organically has already crossed 400,000 MAU in Q2 and it's climbing. This is simply just by us basically getting into these markets, and there are no big markets we've gone into. We're being very cautious. As we look ahead, we're basically working on content, social features, retention features and building towards a monetization level we feel very confident with. That's where we are on both games and making strong progress and keeping our commitments to launch.

Luke Hannan — Analyst, Canaccord Genuity

Great. In that 400,000, has there been a big migration from Toca Life World in to Toca Days? Or, are these net new organic users?

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

They're mostly organic users. Obviously, there are some people who are playing both. As we stated, our MAU on Toca Life world actually climbed to an all-time high, at the same time we're launching in these markets. Obviously, we have (inaudible) at the market level, and we're encouraged with any cannibalization that we would have expected.

Luke Hannan — Analyst, Canaccord Genuity

Great. Okay. Last question for me and then I'll pass the line. For Toca Life World, I'm curious to know, amongst your player cohorts, where is it exactly that you're seeing fewer in-app purchases? Is it with those players that have been part of the player base for a while? Or, is it some of those newer players?

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

We actually have increasing ARPU with some of our current players, and we needed to get more people to come in. We actually have released some free content, which is driving engagement, and this is more towards June. We are now beginning to see the effect of that in July. We're seeing a halo effect of players coming into the game and purchasing other items from our rich catalog of content, that's number one.

Then second, as we look to the back half, beyond that, we have a lot of interventions to continue to drive the monetization. One of the more exciting things about the second half on Toca Life World is, we have 37 percent more content dropping this year than last year, and that is very important.

Second, we secured a strategic collaboration that is going to launch in Q4. Recall we did SpongeBob last year and the year before with the Hello Kitty. We have a super exciting new collab for Q4. We look forward to that. We have two new features set to launch in Q4. We haven't had a new feature on Toca Life World in quite some time, and that will give players an opportunity and value to basically showcase what they're paying for.

Luke Hannan — Analyst, Canaccord Genuity

Great. Thank you very much.

Operator

Your next question comes from Drew McReynolds with RBC. Your line is now open.

Drew Reynolds — Analyst, RBC

Yes. Thanks very much and congrats, Mark. Just a couple of high-level ones. Curious just to see from your perspective, just how the macro environment is evolving. I think, Max, in your prepared remarks, you talked about kind of improving consumer sentiment, but just overall, the consumer being bullet kind of retailers are cautiously optimistic about kind of the back half of the year here. Kind of, it all sounds very to me on this side. Just would an update on just how things have evolved.

Then secondly, just with respect, and I guess, Max, for you on the setup 2025, obviously, on the macro side, there's things you can't control overall. But it does seem like across each of your three segments, the pipeline of whether it's new Toys, new IP is building. I'd love to get your thoughts on the strength of that pipeline across all three segments relative to where you think you've been in prior years and whether you actually do see it as potentially a much stronger setup here looking forward? Thank you.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Great. Really, really good question and very complex question, so I'm going to decompose it for you. From a retail perspective, right, retailers have gone over their inventory situations. Inventories as we get to the back half are cleaner, and that's a really positive thing. It's both retail inventory, our owned inventory. That's number one.

Number two, they've gotten retailers that is from a profitability graph and just making sure they have their fundamentals cleaned to now looking for growth. There is an impetus to grow the category, and that's really positive, too. There's a lot of enthusiasm to invest in the category.

Third, now getting to the consumer, from a consumer perspective, the consumer continues to look for deals, continues to look for opportunities to actually get into the new items as well. We have in our line, addressed price points and the breadth of our line across different price points to be very competitive. Actually, we're seeing success. Prime Day was an example for Melissa & Doug and for us as well, where we actually had well-priced items, how well that did for the Company. As we get into the back half, not only do we have the promotional support for our brands and the key price points.

We also have an entry into the value channel in the U.S., which is going to give us a broader access to the consumer who's looking for that deal. We feel very good about that.

Then importantly, from the consumer, we're still seeing the consumer truly engage with new items in the category. This year, we have more new GPS percent of our total Toy business, both across Melissa & Doug and Spin Master than we did a year ago. In Melissa & Doug specifically, we have two great innovations in the second half of this year, which they would have not had last year. We feel really good about that. I mentioned Blockables as brand new and the wow innovation platform is doing incredibly well.

Beyond, we have a play gym that just launched, and just on the initial launch period is doing incredibly well. We talked Rachel, we talked Bitzee, all those things are now set and gives us confidence because of the early POS that we will have something to chase as we get to the fourth quarter with replenishment, as Mark alluded to.

As we get into the future, and I'm sticking with Toy, we have an incredible portfolio both of innovation. We have full year effects of Ms. Rachel, a full year effect of Hatchimals, we have a full year effect—some of the big things we just (inaudible) launched this year, which is really positive. But on top of that, we have the full year effect of channel expansion into the value channel, for example. On top of that, we also have a great, great set of theatricals that is complementing our brand, our core brands and our basically franchises as well as everything we're doing with a channel perspective. We feel very strongly about 2025 for Toy, both Melissa & Doug and Spin Master.

When it goes beyond that, we have a full year effect of Unicorn Academy, which then gets into licensing and merchandising for the entertainment business. When we're launching the games full out in '25, right, we're just in soft launch mode, as we basically get into the year. A lot of the interventions I mentioned, Toca Life World are just now rolling into market, so you get the full year effect of that, as well as the subscription business, which from a monthly recurring revenue, as Mark alluded to in his remarks, is doing incredibly well.

All of that bodes well for us in 2025, a year we feel very confident about. The last piece on the acquisition of Melissa & Doug is we're going to have the full year effect of the expansion into Canada and Mexico, which is happening here. But we're going to have the first year effect of our full international expansion, which I think adds another building block and a key component for the Melissa & Doug growth. I hope that gives you a better picture and we're quite confident.

Drew Reynolds — Analyst, RBC

Yes, that's great. That's great colour. Thank you.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Thanks, Drew.

Operator

Your next question comes from Brian Morrison with TD Cowen. Your line is now open.

Brian Morrison — Analyst, TD Cowen

Okay, thanks very much. Call providers had some issues today, so I apologize if there's some repeat here. Max, I want to talk about Melissa & Doug a little bit more. We see some sequential improvement in Q2 relative to Q1. You've mentioned some notable success on Amazon Prime. I understand the seasonality. I'm hoping you can go a little deeper with data points as we move into the second half that convey confidence in the outlook for M&D. I think Mark said orders were up double digits in Q2. Is that correct? Maybe repeat that data point?

Then perhaps colour on the level of the Q3 order book relative to last year, how much ballpark inventory catch up in the channel is required to normalize? I think your guidance this year is not far off last year's revenue from the bar report. How are you tracking relative to last year through Q2 on Melissa & Doug?

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Great. This is great. Let me get Mark to clarify the first question you asked, and then I'll pick it up from there. Mark?

Mark Segal — Chief Financial Officer, Spin Master Corp.

Yes. Sure. Brian, what I actually referred to in my prepared remarks was the fact that Melissa & Doug shipments in Q2 were up double digits relative to Q2 last year. On a year-to-date basis, actually, Melissa & Doug for '24 year-to-date is actually flat with Melissa & Doug '23 year-to-date. But what all the growth initiatives that Max has referred to actually come in the second half of the year. Let me hand it back to him to go over those points again.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Brian, I think on Melissa & Doug, we saw a significant improvement in Q2. We also invested to get that improvement. The good news is that the brand is super strong and responded, both at retail and in consumption through the increased marketing. That's the first thing. We have a proof point on the investment and the return on that investment. We'll continue to invest as we now started to in Q3.

Q3's order book is very strong. One thing that has given us confidence, and should give you confidence is the fact that some of the orders have now turned into direct import orders. The retailer also got more confident as they saw the consumption improved. From an order that we would have brought historically, now they're bringing because basically they want to get behind it, okay, that's really important too.

Number three, from an order book and into Q4, as we've told you from the day we actually began to talk about the brand, Q4 is massively critical for Melissa & Doug. The good news is that we have Q3 order books reflecting the planning for Q4. Why? Because we have more innovation in Q4 than we would have had a year ago. A year ago, we didn't have Blockables, a year ago, we didn't have the play gym, and a year ago, we would have not had the broad expansion of the Sticker Wow launch. On top of that, we have Ms. Rachel and the synergy play for Melissa & Doug as well.

From an innovation perspective, and you know how important innovation is to the category, we feel very strongly about the fact that we have those building blocks, which we didn't have a year ago.

Number four, we basically have now Canada shipping with our commercial team at Spin Master, which is actually great. We have Mexico starting as we speak. We're going to have two countries that would have basically been under distributors at very low levels, owned by Spin Master through our own sales force. That also will give us new revenue.

For all those reasons, we feel very confident that Melissa & Doug in the second half will deliver according to what we've guided, and hopefully, will push beyond that.

Brian Morrison — Analyst, TD Cowen

Okay. Max, thank you. That's very thorough. I want to go into the Digital Games segment for a minute. I know there was a question on it, but can you just maybe go into more detail upon the year-over-year softness? Is this simply industry specific? Is there a delay in terms of global launch of Toca Days or Rubik? Then I do have one small follow-up in terms of timing, if that's okay.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Yes, absolutely. I think it's a very fair question. It comes down to Toca Life World and it comes down to basically less in-app purchases for the consumer segment we play with. But on top of that, we basically see that as we began to activate, we have had conversion improvements on Toca Life World. We have great engagement, Brian. We just have to drive conversion, so that we can get the ARPU to the levels we know produces the revenue that we need. It comes down to specifically Toca Life World.

By the way, subscriptions is doing better than we had planned. That's a really positive thing. From new games perspective, they were never intended to be launched and monetized immediately in Q4. We

always planned for this to be a long—we want to launch them right, and we actually had in our planning more of a back half component to the revenue. It's really Toca Life World. It's really a monetization conversion, specifically.

Brian Morrison — Analyst, TD Cowen

Okay. Then my follow-up is the timing for a global launch of Toca Days, I don't know if you know that yet, but also merchandise for Ms. Rachel, Unicorn Academy entering the value chain, should that all show up in the GPS in Q3? Mark, you did say that you expected GPS to be higher in Q3 in the second half this year than it was last year. I think it was 57 percent last year. Any colour on that number?

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

I'll start, and then I'll turn it over to Mark with the numbers. The answer to your question on what has already said in June, specifically, the answer is no. Ms. Rachel was not in the second quarter numbers. What was in the second quarter numbers, Brian, is a bit of Unicorn Academy, a bit of Bitzee and a bit of not Hatchimals yet, Punirunes. All those things give us confidence from a POS, early days, right? But those already began to ship.

The majority of the shipments for new is Q3, including Ms. Rachel. We have not yet set Ms. Rachel to be clear. There's a lot ahead of us. From a Q3 versus a year ago, we are well positioned to exceed a year ago nicely.

Brian Morrison — Analyst, TD Cowen

And, the value chain?

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Value chain is not setting until Q3—starting in Q3. That has not yet come into effect.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Brian, just staying with your question on seasonality, I'm not sure what numbers you're referencing. Let me repeat again. For Spin Master we expect Q3 to represent approximately 40 percent of the full year guidance that we've given you compared to 38 percent last year. Then for Melissa & Doug Q3 to be about 50 percent of the year—sorry, let me repeat. This Q3 and Q4 will be roughly equal in size in relation to each other, but Melissa & Doug overall seasonality is around 80 percent in the second half. It would represent around 40 percent and 40 percent Q3, Q4. I hope that clarifies.

Brian Morrison — Analyst, TD Cowen

Yes, I'll take it offline. I had one more but I'll take it offline. Thank you very much.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Okay. I think we have two more questions.

Operator

Your next question comes from Adam Shine with National Bank. Your line is now open.

Adam Shine — Analyst, National Bank

Thanks a lot. Good morning. Most of my questions were asked after I had to requeue up. But maybe one for you, Mark. Can you give us the split like you often did in the past in terms of FOB versus direct, especially given some of the moving pieces that you alluded to today?

Mark Segal — Chief Financial Officer, Spin Master Corp.

Yes. Historically, Adam, if you go back to earlier days, it was typically up around 60 percent FOB, 40 percent domestic. In the last few years that shifted down to the mid-50s percent, as Europe has grown which is much more of a domestic market. Now increasingly more so with Melissa & Doug because a lot of Melissa & Doug's Q4 volume is actually domestic. Overall, our FOB versus domestic split for 2024 is estimated to be around 52 percent FOB, 48 percent domestic.

Adam Shine — Analyst, National Bank

Okay. Great. I guess going back to the prior answers, a lot of confidence around as Q3 as Max alluded to and outlined, obviously, some help just in terms of the delayed shipments from Q3—sorry, Q2 into Q3. When we think about some of the concerns in prior years, just vis-à-vis the guidance, the issue has not historically been Q3 of course. It's been sort of early part of Q4 showing signs of slowdown. I'm not so much talking about Melissa & Doug, Max, because I think you already explained that very clearly. But, as it relates to the core business, particularly going into Q4, can you maybe just elaborate a little bit further on some of the confidence? Is it significantly related to the state of inventories and the anticipation

of replenishment going into Q4 that may have been absent in prior years? Maybe there's one or two other things that you could allude to.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Yes. I will start, and then I'll pass it on to Mark from a numbers perspective. But the confidence, Adam—and good morning—is driven by three things: Number one, the percent of new for us this year in Spin Master is higher and some of that has not set yet. As we get into Q4, we've also got more marketing for us into late Q3, Q4 than we did a year ago. We have new with a lot more marketing support, which actually bodes well for us, number one. Why? Because on some of those, we already began to see some early POS signs of we're going to chase and that's really positive.

Number two is we basically have the expansion into new channels that is going to help us get more revenue as well. That's very, very important. Number three, unlike last year, where people were not reordering because they had inventory, our inventory positions are better, and you actually stated that in your question, and you're correct. Not only for replenishment in Q4, but as actually, we said the first quarter of 2025. Because we have new things coming in 2025, for those things to set, we have to ship in November, December. Therefore, we see Q4 from a GPS perspective, as also having something we didn't have last year.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Yes. Max, I think you've covered mostly all of it. I will say we are confident in our outlook Adam, for all the reasons we've discussed on the call and we've alluded to in the Q&A afterwards. Obviously, if

you look at it by creative center, in the Toy area, there is the element of replenishment, which is very tough to call, well ahead of the actual season. There's always the element of replenishment potentially providing upside or downside, depending on what's happening in the market. Just keep that in mind as you well know. But on the Entertainment side, we have good visibility into what's happening. On the Digital Game side, as Max described, we have a lot of activity in the second half of the year and for all the reasons.

When you put that all together, together with our cost control, we feel confident in our outlook for the second half and for the full year.

Adam Shine — Analyst, National Bank

Okay, thank you very much. Appreciate it.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

I think we will take one last question, Anna, please.

Operator

Your next question comes from David McFadgen with Cormark Securities. Your line is now open.

David McFadgen — Analyst, Cormark Securities

Okay, thank you. I don't know if you provided this on the call, I may have missed it. But if you look at your Q1 presentation, on Slide 12, if you have it handy, you provided us point-of-sale metrics or some of the key properties, and I was wondering if you could provide that for Q2, specifically PAW Patrol would be really helpful.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Yes, sure. On PAW Patrol, we were just slightly below the—and I alluded to in my remarks, slightly below the Infant/Preschool category, which was down. We were down a little bit more than that, and that is really more because we, last year in Q2, had begun to ship and began to see consumption for movie items. When you exclude that, basically, you would basically find that we were just in line.

Mark Segal — Chief Financial Officer, Spin Master Corp.

David, if there's anything else specific that you want, Sophia (phon) can be in touch with you after the call on any particular other item.

David McFadgen — Analyst, Cormark Securities

Okay. That would be helpful. Thanks.

Max Rangel — Global President and Chief Executive Officer, Spin Master Corp.

Okay. Well, I think we're going to wrap it up at that point. Thank you so much for participating, and we'll talk to you again after Q3 results in early November. Thanks, everyone. Have a good day.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines.