FINAL TRANSCRIPT

Spin Master Corp.

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PRESENTATION

Operator

Good morning. My name is Suzanne (phon), and I will be your conference Operator today. At this time, I would like to welcome everyone to the Spin Master Fiscal 2016 Second Quarter Results Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during this time, simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, please press the # key. Thank you.

Mr. Segal you may begin your conference.

Mark Segal — Chief Financial Officer, Spin Master Corp.

Thank you. Good morning, and welcome to Spin Master's financial results conference call for the second quarter and six months ended June 30, 2016. My name is Mark Segal, and I am Spin Master's Chief Financial Officer.

I'm joined this morning by Ronnen Harary, Co-Chief Executive Officer, and Ben Gadbois, Global President and Chief Operating Officer.

Following our formal remarks, we will open up the line for your questions. For your convenience, the press release containing our second quarter financial results is available on the Investor Relations section of the Company's website at www.spinmaster.com, as are our Q2 MD&A and financial statements. This information is also available on SEDAR.

Before we start, 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; or 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 believe are appropriate and reasonable in the circumstances.

However, there can be no assurance that such estimates and assumptions will prove to be correct. Many factors could cause actual results to differ materially from those expressed 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 this forward-looking statements.

Except as may be required by law, Spin Master has no obligation to update or revise any forward-looking statement, whether as a result as new information, future events, or otherwise. For additional information on these assumptions and risks, please consult the cautionary statement regarding forward-looking information contained in the Company earnings release dated August 4, 2016.

Please note also that Spin Master reports in US dollars, and all dollar amounts to be expressed herein today are in United States currency.

I would now like to turn the conference call over to Ronnen Harary.

Ronnen Harary — Co-Chief Executive Officer, Spin Master Corp.

Thank you, Mark. Good morning, and thanks for your interest in Spin Master. Yesterday we reported very strong financial results for the second quarter and six months ended June 30, 2016.

I'll begin the call with some strategic highlights. Following my remarks, Mark will provide you with a review of our financial results, including our outlook for 2016, and Ben will then talk to you about our growth initiatives.

The quarter was highlighted by the closing of the acquisition of Toca Boca and Sago Mini, developers of mobile game apps that emphasize children's natural sense of curiosity, experimentation, and self-expression. Kids are consuming more content on mobile devices, and so that's where we need an expanding presence.

Toca Boca focuses on kids aged 3 to 9, while Sago Mini focuses on the pre-school age group of 2 to 5 years old. Combined, they have over 150 million downloads and over 15 million monthly active global users.

Our vision is to take our proven capabilities in toys and entertainment and combine it with Toca Boca and Sago Mini's mobile digital capabilities to provide an end-to-end experience for kids. We're super excited about the potential of Toca TV, the subscription-based video streaming business which just launched in Canada, and which will launch in the United States in 2017.

Toca TV is an interactive video platform aimed at kids aged 5 to 9. It delivers content for them to discover and play with, including thousands of handpicked videos curated from around the web. Toca TV is not just about the videos that are available, but also about what videos aren't.

Every piece of content is prescreened and reviewed to ensure it lives up to Toca Boca's standards. There is no third-party advertising or sponsored-product placement. They carefully select, catalogue, and offer anything kids need to laugh, be inspired, and have fun. Toca Boca is also about creation tools, film editing, and picture editing.

As we've indicated before, one of our core strategies is to create evergreen TV franchises that maximize long-term revenue potential.

We develop our TV shows and toy lines together with a strategy to maximize integration/distribution on a global basis. The success of PAW Patrol highlights this strategy, and has established Spin Master as a major player in the pre-school segment.

We are now preparing to build on that success with the launch of the first season of Rusty Rivets on Nickelodeon, which is scheduled for 26 half-hour episodes. The preliminary launch date of Rusty is late August, but this may change.

The new show, targeted boys and girls aged 2 to 5, follows Rusty, a 21st century kid, who with his friend Ruby, always saves the day by relying on his imagination and resourcefulness. Rusty and Ruby invent their way out of every jam by repurposing spare parts and found objects into wild, cool contraptions.

Inspired by the DIY culture of the maker movement, Rusty helps to fuel pre-schooler's confidence and creativity with a strong focus on inventing, creating, and problem-solving, similar to Mark Segal.

In addition to Rusty Rivets, we have a number of other exciting TV properties under development for 2017 and beyond, including the relaunch of Bakugan.

Before I turn over to Mark to review the financial results, I'd like to comment briefly on the recent secondary share offering from our perspective as founders.

Since our IPO, we've been cognizant of the fact that Spin Masters float was an issue for a number of institutional investors. Accordingly, in conjunction with the treasury offering that further strengthens our balance sheet, the founders sold 2.45 million shares.

Let me be clear: all of us are fully committed to making sure that Spin Master realizes its potential globally. That's why we took the Company public in the first place.

Looking forward, I continue to be excited about the potential of Spin Master. With the acquisition since our IPO of Cardinal, Etch A Sketch, EG Games, Toca Boca, and Sago Mini and now Swimways, our product development team has multiple opportunities to do what we do best: innovate for the kids.

The Swimways acquisition gives us a leadership position in the large and growing outdoor category. Swimways also gives us an experienced and proven senior management team and consistent financial performance to build on in North America and internationally. The acquisition is a beachhead for us in our new Outdoor business segment, and we see the outdoor category as ripe for innovation and an area to make further acquisitions.

As always, we continue to execute on all of growth strategies to drive value.

I'll now hand over to Mark Segal, our Chief Financial Officer, to review our financial results in more detail.

Mark Segal

Thanks, Ronnen. In Q2 2016 we maintained our strong momentum with excellent year-over-year performance.

Q2 gross product sales increased 33.7 percent to 186 million from $139 million last year. Excluding Cardinal, which was acquired in Q4 2015, gross product sales increased 19.5 percent to 166 million.

Spin Master's revenues increased 40.5 percent from last year, growing from 127.7 million to 179.4 million.

FX headwinds reduced overall revenue by 1.7 million. In constant currency terms, revenue increased 41.8 percent compared to Q2 2015. Excluding Cardinal, revenue increased 26.5 percent on year-over-year basis.

On a segment basis for the quarter, gross product sales in the Activities, Games and Puzzles, and Fun Furniture segment increased 89 percent to 53.5 million. Excluding Cardinal, the segment grew 20 percent, driven primarily by growth in Bunchems, our 2015 Activity Toy of the Year.

In the Remote Control and Interactive Characters segment, gross product sales decreased 27 percent to 20.4 million, primarily due to decline in DigiBirds and Zoomer, partially offset by increases in Air Hogs.

The decline in Zoomer was largely timing. Zoomer sales in 2016 will be weighted more towards the second half than they were last year as a result of the launch of a number of new characters in Q3.

Gross product sales in the Boys Action and High-Tech Construction segment increased 57 percent to 37.5 million due to toy sales related to the Secret Life of Pets and Angry Birds movies, more than offsetting lower sales of How To Train Your Dragon- and Minecraft-related toys.

In the Pre-school and Girl segment, gross product sales maintained their positive momentum, increasing 27 percent to 74.6 million. The growth reflects the continued strength of the PAW Patrol franchise in addition to shipments of Popples and Chubby Puppies and products associated with the relaunch of Powerpuff Girls.

On a geographic basis, Spin Master's strong global platform drove gross product sales increases of 29.9 percent in North America, 48.2 percent in Europe, and 34.3 percent in the rest of the world.

Other revenue, which primarily reflects merchandising royalty and television distribution income from products marketed by third parties using Spin Master's owned intellectual property, in addition to App revenue from Toca Boca and Sago Mini, increased 310 percent to 12.4 million from 3 million in Q2 2015.

Our gross profit for Q2 2016 increased 40.2 percent to 91.6 million compared with 65.4 million last year. Gross profit margins were flat with 2015 at 51.1 percent of revenue compared to 51.2 percent last year.

SG&A expenses for the quarter, excluding share-based compensation expenses, was 74 million, representing 41.3 of revenue compared with 54.9 million, or 43 percent last year, reflecting the Company's operating leverage.

Within SG&A, marketing expenses represented 6.8 percent of revenue compared with 7.7 percent last year. Product development expenses were 2.8 percent of revenue compared with 2.7 percent last year.

Selling expenses represented 7.6 percent of revenue versus 5.4 percent last year, driven by a heavier mix of licensed properties in the quarter versus 2015, primarily related to Star Wars, Secret Life of Pets, and Angry Bird products.

Distribution expenses were 3.6 percent of revenue compared with 2.6 percent in 2015. The increase was driven by the inclusion of Cardinal's distribution costs.

Admin expenses represented 24.4 percent of revenue versus 24.7 percent last year. Excluding the impact of share-based compensation expenses, admin expenses as a percentage of revenue were significantly lower in the quarter at 20.5 percent compared with 24.7 percent in Q2 2015.

The improvement reflects the Company's continued positive operating leverage and disciplined management of costs.

All of this resulted in net income of 3.6 million, or $0.04 per share compared with 7.6 million last year.

Adjusted net income in Q2 was 11.7 million, or $0.12 per share, 44 percent above 8.1 million in 2015.

Adjusted EBITDA for Q2 2016 was strong, increasing 41.5 percent to 25.4 million from 17.9 million last year. Please note there was a small typo in the adjusted EBITDA reconciliation table in the press release last night. The correct adjusted EBITDA number is 25.4 million, as I just mentioned, not 23.4 million, and this has now been corrected on our website.

Adjusted EBITDA margins increased slightly to 14.2 percent compared with 14.1 percent last year.

The Company had negative free cash flow of 11 million in the quarter and compares with positive 5.8 million in Q2 last year. This was primarily the result of a payment to the CRA during the quarter related to the settlement of the transfer pricing matter described previously, as well as higher tooling to support growth.

Inventory increased by approximately $16 million at the end of Q2. This was primarily driven by Cardinal inventory to support its growth, as well as to support higher levels of upcoming shipments for Secret Life of Pets, Teenage Mutant Ninja Turtles, and Angry Birds, and for PAW Patrol, driven by line extensions and to support international growth. Etch A Sketch also contributed partially to the inventory increases over 2015.

Overall, inventory levels are in line with our planned growth outlook, and remain a key point of ongoing management focus.

Turning now to the six months ended June 30. Spin Master generated revenue of 341.1 million, an increase of 45.6 percent from 234.2 million for the same period in 2015. In constant currency terms, revenue increased by 47.3 percent year to date relative to the comparable period in 2015. Excluding the acquisition of Cardinal, year-to-date revenue increased 30.7 percent to 306.1 million.

Gross product sales increased 40.7 percent to 359.8 million from 255.7 million last year. Excluding the acquisition of Cardinal, gross product sales increased 26 percent to 322.3 million. On a geographic basis, gross product sales increased by 42.4 percent in North America, 34.8 percent in Europe, and 41.9 percent in the rest of the world. Year to date gross profit increased to 177 million, or 51.9 percent of revenue compared with 122.1 million, or 52.1 percent of revenue in 2015.

The slight reduction in gross margin was primarily attributable to Cardinal and FX, offset by increased licensing and merchandising royalty income and productivity initiatives.

Adjusted EBITDA for the six months ended June 30 increased to 49.4 million, up 75.5 percent from 28.1 million in 2015. Adjusted EBITDA margins increased to 14.5 percent year to date from 12 percent in 2015, reflecting continued positive operating leverage.

Free cash flow year to date was 5.3 million compared to negative 2.4 million in 2015.

On June the 6th we closed the public offering of 4.9 million subordinate voting shares at a price of CAD $26.60 per share. This included a treasury offering of 2.5 million shares for gross proceeds to the Company of approximately CAD $65 million, and as you heard from Ronnen, a secondary offering of 2.5 million shares by the founders.

We deployed the net proceeds of the treasury offering to reduce indebtedness, further enhancing our balance sheet to facilitate future growth, including the recently announced Swimways acquisition.

The purchase price for the Swimways transaction will be satisfied by $85 million in cash on closing, plus up to $8.5 million payable over four years based on Swimways' sales growth. The transaction was financed through our existing credit facility.

Swimways will operate as a stand-alone operation within Spin Master, and will help establish our newly created Outdoor segment. Swimways' gross sales in 2015 were approximately

90 million and revenue was approximately 86 million. 2015 gross margins were in the 40 percent range and EBITDA margins were in low teens.

Regarding sales seasonality, Swimways' sales are weighted 70 to 80 percent in the first half of the year.

As I mentioned, we have created a new business segment called Outdoor as a result of the acquisition, and we'll be reporting five business segments in future. Outdoor will contain Swimways and other outdoor-related lines that we will begin to develop or acquire.

I will conclude with our revised outlook for 2016. For the full year, Spin Master now expects organic gross product sales growth to be higher than the guidance provided in connection with the release of Q1 results in May, with organic gross product sales expected to grow in the high teens relative to 2015. Previous guidance reflected organic gross product sales growth in the mid-teens relative to 2015.

From a seasonality perspective, Spin Master now expects gross product sales for the first half of 2016 to represent approximately 30 percent of full year gross product sales, which is in line with our typical sales seasonality. Previous guidance reflected gross product sales comprising between 30 to 35 percent of total gross product sales for 2016.

Adjusted EBITDA margins for 2016 are now expected to increase slightly compared with prior guidance in 2015.

As a reminder, our long-term organic gross product sales growth target is mid- to high-single digits. There will be some years of higher growth and some years of more modest growth, but mid to high-single digits is the organic growth rate we believe we can sustainably deliver over the long term.

For 2016, the impact of the Swimways acquisition on Spin Master's adjusted EBITDA and net income will be slightly dilutive, but largely immaterial. Swimways' EBITDA margin in 2016 and in its first full year in our hands in 2017 will be consistent with its 2015 results, and will be accretive to Spin Master overall once we're able to drive operating leverage and productivity initiatives that we expect to be able to do.

Swimways counter-seasonal sales pattern will change Spin Master's H1/H2 gross product sales seasonality profile from 2017 onwards. We will provide more guidance on 2017 and the progress we are making on Swimways in upcoming quarters.

I'd now like to turn it over to Ben Gadbois. Ben?

Ben Gadbois — Global President and Chief Operating Officer, Spin Master Corp.

Thank you, Mark. Good morning to everyone. Overall, we continue to be very pleased with the financial and operating performance of the Company.

With growth of 7 percent in the US, the toy industry continues to perform very well, and our growth continues to significantly exceed that of the industry.

As Mark mentioned earlier, the increase in inventory we have seen is to support our expected continued growth. We closely monitor point of sale and supply and demand, and are focused on ensuring that we're clean at the end of the year, both internally and at retail.

The management of inventory at retail and on our balance sheet is very tightly monitored, and is one of the key metrics for managing our company.

Our growth is grounded in clearly defined strategies. We're sticking to them, as they are working.

First, we will continue to consistently infuse innovation into our portfolio of brands and products. Our internal 36-month brand innovation process facilitates the identification and market opportunity that we capitalize on through product development or acquisitions.

In the year-to-date, we're very pleased with the performance of our product portfolio. Meccano continues to respond to the innovation effort we have infused into the brand since its acquisition; Secret Life of Pets exceeded our expectations. Bunchems continues to grow globally.

Popples, Powerpuff Girls, Noddy, and Teletubbies have all just launched and have received strong retail support in anticipation of successful first seasons. We saw continued strong consumer reaction globally to the new PAW Patrol content and line extensions.

Looking forward for the balance of the year, among the products that we're excited about are several key launches. In Boys Action and High-Tech Construction, Meccano continues to grow, and we are expanding the basic line through innovation and licensing. The Meccano tech line continues to evolve with the introduction of Meccanoid 2.0, as well as the Meccasaur and the lower price-point Micronoids.

The RC and Interactive Characters segment has some exciting new products launching in the fall as well. We have a number of strong internally developed products, including racing drones in Remote Control and are introducing a number of new Star Wars products. We continue to focus on robotics and engineering to improve breadth, reduce price points, and incorporate licences.

Hatchimal is highly innovative and looks very promising. We shifted most of our marketing effort on Zoomer into the back half of the year compared to 2015, and are excited about the launch of the Chimp, Meowzies, Hedgiez, and year two of the Kitty. And of course, PAW Patrol is continuing to grow and expand globally.

Second is to significantly grow our international sales, which we're targeting to represent 35 to 40 percent of our total sales in the medium term. As Mark highlighted, gross product sales internationally grew significantly. Europe increased over 48 percent in Q2 '16 and 35 percent for the first half year over year. The balance of our international business grew 34 percent in the quarter and 42 percent year to date compared to '15—compared to 2015.

Let me spend a moment talking about our success. Many of our European markets have now reached a meaningful size with P&Ls that allows us to take on more revenue opportunities while effectively managing risk.

A few examples: PAW Patrol is growing to meet its consumer demand potential; Bunchems launched successfully in the spring, and is growing faster in Europe than anywhere else; we had successful new brand launched like Popples, Noddy, and Teletubbies; and we continue to successfully integrate acquisitions, including Cardinal and EG Games.

Cardinal is continuing to show growth in Europe, and we're encouraged by its potential.

Most of our European markets are now carrying all of our brands, an improvement from our past lag strategy. This has helped in terms of both retail execution and brand penetration. Retailers are widely supporting our lineup, and consumers are very receptive to our product line. We're opening more doors and channels as our sales team expands coverage.

Our third strategy is to develop evergreen global entertainment properties. Our strategy is to develop new properties based on our objective of one to two new properties every year, integrated with our toy line.

As a reminder, PAW Patrol is airing season 2 in Europe in 2016; season 3 is running in North America for 2016; season 4 is in production and will air in North America in 2017; and season 5 is currently in development. We are continuing to invest in keeping the PAW Patrol content fresh with new characters and themes in order to increase the longevity of the franchise.

PAW Patrol continues to generate high ratings, crosses many cultural boundaries, and has strong support from our partners globally. There are also opportunities to expand PAW Patrol into new markets, such as Asia, which have not yet been launched. We have a number of other exciting TV properties under development for 2017 and beyond, including the relaunch of Bakugan.

Fourth is leveraging our global platform through strategic acquisition. We're very excited about the acquisition of Swimways, our fifth acquisition since the IPO last summer and our largest to date.

Swimways has a diverse portfolio of toys, games, and sporting goods for the pool, beach, and backyard. They are sold under the Swimways, Kelsyus, and Coop brands, and include the popular patented Spring Float line of products. Their brands are complemented by licences from a number of popular franchises in the pool category.

Swimways is a leader in the outdoor and sport toy category, which is one of the largest and fastest-growing US toy categories, with $1.7 billion in year-to-date sales. In fact, the category represented 32 percent of total toy industry growth on a year-over-year basis.

NPD attributes the growth to millennial parents' preference for healthier lifestyle and more creative outdoor play. Swimways brings us the number-one market share position in two US NPD subcategories, float and inflatable and water toys. In the larger water sports segment, Swimways is number two.

Swimways is a great fit for Spin Master. The acquisition delivers on several key business strategies, including giving us the opportunity to drive sales outside of the seasonality traditionally associated with toys and games. This will allow us to maximize our operational structure as well.

Swimways has a strong management team who will remain in place running the business and helping to grow the Outdoor segment for Spin Master. We look forward to working with them to infuse Spin Master's innovation and fun into the Swimways product portfolio.

To conclude, we're pleased with our results to date. Our team is motivated and continuing to execute well. We're still a relatively young company in our industry with great growth potential.

We're extremely focused on our four core growth strategies which we believe can deliver strong results for our shareholders. Our growth strategies provide multiple opportunities to grow, and we are always seeking more.

That concludes our formal remarks at this time. Ronnen, Mark, and I will now be pleased to answer your questions. Operator, please begin the question period.

Q&A

Operator

Thank you. And just a reminder, in order to ask a question, simply press *, then the number 1 on your telephone keypad. We'll pause for just a moment to compile the Q&A roster.

Your first question comes from the line of Sabahat Khan of RBC Capital Markets. Your line is open.

Sabahat Khan — RBC Capital Markets

All right. Thank you. Now that you're halfway through your Q3, can you maybe comment on what you're hearing from your retail partners in terms of the back-to-school season and how inventories are at the retail level and for the industry overall?

Ben Gadbois

Yeah. Good morning, Sabahat. Yeah. Overall, I think the retailers are where they want to be. That's what we are hearing. They're very optimistic for the back half of the year.

So far the category, the toy category, has grown year to date 7.2 percent globally. And North America is expected to grow 6 percent, of which most of it will happen in the back half of the year, as per the seasonality that you're familiar with.

And as far as our positioning and our conversation with them with our products lineup up for the fall, I think everyone is very optimistic and we feel very good about it.

Sabahat Khan

Okay. And just on the margin guidance revision that was increased slightly, is there certain categories that did better than you expected? Was it the content-based stuff; just some additional colour there?

Mark Segal

So, Sabahat, the margin guidance that we increased for 2016 on the EBITDA side really was just a mix of a number of factors. Obviously, sales volumes are increasing. We're seeing an increase in licensing and merchandising income more than we expected.

We're continuing to focus on cost discipline and operating leverage. There's a slight mixture of towards owned IP, which is helping us. We're also very focused on managing sales allowances and our marking spend.

Toca Boca's EBITDA is slightly negative from an EBITDA perspective, but overall we think a slight increase in the EBITDA margin is reasonable and expected for the year, just given where we're at. We don't want to get too far ahead of ourselves because we've still got some meaningful work to do.

Sabahat Khan

Okay. And then just one last one for me just in terms of your overall gross product sales growth guidance; is that including or excluding the contribution that we saw from Toca Boca, which is in the other revenue line? Would that be in addition to your guidance?

Mark Segal

Yeah. So the guidance, Sabahat, is in relation to gross product sales, which actually excludes other revenue. The revenue from Toca Boca and Sago Mini is included in the other revenue segment.

So it's App revenue, which is inclusive—it's included together with licensing and merchandising income. I did not give you guidance on that. I gave you guidance on the gross product sales line.

Sabahat Khan

Okay. So just it's fair to assume that any Toca Boca revenue would be on top of that guidance that you gave, right?

Mark Segal

Yes. Yes. That is a fair assumption.

Sabahat Khan

All right. Thank you.

Operator

And your next question comes from the line of Peter Stusio of National Bank Financial. Your line is open.

Peter Stusio — National Bank Financial

Yeah. Thanks a lot. So just sticking to the guidance, if we look at Q3 and Q4 GPS trends of '15, is that how we should be thinking of in 2016? Or are there any other nuances worth noting?

Mark Segal

Yeah. We gave you a slight guidance change in terms of seasonality for the balance of the year, but we expect Q3 and Q4 of '16 to be very much in line with historical quarters and for the six months at around 70 percent of sales. The only nuance that I would just call out is that we now will have some Swimways revenue coming in to the year as well…

Peter Stusio

Right.

Mark Segal

Which is going to be relatively immaterial, given their seasonality because they're around 70 to 80 percent H1 and only 20 to 30 percent H2. But from a modelling perspective, our seasonality H1 and H2 is going to be very similar to prior years, and then you have to just add on to that the impact of the Swimways acquisition, which is largely immaterial on the top line.

Peter Stusio

Excellent. And you've made positive adjustments obviously to your '16 guidance. I'm sure you don't want to get into a detailed discussion of '17, but when we think about the launch of Australia and the new initiatives for Central and Eastern Europe, is there any colour you can provide in terms of the above-average organic growth rate that may ensue in '17? Or should we think more of a sort of measured ramp over multiple years post '16?

Ben Gadbois

Yeah. I think we, Peter, we have to look at this as a gradual ramp-up. I mean obviously we're opening these markets in Australia and Central and Eastern Europe because we believe they will be accretive, but they're also start-up operations, so it will gradually ramp up in the upcoming years.

Peter Stusio

Okay. Perfect. And finally, Mark, you mentioned in your remarks free cash flow was impacted by the CRA payment. I don't remember seeing this amount in the MD&A. What is the amount that was paid in Q2 to the CRA?

Mark Segal

It was about—it was between 15 million and $16 million, Peter. So remember we actually accrued for this amount in the—

Peter Stusio

Right. Yes.

Mark Segal

So Q4 we actually accrued for it in 2015. In Q2 of '16 we actually paid for it, so that's why you see the actual cash payment going out in our free cash flow.

Peter Stusio

That—

Mark Segal

Sorry, go ahead.

Peter Stusio

Yeah. The 15 million to 16 million, is it Canadian or US?

Mark Segal

Canadian.

Peter Stusio

Canadian dollars. Perfect. All right. That's it for me. Thank you.

Mark Segal

Thank you.

Operator

And your next question comes from the line of Steph Wissink of Piper Jaffray. Your line is open.

Steph Wissink — Piper Jaffray

Thank you. Good morning, everyone. We have a follow-up question just on the Q3/Q4 balance, Mark, that you suggested with respect to the percentage of the year. Can you give us any sense of how the two quarters should balance out? Specifically related to that Remote Control and Interactive Character segment it sounds like there was some shifting maybe from Q2 into Q3.

Mark Segal

Okay. So, Steph, as I said, the guidance for the second half of the year is around 70 percent, which is consistent with the historical. And in the breakdown between Q3 and Q4 is, again, relatively consistent between Q3 and Q4. Q3 will be by far the bigger of the two quarters at around 45 percent and then Q4 around 25. Those are approximate numbers for the seasonality.

Ben, do you want to add anything to that?

Ben Gadbois

Yeah. The only piece of information to that I think is important to note is that if you look at the segment between the first half and the back half, and we have to tie it to our product launch for the fall, so on Zoomer for example, which is an interactive character, we're launching Zoomer Chimp; we're launching Zoomer PAW Patrol Marshall; we have the Zoomer Meowzies; we have the Zoomer Hedgiez; we also have Hatchimal that's launching in the fall. So for this category we also have Air Hogs Star Wars product launching in the fall; we have the racing drone.

So our launch for this business segment in Q3, in Q4 is extremely robust. And what we've done internally is we've also reduced our marketing spend on the first half of the year and shifted it into the second half of the year to really match the product launch, which is why you're seeing like a little bit of a change in the segment.

Steph Wissink

Ben, it's really helpful. And I know last year fourth quarter you had a pricing adjustment that you took on your higher-end goods, I think, midway—

Ben Gadbois

Yeah.

Steph Wissink

—through the holiday season. So you'll be lapping that in the fourth quarter this year. How should we think about the price unit mix in that segment as you plan into holiday '16?

Ben Gadbois

Yeah. I think it's a great question, Stephanie. I think when we look at the pricing of all of our items, what you're referring to is mainly on the Meccanoid, which was for the higher—we ended up with a very high price point, and we learned early on that it was more important for us to making sure we push the brand with all the consumers; they get the trial.

And so this year what we've done is we’ve launched different price point in the brand. So we have the Micronoid, which is going to be approximately $40. We have the Meccasaur, which will be around $100. We have the Meccanoid 2.0 that will be at a lower price point. We've been able to achieve a lot of productivity into our cost base.

So when you look at the lineup, I think we've learned a lot last year, and I think our product line this year is reflecting all these learnings, not just in the Meccano brand, but across the whole portfolio.

Steph Wissink

That's great. And then final question, Mark, for you is just on the international business. It's had some nice growth here over the last several quarters, and it looks like the profitability is also starting to step up. So how should we think about the mix not only of revenues, but also of contribution margins across the global markets?

Mark Segal

So, Steph, there isn't a major difference in profitability across the markets globally. Our pricing and our profit margins are relatively consistent.

The only exception to that would be when we sell on an FOB basis to distributors around the world, at that point we actually sell at a discount obviously because they're having to buy the goods and then mark them up in their own countries. And so that segment is slightly less profitable than when we sell at a wholesale price.

But from a cash flow perspective, it's very helpful to us because we get paid immediately, so there's a little bit of a trade-off. But in terms of international growth, we're actually continuing to meet and reach towards our target of 35 to 40 percent. For the first half of the year our international business was at 34 percent. If you remember from our year-end, we were at 30 percent on international.

And so you're continuing to see a robust expansion in Europe and in the rest of the world on our international business. And so we're at 34 percent, and we think we can continue to grow that towards our target of 35 to 40 percent.

Steph Wissink

Okay. Great. Best of luck, gentlemen. Thank you.

Ronnen Harary

Thank you, Stephanie.

Operator

And your next question comes from the line of Brian Morrison of TD Securities. Your line is open.

Brian Morrison — TD Securities

Good morning.

Mark Segal

Good morning, Brian.

Brian Morrison

If I can ask a question on Cardinal to start with? You had very strong first half sales. I think it was around 37 million. And I recall around the IPO you mentioned that the sales seasonality was forecast to be similar to that of the traditional toy market. So is that still the case? And then also, all of this growth appears to be in the North American market. I'm wondering if you can just address the strength there and if you continue to see international opportunity here?

Mark Segal

Yeah. So to answer your first question, Brian, the seasonality of Cardinal is roughly the same as Spin Master; probably a little bit more weighted towards the first half than Spin Master is, but roughly the same.

The growth that we're experiencing in Cardinal is it comes from a couple of different places. There is domestic growth happening because of the way we've professionalized the sales relationships with Wal-Mart, Target, and Toys"R"Us, who have responded very favourably. What we've also done—and this has been a significant part of the growth in Cardinal—is actually grow their FOB business very significantly. That does come into North America as well.

The third element to our growth on Cardinal is our expansion into Europe, and that's definitely been a big part of our factor as well.

Ben, do you want to add anything to that?

Ben Gadbois

Yeah. As far as Cardinal outside of North America where Cardinal, as you know, was not widely distributed outside of North America, which represented one of the key investment pieces to acquire Cardinal. So we're now presenting the lines to the rest of the world, and it is gaining traction, but it will take time.

So we're starting to get listing in Europe and other parts of the world, and it's going to continue to ramp up, so you will see more growth internationally as we go forward with Cardinal.

Brian Morrison

Okay. Second question for Ronnen; if I go back to your comments at the beginning of the call, I'm wondering if you just might be able to address the progress of a few of the key metrics that you watch in order to advance PAW Patrol to an evergreen property? I also was interested to know what region did it grow in the rest of world and what needs to be accomplished to launch this into Asia and the potential there?

Ronnen Harary

Brian, first of all, I'm so happy someone asked me a question, so thank you. I think that, again, for us it's keeping the content fresh. The team's worked very, very hard to come up with a new theme or multiple new themes for every single year and producing 52 11-minute episodes that we share with the broadcasters around the year. So I think that's the first and foremost thing is just keeping the content fresh, keeping it relevant, staying very close to being on-brand, being on-message.

I think we've been very fortunate to create characters that are truly loved by kids globally around the world. I just got back from holiday in Spain, and I saw kids wrapped in—the most impactful thing was a father holding his son wrapped in a PAW Patrol towel. And that was in Formentera in Spain. So this is crossing cultural boundaries, and keeping those themes fresh is super-important.

The other thing is supporting the broadcasters around the world, which we're doing with the fresh content.

And what was your other question, Brian? You had something...

Mark Segal

Asia.

Ben Gadbois

Asia.

Ronnen Harary

No, but there was a question before Asia.

Mark Segal

The metrics.

Ronnen Harary

Oh, the metrics. No, in terms of Asia, Asia is a tough, tough, tough market. We've been focused on how do we actually get it into China and how do we launch it in Japan? And we have not actually cracked the two markets yet, but we are actively focused on figuring out a way to actually get PAW Patrol into these two markets.

We are—I believe that it will cross those cultural boundaries and resonate with the kids, just as much as it resonates with kids in Spain or in other parts around the world. So we are actively working on it, but we don't have anything in place just yet.

I would say if I had to put out a marker—and I don't normally put out markers—but I would say probably sometime in 2018 would be the marker.

Brian Morrison

Okay. That's helpful.

Ben Gadbois

And then maybe, Brian, just on the metrics on the other piece of the question on metrics for PAW Patrol; for all of our key brands and franchises, obviously PAW Patrol being one of them, so we—if there's an entertainment content we obviously monitor the viewership and the ratings at the country level. But internally what we also do is for all of our key markets at the retailer level we measure the amount of inventory shipped in every month, the POS related to this inventory every month, as well as the beginning inventory at the end of each month.

And what that does is it really tells us and it allows us to see how the property is doing so we can actually have a very good grasp globally on the mix, on the growth, and making sure that we keep everything in balance as the property continues to grow.

Brian Morrison

Okay. Sorry, last question then for Mark. Just with respect to the other revenue line, the IP to third parties. Obviously it was a big jump, and I realize Toca Boca was in there, but how do you see that unfolding for the back half of the year? Is this a straight-line number for Q2? Or...

Mark Segal

Other revenue is really a composite now of a few different categories. It’s primarily licensing and merchandising income from PAW Patrol and other IP that we own, and then it’s now the App revenue from Toca Boca. So part of the reason we’re calling up the adjusted EBITDA margins is the fact that we do see some growth occurring in that.

It also, to some extent, flexes with the seasonality of the business, but not in the same way that the toy sales do. So we do see some growth in that, Brian, in relation to the numbers that are out there, the consensus numbers that are out there. I think the actual results will be a little bit higher, but it’s not in the same 30/70 split that you would see for toys.

Brian Morrison

Okay. Thanks very much.

Operator

And again, that is *, then the number 1 on your telephone keypad if you would like to ask a question.

Your next question comes from the line of Garrett Johnson of BMO Capital Markets. Your line is open.

Garrett Johnson — BMO Capital Markets

Hey. Good morning. I have three quick ones here. First, your comments on Swimways being slightly dilutive; is that excluding transaction costs? Or including them? Two, can you just discuss what your organic retail sales growth looked like in the quarter? And then finally, what are you targeting for PAW Patrol as a percent of sales this year? Thank you.

Mark Segal

Okay. I'll deal with the first and the third questions quickly. When I referred to dilutive for Swimways, Garrett, what I was referring to was kind of an all-in impact of Swimways. I mean there's obviously transaction costs that will hit to some extent—a small amount of it hits in Q2, but some in Q3 as well; nothing particularly material.

But what I was primarily referring to was the fact that Swimways' revenue for the second half of the year is quite low, and, therefore, the costs that are coming in are somewhat flatlined over the year, and they will generate basically breakeven to slightly negative EBITDA for the second half of the year in our hands, and that will dilute our EBITDA a little bit; again, not material at all.

In relation to PAW Patrol, PAW Patrol was around 25 percent of sales in 2015, and we expect it to be in that same zone for 2016.

Your second question was on retail...

Ben Gadbois

Sales. Yeah. I can answer that. Yeah.

Mark Segal

Which Ben will pick up.

Ben Gadbois

Yeah. Good morning, Garrett. So as far as the way we look at our sales internally is we're very focused on POS with all the key retailers and also by market. So if we look at POS in the US, UK, France, Germany, Italy, Spain, and Belgium, we track all those and a few more. But in the instance of, the US for example, the market, the POS in the first half of this year was up 7.5 percent and we're up over 35 percent. In the UK, the market is up 5.6 percent, and we're up like a multiple of this. And it's the truth for most markets.

So what we do is we really look at the POS. We understand the mix. We obviously replenish this mix and we plan going forward, and all of this when you put it all together, obviously it drives our organic growth rate. But the way we manage it, Garrett, is POS is very, very, very important for us, and we spend more time on POS than really to ship-in because the POS is obviously where the consumers vote with their wallet, which is obviously an indication of how the business is doing.

Garrett Johnson

Okay. And just to be clear, that plus 35 percent is organic, right?

Ben Gadbois

Well, there is some Cardinal in that number. If you back out Cardinal, we're still ahead of the US market, so we're still running higher.

Garrett Johnson

Okay. Thank you.

Mark Segal

Thanks, Garrett.

Ronnen Harary

Thanks, Garrett.

Operator

And there are no further questions in the queue at this time. I turn the call back to the presenters.

Mark Segal

Okay. Well, thank you, everyone. If there are no further questions, we'll conclude the call at this time, and we look forward to talking to you in November with our Q3 results.

Thank you very much, everyone.

Ben Gadbois

Have a great weekend, everyone.

Operator

And this concludes today's conference call. You may now disconnect.

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