

Mattel, Inc. 1998 Annual Report





Financial Highlights

Operating Results (In millions)	For the Year				
	1994	1995	1996	1997	1998
Net Sales	\$3,971	\$4,370	\$4,535	\$4,835	\$4,782
Income (Before Restructuring, Extraordinary Item and Special Charges)	276	347	372	500	364
Net Income	225	338	372	285	332

Financial Position (In millions)	As of Year End				
	1994	1995	1996	1997	1998
Cash and Marketable Securities	\$ 290	\$ 511	\$ 550	\$ 695	\$ 212
Long-Term Debt	521	627	520	676	984
Total Stockholders' Equity	1,386	1,552	1,806	1,822	1,820



To Our Shareholders:

1998 was a disappointing year for Mattel. Changes in our business, which we had anticipated would happen, occurred much more quickly and more dramatically than we ever expected. But we had initiatives well underway to address these changes, and we believe they will deliver positive, long-term results. So let's review what happened and then tell you why we are so confident about our future.

We were informed early in the year of a major buying shift by our key retailer, Toys "R" Us, as they moved to reduce their inventories by \$500 million over three years. In fact, they accomplished most of this reduction in just one year, which affected Mattel by \$250 million in total. But we didn't foresee that this inventory reduction trend would accelerate to most of our key retailers, resulting in across-the-board cutbacks in year-end buying. So when historical re-orders didn't materialize in December, we decided to take the appropriate actions to adjust our own shipping to a more just-in-time pattern. As a result, we pre-announced that we expected to see flat top-line growth, and that our earnings would decrease to approximately \$1.20 per share. And the year-end results we reported were earnings of \$1.20 per share, before charges, on a 1 percent decrease in sales.

The positive news coming out of 1998 was that retail sell-through of our products at our top U.S. accounts was up 12 percent, and retail inventories were down 30 percent in total, and down 50 percent at Toys "R" Us.

As I said earlier, we knew that our world was changing, and we began taking strategic action as early as 1997 to position Mattel for the future.



Our first step was taken in March 1997 when we announced our merger with Tyco, the third largest U.S. toy company. This merger, which gave us brands such as Matchbox and Tyco Radio Control, enabled us to transform our Hot Wheels brand franchise into a broader global Wheels strategy that has grown three-and-a-half times in just 2 years. We now hold the #1 market share position in vehicles, having gone from a \$200 million Hot Wheels business in 1996 to a worldwide Wheels franchise totaling \$700 million last year. The Tyco merger also gave us the opportunity to integrate the Infant and Preschool brands of Sesame Street, Magna Doodle and View-Master into the Fisher-Price brand, which along with Disney Infant and Preschool and Winnie the Pooh, is now a \$1.7 billion franchise.

Then, in June of last year, we announced our acquisition of Pleasant Company and its blue-chip American Girl brand, which immediately brought us an additional \$300 million in direct-to-consumer business, and gives us the infrastructure to take many of Mattel's brands directly to the consumer. This makes infinite sense as we seek to expand our channels of distribution.

But to achieve our long-term goals, we did more than just make strategic acquisitions last year. We put our core brands back in order — most importantly, Barbie. For the first four months of 1998, we focused on cleaning up our Barbie retail inventory, which had been affected by 1997's late shipping of Barbie products. Because we focused on clean sell-through, we did have a 14 percent shipping decline for 1998, but we sold more Barbie products over the counter in 1998 than any other year in Barbie doll's history. And we reduced our retail inventory by more than



the 1999 Barbie collector line.

40 percent at our top U.S. accounts, and over 60 percent at Toys “R” Us.

We also put our Fisher-Price business back on course, achieving a strong return to profitability and an improved inventory position at retail — down 30 percent from last year.

The most positive outcome of 1998 was that our margins remained strong, despite the decline in Barbie, as evidenced by our gross margin of 49.4 percent, off only slightly from 49.6 percent in 1997. This resulted from improved margins in our fast-growing Wheels business, the much improved profitability at Fisher-Price and manufacturing efficiencies coming out of Asia.

Though our margins held up well, our selling, general & administrative and advertising ratios were out of line, as we incurred costs in anticipation of reaching the higher volume. In 1999, we will manage our SG&A and advertising ratios back to their 1997 levels, which were at historical highs. Then we will cut costs even further after we complete our merger with The Learning Company and realign the Mattel business in keeping with our long-term strategic vision.

Now I'd like to talk about our brands, and how we plan to expand them across multiple platforms as we work to become even more relevant in the lives of kids and their families.

Our \$2 billion-plus girls category now includes the brands of Barbie and American Girl, which together make Mattel the world's premier consumer products company for girls. Barbie ended the year with \$1.7 billion in worldwide sales, and she has entered her 40th anniversary year ready to



children's software title in 1998.

show she's not getting older — she's getting smarter. We will have more new dolls shipping each and every quarter, strategically spread throughout the year, and a new marketing plan to build a stronger Barbie brand relationship with adults, older girls beyond 8 years, and our core girls 3 to 7 years of age.

A new "Generation Girl" Barbie doll segment, targeted to an older girl, features friends from around the world, each with a contemporary look and individual personality. And Barbie will represent many new looks and body types in her 40th year, including a new full-bodied friend known and loved by all, Rosie O'Donnell.

Our Barbie collector products for 1999 will be led by a 40th anniversary limited edition Barbie and our very limited edition Millennium Bride. Frank Sinatra, and Elizabeth Taylor as Cleopatra, will join our growing celebrity collector business, which already includes Lucille Ball, Elvis Presley and Audrey Hepburn. Our direct-to-consumer collector catalog has been a very successful tool for us and will be made even stronger when it is available online starting in the second half of this year.

Our Barbie media business grew 39 percent to \$80 million in 1998, versus our total \$100 million interactive business. We had 7 of the top 10 children's software titles in the U.S., and Barbie CD-ROM titles achieved top 10 rankings in every country in Europe in December. Our interactive growth was led by the Barbie Digital Camera, which sold over 300,000 units, and was the #1 new software product of the year, according to *PC Data*.



And Barbie made her way successfully to the Internet in 1998. Barbie.com was named by *Media Metrix* to be one of the fastest-growing new shopping sites on the worldwide web, thanks to “My Design,” our design-your-own Barbie, which drew an average of 16.4 million daily hits in the month of December alone.

American Girl, the second largest girls brand in the world, produced \$300 million in full-year sales for 1998. We opened our first flagship store — called “American Girl Place” — in Chicago in November and achieved results that exceeded every benchmark we set for ourselves. More importantly, Pleasant Company will be selling all of its products online beginning in September of this year.

And since all of Pleasant Company’s business has been in the U.S., we plan to use Mattel’s international expertise to take the American Girl concept global, beginning in the year 2000.

At \$1.7 billion in sales, our Infant and Preschool business is now equal to Barbie in volume. Our profitability for this category is growing at exciting levels, which will add to our brightened future. And, all of our Infant and Preschool brands and characters will now be marketed under the Fisher-Price umbrella all around the world, allowing us to gain full leverage for this most important market share leader.

Winnie the Pooh was our fastest-growing brand last year, with sales up well over 50 percent and more than doubling outside of the U.S. This year, we will launch new segments for Pooh, including a girls and activity toy line. And our Sesame Street business, after tripling in 1997, saw a decline



licensing agreement with Ferrari.

in plush in 1998, but a big increase in basic Infant and Preschool toys. For 1999, we expect growth for this segment, driven by strong new introductions and Sesame Street's first new movie in 15 years — "Elmo in Grouchland."

I am very excited about our plans to launch our first-ever, direct-to-consumer catalog for Fisher-Price brands, which we will deliver in the second half of this year. Our Internet site is already in operation and our catalog products will be sold through our Web site as well.

At \$700 million in sales last year, Wheels is now our third largest category. Our combined Hot Wheels, Matchbox and Tyco Radio Control shipping increased by 21 percent in 1998, and our die-cast car unit sales increased to \$300 million, up from \$200 million in 1997.

We'll further fuel this growth with important new partnerships, such as our worldwide exclusive Ferrari relationship and our entry into Formula One Racing, the counterpart to NASCAR in Europe. We will continue to build our Wheels business around the world by continuing to implement the country-by-country focused strategy we developed with the Boston Consulting Group, which enabled us to realize a 30 percent growth in our international Wheels business last year. We will also introduce direct-to-consumer collector catalogues for both Hot Wheels and Matchbox, which will also be sold online in the second half.

Our Entertainment category — which includes Disney and Nickelodeon — had a very strong year in 1998, approaching \$500 million on the strength of "Mulan," "A Bug's Life" and "The Rugrats Movie." In fact, Mattel



partnership between Mattel and Intel.

Entertainment properties were up 14 percent. Our Nickelodeon business tripled last year, fueled by products based on the very popular "Rugrats," and on "Blue's Clues," the new top-ranked T.V. show from Nickelodeon. And our Disney business alone was up 16 percent for the year and now equals almost \$700 million around the world.

We have a great line-up of new entertainment properties for 1999. "A Bug's Life" will launch in Europe in the first quarter, and U.S. home video releases of "Mulan," "A Bug's Life" and "The Rugrats Movie" all will come this year. Then Disney's "Tarzan" will be released in June, and Disney's and Pixar's much anticipated "Toy Story 2" will debut in November.

Our future looks very bright, based on the strategic initiatives we have underway.

Growth of our core businesses will remain a key priority, and our global brand building strategy will continue to be a big part of that, as we seek to double our international sales.

To do that, we will implement the systematic approach developed through our work with the Boston Consulting Group. Our Wheels, Infant and Preschool, and Barbie franchises will be the targeted brands — and Europe and Japan the target markets.

Our second initiative has been to develop a \$1 billion software business. We began Mattel

Media in 1996 with \$20 million in sales and one

Barbie title. Over the last two years, we have grown to a \$100 million interactive franchise with the #1 top-selling children's title for three years in a row. This year, we will have 25 new Mattel Media titles, including CD-ROMs based on American Girl, Sesame Street and Caterpillar, which is part of the Matchbox brand. We will also have



offered through Mattel.com.

software for new platforms including Sony Playstation and Nintendo's Game Boy.

Deepening our entry into technology, we entered into a relationship with Intel last year. I am very proud of the products that have been developed through that partnership. The mission of our alliance has been to create PC-related products that allow children to see and do things they have never done before. We're delivering on that mission, with the X3 Microscope and the Me2Cam, which are being heralded as two of the most innovative new products of 1999. They will launch in the second half.

Mattel Media and Intel have given us a strong position in the interactive arena, but it made great sense for us to seek out a partner to help us realize our \$1 billion goal. The only company that met all the criteria we established was The Learning Company. We announced our proposed merger with The Learning Company in December. This merger will provide Mattel with tremendous opportunities for synergies, cross branding, age expansion, consumer relevancy and channel expansion. The Learning Company holds the #1 market share for both education software and productivity software, the #2 position for reference, and the #3 ranking for entertainment.

After the merger's completion, we will become the second largest consumer software company in the world, second only to Microsoft.

Our third initiative is to build a \$1 billion direct-to-consumer business. We have nearly \$500 million in direct sales today, most of it through catalogs, and we will have catalogs for all of our key brands available in the second half of the year. But the real opportunity in direct marketing is through an



Mattel Children's Hospital at UCLA.

Internet strategy based on all that our merger with The Learning Company will bring.

Mattel.com will bring every Mattel and Learning Company brand together at one family destination portal. Once there, consumers will be able to make purchases through one shopping cart, one database and one fulfillment center, with all of the customer service, friendliness and product quality that people would expect from our company.

We've come a long way in just three years. Let me share a timeline with you that shows how far we've come in building our brands, and where we're headed.

In 1996, our principal brands were Barbie, Fisher-Price, Disney, Hot Wheels, Nickelodeon and Cabbage Patch. Through our 1997 merger with Tyco, we added Matchbox, Tyco R/C, Sesame Street, View-Master and Magna Doodle. Last year, we added American Girl and the worldwide rights to Polly Pocket, which we will relaunch all around the world this year. And with our proposed merger with The Learning Company, we will add brands like Carmen Sandiego, Reader Rabbit, The Oregon Trail, National Geographic, American Greetings, The Print Shop, Riven and My:

Importantly, this growth in brand power has enhanced our category leadership. We're the #1 leader in Girls' brands at \$2 billion in annual sales, and #1 in Infant and Preschool, which is also headed for \$2 billion. We're #1 in Wheels, which is fast approaching \$1 billion, and #1 in Entertainment, at nearly a half-billion dollars. And with The Learning Company merger, we will reach \$1 billion in interactive sales.

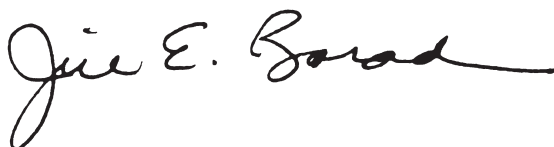


Perhaps our proudest moment of 1998 came in November, when we announced a \$25 million gift to UCLA Children's Hospital. In honor of the gift, the hospital has been renamed the Mattel Children's Hospital at UCLA, and this name will appear on a spectacular new I.M. Pei-designed facility that will be completed by 2004, providing a new landmark for the city. We are so incredibly proud to provide a gift of such lasting benefit to Mattel's hometown, while — through the hospital's renowned research and teaching activities — helping boys and girls in need all around the world.

Mattel is a strong company and will be even stronger. We should generate \$600 million in annual cash flow from operations going forward, which should increase to \$800 million following our merger with The Learning Company.

Our solid financial position, the power of our brands and the initiatives we have underway will help take us to a new level of strength and leadership. With all of this, and the support of our shareholders, we will continue to build the brand name of Mattel to mean what we hold so dearly as our mission — to serve the world's children and their families.

Sincerely,



Jill E. Barad

Chairman of the Board and Chief Executive Officer

March 22, 1999



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A Nos Actionnaires:

1998 a été une année décevante pour Mattel. Des changements dans notre activité, que nous avons certes anticipés, se sont produits beaucoup plus rapidement et plus intensément que prévu. Mais, en prévision de ces changements, nous avons déjà engagé des initiatives qui vont aboutir à des résultats positifs à long terme.

Nous avons été informés en début d'année d'une modification très importante du mode de commandes de notre principal client, Toys "R" Us, à la suite de leur décision de réduire leurs stocks de 500 millions \$ sur trois ans. Cependant, nous n'avions pas prévu que cette tendance de réduction des stocks gagnerait rapidement la plupart de nos principaux clients, aboutissant à une réduction générale des commandes de fin d'année. Aussi, lorsque les commandes de réapprovisionnement habituelles ne se sont pas matérialisées en décembre, nous avons décidé de prendre les mesures nécessaires pour adapter nos propres expéditions au plus près du système juste-à-temps. En conséquence, nous avons annoncé par anticipation une croissance stable du chiffre d'affaires et un bénéfice en baisse à approximativement 1,20 \$ par action. Et en fin d'année, nous avons publié comme résultat un bénéfice de 1,20 \$ par action avant charges exceptionnelles, et une baisse de 1 % des ventes.

La nouvelle positive de l'année 1998 a été que les ventes consommateurs de nos produits chez nos principaux clients américains ont augmenté de 12 %, et que les stocks de nos clients ont baissé au total de 30 %, et de 50 % chez Toys "R" Us.

Comme je l'ai dit précédemment, nous savions que notre monde changeait, et nous avons commencé à prendre des mesures stratégiques dès 1997 afin de préparer Mattel pour le futur.

La première mesure que nous avons prise date de mars 1997 lorsque nous avons annoncé la fusion avec Tyco, la troisième plus grande société de jouets des États-Unis.

Puis, en juin de l'année dernière, nous avons annoncé l'acquisition de Pleasant Company et de sa marque phare "American Girl", qui nous a immédiatement permis d'augmenter nos ventes directes aux consommateurs de 300 millions \$, et nous a dotés de l'infrastructure nécessaire pour vendre de nombreuses marques Mattel directement au consommateur.

Mais pour atteindre nos objectifs à long terme, nous avons fait plus l'année dernière que simplement réaliser des acquisitions stratégiques. Nous avons réorganisé nos principales marques, dont la plus importante, Barbie.

Durant les quatre premiers mois de 1998, nos efforts ont porté sur l'assainissement des stocks Barbie chez nos clients. De ce fait, nos expéditions ont certes diminué de 14 % en 1998, mais nous avons vendu davantage de produits Barbie en magasin en 1998 que durant toute autre année de l'histoire de Barbie.

Nous avons également relancé notre activité Fisher-Price, réussissant un important retour à la rentabilité et une amélioration de l'état de nos stocks chez nos clients (réduction de 30 % par rapport à l'année dernière).

Le résultat le plus positif de 1998 a été que nos marges sont restées fortes, malgré le déclin de Barbie, comme le témoigne notre marge brute de 49,4 %, inférieure seulement de peu à 1997 où elle était de 49,6 %.

À présent, j'aimerais vous parler de nos marques. La catégorie des jouets Filles, qui atteint plus de 2 milliards \$, inclut maintenant les marques Barbie et American Girl, qui à elles deux font de Mattel la première société mondiale de produits de consommation pour les filles. Barbie a fini l'année avec 1,7 milliard de ventes mondiales.

Notre activité Barbie Média a augmenté de 39 % en 1998 pour atteindre 80 millions \$.

Et en 1998, Barbie est entrée avec succès sur Internet. D'après Media Metrix, Barbie.com a été un des nouveaux sites de ventes le plus en expansion sur le web mondial, grâce à "My Design Barbie", la nouvelle poupée Barbie que l'on peut créer sur mesure.

American Girl, la deuxième plus grande marque mondiale pour filles, a réalisé 300 millions \$ de ventes annuelles en 1998. Et comme toute l'activité de Pleasant Company est aux États-Unis, nous prévoyons d'utiliser l'expérience internationale de Mattel pour étendre le concept 'American Girl' au monde entier à partir de l'an 2000.

Avec 1,7 milliard \$ de ventes, notre activité Premier Âge et Pré-Scolaire égale à ce jour Barbie en volume. Et à présent, toutes nos marques et personnages Premier Âge et Pré-Scolaire vont être commercialisés sous l'enseigne Fisher-Price dans le monde entier, nous permettant ainsi d'obtenir un effet de levier maximum pour ce leader le plus important du marché.

Avec 700 millions \$ de ventes l'an passé, l'univers des Wheels est à présent notre troisième plus grande catégorie. Nous allons continuer de développer l'activité Wheels dans le monde entier cette année, en poursuivant notre stratégie d'individualisation pays par pays élaborée avec le Boston Consulting Group, qui nous a permis d'augmenter de 30 % l'activité Wheels à l'international.

Notre segment de produits sous licences - qui inclut Disney et Nickelodeon - a réalisé une bonne année en 1998, approchant les 500 millions \$ grâce au succès de "Mulan", "1001 Pattes, A Bug's Life" et le film "Les Razmoket". Au total, les produits Mattel sous licences ont augmenté de 14 %.

Compte tenu des initiatives stratégiques que nous avons prises, notre futur est très prometteur. La croissance de nos activités principales va rester une priorité, et notre stratégie de croissance de marque globale va continuer de représenter une part importante de celle-ci, notre objectif étant de doubler nos ventes à l'international. Nos capitaux marques Wheels, Premier Âge, Pré-Scolaire et Barbie vont être nos principales priorités, et l'Europe et le Japon nos marchés cibles.

Notre deuxième initiative a consisté à développer une activité de logiciels de 1 milliard \$. Durant les deux dernières années, nous avons développé un capital marque de 100 millions \$. Nous avons annoncé notre offre de fusion avec The Learning Company en décembre, et une fois que la fusion sera achevée, nous deviendrons la deuxième société de logiciels grand public dans le monde, juste après Microsoft.

Notre troisième initiative consiste à construire une activité de vente directe aux consommateurs de 1 milliard \$. À ce jour, nous avons réalisé presque 500 millions \$ de ventes directes, mais la véritable opportunité de marketing direct réside dans une stratégie Internet basée sur l'avantage que va nous donner notre fusion avec The Learning Company.

Notre position financière solide, la puissance de nos marques et les initiatives que nous avons lancées vont dynamiser notre expansion et notre position de leader. Au vu de tout ceci, et avec l'aide de nos actionnaires, nous allons continuer de construire la marque Mattel pour que celle-ci représente la mission qui nous tient le plus à coeur, à savoir servir le monde des enfants et leur famille.

An Unsere Aktionäre

1998 war ein für Mattel enttäuschendes Jahr. Veränderungen in unserem Geschäft, die wir vorausgesehen hatten, stellten sich viel schneller und dramatischer ein, als wir es jemals erwartet hatten. Viele Initiativen sind vorangetrieben worden, um diese Veränderungen aufzufangen, und wir sind der Überzeugung, daß diese Initiativen zu langfristigen, positiven Erfolgen führen.

Früh im Jahr 1998 erfuhren wir, daß unser wichtigster Einzelhändler Toys "R" Us einen wesentliche Veränderung hinsichtlich seiner Einkaufspolitik beabsichtigte, indem die Warenbestände in einem Zeitraum von 3 Jahren um \$ 500 Millionen reduziert werden sollen. Wir sahen jedoch nicht vorher, daß dieser Trend zur Verringerung der Warenbestände so schnell auf die meisten unserer wichtigsten Einzelhändler übergehen würde. Diese Entwicklung resultierte in einer allgemeinen Verringerung der Aufträge am Ende des Jahres. Als daher im Dezember nicht wie gewohnt nachgeordert wurde, handelten wir der Situation angemessen, indem wir uns nun auf eine kurzfristige Bestell- und Lieferpraxis einstellten. Folglich kündigten wir vorab an, daß wir nur ein schwaches Wachstum erwarteten und unsere Gewinne wahrscheinlich auf etwa \$ 1.20 pro Aktie zurückgehen würden. Die Jahresabschlussergebnisse, die wir vorlegten, zeigten dann einen Gewinn pro Aktie von \$ 1.20 vor Berücksichtigung von außergewöhnlichen Belastungen, bei einem 1prozentigen Rückgang des Umsatzes.

Die positive Nachricht, die wir aus 1998 ziehen können, ist der Umstand, daß der Durchverkauf unserer Waren im Einzelhandel bei unseren Hauptkunden in den USA um 12 Prozent gestiegen ist. Der Warenbestand im Einzelhandel ist um 30 Prozent insgesamt gesunken und bei Toys "R" Us sogar um 50 Prozent.

Wie ich schon oben ausführte, wußten wir, daß sich unsere Geschäftswelt veränderte. Und so setzten wir schon 1997 strategische Maßnahmen durch, um Mattel auch zukünftig ideal zu positionieren.

Der erste Schritt in diese Richtung wurde im März 1997 unternommen, als wir die Fusion mit Tyco, dem drittgrößten Spielwarenhersteller der USA, ankündigten.

Im Juni letzten Jahres gaben wir dann die Übernahme der Pleasant Company und seiner erstklassigen Marke "American Girl" bekannt, welches uns sofort ein zusätzliches Geschäft von \$ 300 Millionen im Direktversand einbrachte und uns die geeignete Infrastruktur bietet, viele der Mattel-Marken direkt an den Endverbraucher zu bringen.

Zur Erreichung unserer langfristigen Ziele unternahmen wir letztes Jahr jedoch mehr als nur strategische Unternehmensübernahmen. Wir brachten unsere Kernmarken wieder in Linie - am wichtigsten hierbei war Barbie. In den ersten vier Monaten 1998 setzten wir den Fokus auf die Bereinigung unseres Barbie Warenbestandes im Einzelhandel. Da wir uns auf einen sauberen Durchverkauf konzentrierten, verzeichneten wir 1998 einen Umsatzrückgang von 14 Prozent. Wir verkauften in diesem Jahr allerdings mehr Barbie Produkte über den Ladentisch als jemals zuvor in der Geschichte von Barbie.

Des weiteren brachten wir unser Fisher-Price Geschäft wieder auf den richtigen Kurs und kehrten zu großer Rentabilität zurück und konnten so die Position unseres Warenbestandes im Einzelhandel verbessern - minus 30 Prozent gegenüber dem vergangenen Jahr.

Das positivste Ergebnis aus 1998 war, daß unsere Margen, trotz des Rückgangs bei Barbie, stark blieben, welches sich in unserer Bruttomarge von 49,4 Prozent ausdrückt. Dies ist nur geringfügig niedriger gegenüber 49,6 Prozent im Jahr 1997.

Ich möchte nun über unsere Marken sprechen. Unser \$ 2 Milliarden plus Mädchenbereich schließt nun Marken wie Barbie und American Girl ein, welche Mattel zusammengenommen zum weltweit größten Konsumgüterhersteller für Mädchen machen. Barbie beendete das Jahr mit einem weltweiten Umsatz von \$ 1,7 Milliarden.

Unser Barbie Media Geschäft wuchs 1998 um 39 Prozent auf \$ 80 Millionen. 1998 fand Barbie zudem erfolgreich den Weg ins Internet. Barbie.com wurde von Media Metrix als eine der am schnellsten wachsenden neuen Einkaufsseiten im weltweiten Web genannt, und dies dank "My Design", wo Mädchen eine Barbie Puppe nach ihren Wünschen herstellen können.

American Girl, die zweitgrößte Mädchenmarke der Welt, produzierte für 1998 einen Umsatz von \$ 300 Millionen. Und da das gesamte Geschäft der Pleasant Company bisher in den USA gewesen ist, planen wir, Mattels internationale Erfahrung und Expertise zu nutzen, um das Konzept des American Girl mit Beginn des neuen Jahrtausends global einzuführen.

Mit einem Umsatz von \$ 1,7 Milliarden ist unser Baby- und Vorschulspielzeugbereich inzwischen so groß wie Barbie. Alle unsere Baby- und Vorschulproduktmarken und Charaktere werden weltweit nun unter der Dachmarke Fisher-Price vermarktet. Dies erlaubt uns, das Potential dieser Marke maximal zu nutzen.

Mit einem Umsatz von \$ 700 Millionen im letzten Jahr ist Wheels nun unsere drittgrößte Kategorie. Wir werden unser Wheels-Geschäft dieses Jahr weltweit weiter ausbauen, indem wir die in Zusammenarbeit mit der Boston Consulting Gruppe auf die jeweiligen Länder abgestimmten Strategien umsetzen. Dies ermöglichte uns, in unserem internationalen Wheels-Geschäft ein Wachstum von 30 Prozent zu verwirklichen.

Unser Entertainment-Bereich - der Disney und Nickelodeon umfaßt - hatte 1998 ein starkes Jahr mit annähernd \$ 500 Millionen durch die Stärke von Filmen wie "Mulan", "Das große Krabbeln" und dem "Rugrats"-Film. Die Mattel Entertainment Linien stiegen gar um 14 Prozent.

Mit den strategischen Maßnahmen, die wir durchführen, sieht unsere Zukunft sehr positiv aus. Das Wachstum für unsere Kernmarken wird unsere oberste Priorität bleiben, und unsere Strategie der globalen Markenbildung wird hierbei weiterhin eine große Rolle spielen, da wir danach streben, unseren internationalen Umsatz zu verdoppeln. Unsere Marken im Bereich Wheels, Baby und Vorschule sowie Barbie werden erste Priorität haben - und Europa und Japan sind unsere Zielmärkte.

Unsere zweite Initiative war der Aufbau eines \$ 1 Milliarden Software-Geschäfts. Während der letzten zwei Jahre wuchsen wir zu einem \$ 100 Millionen interaktiven Franchise-Unternehmen.

Wir verkündeten unsere vorgeschlagene Fusion mit der Learning Company im Dezember und werden mit endgültigem Vollzug dieser Fusion gleich hinter Microsoft der zweitgrößte Hersteller von Konsumsoftwaregütern weltweit sein.

Unsere dritte Maßnahme hat den Aufbau eines \$1 Milliarden Direktverkaufs an den Endverbraucher zum Ziel. Heute verzeichnen wir bereits etwa \$ 500 Millionen. Das wahre Potential des Direktverkaufs liegt jedoch auf einer Internetstrategie, die auf den Möglichkeiten, die sich durch unsere Fusion mit der Learning Company eröffnen, basiert.

Unsere solide finanzielle Position, die Stärke unserer Marken sowie die Maßnahmen, die wir ergriffen haben, werden uns auf eine neue Ebene von Stärke und Führungsposition bringen. Mit all diesen Aktivitäten und der Unterstützung unserer Aktionäre werden wir weiter daran arbeiten, den Markennamen Mattel mit der Mission gleichzusetzen, die uns am wichtigsten ist - den Kindern dieser Welt und ihren Familien zu dienen.

Ai Nostri Azionisti:

Il 1998 è stato un anno deludente per Mattel. I cambiamenti nella nostra attività, che avevamo previsto, si sono verificati più rapidamente e drasticamente di quanto avessimo mai potuto prevedere. Avevamo comunque avviato iniziative per affrontare questi cambiamenti e crediamo che porteranno risultati positivi a lungo termine. Eravamo stati informati all'inizio dell'anno di un massiccio cambiamento nella politica degli acquisti da parte di un cliente chiave, Toys <<R>> Us, il quale ha deciso di ridurre il proprio inventario di \$500 milioni in tre anni. Ma non avevamo previsto che questa tendenza sarebbe stata trasmessa alla maggior parte dei nostri clienti chiave, portando a tagli indiscriminati negli ordini di fine anno. Per cui quando gli storici ri-ordini di dicembre non si sono materializzati, abbiamo deciso di prendere le misure necessarie per adattare le nostre spedizioni ad un modello del tipo "just in time". Come risultato, avevamo preannunciato una crescita zero delle vendite e una diminuzione degli utili a circa \$1.20 per azione. Ed i risultati finali son infatti di \$1.20 per azione, in presenza di un calo dell'1% nelle vendite.

La buona notizia del 1998 è rappresentata dal fatto che le vendite al dettaglio dei nostri prodotti presso i nostri clienti negli U.S erano cresciute del 12% e che gli inventari al dettaglio erano scesi del 30%, e del 50% per la Toys <<R>> Us.

Come già detto in precedenza, sapevamo che il nostro mondo stava cambiando e abbiamo avviato fin dal 1997 un'azione strategica per il futuro posizionamento di Mattel.

Il primo passo venne effettuato nel marzo 1997 con l'annuncio della nostra fusione con Tyco, la terza azienda di giocattoli più grande degli USA.

Poi, nel giugno scorso, abbiamo annunciato l'acquisizione della Pleasant Company e del suo marchio blue-chip <<American Girl>>, che ha portato un aumento immediato di \$300 milioni nel volume d'affari delle vendite dirette. Questo ci fornisce l'infrastruttura necessaria per portare molti dei marchi Mattel direttamente al consumatore.

Ma per raggiungere gli obiettivi programmati a lungo termine, nello scorso anno abbiamo fatto molto di più delle acquisizioni strategiche. Abbiamo riorganizzato le nostre linee portanti - e soprattutto Barbie.

Durante i primi quattro mesi del 1998, ci siamo concentrati sulla riduzione delle giacenze di Barbie presso il Trade. Dal momento che abbiamo puntato sulle rivendite, si è verificata una perdita del 14% nelle spedizioni per il 1998, ma abbiamo venduto più prodotti Barbie ai consumatori durante il 1998 di quanto si sia mai registrato nella storia di Barbie.

Abbiamo inoltre riorganizzato la linea Fisher-Price, realizzando notevoli profitti e migliorando la situazione dell'inventario al dettaglio - con una diminuzione del 30% rispetto allo scorso anno.

Il miglior risultato del 1998 è rappresentato dal fatto che i nostri margini sono ancora notevoli, nonostante le perdite nella linea Barbie, e il margine lordo del 49.4% ne è la prova, solo leggermente inferiore al 49.6% del 1997.

Ora vorrei parlare delle nostre linee. La nostra linea per bambine del valore di oltre \$2 miliardi ora include le linee Barbie e American Girls, che insieme fanno di Mattel l'azienda leader di prodotti per bambine. Barbie ha concluso l'anno con un volume di vendita di \$1.7 miliardi su scala mondiale.

I ricavi della linea Barbie Media sono aumentati del 39% fino a \$80 milioni nel 1998.

E Barbie ha inoltre ottenuto un notevole successo su Internet nel 1998. E infatti Barbie.com è stato citato da Media Metrix come uno dei nuovi siti shopping Internet con il tasso di crescita più alto, grazie a <<My Design>>, il nostro nuovo prodotto Disegna la tua Barbie.

American Girl, la seconda linea di prodotti per bambine più nota al mondo, ha raggiunto i \$300 milioni di vendite globali per il 1998. E dal momento che tutto il giro d'affari della Pleasant Company era limitato agli U.S., abbiamo in previsione di sfruttare l'esperienza internazionale di Mattel per diffondere il concetto di American Girl su scala mondiale, a partire dall'anno 2000.

Con vendite di \$1.7 miliardi, il business delle nostre linee Infant e Preschool è ora equivalente al volume d'affari di Barbie. Inoltre, tutte le nostre linee e i personaggi Infant e Preschool verranno da ora in poi commercializzate sotto il marchio Fisher-Price a livello mondiale, consentendoci di acquisire totale leadership in questo settore di mercato.

Con vendite di \$700 milioni durante lo scorso anno, Wheels rappresenta oggi la nostra terza linea portante. Continueremo a rafforzare la vendita di Wheels in tutto il mondo, applicando la strategia per ogni singolo paese studiata con la Boston Consulting Group, la quale ci ha permesso di realizzare una crescita del 30% del nostro volume d'affari internazionale Wheels.

Il 1998 è stato un anno positivo per la nostra linea Entertainment - che include Disney e Nickleodeon, con un volume d'affari di quasi \$500 milioni, sulla scia di <<Mulan>>, <<A Bug's Life>> e <<The Rugrats Movie>>. Infatti, le vendite di prodotti di Mattel Entertainment sono aumentate del 14%.

Il nostro futuro, considerate le iniziative strategiche già in atto, appare brillante.

La crescita delle nostre linee portanti sarà priorità assoluta e la nostra strategia di vendita globale continuerà a rappresentarne una componente essenziale, avendo come obiettivo il raddoppio delle vendite internazionali. I nostri prodotti Wheels, Infant, Preschool e Barbie saranno la prima priorità - e l'Europa e il Giappone sono i nostri prossimi target di mercato.

La seconda iniziativa è stata quella di sviluppare un software business di \$1 miliardo. Durante gli ultimi due anni, abbiamo raggiunto un volume d'affari di \$100 milioni per i prodotti interattivi.

Abbiamo annunciato l'intenzione di fonderci con la Learning Company in dicembre, e a completamento di tale fusione, diventeremo la seconda azienda del mondo per i prodotti software, dopo Microsoft.

La terza iniziativa è quella di arrivare ad un volume di vendite dirette di \$1 miliardo. A oggi abbiamo raggiunto circa \$500 milioni in vendite dirette, ma lo scopo finale è quello di studiare una strategia di vendita via Internet, obiettivo che ci sarà possibile raggiungere grazie alla fusione con la Learning Company.

La nostra solida posizione finanziaria, la forza delle nostre linee e le iniziative attualmente in atto, ci aiuteranno a raggiungere un nuovo livello di forza e leadership. Grazie a tutto questo e al supporto dei nostri azionisti, continueremo a rafforzare il nome Mattel, quale simbolo di quanto ci sta veramente a cuore - servire i bambini di tutto il mondo e le loro famiglie.

A Nuestros Accionistas:

1998 fue un año decepcionante para Mattel. Tal como habíamos previsto, se produjeron ciertos cambios en nuestro negocio, pero éstos ocurrieron con mayor celeridad de la esperada y fueron más drásticos de lo que habíamos anticipado. En cualquier caso, ya habíamos puesto en marcha iniciativas para contrarrestar estos cambios, y creemos firmemente que dichas acciones darán unos resultados muy positivos a largo plazo.

A principios de año, tuvimos conocimiento de un cambio radical en la estrategia de compra de nuestro principal cliente, Toys "R" Us, con el objetivo de reducir sus existencias por valor de 500 millones de dólares en el plazo de 3 años. Pero lo que no habíamos previsto es que esta tendencia de reducción de existencias se generalizaría entre todos nuestros principales clientes, provocando reducciones generales en los pedidos de final de año. Por ello, cuando en diciembre no se materializaron los habituales pedidos de repetición, decidimos tomar las medidas necesarias para adaptar nuestra propia facturación a un modelo más "justo a tiempo" y, como primera medida, anunciamos que esperábamos un mantenimiento de nuestra cifra de ventas, y que nuestros beneficios se reducirían a aproximadamente 1,20 dólares por acción. Los resultados que finalmente anunciamos a cierre de año fueron efectivamente unos beneficios de 1,20 dólares por acción antes de impuestos, y un 1% de disminución en ventas.

La noticia positiva de 1998 fue que el total de ventas al consumidor de nuestros productos en las principales cuentas de Estados Unidos experimentó un aumento del 12%, y que sus existencias bajaron un 30% en total, y un 50% en Toys "R" Us.

Como he mencionado anteriormente, sabíamos que nuestro sector estaba sufriendo importantes transformaciones, y ya en 1997 habíamos iniciado acciones estratégicas para situar a Mattel en una posición favorable de cara al futuro.

La primera de estas acciones se llevó a cabo en marzo de 1997, con el anuncio de nuestra fusión con Tyco, la tercera compañía juguetera de Estados Unidos.

Posteriormente, en junio de 1998, hicimos pública la adquisición de Pleasant Company y su marca estrella "American Girl", que supone un negocio de venta directa al consumidor por valor de 300 millones de dólares y nos proporciona la infraestructura necesaria para hacer llegar nuestras marcas directamente al consumidor.

Sin embargo, no sólo realizamos adquisiciones estratégicas para conseguir nuestros objetivos a largo plazo, sino que además reestructuramos nuestras marcas clave, en especial Barbie.

Durante el primer trimestre de 1998, nos centramos en el objetivo de liquidar las existencias sobrantes de Barbie que tenían nuestros clientes. Aunque esto produjo una reducción del 14% en facturación en 1998, conseguimos más ventas al consumidor de referencias de Barbie que cualquier otro año en la historia de la muñeca.

Asimismo, recondujimos nuestro negocio de Fisher-Price, recuperando la gran rentabilidad de esta línea y una buena situación de existencias en tiendas, un 30% inferior al año anterior.

El resultado más positivo de 1998 fue que nuestros márgenes se mantuvieron fuertes, a pesar del descenso en Barbie, lo que queda perfectamente evidenciado por nuestra cifra de margen bruto, un 49,4%, en comparación con el ligeramente superior 49,6% de 1997.

A continuación desearía comentar nuestras marcas. Nuestra categoría de niñas, con un volumen de más de 2 mil millones de dólares, incluye ahora las marcas Barbie y American Girl, que juntas convierten a Mattel en la primera compañía de productos para niñas a nivel mundial. Barbie cerró el año con unas ventas a nivel mundial de 170 mil millones de dólares.

Nuestro negocio de CD-ROMs de Barbie aumentó un 39%, alcanzando 80 millones de dólares en 1998.

Barbie también se abrió camino con éxito en Internet durante el año 1998. La página web Barbie.com fue considerada por Media Metrix una de las páginas web de compra directa con mayor crecimiento de la red mundial, gracias a la sección "My Design", donde las niñas tienen la oportunidad de pedir por Internet su propia muñeca Barbie, especificando las características que prefieren.

American Girl, la segunda marca de productos para niñas del mundo, alcanzó en 1998 unas ventas totales de 300 millones de dólares y, teniendo en cuenta que el negocio de Pleasant Company hasta ahora sólo se ha producido en Estados Unidos, esperamos aprovechar la experiencia de Mattel para globalizar el concepto "American Girl" a partir del año 2000.

Nuestro negocio de Bebé y Preescolar, con unas ventas de 170 mil millones de dólares, se sitúa al mismo nivel de volumen que Barbie. A partir de este año, comercializaremos todas nuestras marcas de Bebé y Preescolar bajo la marca paraguas de Fisher-Price en todo el mundo, lo que nos permitirá aprovechar la importancia de esta marca líder en participación de mercado.

Coches y Pistas, con ventas por valor de 700 millones de dólares en 1998, se ha convertido en nuestra tercera categoría en volumen. Este año, pensamos seguir aumentando nuestro negocio de esta categoría a nivel mundial mediante la misma estrategia que utilizamos en 1997; es decir, implementando estrategias adaptadas a cada país, que el año pasado desarrollamos en colaboración con Boston Consulting Group y que nos permitieron alcanzar un crecimiento del 30% en nuestro negocio de Coches y Pistas a nivel internacional.

1998 fue un año extraordinario para la categoría de productos licenciados, que incluye Disney y Nickelodeon. Las ventas llegaron a la cifra de 500 millones de dólares, gracias al éxito de las películas Mulan, Bichos y Rugrats. Esta categoría experimentó un aumento del 14% en 1998.

El futuro es prometedor; en base a las iniciativas estratégicas que hemos puesto en marcha. Este año, mantendremos como prioridad el crecimiento en nuestros negocios clave y, como parte crucial de este proceso, se encuentra nuestra estrategia de crecimiento global de nuestras marcas, con el objetivo de duplicar nuestra cifra de ventas a nivel mundial. Las categorías de Coches y Pistas, Bebé y Preescolar y Barbie serán prioritarias, y nuestros mercados objetivo serán Europa y Japón.

Nuestra segunda iniciativa ha sido la de desarrollar un negocio de software de mil millones de dólares. En los últimos dos años, hemos crecido hasta situar nuestros productos de software en la cifra de 100 millones de dólares.

Anunciamos la propuesta de fusión con The Learning Company en diciembre. Una vez que se haya efectuado esta fusión, nos convertiremos en la segunda compañía de software a nivel mundial, tras Microsoft.

Nuestra tercera iniciativa es crear un negocio de venta directa al consumidor de mil millones de dólares. En la actualidad, nuestra cifra de ventas directas es de aproximadamente 500 millones de dólares, pero la gran oportunidad de crecimiento en comercio directo nos la proporciona una estrategia basada en Internet y en las oportunidades generadas por nuestra próxima fusión con The Learning Company.

Nuestra sólida posición financiera, la importancia de nuestras marcas y las iniciativas que hemos puesto en marcha nos permitirán alcanzar un nuevo nivel de fuerza y liderazgo en el sector. Estos tres factores unidos al apoyo de nuestros accionistas, harán que la marca Mattel continúe creciendo para conseguir nuestro objetivo más importante: satisfacer las necesidades de los niños y de sus familias.

株主の皆様

1998年はマテル社にとって残念な年でした。予想していたビジネスにおける変化は、思ったより急激にやってきました。しかし弊社はこの変化に対してイニシアティブをとっているため、プラスになる長期的な実績を上げることができると思っています。

弊社にとって主要小売店であるToys "R" Usは、年頭に、彼らの在庫を3年間にわたって5億ドルにまで削減する旨を通知してきました。しかしこの在庫削減のトレンドが、他の主要小売店にまで急速に広がって行くことは予想できず、最終的に年末の購入が全般的に削減されることになりました。従って12月に慣例の再オーダーが現実化しなかった時点で、弊社の荷送りパターンを「即時着」に調整することを決定しました。結果としては成長が頭打ちにあることが予想されるとして、収益は1株で約\$1.2にまで低下するものとあらかじめ発表しました。年末の報告では、販売が1%低下し、公課前で収益が1株\$1.2となっています。

1998年度におけるこのましいニュースとしては、小売店における弊社製品の売りつくしが、米国のトップの顧客において12%上昇したことで、小売の在庫が総合的に30%に減少し、Toys "R" Usでは50%の減少となっています。前にも申しましたが、弊社は業界が変化していることを理解し、マテル社の将来の位置を確固たるものにすべく、1997年にすでに戦略的行動を開始しています。

米国の玩具会社で最も大規模なタイコとの合併は、弊社の最初のステップであります。

さらに昨年の6月には、プレザント・カンパニーと優良株の「アメリカン・ガールズ」ブランドを買収し、これによって即時3億ドルの直販ビジネスが追加されることになり、マテル社の製品を直販する土台ができました。

しかし弊社の長期的なゴールを達成するために行なったことは、昨年の戦略的な合併だけではありません。弊社の核心的なブランドのオーダーに尽力しました。最も重要なアイテムはバービーでした。1998年の最初の4ヵ月間は、バービーの小売における売りつくしに力を入れました。完全な売り尽くしを目指したため、1998年には荷積み率が14%減少したものの、1998年度にはバービーの歴史上、店頭でのバービー製品の売上が最高となりました。

またフィッシャー・プライスの販売にも力を入れ、これも利益率が伸びて小売における在庫状況も進展して、昨年に比べて30%低下しています。

1998度において最も確実な実績は、バービーの値下げにも拘わらず、粗利の-marginが定着しており、1997年の49.6パーセントとほんの少ししか変わらない、49.4パーセントとなっています。

ここで弊社のブランドに触れてみたいと思います。20億ドルを上回るガール・カテゴリーにはバービーとアメリカン・ガールがあり、これがマテル社を世界的なガール製品の主要製品会社にしています。年間の売上は世界中で17億ドルとなっています。

1998年には、バービーのメディア・ビジネスは39パーセント上昇して、8千万ドルになりました。さらにバービーは1998年度にインターネットに登場し、成功を納めています。

Barbie.comはメディア・メトリックス社によって、世界的なウェブにおける急成長のショッピング・サイトであると指名されており、これは自由自在にバービーをデザインできる、弊社の「マイ・デザイン」のおかげです。

世界で第2のガール・ブランドであるアメリカン・ガールは、1998年度に全体的に3億ドルの売上を上げました。プレザント・カンパニーのビジネスは全て米国内で行なわれていましたが、マテル社の国際的ビジネス知識を用い、2000年度からは「アメリカン・ガール」のコンセプトを世界的なものにする予定です。

17億ドルの売上を上げている幼児とプレスクールのビジネスは、その量においてバービーに匹敵しています。この幼児とプレスクールブランドおよびキャラクターは、今後世界中でフィッシャー・プライスの下にマーケットされることとなり、最も重要な市場シェアを得る上での強力なデコになることと思います。

昨年の売上が7億ドルのホイール・ビジネスは、現在弊社にとって第3番目のカテゴリーとなっています。今年もボストン・コンサルティング・グループと共に開発した、国毎に焦点をあてる戦略を継続することでこのホイール・ビジネスを世界的に固めて行く予定であり、この戦略によってこれまでに国際ホイール・ビジネスが30%成長しています。

弊社のエンターテインメント・カテゴリーであるディズニーとニコロデオンは1998に着実な成果を上げており、「ムーラン」、「バグズ・ライフ」、「ラグラッツ・ムービー」を中心に、ほぼ5億ドルを売り上げました。事実、マテル・エンターテインメントの領域は14パーセントの増加です。

弊社の未来は、現在実行中の戦略的イニシアティブによって、大変明かるいものであるといえます。弊社の核心となる製品の成長はこれからも優先となり、国際的な売上を2倍化するにあたり、世界的なブランドを確立して行く戦略も大きな要素となることと思います。ホイール、幼児とプレスクール、バービーのフランチャイズは最優先であり、ヨーロッパと日本を市場ターゲットとしています。

弊社の第2のイニシアティブは、10億ドルのソフトウェアの開発です。過去2年間にわたり、1億ドルの相互作用フランチャイズとして成長しました。

12月にはザ・ラーニング・カンパニーとの合併を発表しましたが、この合併が完了したあかつきには、マイクロソフト社に続く、世界第2の大規模な消費者ソフトウェア会社となります。

弊社の第3のイニシアティブは、10億ドルの直販ビジネスを確立することです。現在ほぼ5億ドルの直販の売上がありますが、直販における絶好の機会は、ザ・ラーニング・カンパニーとの合併によるインター戦略にあります。弊社の確固たる財政状況、ブランド力、さらにイニシアティブにより、新たなレベルのリーダーシップを取って行くことができることと思います。これらの要素と株主の皆様のご支援により、世界中の子供達やその家族にご奉仕する弊社のすばらしい使命をもって、マテルのブランド名を高めていきたいと思います。

致我们的股东:

对 Mattel 来说, 1998 年是一个令人失望的一年。我们在生意上出现的变化—尽管我们曾预料到这些变化会发生—发生之迅速和之富于戏剧性, 完全是我们始料所不及的。然而我们在起初采取的一些步骤正在生效, 来应付这些变化。我们相信, 这些步骤会带来积极的和长远的效果。

在年初时, 我们得知, 我们的主要零售商—Toys "R" Us—在过去的 3 年中采取措施, 减少了 5 亿美元价值的库存。然而我们并没有预见到, 这种减少库存的趋势会很快波及到我们的大多数零售商, 造成年终购买额的全面下降。所以在 12 月份, 在以往的重新订货没有实现时, 我们决定采取适当的措施, 以刚好运到的做法调整我们的货运。结果, 我们提前宣布, 我们可以预计货运会有高额度的增长, 同时, 我们赢利将会降低, 大约每股份为 1.20 美元。我们所报告的年终结果是, 销售额为每股份 1.20 美元(减除开销之前), 即销售额减少百分之一。

1998 年度的好消息是, 我们产品的零售额在美国国内的销售居于首位, 增长了百分之十二, 而零售的库存总量下降了百分之三十, Toys "R" Us 的库存总量下降为百分之五十。

正如我前面所讲的一样, 我们的世界正在发生变化, 我们从 1997 年起便开始采取一些战略性的措施, 以使 Mattel 准备应付未来。

在 1997 年 3 月我们采取的第一项措施是, 我们宣布了与 Tyco 公司—美国第三大玩具公司的合并。

接着, 到去年的 6 月份, 我们又宣布了购买 Pleasant 公司及其上市名牌产品“美国女孩”(American Girl), 这立即为我们在直销的生意中带来了 3 亿美元的生意, 并为我们提供了使许多 Mattel 的名牌产品也可以直接销售给客户的渠道。然而, 为了达到我们长远的目标, 我们去年所做的不仅仅是战略性的兼并。我们还把我们的一些核心名牌产品加以整顿, 其中最重要的产品之一就是 Barbie 娃娃。在 1998 年的头 4 个月当中, 我们集中清理了我们的 Barbie 娃娃零售的库存。由于我们集中精力进行清仓销售, 我们 1998 年的出货的确有百分之十四的下降。但是, 我们在 1998 年度的零售中, Barbie 娃娃

产品的销售额在 Barbie 娃娃的历史中好过其他任何一年。

我们还重新整顿了我们 Fisher-Price 的生意, 并且取得了很好的利润, 同时还改善了零售库存的状况, 使其与去年比较下降了百分之三十。

1998 年最好的成果是我们的盈余始终很好。尽管 Barbie 娃娃的销售有所下降, 根据我们 49.4% 总赢利来计算, 仅比 1997 年的 49.6% 下降了一点。

现在, 我想来谈谈我们自己的名牌产品。我们有 20 多亿美元生意的女孩子产品, 类别目前包括 Barbie 娃娃和“美国女孩”(American Girl) 名牌产品。这些名牌产品一起使 Mattel 成为世界上为女孩提供消费品的最主要的公司。到去年底, Barbie 产品在世界范围的销售额达到 10.7 亿美元。

1998 年度, 我们与 Barbie 相关的媒介生意增长了 39%, 达到 8 千万美元。

同时, Barbie 在 1998 年度也成功地进入了国际网络。Barbie.com 被 Media Metrix 称为世界网络上成长最快的新形采购网址之一。这也要感谢 "My Design," (“我的设计”) 这一网址, 它可以自行设计您自己的 Barbie 娃娃。American Girl (美国女孩), 是世界上第二大的女孩名牌产品。1998 年度的总销售额达到 3 亿美元。同时, 由于 Pleasant 公司的全部生意始终都在美国境内, 我们计划利用 Mattel 的国际经验, 自 2000 年起将 'American Girl' (美国女孩), 的观念推向全球。

我们其销售额达到 10.7 亿美元的婴幼儿和学龄前儿童产品的生意目前在销售额方面与 Barbie 娃娃产品并驾齐驱。同时, 我们所有的婴幼儿和学龄前儿童名牌产品及其特征都将在 Fisher-Price 的名下在世界范围内进行开发, 这可以为我们在这一重要的市场方面占据领先地位提供优异的条件。

其去年的销售额为 7 亿美元的轮子类产品目前成为我们的第三大类别的产品。我们将继续在世界范围内加强这一生意, 即同 Boston Consulting Group 一道实施我们集中精力一个国家一个国家的突破战略。这一战略使我们在世界轮子产品的生意上实现了百分之三十的增长率。

我们的娱乐性产品类包括迪斯尼和 Nickelodeon 的产品。这类产品在 1998 年里销售很旺。由于“花木兰”, “昆虫的生活”(A Bug's Life), “The Rugrats 电影”的影响, 销售额接近 5 亿美元。事实上, Mattel 娱乐性设施的销售额提高了百分之十四。

由于我们采取的一些行之有效的战略性措施，我们的未来十分光明。保证我们的核心生意的增长仍将是我们的首要任务。同时，在全球发展我们的名牌产品的战略将继续成为这一任务的重要组成部分。因为我们需要成倍增加我们的国际销售额。我们的轮子产品，婴幼儿和学龄前儿童产品以及 **Barbie** 产品的连锁机构将获得第一优先发展。同时，欧洲和日本是我们推销的目标。

我们的第二项措施是开发拥有 10 亿美元价值的软件生意。在过去 2 年期间，我们成长为这一领域中拥有一亿美元的相互联系的连锁企业。

在去年 12 月，我们宣布了我们同 **The Learning Company** 合并的计划。一旦这一合并计划完成，我们将成为仅次于 **Microsoft** 的世界上第二大软件公司。

我们的第三项措施是开发价值为 10 亿美元的客户直销生意。今天，我们已经在直销领域达到 5 亿美元的销售额。但是，通过网际网络的战略，并基于我们与 **The Learning Company** 公司的合并，将为我们带来在直销方面的真正的机会。

我们坚实的财政上的势力，我们的名牌产品产品的影响力，以及我们采取的措施将帮助我们到达一个新的实力和领先地位的阶段。有了这一切，以及我们股东们的支持，我们将继续建立 **Mattel** 的名牌地位，表明我们坚定地维护我们的使命。这一使命即：服务于世界上的儿童和他们的家庭。

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Five-Year Financial Summary

(In thousands, except per share and percentage information)	For the Year Ended December 31 (a)				
	1998	1997	1996	1995	1994
Operating Results:					
Net sales	\$4,781,892	\$4,834,616	\$4,535,332	\$4,369,816	\$3,971,226
Gross profit	2,362,993	2,400,000	2,219,758	2,067,740	1,881,060
% of net sales	49%	50%	49%	47%	47%
Operating profit (b)	575,896	515,212	636,982	607,651	449,228
% of net sales	12%	11%	14%	14%	11%
Income before income taxes and extraordinary item	465,063	425,082	536,756	504,668	362,157
Provision for income taxes	132,799	135,288	164,532	166,779	137,487
Income before extraordinary item	332,264	289,794	372,224	337,889	224,670
Extraordinary item - loss on early retirement of debt	-	(4,610)	-	-	-
Net income	332,264	285,184	372,224	337,889	224,670
Income Per Common Share (c):					
Income before extraordinary item					
Basic	1.11	0.96	1.26	1.13	0.74
Diluted	1.10	0.94	1.23	1.11	0.73
Net income					
Basic	1.11	0.95	1.26	1.13	0.74
Diluted	1.10	0.93	1.23	1.11	0.73
Dividends Declared Per Common Share (c)	0.31	0.27	0.24	0.19	0.15

(In thousands)	As of Year End (a)				
	1998	1997	1996	1995	1994
Financial Position:					
Cash and marketable securities	\$ 212,454	\$ 694,947	\$ 550,271	\$ 511,061	\$ 290,157
Accounts receivable, net	983,050	1,091,416	948,940	886,344	990,346
Inventories	584,358	428,844	444,178	407,551	405,427
Total assets	4,262,165	3,803,791	3,581,142	3,341,370	3,150,438
Short-term borrowings	134,006	17,468	28,924	76,443	57,531
Long-term liabilities	1,124,756	808,297	633,342	721,739	606,430
Stockholders' equity	1,820,198	1,822,070	1,805,923	1,551,680	1,385,777

(a) Consolidated financial information for 1994-1997 has been restated retroactively for the effects of the March 1997 merger with Tyco Toys, Inc. ("Tyco"), accounted for as a pooling of interests.

(b) Represents income from operations before interest expense and provision for income taxes. In 1998, operating profit was reduced by a nonrecurring charge of \$38.0 million related to a voluntary recall of certain PowerWheels®, ride-on vehicles and a one-time charge of \$6.0 million in connection with the proposed Toys R Us-related antitrust litigation settlement. In 1997, operating profit was reduced by a nonrecurring charge of \$275.0 million for transaction, integration and restructuring costs related to the merger with Tyco. In 1996, operating profit was reduced by a nonrecurring charge of \$21.8 million related to the accounting for certain royalties and participation fees in prior periods. In 1995, operating profit was reduced by a nonrecurring charge of \$8.9 million related to a restructuring program implemented to reduce operating expenses at certain of Tyco's business units. In 1994, operating profit was reduced by a nonrecurring charge of \$76.7 million principally related to the consolidation of manufacturing operations and the reduction of headquarters expense and support functions worldwide.

(c) Per share data reflect the retroactive effect of stock splits distributed to stockholders in March 1996, January 1995 and January 1994, and the 1997 merger with Tyco.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Statement

Certain expectations and projections regarding the future performance of Mattel, Inc. and its subsidiaries ("Mattel" or the "Company") discussed in this annual report are forward-looking and are made under the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. These expectations and projections are based on currently available competitive, financial, and economic data along with the Company's operating plans and are subject to certain future events and uncertainties. Forward-looking statements can be identified by the use of forward-looking terminology, such as may, will, should, expect, anticipate, estimate, continue, plans, intends or other similar terminology. Management cautions you that the following factors, among others, could cause the Company's actual consolidated results of operations and financial position in 1999 and thereafter to differ significantly from those expressed in forward-looking statements:

Marketplace Risks

- Increased competitive pressure, both domestically and internationally, which may affect the sales of the Company's products
- Significant changes in the buying patterns of major customers, such as the recent shift by some retailers to just-in-time inventory management, which may limit the Company's ability to accurately forecast reorders or cause a decrease in sales after related expenses have already been incurred
- Dependence on the timely development, introduction and customer acceptance of new products, which may affect the Company's ability to successfully redesign, restyle and extend existing core products and product lines and to successfully bring new products to market
- Possible weaknesses in economic conditions, both domestically and internationally, which may affect the sales of the Company's products and the costs associated with manufacturing and distributing these products

Financing Considerations

- Currency fluctuations, which may affect the Company's reportable income
- Significant changes in interest rates, both domestically and internationally, which may affect the Company's cost of financing both its operations and investments

Merger-Related Risks

- Difficulty integrating the operations of The Learning Company, Inc. into the Company following the proposed merger, which may impede the Company's ability to achieve savings or operating synergies from the merger

Year 2000 Compliance

- Potential inability of computer systems or software products used by the Company and/or its customers and suppliers to properly recognize and process date-sensitive information beyond January 1, 2000, which may result in an interruption in normal business operations of the Company, its suppliers and customers

Other Risks

- Inability to achieve cost savings expected as part of restructuring activities, which may result in higher than expected costs following such restructurings

- Development of new technologies, including the Internet, which may create new risks to the Company's ability to protect its intellectual property rights
- Changes in laws or regulations, both domestically and internationally, including those affecting consumer products or environmental activities or trade restrictions, which may lead to increased costs or interruption in normal business operations of the Company
- Adverse results of litigation, governmental proceedings or environmental matters, which may lead to increased costs or interruption in normal business operations of the Company

Summary

You should read this analysis in conjunction with the Company's consolidated financial statements that begin on page 33.

Mattel designs, manufactures, and markets a broad variety of children's products on a worldwide basis through both sales to retailers and direct to consumers. The Company's business is dependent in great part on its ability each year to redesign, restyle and extend existing core products and product lines, to design and develop innovative new products and product lines, and to expand its marketing capability.

The Company plans to continue to focus on its portfolio of brands that have fundamental play patterns and have historically had worldwide appeal, have been sustainable, and have delivered consistent profitability. The Company's portfolio of brands can be grouped in the following four categories:

Girls - including Barbie® fashion dolls and accessories, collector dolls, software, Fashion Magic®, American Girl®, Cabbage Patch Kids®, and Polly Pocket®

Infant and Preschool - including Fisher-Price®, Disney preschool and plush, Power Wheels®, Sesame Street®, See 'N Say®, Magna Doodle®, and View-Master®

Entertainment - including Disney, Nickelodeon®, games, and puzzles

Wheels - including Hot Wheels®, Matchbox®, Tyco® Electric Racing, and Tyco® Radio Control

Results of Operations

The following is a percentage analysis of operating results for the past three years:

	For the Year		
	1998	1997	1996
Net sales	100%	100%	100%
Gross profit	49.4%	49.6%	48.9%
Advertising and promotion expenses	17.0	16.1	17.2
Other selling and administrative expenses	18.5	16.5	17.0
Amortization of intangibles	0.9	0.6	0.7
Restructuring and integration charges	-	5.7	-
Special charges	0.9	-	-
Other expense (income), net	0.1	-	-
Operating profit	12.0	10.7	14.0
Interest expense	2.3	1.9	2.2
Income before income taxes and extraordinary item	9.7%	8.8%	11.8%

1998 Compared to 1997

Net income for 1998 was \$332.3 million or \$1.10 per diluted share as compared to \$285.2 million or \$0.93 per diluted share in 1997. 1998 net income was impacted by a \$27.2 million after-tax charge (\$0.09 per diluted share) related to a voluntary recall of certain Power Wheels® ride-on vehicles and a one-time charge of \$4.3 million after taxes (\$0.01 per diluted share) in connection with the proposed Toys R Us-related antitrust litigation settlement. Net sales for 1998 reached \$4.78 billion, a decrease of 1% from \$4.83 billion in 1997. Cutbacks in purchases by retailers to adjust to a just-in-time buying pattern negatively impacted sales. Sales in the Girls category decreased 4% largely due to a 14% decline in Barbie® products, as a result of high retail inventory levels entering 1998. As a result of the Pleasant Company acquisition in July 1998, the American Girl® brand contributed \$213.2 million in gross sales, which helped to partially offset the decline in Barbie®. Sales in the Infant and Preschool category decreased 3%, largely attributable to declines in Sesame Street® and Fisher-Price® products, partially offset by an increase in Disney's Winnie the Pooh®. Sales in the Wheels category grew 21%, reflecting growth in both Hot Wheels® and Matchbox® vehicles and playsets. Sales in the Entertainment category, which includes Disney and Nickelodeon®, increased 14% largely due to this year's introduction of toys associated with the feature motion pictures "A Bug's Life" and "The Rugrats Movie".

Sales to customers within the US declined 2% and accounted for 66% of consolidated gross sales in both 1998 and 1997. Sales to customers outside the US were down 1%, including an unfavorable foreign exchange effect of approximately \$30 million due to the generally stronger US dollar relative to 1997. At comparable foreign exchange rates, sales internationally grew 1%.

Gross profit as a percentage of net sales remained relatively constant at 49.4% compared to 49.6% in 1997. As a percentage of net sales, advertising and promotion expenses increased approximately one percentage point to 17.0%, and selling and administrative expenses increased two percentage points to 18.5%. Both these ratios increased relative to last year as a result of unanticipated cutbacks in buying by retailers due to a continuing shift by these retailers to just-in-time inventory management. To respond to such shifts, the Company took appropriate actions to adjust its own shipping to more of a just-in-time pattern. As a result, products that would have previously been shipped in December will be shipped closer to the time that they will be purchased by the consumer. The Company plans to manage its advertising and selling and administrative levels in 1999 to bring them back in line with its historical ratios. Amortization of intangibles increased by \$9.8 million, mainly due to the amortization of goodwill in connection with the 1998 acquisitions of Pleasant Company and Bluebird Toys PLC ("Bluebird").

Interest expense increased \$20.7 million primarily due to increased short- and long-term borrowings to finance the Company's 1998 acquisitions of Pleasant Company and Bluebird.

1997 Compared to 1996

Net income for 1997 was \$285.2 million or \$0.93 per diluted share as compared to \$372.2 million or \$1.23 per diluted share in 1996. 1997 net income was impacted by a \$209.7 million after-tax charge

(\$0.71 per diluted share) related to a nonrecurring charge for transaction, integration and restructuring costs related to the Mattel restructuring and Tyco integration, and an extraordinary loss of \$4.6 million net of taxes (\$0.01 per diluted share) for the early retirement of debt assumed as part of the Tyco merger. Net sales for 1997 were \$4.83 billion, an increase of 7% from \$4.54 billion in 1996. Sales growth included a \$138.5 million unfavorable foreign exchange effect from the generally stronger US dollar relative to 1996. Sales in the Girls category grew 4% due to the strength in Barbie® and Barbie®-related products, partially offset by declines in large and small dolls. Sales in the Infant and Preschool category increased 15%, led by strength in Sesame Street® and Disney's Winnie the Pooh®, partially offset by a decline in Fisher-Price® products. The Wheels category increased 21%, driven by an increase in Hot Wheels®. Sales in the Entertainment category, which includes Disney and Nickelodeon®, decreased 4%.

Sales to customers within the US grew 14% and accounted for 66% of consolidated gross sales in 1997 compared to 62% in 1996. Sales to customers outside the US decreased 5%, including the unfavorable foreign exchange effect of the generally stronger US dollar relative to the prior year. At comparable foreign exchange rates, sales internationally grew 3%.

Gross profit as a percentage of net sales increased to 49.6% from 48.9%, principally due to improved product mix. As a percentage of net sales, advertising and promotion expenses decreased approximately one percentage point to 16.1%, primarily due to cost savings realized from the Company's merger with Tyco. As a percentage of net sales, other selling and administrative expenses decreased to 16.5% from 17.0%, reflecting the impact of the Company's effort to control costs and direct cost savings realized from the 1997 Tyco integration and Mattel restructuring plan.

Interest expense decreased \$10.1 million largely due to lower average domestic short-term borrowings during 1997.

Income Taxes

The effective income tax rate was approximately 29% in 1998 compared to 32% in 1997 and 31% in 1996. The effective tax rate decreased in 1998 due to an increase in income earned in locations with lower tax rates and a reduction in restructuring expenses without income tax benefits.

Pre-tax income earned from US operations as a percentage of the consolidated pre-tax income is less than the sales to US customers as a percentage of the consolidated gross sales. This difference results from corporate headquarters expenses incurred in the US that decreased US pre-tax income and from profits from foreign manufacturing activities that relate to sales ultimately made to US customers.

Financial Position

The Company's financial position remained strong in 1998 primarily due to its profitable operating results. At December 31, 1998, the Company's cash position was \$212.4 million, compared to \$694.9 million as of the end of 1997. Cash decreased \$482.5 million primarily due to cash consideration paid in connection with the acquisitions of Pleasant Company and Bluebird. Accounts receivable decreased \$108.4 million to \$983.1 million due to lower orders by major

retailers in fourth quarter 1998. Inventories increased \$155.5 million to \$584.4 million, reflecting the sales shortfall in the 1998 fourth quarter and the addition of Pleasant Company inventory. Property, plant and equipment, net grew \$134.9 million to \$736.5 million due to assets acquired as part of the acquisition of Pleasant Company and investments in the expansion of the Company's manufacturing facilities located in Mexico and Asia. Intangibles increased \$719.4 million to nearly \$1.25 billion due to goodwill generated from the Pleasant Company and Bluebird acquisitions.

Short-term borrowings increased \$116.5 million compared to 1997 from financing the acquisitions of Pleasant Company and Bluebird. Current portion of long-term liabilities increased \$19.9 million primarily due to the reclassification of \$30.0 million in medium-term notes payable in 1999 from long-term debt.

A summary of the Company's capitalization is as follows:

(In millions)	As of Year End			
	1998		1997	
Medium-term notes	\$ 540.5	18%	\$ 520.5	20%
Senior notes	400.0	14	100.0	4
Other long-term debt obligations	43.0	1	55.0	2
Total long-term debt	983.5	33	675.5	26
Other long-term liabilities	141.3	5	132.8	5
Stockholders' equity	1,820.2	62	1,822.1	69
	\$2,945.0	100%	\$2,630.4	100%

Total long-term debt increased \$308.0 million mainly due to the issuance of \$300.0 million of senior notes to finance the acquisitions of Pleasant Company and Bluebird. Medium-term notes increased by \$20.0 million due to the issuance of \$50.0 million in notes, partially offset by the reclassification of \$30.0 million payable in 1999 to current portion of long-term debt. The Company expects to satisfy its future long-term capital needs through the retention of corporate earnings and the issuance of long-term debt instruments. In November 1998, the Company filed its current universal shelf registration statement allowing it to issue up to \$400.0 million of debt and equity securities, all of which was available to be issued as of December 31, 1998. Stockholders' equity of \$1.8 billion remained consistent with 1997 as a result of treasury stock purchases and dividend declarations on common and preferred stock, which were largely offset by profitable operating results and reissuance of treasury stock for the exercise of nonqualified stock options by the Company's employees.

Liquidity

The Company's primary sources of liquidity over the last three years have been cash on hand at the beginning of the year; cash flows generated from operations, long-term debt issuances and short-term seasonal borrowings. Profitable operating activities generated cash flows of \$547.5 million during 1998, compared to \$481.9 million in 1997 and \$524.8 million in 1996.

The Company invested its cash flows during the last three years in the acquisitions of Pleasant Company and Bluebird, additions to tooling in support of new products, and construction of new manufacturing facilities.

The Company received cash flows from the issuance of senior notes in 1998 and medium-term notes in 1998 and 1997. Cash received from these debt issuances was used to fund the acquisitions of Pleasant Company and Bluebird, to retire higher-cost debt and to support operating activities. In 1998, the Company repaid the long-term debt and mortgage note assumed as part of the Pleasant Company acquisition. In 1997, the Company redeemed the 10-1/8% notes assumed as part of the acquisition of Tyco and repaid its 6-7/8% senior notes upon maturity. Cash was also spent during the last three years to purchase treasury stock to provide shares for issuance under the Company's employee stock option plans and the exercise of outstanding warrants. In addition, over the last three years, the Company has consistently increased its cash payments for common dividends.

Seasonal Financing

The Company expects to finance its seasonal working capital requirements for the coming year by using existing and internally generated cash, issuing commercial paper, selling certain trade receivables and using various short-term bank lines of credit. The Company's domestic committed unsecured credit facility provides \$1.0 billion in short-term borrowings from a commercial bank group. This facility provides for up to \$700.0 million in advances and backup for commercial paper issuances, and up to an additional \$300.0 million for nonrecourse purchases of certain trade accounts receivable by the bank group over the next four years. Under its domestic credit facility, the Company is required to meet financial covenants for consolidated debt-to-capital and interest coverage. Currently the Company is in compliance with such covenants.

The Company also expects to have approximately \$370 million of individual short-term foreign credit lines with a number of banks available in 1999, which will be used as needed to finance seasonal working capital requirements of certain foreign affiliates.

Pending Business Combination

In December 1998, Mattel and The Learning Company entered into a merger agreement. The stock-for-stock transaction is subject to approval by the stockholders of both Mattel and The Learning Company and by certain regulatory agencies. The merger will be accounted for as a pooling of interests, which means that for accounting and financial reporting purposes, Mattel and The Learning Company will treat their companies as if they had always been combined. The combined company will likely incur transaction costs of approximately \$75 million to \$85 million, including investment banking, legal and accounting fees, and contractual incentive benefits. Management believes the merger will be completed in the second quarter of 1999. The number of shares of Mattel common stock to be issued to The Learning Company's common and preferred stockholders, together with the Mattel common stock to be issued upon the exchange of the exchangeable shares of The Learning Company's Canadian subsidiary, is expected to represent between approximately 27% and 30% of Mattel's outstanding voting power after the merger, depending on the actual exchange ratio at the time of the merger.

Acquisitions

During 1998, the Company acquired Pleasant Company and Bluebird. These acquisitions were accounted for using the purchase method of accounting, which means that the results of operations of the acquired companies have been included in Mattel's consolidated financial statements from their respective dates of acquisition. Proforma financial information for these acquisitions has not been presented since they did not meet the test of significance individually or in the aggregate.

In July 1998, the Company completed its acquisition of Pleasant Company, a Wisconsin-based direct marketer of books, dolls, clothing, accessories, and activity products included under the American Girl® brand name. The Company paid approximately \$715 million, including investment advisor and other costs directly related to the acquisition. The excess of cost over the estimated fair market value of tangible net assets acquired was approximately \$690 million. Total excess has been allocated to customer lists, a covenant not-to-compete, and magazine subscription lists that are being amortized on a straight-line basis over a 3 to 15 year period, with the remaining excess being amortized on a straight-line basis over 40 years.

In June 1998, the Company acquired Bluebird, a company organized in the United Kingdom, from which Mattel previously licensed the product designs for the Polly Pocket® and Disney Tiny Collections brands, as well as the Polly Pocket® trademarks. The Company paid approximately \$80 million, which included investment advisor and other directly related expenses. Intercompany accounts and transactions between Mattel and Bluebird have been eliminated from the consolidated financial statements. The excess of cost over the estimated fair market value of tangible net assets acquired was approximately \$60 million, which is being amortized on a straight-line basis over 40 years.

Business Combination and Related Integration and Restructuring Charge

In March 1997, the Company completed its merger with Tyco. The merger was accounted for as a pooling of interests, which means that for accounting and financial reporting purposes, Mattel's consolidated financial statements have been restated to present the combined companies' financial position and results of operations for 1996 through 1997. Under the merger agreement, each Tyco common stockholder received 0.48876 shares of Mattel common stock for each share of Tyco common stock outstanding, which resulted in the issuance of approximately 17 million Mattel common shares. Each share of Tyco Series B and Series C preferred stock was converted into like Mattel preferred stock.

In connection with this merger, the Company commenced an integration and restructuring plan and recorded a \$275.0 million pre-tax charge against operations in March 1997. After related tax effects, the Company's 1997 earnings were impacted by \$0.71 per diluted share as a result of the net \$209.7 million charge. The integration and restructuring activity was substantially complete as of December 31, 1998. The Company realized annualized cost savings of approximately \$160 million, mainly in the areas of cost of production, advertising, selling and administrative expenses, and financing costs.

Special Charges

In the 1998 third quarter, the Company voluntarily recalled certain Power Wheels® ride-on vehicles and recognized a \$38.0 million pre-tax charge in its results of operations. After related tax effects, the net \$27.2 million charge impacted the 1998 earnings by \$0.09 per diluted share. The recall did not result from any serious injury, and involves the replacement of electronic components that may overheat, particularly when consumers make alterations to the product. The Company believes the amount reserved will be sufficient to cover all costs associated with the recall.

In the 1998 fourth quarter, the Company recognized a \$6.0 million pre-tax charge related to the proposed settlement of the Toys R Us-related antitrust litigation. After related tax effects, the net \$4.3 million charge impacted the 1998 earnings by \$0.01 per diluted share. The Company is required to make cash and toy contributions prior to November 1999 according to the terms of the proposed settlement agreement.

Litigation

Beaverton, Oregon

The Company operates a manufacturing facility on a leased property in Beaverton, Oregon that was acquired as part of its merger with Tyco. In March 1998, samples of groundwater used by the facility for process water and drinking water disclosed elevated levels of certain chemicals, including trichloroethylene ("TCE"). The Company immediately closed the water supply and self-reported the sample results to the Oregon Department of Environmental Quality ("DEQ") and the Oregon Health Division. The Company also implemented an employee communication and medical screening program.

In November 1998, the Company and another potentially responsible party entered into a consent order with the DEQ to conduct a remedial investigation/feasibility study at the site, to propose an interim remedial action measure and to continue the community outreach program to employees, former employees and surrounding landowners. It is not presently possible to estimate the cost to the Company related to the DEQ's investigation and any subsequent orders for future work.

Toys R Us

On September 25, 1997, an administrative law judge of the Federal Trade Commission issued his initial decision in the matter *In re Toys R Us, Inc.* The administrative law judge made findings of fact and conclusions of law that the toy retailer Toys R Us, Inc. had violated federal antitrust laws and entered into vertical and horizontal arrangements with various toy manufacturers, including Mattel, whereby the manufacturers would refuse to do business with warehouse clubs, or would do business with warehouse clubs only on terms acceptable to Toys R Us. On October 13, 1998, the Federal Trade Commission issued an opinion and a final order affirming the findings and conclusions of the administrative law judge. Toys R Us has now filed a notice of appeal in the United States Court of Appeals for the Seventh Circuit.

Following the announcement of the administrative law judge's decision, the Company was named as a defendant, along with certain other toy manufacturers, in a number of antitrust actions in various

states related to the Toys R Us matter. The Company has also been named as a defendant in a series of private treble damage class actions under federal antitrust laws that have been filed in various federal district courts.

Since May 1998, the Company has participated in settlement negotiations being conducted with the aid of a mediator. In connection with a proposed settlement, the Company recognized a \$6.0 million pre-tax charge in the fourth quarter of 1998. After related tax effects, the net \$4.3 million charge impacted the Company's 1998 earnings by \$0.01 per diluted share. The proposed settlement agreement calls for the Company to make cash and toy contributions prior to November 1999. Until such time as these matters are concluded in the various courts involved, the Company intends to vigorously defend itself in the litigation in which it was named involving Toys R Us.

Greenwald

On October 13, 1995, Michelle Greenwald filed a complaint against the Company in Superior Court of the State of California, County of Los Angeles. Ms. Greenwald is a former employee whom the Company terminated in July 1995. Her complaint sought \$50 million in general and special damages, plus punitive damages, for breach of oral, written and implied contract, wrongful termination in violation of public policy and violation of California Labor Code Section 970. Ms. Greenwald claimed that her termination resulted from complaints she made to management concerning general allegations that the Company did not properly account for sales and certain costs associated with sales and more specific allegations that the Company failed to properly account for certain royalty obligations to The Walt Disney Company. During 1996 and 1997, the Company filed motions for summary judgment on all areas of her complaint and these motions were granted. In 1998, Ms. Greenwald filed a notice of appeal, which is scheduled to be considered in March 1999. The Company intends to defend the action vigorously, including her appeal.

Pending Business Combination

During December 1998, a total of six separate purported class action complaints were filed by several stockholders of The Learning Company in the Court of Chancery of the State of Delaware in and for New Castle County against The Learning Company and its board of directors for alleged breaches of fiduciary duties in connection with the proposed merger. The six complaints have since been consolidated. The consolidated complaint seeks the certification as a class of all The Learning Company stockholders, an injunction against the merger, rescission if the merger is consummated, damages, costs and disbursements, including attorneys' fees. The consolidated complaint alleges that The Learning Company board of directors breached their fiduciary duties to The Learning Company's stockholders by, among other things, failing to conduct due diligence sufficient to have discovered material, adverse information concerning Mattel's anticipated operational and financial results and agreeing to an exchange ratio that failed to protect The Learning Company stockholders against a decline in the value of Mattel common stock. The consolidated complaint names Mattel as an additional defendant, claiming that Mattel aided and abetted the alleged breaches of fiduciary duty. Mattel will aggressively defend itself against the action and will continue to pursue the merger.

Other Matters

The Company is also involved in various other litigation and legal matters, including claims related to intellectual property, product liability, labor, and environmental cleanup, which the Company is addressing or defending in the ordinary course of business. Management believes that any liability, which may potentially result upon resolution of such matters, will not have a material adverse effect on the Company's consolidated financial position or results of operations.

Commitments

In the normal course of business, the Company enters into contractual arrangements for future purchases of goods and services to ensure availability and timely delivery, and to obtain and protect the Company's right to create and market certain products. These arrangements include commitments for future inventory purchases and royalty payments. Certain of these commitments routinely contain provisions for guaranteed or minimum expenditures during the term of the contracts.

As of December 31, 1998, the Company had outstanding commitments for 1999 purchases of inventory of approximately \$60 million. Licensing and similar agreements with terms extending through the year 2003 contain provisions for future guaranteed minimum payments aggregating approximately \$371 million. In addition, under a certain licensing agreement, the Company may have additional commitments of up to \$37.8 million in the year 2000 payable over three years.

Foreign Currency Risk

The Company's results of operations and cash flows can be impacted by exchange rate fluctuations. To limit the exposure associated with exchange rate movements, the Company enters into foreign currency forward exchange and option contracts primarily to hedge its purchase of inventory, sales and other intercompany transactions denominated in foreign currencies. The Company's results of operations can also be affected by the translation of foreign revenues and earnings into US dollars.

Market risk exposures exist with respect to the settlement of foreign currency transactions during the year because currency fluctuations cannot be predicted with certainty. The Company seeks to mitigate its exposure to market risk by monitoring its currency exchange exposure for the year and partially or fully hedging such exposure. In addition, the Company manages its exposure through the selection of currencies used for foreign borrowings and intercompany invoicing. The Company does not trade in financial instruments for speculative purposes.

The Company's foreign currency forward exchange contracts that were used to hedge firm foreign currency commitments as of December 31, 1998 and 1997 are shown in the following table.

These contracts generally mature within 18 months from the date of execution. Contracts outstanding at year-end mature during the next 13 months. All contracts are against the US dollar and are maintained by reporting units with a US dollar functional currency, with the exception of the Indonesian rupiah contracts that are maintained by an entity with a rupiah functional currency.

For the purchase of foreign currencies, fair value reflects the amount, based on dealer quotes, that the Company would pay at maturity for contracts involving the same currencies and maturity dates, if they had been entered into as of year-end 1998 and 1997. For the sale of foreign currencies, fair value reflects the amount, based on dealer quotes, that the Company would receive at

maturity for contracts involving the same currencies and maturity dates, if they had been entered into as of year-end 1998 and 1997. The differences between the fair value and the contract amounts are expected to be fully offset by foreign currency exchange gains and losses on the underlying hedged transactions.

(In thousands of US dollars)	Buy			Sell		
	Contract Amount	Weighted Average Contract Rate	Fair Value	Contract Amount	Weighted Average Contract Rate	Fair Value
1998						
German marks	\$ 19,119	1.67	\$ 18,984	\$144,660	1.68	\$145,688
Italian lira	20,014	1,764.00	21,155	68,358	1,660.00	67,950
Hong Kong dollars	55,829	8.02	57,790	-	-	-
French francs	27,435	5.62	27,536	9,105	5.82	9,479
British pounds sterling	6,548	0.60	6,415	66,856	0.61	66,950
Canadian dollars	16,144	1.55	16,545	18,794	1.46	18,119
Spanish pesetas	5,625	142.30	5,577	2,899	148.23	2,997
Dutch guilders	5,079	1.89	5,050	8,086	1.96	8,342
Japanese yen	-	-	-	12,501	116.00	12,759
Australian dollars	4,988	1.66	5,268	21,610	1.58	21,732
Belgian francs	-	-	-	11,641	35.46	11,871
Swiss francs	18,341	1.37	18,251	-	-	-
Mexican peso	-	-	-	22,000	10.02	21,956
Indonesian rupiah	10,000	15,720.50	19,183	-	-	-
Singapore dollar	-	-	-	3,962	1.64	3,943
Brazilian real	-	-	-	2,500	1.25	2,554
	\$189,122		\$201,754	\$392,972		\$394,340
1997						
German marks	\$19,179	1.78	\$ 18,972	\$ 65,119	1.77	\$ 64,941
Italian lira	38,277	1,800.00	39,203	53,161	1,749.00	52,585
Malaysian ringitts	53,304	3.08	41,551	-	-	-
Hong Kong dollars	148,084	8.04	149,108	2,527	7.76	2,532
French francs	-	-	-	38,166	5.86	37,639
British pounds sterling	32,548	0.61	32,751	72,580	0.63	73,570
Canadian dollars	22,608	1.42	22,474	-	-	-
Spanish pesetas	-	-	-	13,858	148.99	13,668
Dutch guilders	12,778	2.00	12,666	36,285	1.96	35,719
Japanese yen	-	-	-	7,956	125.73	7,659
Australian dollars	6,398	1.54	6,391	-	-	-
Belgian francs	-	-	-	55,126	36.48	54,515
Swiss francs	13,677	1.44	13,454	-	-	-
Mexican peso	-	-	-	4,200	8.05	4,138
Indonesian rupiah	15,230	3,930.78	9,891	-	-	-
Singapore dollar	-	-	-	4,107	1.72	4,203
	\$362,083		\$346,461	\$353,085		\$351,169

The Company did not enter into any new foreign currency option contracts during 1998, and no option contracts remained outstanding as of December 31, 1998. As of December 31, 1997, the total amount of the option contracts was \$93.5 million and the fair value was \$90.5 million. Fair value reflects the amount of US dollars the Company would receive from the current contracts, less the option value. The option value is determined based on dealer quotes for contracts involving the same currencies and maturity dates.

Euro

The Treaty on European Economic and Monetary Union provides for the introduction of a single European currency, the Euro, in substitution for the national currencies of the member states of the European Union that adopt the Euro. The transition period for member states joining the Monetary Union began on January 1, 1999 and will end on July 1, 2002 when the national currencies of member states will cease to exist. Currently, the Company is unable to assess whether the

adoption of the Euro by the Monetary Union will have a material impact on its financial position or results of operations in the future.

Manufacturing Risk

The Company owns and operates manufacturing facilities and utilizes third-party manufacturers throughout Asia, primarily in China, Indonesia, Malaysia and Thailand. A risk of political instability and civil unrest exists in these countries, which could temporarily or permanently damage the Company's manufacturing operations located there. The Company's business, financial position and results of operations would be negatively impacted by a significant disruption to its manufacturing operations or suppliers.

Effects of Inflation

Inflation rates in the US and in major foreign countries where the Company does business have not had a significant impact on its results of operations or financial position during the three years

ended December 31, 1998. The US Consumer Price Index increased 1.6% in 1998, 1.7% in 1997 and 3.3% in 1996. The Company receives some protection from the impact of inflation from high turnover of inventories and its ability to pass on higher prices to consumers.

Year 2000 Update

Many currently installed computer systems and software products, including several used by the Company, are coded to accept only two-digit (rather than four-digit) entries in the date code field used to define the applicable year. In such instances, the first two characters are assumed to be "19". Beginning in the year 2000 or perhaps earlier if referencing a date in the year 2000, such computer systems and software products may recognize a date using "00" as the year 1900, rather than the year 2000, which could result in miscalculations or system failures. To address the year 2000 issue, in early 1998 the Company established a project team and initiated a comprehensive plan that is designed to assess, remediate and test Mattel's internal systems, hardware and processes, including key operational, manufacturing and financial systems. The progress of this plan is continually monitored and regularly reported to management. In addition, the Company's board of directors is regularly informed about the year 2000 issue both generally and as it may affect the Company's business.

The Company's internal year 2000 project team oversees all aspects of implementing the plan. The team is comprised of staff members from the information systems department having the requisite knowledge of the Company's computer systems, including all the technical aspects of the systems. Key user group designees from business areas are included on each system team, which is guided by a central project team. The Company does not plan on engaging outside consultants, technicians or other external resources to assist in formulating and implementing the program.

The Company's plan adheres to a multi-step process that includes five distinct phases of activity: (1) awareness; (2) inventory and risk assessment; (3) code and system modification; (4) testing; and (5) contingency planning.

Under the first two phases of the plan, all operational, manufacturing and financial systems were inventoried and evaluated. This inventory included all software systems, computer hardware, facilities, and production equipment containing or depending upon a computer chip. As a result of such evaluation, the Company established detailed plans and action steps required to address all aspects of the year 2000 issue, including all code and system modifications (phase 3). The Company has completed the awareness, inventory and code change phases of the plan as scheduled prior to December 1998. Critical system verification and testing (phase 4) is expected to be complete by July 1999.

The Company initiated formal communications with each of its significant suppliers and customers to determine the extent to which they are addressing the year 2000 issue and the effect on its business should those parties fail to adequately address the issue. To date, the Company has received responses from the majority of the initial contacts. These responses have been positive and support the overall initiatives toward achieving year 2000 compliance. The Company is actively following-up with those customers and suppliers failing to reply to the initial inquiry.

Due to the general uncertainty inherent in the year 2000 issue, largely resulting from uncertainty of the readiness of third-party suppliers and customers, the Company is currently unable to assess the overall impact on its business. The risk of third-party suppliers and customers not correcting a material year 2000 problem could result in an interruption in, or a failure of, certain normal business activities or operations of such suppliers, customers, and/or the Company. Such failures could materially and adversely affect the Company's results of operations, liquidity and financial position. As a result, during the first half of 1999 the Company is developing contingency plans (phase 5), which it expects to be complete by July 1999. Contingency planning is being done on a worldwide basis by all the business units. Each unit will concentrate on factors external to the Company which may adversely impact their ability to conduct operations. Specifically, for those locations where a high likelihood of a material failure exists, the Company will establish revised procedures for managing operations, including identification of alternate suppliers and vendors whose systems are year 2000 compliant.

While there is no guarantee, management believes that the Company's year 2000 plan should greatly reduce its level of uncertainty about the issue and mitigate the possibility of significant interruptions of ongoing operations. Additionally, its global presence and broad-based manufacturing capability should provide the Company with numerous options to further mitigate the risk of year 2000 non-compliance.

As of December 31, 1998, the Company has spent approximately \$6 million and expects to incur a total of approximately \$10 million in connection with addressing the year 2000 issue. These costs are largely due to the use of internal resources dedicated to achieving year 2000 compliance. Costs are charged to expense as they are incurred. Work on the year 2000 issue has not delayed any internal projects that would have a material effect on the Company's consolidated financial position or results of operation. All costs of addressing the year 2000 issue will be funded from internally generated cash.

The Company sells software products as part of its core businesses. All software products currently available for sale to consumers and those products previously purchased by consumers are year 2000 compliant. Software products manufactured for the Company by third-parties under licensing agreements have been certified as year 2000 compliant by such manufacturers. The Company will continue to ensure that all its software products in development are year 2000 compliant.

New Accounting Pronouncement

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities*. This statement requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. It also requires that gains or losses resulting from changes in the values of those derivatives be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. The Company is required to adopt this statement for its fiscal year beginning January 1, 2000. Management believes the adoption of this statement will not have a material impact on the Company's consolidated financial position or results of operations.

Consolidated Balance Sheets

	December 31, 1998	December 31, 1997
(In thousands)		
Assets		
Current Assets		
Cash	\$ 212,454	\$ 694,947
Accounts receivable, less allowances of \$41.2 million at December 31, 1998 and \$30.7 million at December 31, 1997	983,050	1,091,416
Inventories	584,358	428,844
Prepaid expenses and other current assets	277,948	246,529
Total current assets	2,057,810	2,461,736
Property, Plant and Equipment		
Land	35,113	29,556
Buildings	271,580	198,396
Machinery and equipment	512,225	453,978
Capitalized leases	23,271	24,625
Leasehold improvements	82,643	68,179
	924,832	774,734
Less: accumulated depreciation	375,724	336,946
	549,108	437,788
Tools, dies and molds, net	187,349	163,809
Property, plant and equipment, net	736,457	601,597
Other Noncurrent Assets		
Goodwill, net	1,253,531	534,128
Other assets	214,367	206,330
	\$4,262,165	\$3,803,791
Liabilities and Stockholders' Equity		
Current Liabilities		
Short-term borrowings	\$ 134,006	\$ 17,468
Current portion of long-term liabilities	33,518	13,659
Accounts payable	293,421	310,117
Accrued liabilities	651,013	629,445
Income taxes payable	205,253	202,735
Total current liabilities	1,317,211	1,173,424
Long-Term Liabilities		
6-3/4% senior notes, due 2000	100,000	100,000
6% senior notes, due 2003	150,000	-
6-1/8% senior notes, due 2005	150,000	-
Medium-term notes	540,500	520,500
Mortgage note	43,007	43,573
Other	141,249	144,224
Total long-term liabilities	1,124,756	808,297
Stockholders' Equity		
Preferred stock, Series C \$1.00 par value, \$125.00 liquidation preference per share, 772.8 thousand shares authorized; 771.9 thousand shares issued and outstanding in 1998 and 1997, respectively	772	772
Common stock \$1.00 par value, 1.0 billion shares authorized; 300.4 million shares issued in 1998 and 1997, respectively	300,381	300,381
Additional paid-in capital	482,662	509,172
Treasury stock at cost; 14.3 million and 8.8 million shares in 1998 and 1997, respectively	(495,347)	(285,420)
Retained earnings	1,724,677	1,490,804
Accumulated other comprehensive loss	(192,947)	(193,639)
Total stockholders' equity	1,820,198	1,822,070
	\$4,262,165	\$3,803,791

Commitments and Contingencies (See accompanying notes.)

The accompanying notes are an integral part of these statements.

Consolidated Statements of Operations

(In thousands, except per share amounts)	For the Year		
	1998	1997	1996
Net Sales	\$4,781,892	\$4,834,616	\$4,535,332
Cost of sales	2,418,899	2,434,616	2,315,574
Gross Profit	2,362,993	2,400,000	2,219,758
Advertising and promotion expenses	813,293	779,139	778,919
Other selling and administrative expenses	882,127	796,952	772,335
Amortization of intangibles	41,929	32,179	32,489
Special charges	44,000	-	-
Restructuring and integration charges	-	275,000	-
Interest expense	110,833	90,130	100,226
Other expense (income), net	5,748	1,518	(967)
Income Before Income Taxes and Extraordinary Item	465,063	425,082	536,756
Provision for income taxes	132,799	135,288	164,532
Income Before Extraordinary Item	332,264	289,794	372,224
Extraordinary item - loss on early retirement of debt	-	(4,610)	-
Net Income	332,264	285,184	372,224
Preferred stock dividend requirements	7,960	10,505	7,391
Net Income Applicable to Common Shares	\$ 324,304	\$ 274,679	\$ 364,833
Basic Income Per Common Share			
Income before extraordinary item	\$ 1.11	\$ 0.96	\$ 1.26
Extraordinary item - loss on early retirement of debt	-	(0.01)	-
Net income	\$ 1.11	\$ 0.95	\$ 1.26
Weighted average number of common shares	291,481	290,450	290,393
Diluted Income Per Common Share			
Income before extraordinary item	\$ 1.10	\$ 0.94	\$ 1.23
Extraordinary item - loss on early retirement of debt	-	(0.01)	-
Net income	\$ 1.10	\$ 0.93	\$ 1.23
Weighted average number of common and common equivalent shares	303,243	295,653	303,057
Dividends Declared Per Common Share	\$ 0.31	\$ 0.27	\$ 0.24

The accompanying notes are an integral part of these statements.

Consolidated results for 1997 and 1996 have been restated retroactively for the effects of the March 1997 merger with Tyco, accounted for as a pooling of interests. See Note 7.

Consolidated Statements of Cash Flows

(In thousands)	For the Year		
	1998	1997	1996
Cash Flows From Operating Activities:			
Net income	\$ 332,264	\$ 285,184	\$ 372,224
Adjustments to reconcile net income to net cash flows from operating activities:			
Noncash restructuring and integration charges	-	90,382	-
Loss on early retirement of debt, net of tax	-	4,610	-
Depreciation	169,116	154,994	144,672
Amortization	45,789	34,917	36,671
Increase (decrease) from changes in assets and liabilities:			
Accounts receivable	140,248	(201,909)	(71,348)
Inventories	(47,715)	(33,012)	(38,304)
Prepaid expenses and other current assets	(16,295)	(75,810)	15,310
Accounts payable, accrued liabilities and income taxes payable	(83,865)	161,640	58,072
Deferred compensation and other retirement plans	2,690	369	9,110
Deferred income taxes	(999)	64,015	(2,147)
Other, net	6,268	(3,526)	551
Net cash flows from operating activities	547,501	481,854	524,811
Cash Flows From Investing Activities:			
Purchases of tools, dies and molds	(114,387)	(96,006)	(108,641)
Purchases of other property, plant and equipment	(161,860)	(125,567)	(122,498)
Payment for acquisitions, net of cash acquired	(782,588)	(8,625)	(8,625)
Investment in other long-term assets	(10,783)	(7,816)	(25,114)
Proceeds from sale of business and other property, plant and equipment	18,667	31,484	6,250
Net proceeds from sales of marketable securities	-	-	17,315
Other, net	(1,484)	566	317
Net cash flows used for investing activities	(1,052,435)	(205,964)	(240,996)
Cash Flows From Financing Activities:			
Short-term borrowings, net	109,110	(6,957)	(45,652)
Proceeds from issuance of notes	350,000	310,000	-
Payments of long-term debt	(99,310)	(234,823)	(33,717)
Exercise of stock options and warrants including related tax benefit	114,656	59,677	99,614
Purchase of treasury stock	(351,093)	(227,932)	(269,771)
Sale of treasury stock	-	71,248	-
Issuance of preferred stock	-	-	92,702
Payment of dividends on common and preferred stock	(97,970)	(84,537)	(66,473)
Other, net	(1,050)	(2,904)	(3,127)
Net cash flows from (used) for financing activities	24,343	(116,228)	(226,424)
Effect of Exchange Rate Changes on Cash	(1,902)	(14,986)	(806)
(Decrease) Increase in Cash	(482,493)	144,676	56,585
Cash at Beginning of Year	694,947	550,271	493,686
Cash at End of Year	\$ 212,454	\$ 694,947	\$ 550,271

The accompanying notes are an integral part of these statements.

Consolidated results for 1997 and 1996 have been restated retroactively for the effects of the March 1997 merger with Tyco, accounted for as a pooling of interests. See Note 7.

Consolidated Statements of Stockholders' Equity

(In thousands)	Preferred Stock	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance, December 31, 1995	\$ 52	\$296,080	\$432,150	\$ (75,574)	\$ 994,645	\$ (95,673)	\$1,551,680
Comprehensive income:							
Net income					372,224		372,224
Currency translation adjustments						8,728	8,728
Comprehensive income					372,224	8,728	380,952
Purchase of treasury stock				(269,771)			(269,771)
Restricted stock activity			2,770	(6,627)			(3,857)
Exercise of stock options		11	26,414				26,425
Issuance of treasury stock			(53,554)	124,315			70,761
Issuance of stock warrant			26,444				26,444
Issuance of preferred stock	773		91,929				92,702
Exercise of stock subscription warrants			(9,507)	11,658			2,151
Dividends declared on common stock					(65,825)		(65,825)
Dividends declared on preferred stock	2		1,650		(7,391)		(5,739)
Balance, December 31, 1996	827	296,091	518,296	(215,999)	1,293,653	(86,945)	1,805,923
Comprehensive income (loss):							
Net income					285,184		285,184
Currency translation adjustments						(106,694)	(106,694)
Comprehensive income (loss)					285,184	(106,694)	178,490
Purchase of treasury stock				(227,932)			(227,932)
Issuance of treasury stock			(45,486)	158,511			113,025
Exercise of stock options		636	23,927				24,563
Conversion of 7% notes		893	15,141				16,034
Conversion of preferred stock	(55)	2,761	(2,706)				-
Dividends declared on common stock					(77,528)		(77,528)
Dividends declared on preferred stock					(10,505)		(10,505)
Balance, December 31, 1997	772	300,381	509,172	(285,420)	1,490,804	(193,639)	1,822,070
Comprehensive income:							
Net income					332,264		332,264
Currency translation adjustments						692	692
Comprehensive income					332,264	692	332,956
Purchase of treasury stock				(351,393)			(351,393)
Issuance of treasury stock			(65,210)	141,466			76,256
Exercise of stock options			38,700				38,700
Dividends declared on common stock					(90,431)		(90,431)
Dividends declared on preferred stock					(7,960)		(7,960)
Balance, December 31, 1998	\$772	\$300,381	\$482,662	\$(495,347)	\$1,724,677	\$(192,947)	\$1,820,198

The accompanying notes are an integral part of these statements.

Consolidated results for December 31, 1995 and 1996 have been restated retroactively for the effects of the March 1997 merger with Tyco, accounted for as a pooling of interests. See Note 7.

Notes to Consolidated Financial Statements

Note 1 - Summary of Significant Accounting Policies

Principles of Consolidation and Basis of Preparation

The consolidated financial statements include the accounts of Mattel, Inc. and its subsidiaries ("Mattel" or the "Company"). All significant intercompany accounts and transactions have been eliminated in consolidation, and certain amounts in the financial statements for prior years have been reclassified to conform with the current year presentation. Investments in joint ventures and other companies are accounted for by the equity method or cost basis depending upon the level of the investment and/or the Company's ability to exercise influence over operating and financial policies. Financial data for 1997 and 1996 reflect the retroactive effect of the merger, accounted for as a pooling of interests, with Tyco Toys, Inc. consummated in March 1997 (see Note 7).

Preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Foreign Currency Translation

Assets and liabilities of foreign subsidiaries are translated into US dollars at fiscal year-end exchange rates. Income, expense and cash flow items are translated at weighted average exchange rates prevailing during the fiscal year. The resulting currency translation adjustments are recorded as a component of other comprehensive income or loss within stockholders' equity.

Cash

Cash includes cash equivalents, which are highly liquid investments with maturities of three months or less when purchased. Because of the short maturities of these instruments, the carrying amount is a reasonable estimate of fair value.

Inventories

Inventories, net of an allowance for excess quantities and obsolescence, are stated at the lower of cost or market. Cost is determined by the first-in, first-out method.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over estimated useful lives of 10 to 40 years for buildings, 18 months to 10 years for machinery and equipment, and 10 to 20 years, not to exceed the lease term, for leasehold improvements. Tools, dies and molds are amortized using the straight-line method over 18 months to 3 years.

Intangibles and Long-Lived Assets

Intangible assets consist of the excess of purchase price over the fair value of net assets acquired in purchase acquisitions, and the cost of acquired patents and trademarks. Intangible assets are amortized using the straight-line method over periods ranging from 18 months to 40 years. Accumulated amortization was \$228.2 million and \$186.1 million as of December 31, 1998 and 1997, respectively.

The Company periodically reviews the carrying value of its fixed and intangible assets to identify and assess any impairment by evaluating the operating performance and future undiscounted cash flows of the underlying assets.

Revenue Recognition

Net sales are recognized when products are shipped. Accruals for customer discounts and rebates, and defective returns are recorded as the related revenues are recognized.

Advertising Costs

The Company expenses the costs of media advertising the first time the advertising takes place, except for direct-response advertising, which is capitalized and amortized over its expected period of future benefits. Direct-response advertising consists primarily of catalogue production and mailing costs that are generally amortized within three months from the date catalogues are mailed. Advertising costs associated with customer benefit programs are accrued as the related revenues are recognized.

Stock-Based Compensation

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation*. Accordingly, no compensation cost has been recognized in the results of operations for nonqualified stock options granted under the Company's plans as such options are granted at not less than the quoted market price of the Company's common stock on the date of grant.

Income Taxes

The Company accounts for certain income and expense items differently for financial reporting and income tax purposes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities, applying enacted statutory tax rates in effect for the year in which the differences are expected to reverse.

Income and Dividends Per Common Share

The 1997 and 1996 share and per share data presented in these financial statements reflect the retroactive effects of the March 1997 Tyco merger.

In the 1997 fourth quarter, the Company adopted Statement of Financial Accounting Standards No. 128, *Earnings per Share*. Accordingly, data for 1997 and 1996 have been restated to present basic and diluted income per common share.

Basic income per common share is computed by dividing earnings available to common stockholders by the weighted average number of common shares outstanding during each period. Earnings available to common stockholders represent reported net income less preferred stock dividend requirements.

Diluted income per common share is computed by dividing diluted earnings available to common stockholders by the weighted average number of common and common equivalent shares outstanding during each period. The calculation of common equivalent shares assumes the exercise of dilutive stock options and warrants, net of assumed treasury share repurchases at average market prices, and conversion of dilutive preferred stock and convertible debt, as applicable. Diluted earnings available to common stockholders represent earnings available to common stockholders plus preferred stock dividend requirements and interest savings resulting from the assumed conversions of dilutive securities.

A reconciliation of earnings available to common stockholders and diluted earnings available to common stockholders and the related weighted average shares for the years ended December 31 follows (in thousands):

	1998		1997		1996	
	Earnings	Shares	Earnings	Shares	Earnings	Shares
Income before extraordinary item	\$332,264		\$289,794		\$372,224	
Extraordinary item - loss on early retirement of debt	-		(4,610)		-	
Net income	332,264		285,184		372,224	
Less: preferred stock dividend requirements	(7,960)		(10,505)		(7,391)	
Earnings available to common stockholders	\$324,304	291,481	\$274,679	290,450	\$364,833	290,393
Dilutive securities:						
Dilutive stock options		3,369		3,975		4,087
Warrants		662		639		927
7% Notes	-	-	479	589	728	783
Preferred stock dividend requirements	7,960	7,731	-	-	7,391	6,867
Diluted earnings available to common stockholders	\$332,264	303,243	\$275,158	295,653	\$372,952	303,057

Premium price stock options totaling 18.7 million were excluded from the calculation of diluted earnings per share in 1998 because they were anti-dilutive in each quarter and for the full year. Preferred stock was excluded from the calculation of diluted earnings per share in 1997 because it was anti-dilutive. A warrant issued in 1996 to purchase 3.0 million shares of the Company's common stock was excluded from the calculation of diluted earnings per share because it was anti-dilutive in

1997 and 1996. The dilutive impact of this warrant was minimal in the first quarter and full year 1998 calculations and was anti-dilutive in the remaining quarters of 1998.

Foreign Currency Contracts

The Company enters into foreign currency forward exchange and option contracts primarily as hedges of inventory purchases, sales and other intercompany transactions denominated in foreign currencies to limit the effect of exchange rate fluctuations on its results of operations and cash flows. The Company does not enter into contracts for speculative purposes. Gains and losses related to firm commitments, which qualify for hedge accounting, are deferred and are recognized in the results of operations, balance sheet, and statement of cash flows as part of the underlying transaction. Contracts that do not qualify for hedge accounting are marked to market with gains and losses recognized in the results of operations currently. If a derivative previously designated as a hedge of a foreign currency commitment is terminated prior to the transaction date of the related commitment, the resultant gain or loss is recognized at the time of maturity of the original contract as a component of other expense, net.

Note 2 - Income Taxes

Consolidated pre-tax income consists of the following (in thousands):

	For the Year		
	1998	1997	1996
US operations	\$ 57,965	\$ 70,225	\$206,668
Foreign operations	407,098	354,857	330,088
	\$465,063	\$425,082	\$536,756

The provision for current and deferred income taxes consists of the following (in thousands):

	For the Year		
	1998	1997	1996
Current			
Federal	\$ 41,274	\$ 55,056	\$ 89,781
State	5,500	15,745	13,200
Foreign	98,800	80,395	64,165
	145,574	151,196	167,146
Deferred			
Federal	1,825	(14,283)	549
State	(1,400)	3,640	1,000
Foreign	(13,200)	(7,962)	(4,163)
	(12,775)	(18,605)	(2,614)
Provision including extraordinary item	132,799	132,591	164,532
Benefit allocated to extraordinary item	-	2,697	-
Total provision for income taxes	\$132,799	\$135,288	\$164,532

Deferred income taxes are provided principally for net operating loss carryforwards, certain reserves, depreciation, employee compensation-related expenses and certain other expenses that are

recognized in different years for financial statement and income tax purposes. The Company's deferred income tax assets (liabilities) were comprised of the following (in thousands):

	As of Year End	
	1998	1997
Operating loss and tax credit carryovers	\$ 96,410	\$102,713
Sales allowances and inventory reserves	83,573	71,990
Deferred compensation	36,123	27,680
Excess of tax basis over book basis	15,825	15,545
Restructuring and integration charges	15,349	36,446
Postretirement benefits	12,842	12,645
Other	42,000	20,651
Gross deferred income tax assets	302,122	287,670
Excess of book basis over tax basis	(14,392)	(13,453)
Retirement benefits	(15,570)	(12,752)
Other	(9,159)	(10,816)
Gross deferred income tax liabilities	(39,121)	(37,021)
Deferred income tax asset valuation allowances	(63,654)	(64,077)
Net deferred income tax assets	\$199,347	\$186,572

Management considered all available evidence and determined that a valuation allowance of \$63.7 million was required as of December 31, 1998 for certain tax credit and net operating loss carryforwards that would likely expire prior to their utilization. However, management feels it is more likely than not that the Company will generate sufficient taxable income in the appropriate carryforward periods to realize the benefit of the remaining net deferred tax assets of \$199.3 million.

Differences between the provision for income taxes at the US federal statutory income tax rate and the provision in the consolidated statements of operations were as follows (in thousands):

	For the Year		
	1998	1997	1996
Provision at federal statutory rates	\$162,772	\$148,779	\$187,864
Increase (decrease) resulting from:			
Losses without income tax benefit	1,821	1,468	835
Foreign earnings taxed at different rates, including withholding taxes	(44,301)	(42,503)	(30,517)
State and local taxes, net of federal benefit	2,665	12,287	9,230
Non-deductible restructuring costs	-	20,150	-
Other	9,842	(4,893)	(2,880)
Total provision for income taxes	\$132,799	\$135,288	\$164,532

Appropriate US and foreign income taxes have been provided for earnings of foreign subsidiary companies that are expected to be remitted in the near future. The cumulative amount of undistributed earnings of foreign subsidiaries that the Company intends to permanently invest and upon which no deferred US income taxes have been provided is \$1.2 billion at December 31, 1998. The additional US income tax on the unremitted foreign earnings, if repatriated, would be offset in whole or in part by foreign tax credits.

As of December 31, 1998, the Company has US net operating loss and credit carryforwards for federal income tax purposes of \$40.0 million and \$8.2 million, respectively. These carryforwards were generated primarily by Tyco prior to the March 1997 merger with Mattel. These net operating loss carryovers expire during the years 2007 to 2011, while \$4.5 million of the tax credits have no

expiration date and \$3.7 million of the tax credits will expire during the years 1999 to 2003. Both carryforwards are subject to an annual limitation, but the Company expects to utilize the losses and credits before the expiration of their carryforward periods.

In addition, the Company has a US net operating loss carryforward of approximately \$46.1 million, which was generated by Universal Matchbox Ltd. and subsidiaries ("Matchbox") prior to their acquisition by Tyco. These loss carryforwards expire during the years 2000 to 2005 and are subject to an annual limitation, but the Company expects to utilize these losses before the expiration of the carryforward periods. Accordingly, the goodwill reported in the consolidated balance sheets attributable to Tyco's 1991 acquisition of Matchbox has been reduced to reflect the adjustment related to the tax effect of these losses.

Certain foreign subsidiaries have net operating loss carryforwards totaling \$119.9 million (\$87.2 million with no expiration date, \$32.6 million expiring during the years 1999 to 2003, and \$0.1 million expiring after 2003).

Generally accepted accounting principles require that tax benefits related to the exercise by employees of nonqualified stock options be credited to additional paid-in capital. In 1998, 1997 and 1996, nonqualified stock options exercised resulted in credits to additional paid-in capital totaling \$38.7 million, \$17.9 million and \$26.3 million, respectively.

The Internal Revenue Service has completed its examination of the Company's federal income tax returns through December 31, 1991.

Note 3 - Employee Benefits

The Company and certain of its subsidiaries have retirement plans covering substantially all employees of these companies. Expense related to these plans totaled \$20.0 million, \$19.0 million and \$16.2 million in 1998, 1997 and 1996, respectively.

Pension Plans

The Company provides defined benefit pension plans, which satisfy the requirements of the Employee Retirement Income Security Act of 1974 ("ERISA"). With the exception of the Fisher-Price Pension Plan, activity related to the Company's pension plans, including those of foreign affiliates, was not significant during any year.

The components of net pension income for the Fisher-Price Pension Plan, based upon an October valuation date, for the years ended December 31, 1998, 1997 and 1996 are detailed below (in thousands):

	For the Period Ended		
	1998	1997	1996
Service cost	\$ 2,508	\$ 2,594	\$ 2,671
Interest cost	10,929	10,327	8,866
Expected return on plan assets	(18,949)	(16,163)	(14,784)
Amortization of:			
Unrecognized prior service cost	108	134	150
Unrecognized net asset	(2,569)	(2,569)	(2,569)
Plan amendment loss (gain)	1,154	(826)	-
Net pension income	\$ (6,819)	\$ (6,503)	\$ (5,666)

Reconciliation of the funded status of Fisher-Price's domestic pension plan to the related prepaid asset included in the consolidated balance sheets are as follows (in thousands):

	As of Year End	
	1998	1997
Funded status of the plan	\$41,335	\$60,809
Unrecognized net gain	(4,438)	(28,271)
Unrecognized prior service cost	1,366	1,474
Unrecognized net transition asset	(1,285)	(3,854)
Prepaid pension asset	\$36,978	\$30,158

Reconciliation of the assets and liabilities of Fisher-Price's domestic pension plan are as follows (in thousands):

	As of Year End	
	1998	1997
<i>Change in Plan Assets</i>		
Plan assets at fair value, beginning of year	\$202,887	\$157,507
Actual return on plan assets	2,793	51,218
Benefits paid	(7,768)	(5,838)
Plan assets at fair value, end of year	\$197,912	\$202,887
<i>Change in Projected Benefit Obligation</i>		
Projected benefit obligation, beginning of year	\$142,078	\$131,379
Service cost	2,508	2,594
Interest cost	10,929	10,327
Plan amendments	1,154	(826)
Actuarial loss	7,676	4,442
Benefits paid	(7,768)	(5,838)
Projected benefit obligation, end of year	\$156,577	\$142,078

	For the Period		
	1998	1997	1996
<i>Assumptions:</i>			
Weighted average discount rate	7.50%	7.75%	7.75%
Rate of future compensation increases	4.00%	4.00%	4.00%
Long-term rate of return on plan assets	11.00%	11.00%	11.00%

Other Retirement Plans

Domestic employees are eligible to participate in the Company's 401(k) savings plans, which are defined contribution plans satisfying ERISA requirements. The Company also maintains unfunded supplemental executive retirement plans which are nonqualified defined benefit plans covering certain key executives. For 1998, 1997 and 1996, the accumulated and vested benefit obligations and related expense of these plans were not significant.

Deferred Compensation and Excess Benefit Plans

The Company provides a deferred compensation plan which permits certain officers and key employees to elect to defer portions of their compensation. The deferred compensation plan, together with certain Company and employee contributions made to an excess benefit plan, earn various rates of return. The liability for these plans as of December 31, 1998 and 1997 was \$47.8 million and \$39.2 million, respectively. The Company's contribution to these plans and the related administrative expense were not significant to the results of operations during any year.

In 1996, the Company purchased group trust-owned life insurance contracts designed to assist in funding these programs. The cash surrender value of these policies, valued at \$40.7 million and \$32.9 million as of December 31, 1998 and 1997, respectively, are held in an irrevocable rabbi trust which is included in other assets in the consolidated balance sheets.

Postretirement Benefits

Fisher-Price has an unfunded postretirement health insurance plan covering certain eligible domestic employees hired prior to January 1, 1993. Details of the expense for the Fisher-Price plan recognized in the consolidated financial statements for the years ended December 31, 1998, 1997 and 1996 are as follows (in thousands):

	For the Year		
	1998	1997	1996
Service cost	\$ 218	\$ 284	\$ 344
Interest cost	2,416	2,465	2,496
Net postretirement benefit cost	\$2,634	\$2,749	\$2,840

Amounts included in the Company's consolidated balance sheets for this plan are as follows (in thousands):

	As of Year End	
	1998	1997
Current retirees	\$25,140	\$23,846
Fully eligible active employees	4,222	4,640
Other active employees	4,239	4,829
Accumulated postretirement benefit obligation	33,601	33,315
Unrecognized net loss	(1,716)	(1,213)
Accrued postretirement benefit liability	\$31,885	\$32,102

Reconciliation of the liabilities of Fisher-Price's postretirement health insurance plan are as follows (in thousands):

	As of Year End	
	1998	1997
<i>Change in Accumulated Postretirement Benefit Obligation</i>		
Accumulated postretirement benefit obligation, beginning of year	\$33,315	\$33,182
Service cost	218	284
Interest cost	2,416	2,465
Actuarial loss (gain)	503	(383)
Benefits paid, net of participant contributions	(2,851)	(2,233)
Accumulated postretirement benefit obligation, end of year	\$33,601	\$33,315

The discount rates used in determining the accumulated postretirement benefit obligation were 7.50% for 1998 and 7.75% for 1997 and 1996. For all participants, the health care cost trend rate for expected claim costs was assumed to be 5.50% in 1998 and remaining constant thereafter. A one percentage point increase or decrease in the assumed health care cost trend rate for each future

year would have the following effect on the accumulated postretirement benefit obligation and the service and interest cost recognized as of and for the year ended December 31, 1998 (in thousands):

	One Percentage Point	
	Increase	Decrease
Accumulated postretirement benefit obligation	\$3,531	\$(3,009)
Service and interest cost	256	(218)

The Company also maintains a contributory postretirement benefit plan for domestic employees of Mattel. The ongoing costs and obligations associated with the Mattel, Inc. plan are not significant to the Company's financial position and results of operations during any year.

Incentive Awards

The Company's Long-Term Incentive Plan is a three-year plan available to certain key executives of Mattel, Inc. Interim awards are paid annually based upon the financial performance of the Company over a three-year period. Amounts charged to operating expense in 1998, 1997 and 1996 under the current plan were \$10.8 million, \$13.8 million and \$3.9 million, respectively.

The Company also has annual incentive compensation plans for officers and key employees based on the Company's performance and subject to certain approvals of the Compensation/Options Committee of the board of directors. For the years ended December 31, 1998, 1997 and 1996, \$11.7 million, \$23.2 million and \$12.9 million, respectively, were charged to operating expense for awards under the Mattel plans and \$10.0 million, in 1996, for Tyco.

Prior to the merger, Tyco had a Long-Term Incentive Plan for certain senior executives, under which Tyco awarded Restricted Stock Units ("RSU"). The aggregate fair market value of the RSUs was being amortized to compensation expense by Tyco over the restriction period. At the time of the 1997 merger, the RSUs were converted into approximately 244 thousand shares of Mattel common stock which approximated the fair value of the RSUs on the merger consummation date and the remaining unamortized amount of \$5.1 million was charged to expense.

Note 4 - Seasonal Financing and Long-Term Debt

Seasonal Financing

The Company maintains and periodically amends or replaces an unsecured committed revolving credit agreement with a commercial bank group that is used as the primary source of financing the seasonal working capital requirements of its domestic and certain foreign affiliates. The agreement in effect during 1998 consisted of a committed unsecured facility providing a total of \$1.0 billion in seasonal financing. Within the facility, up to \$700.0 million was a standard revolving credit line available for advances and backup for commercial paper issuances (a five-year facility that expires in 2003). Interest was charged at various rates selected by the Company, ranging from market commercial paper rates to the bank reference rate. The remaining \$300.0 million (a five-year facility that expires in 2003) was available for nonrecourse purchases of certain trade accounts receivable of the Company by the commercial bank

group providing the credit line. The agreement required the Company to meet financial covenants for consolidated debt-to-capital and interest coverage and the Company was in compliance with such covenants during 1998. This agreement will continue to be in effect during 1999. In addition, the Company avails itself of uncommitted domestic facilities provided by certain banks to issue short-term money market loans.

To meet seasonal borrowing requirements of certain foreign affiliates, the Company negotiates individual financing arrangements, generally with the same group of banks that provided credit in the prior year. Foreign credit lines total approximately \$370 million, a portion of which is used to support letters of credit. The Company expects to extend these credit lines throughout year 2000 and believes available amounts will be adequate to meet its seasonal financing requirements. The Company also enters into agreements with banks of its foreign affiliates for nonrecourse sales of certain of its foreign subsidiary receivables.

Interest rates charged on the Company's working capital credit lines are adjusted on a periodic basis; therefore, the carrying amounts of such obligations are a reasonable approximation of their fair value. Information relating to Mattel and Tyco's domestic and foreign credit lines and other short-term borrowings is summarized as follows (in thousands):

	For the Year		
	1998	1997	1996
Balance at end of year			
Domestic	\$ 79,175	\$ -	\$ -
Foreign	54,831	17,468	28,924
Maximum amount outstanding			
Domestic	\$1,076,600	\$558,000	\$567,000
Foreign	141,000	67,000	113,000
Average borrowing			
Domestic	\$ 400,800	\$178,000	\$215,000
Foreign	58,000	40,000	72,000
Weighted average interest rate on average borrowing			
Domestic (computed daily)	5.6%	5.7%	6.6%
Foreign (computed monthly)	20.3%	11.9%	11.6%

6-3/4% Senior Notes

In May 1993, the Company issued \$100.0 million aggregate principal amount of 6-3/4% Senior Notes maturing May 15, 2000. Interest is payable semiannually on the fifteenth day of May and November. At December 31, 1998 and 1997, the bid prices for the 6-3/4% Senior Notes, as provided by one of the underwriters, were \$1,014.00 and \$1,011.85, respectively, based on a par value of \$1,000.00.

6% and 6-1/8% Senior Notes

In July 1998, the Company issued \$300.0 million aggregate principal amount of senior notes, \$150.0 million of which were 6% Senior Notes maturing July 15, 2003 and \$150.0 million of which were 6-1/8% Senior Notes maturing July 15, 2005. Interest is payable semiannually on the fifteenth day of January and July. At December 31, 1998, the bid prices for the 6% and 6-1/8% Senior Notes, as provided by one of the underwriters, was \$1,004.40 and \$998.65, respectively, based on a par value of \$1,000.00. The proceeds of these notes were used to finance the acquisitions of Pleasant Company and Bluebird.

Medium-Term Notes ("MT Notes")

During the 1994 third quarter, the Company commenced a program for the issuance of debt and equity securities under various shelf registration statements. In November 1998, the Company filed its current universal shelf registration statement allowing the issuance of up to \$400.0 million of debt and equity securities, all of which was available to be issued as of December 31, 1998. The following is a summary of MT Notes currently outstanding (in millions, except bid prices):

Year Issued	Amount	Maturity Date	Rate (a)	Bid Price (b)	
				1998	1997
1994	\$ 80.5	10/99-12/04	8.00%-8.55%	\$1,018.75 - \$1,112.70	\$1,031.50 - \$1,117.80
1995	130.0	04/02-05/07	7.01%-7.65%	1,043.20 - 1,051.34	1,000.20 - 1,062.90
1997	310.0	11/04-07/12	6.70%-7.49%	1,021.59 - 1,073.45	1,022.58 - 1,064.90
1998	50.0	11/13	6.50%-6.61%	990.52 - 1,000.85	-

(a) Interest is payable semiannually at fixed rates on the fifteenth day of May and November.

(b) Based on a par value of \$1,000.00.

Mortgage Note

In 1990, the Company borrowed \$45.0 million under a mortgage agreement secured by its headquarters office facility in El Segundo, California. Interest accrues at 10.15% and monthly principal and interest payments are due through December 2005. The fair value of the original mortgage note, estimated by discounting future cash flows at interest rates currently available for debt with the same credit rating, similar terms and maturity date, was approximately \$51 million and \$57 million at December 31, 1998 and 1997, respectively.

7% Convertible Subordinated Notes ("7% Notes")

Upon consummation of the merger, the Company assumed Tyco's \$16.0 million obligation related to the 7% Notes. On September 10, 1997, the holder converted all of the 7% Notes into 892.7 thousand shares of Mattel common stock.

10-1/8% Senior Subordinated Notes ("10-1/8% Notes")

Upon consummation of the merger, the Company assumed Tyco's \$126.5 million obligation related to the 10-1/8% Notes. On August 15, 1997, the Company exercised its option and redeemed the 10-1/8% Notes at 103.797% of par together with accrued interest. In the third quarter of 1997, the Company recognized a pre-tax extraordinary loss of \$7.3 million, and a related income tax benefit of \$2.7 million, as a result of the early retirement.

6-7/8% Senior Notes

The Company's \$100.0 million of 6-7/8% Senior Notes issued in August 1992 were repaid upon maturity on August 1, 1997.

Scheduled Maturities

The aggregate amounts of long-term debt and other obligations maturing in the next five years are as follows (in thousands):

	Senior Notes	MT Notes	Mortgage Note	Other	Total
1999	\$ -	\$30,000	\$600	\$2,900	\$ 33,500
2000	100,000	-	600	600	101,200
2001	-	30,500	700	500	31,700
2002	-	30,000	800	200	31,000
2003	150,000	30,000	800	200	181,000

Note 5 - Stockholders' Equity

Preference Stock and Preference Share Purchase Rights

The Company is authorized to issue 20.0 million shares of \$0.01 par value preference stock, of which none is currently outstanding. There are 2.0 million shares of \$0.01 par value preference stock designated as Series E Junior Participating Preference Stock in connection with a distribution of Preference Share Purchase Rights (the "Rights") to the Company's common stockholders. The Rights may be exercised by their holders to purchase shares of the Company's Series E Junior Participating Preference Stock upon the occurrence of a change of control as defined in the rights agreement. The Rights will expire on February 17, 2002, unless the agreement is further extended or the Rights are earlier redeemed or exchanged by the Company.

Preferred Stock

The Company is authorized to issue 3.0 million shares of \$1.00 par value preferred stock, of which 771.9 thousand shares were outstanding as of December 31, 1998 and 1997.

- Series C Mandatorily Convertible Redeemable Preferred Stock ("Series C Preferred Stock")

On June 28, 1996, Tyco received net proceeds of \$92.7 million from the sale of 772.8 thousand shares of Series C Preferred Stock. Each share of Series C Preferred Stock was converted into like Mattel preferred stock as a result of the March 1997 merger. The par value and liquidation preference of the Series C Preferred Stock are \$1.00 and \$125.00 per share, respectively. Dividends are cumulative and payable in cash on the first day of each calendar quarter at the rate of \$10.3125 per annum. Series C Depositary Shares ("Depositary Shares"), each representing one twenty-fifth of a share of Series C Preferred Stock, totaling 19.3 million shares, were sold by the depositary as part of the above offering at an issue price of \$5.00 per share. Each Depositary Share was converted into a like Mattel depositary share as a result of the March 1997 merger.

Shares of the Series C Preferred Stock (and the related Depositary Shares) are convertible, at the option of the holders, at any time prior to July 1, 2000 into Mattel common stock at a rate of 0.40064 common shares for each Depositary Share, subject to adjustment under certain conditions. The Company, at its option, may redeem the Series C Preferred Stock (and the related Depositary Shares) at any time on or after July 1, 1999 for a number of Mattel common shares equal to the call price (which is initially set at \$5.103 per Depositary Share and declines at specified times to

\$5.000 per Depositary Share as of June 30, 2000) divided by the current market price of Mattel common stock (as defined in the Certificate of Designations) or 0.40064 common shares for each Depositary Share, whichever is greater. On July 1, 2000, shares of the Series C Preferred Stock (and the related Depositary Shares) are mandatorily convertible into 0.54301 Mattel common shares for each Depositary Share.

The Series C Preferred Stock entitles the holders of Depositary Shares to vote (at the rate of 0.48876 common shares for each Depositary Share) with the holders of the Company's common stock as a single class on all matters on which the holders of the Company's common stock may vote.

- Series B Voting Convertible Exchangeable Preferred Stock
("Series B Preferred Stock")

During 1994, Tyco sold 47.6 thousand shares of Series B Preferred Stock to a private investment group. Each share of Series B Preferred Stock was converted into like Mattel preferred stock as a result of the March 1997 merger. Until April 15, 1996, Tyco paid dividends in the form of additional shares of Series B Preferred Stock. Dividends issued in shares in lieu of cash during 1996 were valued at \$1.7 million (or 1.6 thousand shares). On December 2, 1997, all outstanding shares of Series B Preferred Stock were converted by the holders into 2.8 million shares of Mattel common stock.

Common Stock

In May 1998, the stockholders of the Company approved an amendment to the Company's Restated Certificate of Incorporation that increased the number of shares of authorized common stock from 600.0 million to 1.0 billion in order to accommodate issuance of common stock in connection with possible future mergers and other financing transactions, future stock dividends or splits, future awards pursuant to the Company's stock option plans, warrant exercises, and other general corporate purposes.

Stock Compensation Plans

- Stock Option Plans

In May 1996, the stockholders of the Company approved the Mattel 1996 Stock Option Plan. Under this plan, incentive stock options, nonqualified stock options, stock appreciation rights, nonvested stock awards, and shares of common stock may be granted to officers, key employees, and other persons providing services to the Company. In addition, nonqualified stock options may be granted to members of the Company's board of directors who are not employees of the Company.

Generally, options are exercisable contingent upon the grantees' continued employment with the Company. Nonqualified stock options are granted at not less than 100% of the fair market value of the Company's common stock on the date of grant, generally vest at the rate of 25% per year of service, and usually expire within ten years from the date of grant. The 1996 Stock Option Plan provides that up to 1.5% of Mattel's outstanding common stock as of the first day

of each calendar year will be available for awards under the plan. Grants made to individual participants cannot exceed 1.0 million shares in any single calendar year. On February 4, 1999, the Company's board of directors approved an amendment to the 1996 Stock Option Plan authorizing an additional 6.0 million shares for grant in connection with new employees of businesses acquired by the Company. The aggregate number of shares of common stock available for grants under the 1996 Stock Option Plan may not exceed 50.0 million shares. This plan expires on December 31, 2005. The Company's previous plans, the 1982 and 1990 Stock Option Plans, expired on April 14, 1992 and December 31, 1996, respectively. All outstanding awards under these plans continue to be exercisable under the terms of their respective grant agreements.

The fair value of Mattel options granted during 1998, 1997 and 1996 has been estimated using the Black-Scholes pricing model. The expected life of these options used in this calculation has been determined using historical exercise patterns. The following weighted average assumptions were used in determining fair value:

	1998	1997	1996
Expected life (in years)	3.60	3.40	3.17
Risk-free interest rate	4.61%	5.69%	6.05%
Volatility factor	15.80%	17.40%	17.98%
Dividend yield	0.83%	0.86%	0.82%

The weighted average fair value of Mattel options granted during 1998, 1997 and 1996 were \$7.32, \$4.86 and \$5.12, respectively.

The following is a summary of stock option information and weighted average exercise prices for Mattel's stock option plans during the year (options in thousands):

	1998		1997		1996	
	Number	Price	Number	Price	Number	Price
Outstanding at January 1	17,307	\$21.73	13,310	\$18.05	14,513	\$14.27
Options granted	3,680	41.66	7,443	25.79	4,294	25.15
Options exercised	(4,284)	17.80	(2,807)	14.89	(5,267)	13.48
Options canceled	(628)	29.79	(639)	22.44	(230)	16.67
Outstanding at December 31	16,075	\$27.02	17,307	\$21.73	13,310	\$18.05
Exercisable at December 31	5,645	\$20.48	5,999	\$16.29	5,263	\$14.41
Available for grant at December 31	2,358		1,072		4,074	

The following table summarizes information about the weighted average remaining contractual life (in years) and the weighted average exercise prices for Mattel stock options outstanding as of December 31, 1998 (options in thousands):

Exercise Price Ranges	Options Outstanding			Options Exercisable	
	Number	Remaining Life	Price	Number	Price
\$ 4.69 to \$15.76	1,775	4.87	\$14.50	1,775	\$14.50
16.16 to 24.00	2,212	6.59	18.96	1,263	17.98
24.70 to 25.50	2,199	7.08	24.72	806	24.73
25.75 to 25.75	5,372	8.10	25.75	1,311	25.75
26.13 to 41.38	1,400	8.23	30.76	490	27.55
42.00 to 42.00	3,117	9.10	42.00	-	-
\$ 4.69 to \$42.00	16,075	7.60	\$27.02	5,645	\$20.48

Prior to the merger, Tyco had various incentive and non-qualified stock option plans that provided benefits for eligible participants. Effective with the March 1997 merger, all stock options previously granted and outstanding under these plans were exchanged for approximately 363 thousand Mattel common shares (which approximated the fair value of the options as of the merger consummation date).

In December 1993, restricted stock awards totaling 927.7 thousand shares were granted to key Mattel executives. During 1996, 244.1 thousand shares were forfeited and returned to the Company. On January 1, 1997, restrictions on the remaining 683.6 thousand shares lapsed. Compensation expense of \$2.8 million was charged to income in 1996. In addition, as a result of the forfeiture, \$6.6 million of compensation expense that was recognized in previous periods was reversed in 1996.

- 1997 Premium Price Stock Option Plan

In November 1997, the Compensation/Options Committee of the board of directors approved the Mattel, Inc. 1997 Premium Price Stock Option Plan, which was subsequently approved by the Company's stockholders at the May 1998 meeting. Under this plan, premium price options may be granted to officers and other key employees of the Company. Grants made to individual participants cannot exceed 4.5 million shares in any three consecutive calendar years. Participants in this plan are not eligible to receive grants under the 1996 Stock Option Plan until the year 2001.

The exercise price of premium price options is calculated at 25% and 33-1/3% above Mattel's six-month average stock price prior to the date of grant. Options are forfeited unless the Company's common stock price reaches the premium exercise price within two years from the date of grant for options with a 25% premium price and within three years from the date of grant for options with a 33-1/3% premium price. Options granted under the plan may not be exercised for three years and expire five years from the date of grant. Each option includes a Tandem Limited Stock Appreciation Right which gives the holder the right to receive cash, shares of common stock or any combination of cash and common stock upon the occurrence of a change of control as defined in the plan. On February 4, 1999, the Company's board of directors approved an amendment to the 1997 Premium Price Stock Option Plan authorizing an additional 3.0 million shares for grant in connection with new employees of businesses acquired by the Company, bringing the aggregate number of shares of common stock available for grant under this plan to 24.0 million shares. This plan expires on December 31, 2002.

Options to purchase 1.0 million shares and 17.7 million shares of common stock were granted during 1998 and 1997, respectively. No options were canceled, forfeited or exercisable during these periods. Shares available for grant under this plan were 2.3 million and 3.3 million as of December 31, 1998 and 1997, respectively.

The fair value of premium price options granted during 1998 and 1997 has been estimated using the Black-Scholes pricing model. The following assumptions were used in determining fair value:

	1998	1997
Expected life (in years)	5.00	5.00
Risk-free interest rate	5.80%	6.33%
Volatility factor	25.50%	24.10%
Dividend yield	0.83%	0.86%

The fair value of options granted during 1998 and 1997 was \$5.10 and \$4.79 for 25% premium price options and \$4.92 and \$4.86 for 33-1/3% premium price options, respectively.

The following table summarizes information about the remaining contractual life (in years) and the exercise prices for premium price options outstanding as of December 31, 1998 (options in thousands):

Number	Options Outstanding	
	Remaining Life	Price
8,894	3.85	\$42.31
8,767	3.85	44.87
500	4.54	50.46
500	4.54	53.83
18,661		\$44.04

- Compensation Cost

Both Mattel and Tyco adopted the disclosure-only provisions of SFAS No. 123. Accordingly, no compensation cost has been recognized in the results of operations for nonqualified stock options granted under these plans during the years ended December 31, 1998, 1997 and 1996. Had compensation cost for nonqualified stock options been determined based on their fair value at the date of grant consistent with the method of accounting prescribed by SFAS No. 123, the Company's net income and earnings per share would have been reduced as follows (amounts in millions except per share data):

	For the Year Ended		
	1998	1997	1996
Net income			
Stock option plans	\$15.7	\$14.3	\$ 7.0
Premium price stock option plan	21.1	-	-
Income per share			
Basic	\$0.13	\$0.05	\$0.02
Diluted	0.12	0.05	0.02

The pro forma effect on the Company's 1998, 1997 and 1996 net income is not indicative of the pro forma effect in future years, because it does not take into consideration the pro forma expense related to grants made prior to 1995.

Stock Subscription Warrants

The Company currently has outstanding warrants exercisable into 751.4 thousand shares of the Company's common stock at an exercise price of approximately \$4.77 per share. These warrants expire on June 30, 2000.

Disney Warrant

In June 1996, the Company entered into a licensing agreement with Disney Enterprises, Inc. Pursuant to this agreement, the Company issued Disney a warrant to purchase 3.0 million shares of the Company's common stock at an exercise price of \$27.375 per share. This warrant cannot be exercised prior to April 2, 1999 and expires no later than April 2, 2004. The warrant's fair value of \$26.4 million was determined using the Black-Scholes pricing model, assuming an expected life of eight years, a dividend yield of 0.88%, a risk-free interest rate of 6.17%, and a volatility factor of 27.60%.

The fair value of the warrant is amortized as a component of royalty expense when the related properties are introduced over the period the related revenues are recognized. During 1998 and 1997, \$3.2 million and \$1.1 million, respectively, was recognized in the results of operations related to this warrant.

Common Stock Repurchase Plan

Mattel's common stock repurchase plan, initiated in May 1990, provides for the repurchase of common shares to fund the Company's stock option plans. The number of shares to be repurchased is authorized on an annual basis by the board of directors based upon anticipated reissuance needs. During 1998, 1997, and 1996, Mattel repurchased 9.7 million, 6.5 million, and 10.0 million shares, respectively.

Dividends and Capital Transactions

A regular quarterly cash dividend has been declared by the Mattel board of directors on the Company's common stock since the second quarter of 1990. The board of directors increased the quarterly cash dividend from \$0.07 per common share to \$0.08 per common share in the second quarter of 1998. Tyco was precluded from paying cash dividends on its common stock for the year ended December 31, 1996 due to limitations set forth in its various debt agreements.

Note 6 - Commitments and Contingencies

Leases

The Company routinely enters into noncancelable lease agreements for premises and equipment used in the normal course of business. The following table shows the future minimum obligations under lease commitments in effect at December 31, 1998 (in thousands):

	Capitalized Leases	Operating Leases
1999	\$ 400	\$ 37,900
2000	300	29,000
2001	300	19,600
2002	300	11,500
2003	300	7,800
Thereafter	9,600	5,600
	\$11,200(a)	\$111,400

(a) Includes \$8.7 million of imputed interest.

Rental expense under operating leases amounted to \$58.4 million, \$61.5 million and \$58.1 million for 1998, 1997 and 1996, respectively, net of sublease income of \$0.5 million, \$0.3 million and \$0.5 million in 1998, 1997 and 1996, respectively.

Commitments

In the normal course of business, the Company enters into contractual arrangements to obtain and protect the Company's right to create and market certain products and for future purchases of goods and services to ensure availability and timely delivery. Such arrangements include royalty payments pursuant to licensing agreements and commitments for future inventory purchases. Certain of these commitments routinely contain provisions for guaranteed or minimum expenditures during the terms of the contracts. Current and future commitments for guaranteed payments reflect the Company's focus on expanding its product lines through alliances with businesses in other industries, such as television and motion picture entertainment companies.

The largest commitment involves the Company's 1991 agreement with The Walt Disney Company. This licensing agreement, which contains annual minimum royalty guarantees, permits the Company to use the Disney name and certain characters on preschool and infant products through September 2002. In related agreements, the Company participates in attractions and toy stores at three Disney theme parks under agreements in effect through June 2002. Under these agreements, the Company makes semi-annual payments to Disney.

In June 1996, the Company entered into a licensing agreement with Disney Enterprises, Inc. for an expanded strategic alliance, which grants the Company exclusive worldwide rights (with certain exceptions) to produce toys based on all children-oriented Disney television and film properties introduced, commencing summer 1997. The agreement spans three years, with the Company having the right for up to two additional years to market merchandise from film properties produced during the second and third years. The initial term of the agreement may be renewed for an additional three-year period upon mutual consent. This agreement contains minimum royalty guarantees that are contingent upon the number and nature of the properties introduced by Disney. Commitments for 1999 introductions are expected to approximate \$19 million payable over a three-year period. Future commitments could be up to \$37.8 million per introduction year. Pursuant to the agreement, the Company issued Disney a stock warrant, valued at \$26.4 million, to purchase 3.0 million shares of the Company's common stock.

Licensing and related agreements provide for terms extending from 1999 through 2003 and contain provisions for future minimum payments as shown in the following table (in thousands):

	Minimum Payments
1999	\$127,000
2000	90,000
2001	88,000
2002	57,000
2003	9,000
	\$371,000

Royalty expense for the years ended December 31, 1998, 1997 and 1996 was \$200.8 million, \$194.1 million and \$155.3 million, respectively.

As of December 31, 1998, the Company had outstanding commitments for 1999 purchases of inventory of approximately \$60 million.

Foreign Currency Contracts

To limit the exposure associated with exchange rate movements, the Company enters into foreign currency forward exchange and option contracts primarily as hedges of inventory purchases, sales and other intercompany transactions denominated in foreign currencies. These contracts generally have maturity dates of up to 18 months. Gains or losses related to firm commitments, which qualify for hedge accounting, are deferred and are recognized in the results of operations as part of the underlying transaction. Contracts that do not qualify for hedge accounting are marked to market with gains and losses recognized in the results of operations currently. Had the Company not entered into hedges to limit the effect of exchange rate fluctuations on results of operations and cash flows, the favorable effect on 1998 pre-tax income would have approximated \$5 million.

As of December 31, 1998 and 1997, the Company held the following contracts to sell foreign currencies (in thousands):

	1998		1997	
	Amount	Fair Value	Amount	Fair Value
Forwards	\$392,972	\$394,340	\$353,085	\$351,169
Options	-	-	93,547	90,500
	\$392,972	\$394,340	\$446,632	\$441,669

Fair value for forwards reflects the amount, based on dealer quotes, the Company would receive at maturity for contracts involving the same currencies and maturity dates, if they had been entered into as of year-end 1998 and 1997, respectively. During 1998, the Company did not enter into any new option contracts and no option contracts remained outstanding as of December 31, 1998. As of December 31, 1997, the fair value for options reflects the amount of US dollars the Company would receive from the current contracts, less the respective year-end option value. The option value is determined based on dealer quotes for contracts involving the same currencies and maturity dates.

As of December 31, 1998 and 1997, the Company held \$189.1 million and \$362.1 million, respectively, of foreign currency forward exchange contracts to purchase foreign currencies. The fair value of these contracts was \$201.8 million and \$346.5 million as of December 31, 1998 and 1997, respectively. Fair value reflects the amount, based on dealer quotes, the Company would pay at maturity for contracts involving the same currencies and maturity dates, if they had been entered into as of year-end 1998 and 1997, respectively.

The following table summarizes the Company's foreign currency contracts by major currency as of December 31, 1998 and 1997 (in thousands of US dollars):

	1998		1997	
	Buy	Sell	Buy	Sell
US dollars	\$392,972	\$189,122	\$446,632	\$362,083
German marks	19,119	144,660	19,179	73,977
Italian lira	20,014	68,358	38,277	53,161
Malaysian ringgits	-	-	53,304	-
Hong Kong dollars	55,829	-	148,084	2,527
French francs	27,435	9,105	-	52,756
British pounds sterling	6,548	66,856	32,548	72,580
Canadian dollars	16,144	18,794	22,608	-
Spanish pesetas	5,625	2,899	-	19,363
Dutch guilders	5,079	8,086	12,778	49,967
Japanese yen	-	12,501	-	7,956
Australian dollars	4,988	21,610	6,398	-
Belgian francs	-	11,641	-	60,038
Swiss francs	18,341	-	13,677	-
Mexican peso	-	22,000	-	50,200
Indonesian rupiah	10,000	-	15,230	-
Other (under \$5,000)	-	6,462	-	4,107
	\$582,094	\$582,094	\$808,715	\$808,715

In order to minimize the risk of counterparty non-performance, the Company executes its foreign currency forward exchange and option contracts with financial institutions believed to be credit-worthy, generally those that provide the Company with its working capital lines of credit.

Market risk exposures exist with respect to the settlement of foreign currency transactions during the year because currency fluctuations cannot be predicted with certainty. The Company seeks to mitigate its exposure to market risk by monitoring its currency exchange exposure for the year and partially or fully hedging such exposure. In addition, the Company manages its exposure through the selection of currencies used for international borrowings and intercompany invoicing. The Company does not trade in financial instruments for speculative purposes.

Litigation

- Beaverton, Oregon

The Company operates a manufacturing facility on a leased property in Beaverton, Oregon that was acquired as part of the Tyco merger. In March 1998, samples of groundwater used by the facility for process water and drinking water disclosed elevated levels of certain chemicals including trichloroethylene ("TCE"). The Company immediately closed the water supply and self-reported the sample results to the Oregon Department of Environmental Quality ("DEQ") and Oregon Health Division. The Company also implemented an employee communication and medical screening program.

In November 1998, the Company and another potentially responsible party entered into a consent order with the DEQ to conduct a remedial investigation/feasibility study at the facility, to propose an interim remedial action measure and to continue the community outreach program to employees, former employees and

surrounding landowners. It is not presently possible to estimate the cost to the Company related to the DEQ's investigation and any subsequent orders for work.

- Toys R Us

On September 25, 1997, an administrative law judge of the Federal Trade Commission issued his initial decision in the matter *In re Toys R Us, Inc.* The administrative law judge made findings of fact and conclusions of law that the toy retailer Toys R Us, Inc. had violated federal antitrust laws and entered into vertical and horizontal arrangements with various toy manufacturers, including Mattel, whereby the manufacturers would refuse to do business with warehouse clubs, or would do business with warehouse clubs only on terms acceptable to Toys R Us. On October 13, 1998, the Federal Trade Commission issued an opinion and a final order affirming the findings and conclusions of the administrative law judge. Toys R Us has now filed a notice of appeal in the United States Court of Appeals for the Seventh Circuit.

Following the announcement of the administrative law judge's decision, Mattel was named as a defendant, along with certain other toy manufacturers, in a number of antitrust actions in various states related to the Toys R Us matter. The Company has also been named as a defendant in a series of private treble damage class actions under federal antitrust laws that have been filed in various federal district courts.

Since May 1998, the Company has participated in settlement negotiations being conducted with the aid of a mediator. In connection with a proposed settlement, the Company recognized a \$6.0 million pre-tax charge in the fourth quarter of 1998. After related tax effects, the net \$4.3 million charge impacted 1998 earnings by \$0.01 per diluted share. The proposed settlement agreement calls for the Company to make cash and toy contributions prior to November 1999. Until such time as these matters are concluded in the various courts involved, Mattel intends to vigorously defend itself in the litigation in which it is named involving Toys R Us.

- Greenwald

On October 13, 1995, Michelle Greenwald filed a complaint against the Company in Superior Court of the State of California, County of Los Angeles. Ms. Greenwald is a former employee of Mattel who was terminated in July 1995. Her complaint sought \$50 million in general and special damages, plus punitive damages, for breach of oral, written and implied contract, wrongful termination in violation of public policy and violation of California Labor Code Section 970. Ms. Greenwald claimed that her termination resulted from complaints she made to management concerning general allegations that the Company did not properly account for sales and certain costs associated with sales and more specific allegations that the Company failed to properly account for certain royalty obligations to The Walt Disney Company. During 1996 and 1997, the Company's motions for summary judgment on all areas of her complaint were granted. In 1998, Ms. Greenwald filed a notice of appeal, which is scheduled to be considered in March 1999. The Company intends to defend the action vigorously, including her appeal.

- Pending Business Combination

During December 1998, a total of six separate purported class action complaints were filed by several stockholders of Learning Company in the Court of Chancery of the State of Delaware in and for New Castle County against Learning Company and its board of directors for alleged breaches of fiduciary duties in connection with the proposed merger. The six complaints have since been consolidated. The consolidated complaint seeks the certification as a class of all Learning Company stockholders, an injunction against the merger, rescission if the merger is consummated, damages, costs and disbursements, including attorneys' fees. The consolidated complaint alleges that Learning Company's board of directors breached their fiduciary duties to Learning Company's stockholders by, among other things, failing to conduct due diligence sufficient to have discovered material, adverse information concerning Mattel's anticipated operational and financial results and agreeing to an exchange ratio that failed to protect Learning Company stockholders against a decline in the value of Mattel common stock. The consolidated complaint names Mattel as an additional defendant, claiming that Mattel aided and abetted the alleged breaches of fiduciary duty. Mattel will aggressively defend itself against the action and will continue to pursue the merger.

- Other Matters

The Company is also involved in various other litigation and legal matters, including claims related to intellectual property, product liability, labor and environmental cleanup, which are being addressed or defended in the ordinary course of business. Management believes that any liability, which may potentially result upon resolution of such matters, will not have a material adverse effect on the Company's consolidated financial position or results of operations.

Note 7 - Acquisitions and Nonrecurring Items

Pending Business Combination

In December 1998, Mattel and Learning Company agreed to a merger. The stock-for-stock transaction, which will be accounted for as a pooling of interests, is subject to approval by the stockholders of both Mattel and Learning Company and by certain regulatory agencies. Under the terms of the merger agreement, Mattel will issue not less than 1.0 nor more than 1.2 shares of Mattel common stock for each share of Learning Company common stock, depending on the actual exchange ratio at the time of merger. In addition, each share of Learning Company Series A Convertible Participating Preferred Stock will be converted into Mattel common stock equal to the exchange ratio multiplied by 20. The outstanding share of Learning Company Special Voting Stock will be converted into one share of Mattel Special Voting Preferred Stock. Each outstanding Exchangeable Non-Voting Share of Learning Company's Canadian subsidiary, Softkey Software Products Inc., will remain outstanding, but will thereafter be exchangeable into a number of shares of Mattel common stock equal to the exchange ratio. Given this range,

the merger would result in the issuance of approximately 102 million to 123 million Mattel common shares for Learning Company common shares. Depending on the exchange ratio, the number of shares of Mattel common stock to be issued to Learning Company's common and preferred stockholders, together with the Mattel common stock to be issued upon the exchange of the exchangeable shares of Learning Company's Canadian subsidiary, is expected to represent between approximately 27% and 30% of Mattel's outstanding voting power after the merger.

The merger should be completed in the second quarter of 1999. However, if the merger is terminated, under certain circumstances, Mattel will receive a termination fee of up to \$35.0 million. Furthermore, if Learning Company subsequently enters into a business combination within twelve months with a third party, then they will pay Mattel an additional termination fee of \$75.0 million. In connection with the merger agreement, Mattel and Learning Company entered into a stock option agreement in December 1998 which granted Mattel an irrevocable option to purchase 15.7 million shares of Learning Company common stock at a price calculated per the terms of the agreement. This stock option is intended to increase the likelihood that the merger will be consummated in accordance with the terms of the merger agreement.

The Company will assume all the debts, liabilities and duties of Learning Company after the merger, including approximately \$201 million aggregate principal amount of 5-1/2% Senior Convertible Notes due 2000.

Acquisitions

During 1998, the Company acquired Pleasant Company and Bluebird, which were accounted for using the purchase method of accounting. The results of operations of the acquired companies have been included in the Company's consolidated financial statements from their respective dates of acquisition.

In July 1998, the Company completed its acquisition of Pleasant Company, a Wisconsin-based direct marketer of books, dolls, clothing, accessories, and activity products included under the American Girl® brand name. The purchase price, including investment advisor and other costs directly related to the acquisition, was approximately \$715 million. The excess of cost over the estimated fair market value of tangible net assets acquired was approximately \$690 million. Total excess has been allocated to customer lists, a covenant not-to-compete, and magazine subscription lists which are being amortized on a straight-line basis over a 3 to 15 year period, with the remaining excess being amortized on a straight-line basis over 40 years.

In June 1998, the Company acquired Bluebird, a company organized in the United Kingdom, from which Mattel licensed the product designs for its Polly Pocket® and Disney Tiny Collections brands, as well as the Polly Pocket® trademarks. The aggregate purchase price, including investment advisor and other directly related

expenses, was approximately \$80 million. Intercompany accounts and transactions between Bluebird and the Company have been eliminated. The excess of cost over the estimated fair market value of tangible net assets acquired was approximately \$60 million, which is being amortized on a straight-line basis over 40 years.

Business Combination and Related Integration and Restructuring Charge

In March 1997, the Company completed its merger with Tyco, accounted for as a pooling of interests. Under the merger agreement, each outstanding share of Tyco common stock was converted into the right to receive 0.48876 Mattel common shares and resulted in the issuance of approximately 17 million shares. Tyco restricted stock units and stock options outstanding as of the merger date were exchanged for approximately 0.6 million Mattel common shares. In addition, each share of Tyco Series B and Series C Preferred Stock was converted into like Mattel preferred stock. Financial information for periods prior to the merger reflect the retroactive restatement of the companies' combined financial position and operating results.

In connection with the Tyco merger, the Company commenced an integration and restructuring plan and recorded a \$275.0 million pre-tax charge against operations in March 1997. After related tax effects, the net \$209.7 million charge impacted 1997 earnings by \$0.71 per diluted share. The plan consisted of consolidating certain manufacturing and distribution operations, eliminating duplicative marketing and administrative offices, terminating various distributor and licensing arrangements and abandoning certain product lines. As of December 31, 1998, the total integration and restructuring activity provided for by this charge was substantially complete and amounts previously accrued had been paid. The type and amount of charges incurred to date approximated the amounts included in the provision.

Special Charges

In the 1998 third quarter, the Company recognized a \$38.0 million pre-tax charge related to a voluntary recall of certain Power Wheels® ride-on vehicles. After related tax effects, the net \$27.2 million charge impacted 1998 earnings by \$0.09 per diluted share. The recall did not result from any serious injury, and involves the replacement of electronic components that may overheat, particularly when consumers make alterations to the product.

In the 1998 fourth quarter, the Company recognized a \$6.0 million pre-tax charge related to the proposed settlement of the Toys R Us-related antitrust litigation. After related tax effects, the net \$4.3 million charge impacted 1998 earnings by \$0.01 per diluted share. The proposed settlement agreement calls for cash and toy contributions by the Company prior to November 1999.

During 1996, the Company received comments from the Securities and Exchange Commission regarding its accounting for certain royalties and participation fees in prior periods. The Company commenced an investigation with the assistance of outside legal counsel and an independent accounting firm. A report issued as a result of the investigation concluded that no evidence was found that the Company accounted for sales and costs associated with sales in a manner that is inconsistent with generally accepted accounting principles. The report also concluded that the Company's accounting treatment for royalties, which was adopted with the concurrence of Mattel's independent accountants, represented a reasonable application of generally accepted accounting principles given the facts and circumstances as they existed at the time the accounting decisions were made. While the Company believes that its accounting treatment was correct, Mattel recognized a catch-up adjustment in the amount of \$21.8 million before taxes in the fourth quarter of 1996.

Note 8 - Segment Information

In the 1998 fourth quarter, the Company adopted Statement of Financial Accounting Standards No. 131, *Disclosures about Segments of an Enterprise and Related Information*. This statement supercedes Statement of Financial Accounting Standards No. 14, *Financial Reporting for Segments of a Business Enterprise*, replacing the "industry segment" approach with the "management" approach. The management approach designates the internal organization that is used by management for making operating decisions and assessing performance as the source of the Company's reportable segments. This statement requires disclosure of certain information by reportable segment, geographic area and major customer.

Mattel designs, manufactures and markets a broad variety of children's products on a worldwide basis. These product lines are grouped into four major categories which represent the Company's operating segments, as follows:

Girls - including Barbie® fashion dolls and accessories, collector dolls, software, Fashion Magic®, American Girl®, Cabbage Patch Kids®, and Polly Pocket®

Infant and Preschool - including Fisher-Price®, Disney preschool and plush, Power Wheels®, Sesame Street®, See 'N Say®, Magna Doodle®, and View-Master®

Entertainment - including Disney, Nickelodeon®, games and puzzles

Wheels - including Hot Wheels®, Matchbox®, Tyco® Electric Racing, and Tyco® Radio Control

These operating segments all have similar economic characteristics, market children's products, and share the same production process. Based on these similarities, the Company's products can be aggregated into one reportable segment for purposes of this disclosure.

The table below presents information by geographic area (in thousands). Revenues are attributed to countries based on location of customer. Long-lived assets principally include net property, plant and equipment, and goodwill.

	Net Sales	Long-Lived Assets
1998		
United States	\$3,298,838	\$1,301,237
Europe and Canada	1,096,287	222,893
Asia and Latin America	386,767	411,118
	4,781,892	1,935,248
Corporate and other	-	245,985
Consolidated total	\$4,781,892	\$2,181,233
1997		
United States	\$3,307,576	\$ 577,727
Europe and Canada	1,143,378	166,423
Asia and Latin America	383,662	346,549
	4,834,616	1,090,699
Corporate and other	-	229,625
Consolidated total	\$4,834,616	\$1,320,324
1996		
United States	\$2,829,123	\$ 582,038
Europe and Canada	1,275,706	231,805
Asia and Latin America	430,503	364,079
	4,535,332	1,177,922
Corporate and other	-	191,917
Consolidated total	\$4,535,332	\$1,369,839

Credit is granted to customers on an unsecured basis, and generally provides for extended payment terms which result in a substantial portion of trade receivables being collected during the latter half of the year. Customers accounting for more than 10% of the Company's consolidated net sales and related accounts receivable are as follows (in millions):

	1998	1997	1996
<i>Worldwide sales for the year ended</i>			
Toys R Us	\$729.3	\$859.5	\$1,039.6
Wal-Mart	790.8	739.1	555.9
<i>Accounts receivable as of December 31</i>			
Toys R Us	\$148.9	\$260.7	\$ 185.0
Wal-Mart	291.4	178.6	90.4

Note 9 - Quarterly Financial Information (Unaudited)

(In thousands, except per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Year Ended December 31, 1998				
Net sales	\$ 705,164	\$861,526	\$1,672,120	\$1,543,082
Gross profit	323,918	404,748	852,237	782,090
Advertising and promotion expenses	98,081	109,875	253,493	351,844
Other selling and administrative expenses	183,791	190,689	218,543	289,104
Amortization of intangibles	7,713	7,741	12,714	13,761
Special charges (a)	-	-	38,000	6,000
Income before income taxes	17,756	84,617	279,486	83,204
Net income	12,669	60,384	199,665	59,546
Preferred stock dividend requirements	(1,990)	(1,990)	(1,990)	(1,990)
Net income applicable to common shares	10,679	58,394	197,675	57,556
Basic income per common share:				
Net income	\$ 0.04	\$ 0.20	\$ 0.68	\$ 0.20
Weighted average number of common shares	293,048	293,433	291,870	287,630
Diluted income per common share:				
Net income	\$ 0.04	\$ 0.20	\$ 0.66	\$ 0.20
Weighted average number of common and common equivalent shares	298,164	297,720	303,551	290,399
Dividends declared per common share	\$ 0.07	\$ 0.08	\$ 0.08	\$ 0.08
Common stock market price:				
High	\$ 45.63	\$ 43.63	\$ 42.31	\$ 39.63
Low	35.63	36.00	28.00	21.69
Year Ended December 31, 1997 (b)				
Net sales	\$ 693,520	\$972,656	\$1,555,347	\$1,613,093
Gross profit	322,811	458,837	800,277	818,075
Advertising and promotion expenses	102,626	131,713	244,231	300,569
Other selling and administrative expenses	185,286	192,707	198,767	220,192
Amortization of intangibles	8,122	8,092	8,033	7,932
Restructuring and integration charges (c)	275,000	-	-	-
Income (loss) before income taxes and extraordinary item	(267,619)	107,944	317,755	267,002
Extraordinary item - loss on early retirement of debt	-	-	(4,610)	-
Net income (loss)	(204,624)	75,634	219,045	195,129
Preferred stock dividend requirements	(2,840)	(2,837)	(2,838)	(1,990)
Net income (loss) applicable to common shares	(207,464)	72,797	216,207	193,139
Basic income (loss) per common share:				
Income (loss) before extraordinary item	\$ (0.72)	\$ 0.25	\$ 0.76	\$ 0.66
Extraordinary item - loss on early retirement of debt	-	-	(0.02)	-
Net income (loss)	\$ (0.72)	\$ 0.25	\$ 0.74	\$ 0.66
Weighted average number of common shares	288,382	291,737	290,650	290,962
Diluted income (loss) per common share:				
Income (loss) before extraordinary item	\$ (0.72)	\$ 0.25	\$ 0.73	\$ 0.64
Extraordinary item - loss on early retirement of debt	-	-	(0.02)	-
Net income (loss)	\$ (0.72)	\$ 0.25	\$ 0.71	\$ 0.64
Weighted average number of common and common equivalent shares	288,382	296,609	306,870	306,053
Dividends declared per common share	\$ 0.06	\$ 0.07	\$ 0.07	\$ 0.07
Common stock market price:				
High	\$ 29.25	\$ 35.25	\$ 35.75	\$ 41.38
Low	24.00	24.00	32.38	33.38

(a) Represents a nonrecurring charge in the third quarter related to a voluntary recall of certain Power Wheels® ride-on vehicles, and a one-time charge in the fourth quarter in connection with the proposed Toys R Us-related antitrust litigation settlement.

(b) Financial information for the first quarter of 1997 has been restated retroactively for the effects of the March 1997 merger with Tyco, accounted for as a pooling of interests.

(c) Represents a nonrecurring charge for transaction, integration and restructuring costs related to the merger with Tyco.

Note 10 - Supplemental Financial Information

(In thousands)	As of Year End	
	1998	1997
Inventories include the following:		
Raw materials and work in process	\$ 42,851	\$ 48,620
Finished goods	541,507	380,224
	\$584,358	\$428,844
Prepaid expenses and other current assets include the following:		
Deferred income taxes	\$178,060	\$170,626
Other	99,888	75,903
	\$277,948	\$246,529
Short-term borrowings include the following:		
Commercial paper	\$ 78,000	\$ -
Notes payable	56,006	17,468
	\$134,006	\$ 17,468
Accrued liabilities include the following:		
Advertising and promotion	\$147,551	\$144,020
Mattel restructuring and Tyco integration	33,497	108,581
Royalties	99,674	79,304
Other	370,291	297,540
	\$651,013	\$629,445

(In thousands)	For the Year		
	1998	1997	1996
Selling and administrative expenses include the following:			
Research and development	\$178,001	\$156,350	\$147,174
Supplemental disclosure of cash flow information:			
Cash paid during the year for:			
Income taxes	\$ 93,936	\$105,812	\$107,944
Interest	103,627	94,320	99,019
Noncash investing and financing activities:			
Issuance of stock warrant	-	-	26,444
Conversion of 7% Notes	-	16,034	-

Note 11 - New Accounting Pronouncement

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities*. This statement requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. It also requires that gains or losses resulting from changes in the values of those derivatives be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. The Company is required to adopt this statement for its fiscal year beginning January 1, 2000. Management believes the adoption of this statement will not have a material impact on the Company's consolidated financial position or results of operations.

Management Report on Responsibility for Financial Reporting

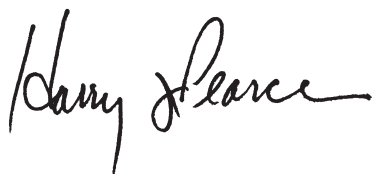
Management is responsible for the preparation of the Company's consolidated financial statements and the related financial and non-financial information appearing in this annual report. The financial statements have been prepared in accordance with generally accepted accounting principles and, in the opinion of management, present fairly the Company's financial position, results of operations and cash flows. The financial statements necessarily contain some amounts that are based on the best estimates and judgments of management.

The Company maintains accounting and internal control systems which management believes are adequate to provide reasonable assurance, in relation to reasonable cost, as to the integrity and reliability of the financial statements and as to protection of assets from unauthorized use or disposition. The selection and training of qualified personnel, the establishment and communication of accounting and administrative policies and procedures, and a program of internal audit are important elements of these control systems.

The Company's internal auditors are directed to examine the adequacy and effectiveness of the Company's system of internal accounting, administrative and operational controls. They conduct formal and systematic reviews to determine that operations are adequately controlled and to assure that assets are effectively safeguarded.

The board of directors has appointed an audit committee, composed entirely of nonemployee directors. The committee meets regularly with financial management, internal auditors and the independent accountants to review accounting control, auditing and financial reporting matters.

PricewaterhouseCoopers LLP, independent accountants, have been retained to audit the Company's consolidated financial statements. They conduct a review of internal accounting controls to the extent required by generally accepted auditing standards and perform such tests and related procedures as they deem necessary to arrive at an opinion on the fairness of the financial statements.



Harry J. Pearce
Chief Financial Officer

Report of Independent Accountants

To the Board of Directors and Stockholders of Mattel, Inc.

In our opinion, based on our audits and the report of other auditors, the accompanying consolidated balance sheets and the related consolidated statements of operations, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Mattel, Inc. and its subsidiaries at December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Tyco Toys, Inc. and its subsidiaries, which statements reflect net sales of \$720,954,000 for the year ended December 31, 1996. Those statements were audited by other auditors whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for Tyco Toys, Inc. and its subsidiaries, is based solely on the report of the other auditors. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for the opinion expressed above.



Los Angeles, California
February 1, 1999

Directors and Officers

Board of Directors

Jill E. Barad ⁽¹⁾ ⁽⁵⁾

Chairman and Chief Executive Officer, Mattel, Inc.

Dr. Harold Brown ⁽⁴⁾ ⁽⁵⁾

Senior Managing Director, E.M. Warburg, Pincus & Co., LLC

Tully M. Friedman ⁽¹⁾ ⁽⁶⁾

Founding Partner and Chairman, Friedman & Fleischer, LLC

Joseph C. Gandolfo ⁽⁵⁾

President, Worldwide Manufacturing Operations, Mattel, Inc.

Ronald M. Loeb ⁽³⁾ ⁽⁶⁾

Retired Partner, Irell & Manella

Ned Mansour ⁽⁶⁾

President, Corporate Operations and General Counsel, Mattel, Inc.

Andrea L. Rich ⁽³⁾ ⁽⁶⁾

President and Chief Executive Officer, Los Angeles County Museum of Art

William D. Rollnick ⁽¹⁾ ⁽²⁾ ⁽³⁾

Retired Chairman, Genstar Rental Electronics, Inc.

Pleasant T. Rowland

Vice Chairman, Mattel, Inc. and President, Pleasant Company

Christopher A. Sinclair ⁽²⁾ ⁽⁴⁾

President and Chief Executive Officer, Quality Food Centers

John L. Vogelstein ⁽¹⁾ ⁽²⁾ ⁽³⁾ ⁽⁶⁾

Vice Chairman of the Board, President, and Director, E.M. Warburg, Pincus & Co., LLC

Corporate Officers

Jill E. Barad

Chairman and Chief Executive Officer

Pleasant T. Rowland

Vice Chairman, Mattel and President, Pleasant Company

Joseph C. Gandolfo

President, Worldwide Manufacturing Operations

Ned Mansour

President, Corporate Operations and General Counsel

Francesca Luzuriaga

Executive Vice President, Worldwide Business Planning and Resources

Harry J. Pearce

Chief Financial Officer

Glenn Bozarth

Senior Vice President, Corporate Communications

Fermin Cuza

Senior Vice President, International Trade and Worldwide Government Affairs

Kevin M. Farr

Senior Vice President and Corporate Controller

John T. Phippen

Senior Vice President and Chief Information Officer

William Stavro

Senior Vice President and Treasurer

Business Unit Executives

Astrid Autolitano

President, Mattel International

Matthew C. Bousquette

President, Boys/Entertainment

Adrienne Fontanella

President, Girls/Barbie

Neil B. Friedman

President, Fisher-Price brands

David Haddad

President, Mattel Media

(1) Member, Executive/Finance Committee

John L. Vogelstein, Chairman

(2) Member, Compensation/Options Committee

John L. Vogelstein, Chairman

(3) Member, Audit Committee

William D. Rollnick, Chairman

(4) Member, Pension Committee

Christopher A. Sinclair, Chairman

(5) Member, Foundation Committee

Dr. Harold Brown, Chairman

(6) Member, Nominations/Corporate Governance Committee

Ronald M. Loeb, Chairman

Corporate Information

Transfer Agent and Registrar

Mattel, Inc. Common Stock
BankBoston, N.A.
c/o EquiServe Limited Partnership

Depository

Mattel, Inc. Depository Shares, each representing one twenty-fifth of a share of Series C Mandatorily Convertible Redeemable Preferred Stock
BankBoston, N.A.
c/o EquiServe Limited Partnership

Note Trustees

Mattel, Inc. 6-3/4% Senior Notes due May 15, 2000
Mattel, Inc. 6% Senior Notes due July 15, 2003
Mattel, Inc. 6-1/8% Senior Notes due July 15, 2005
Mattel, Inc. Medium-Term Notes
Chase Manhattan Bank and Trust Company National Association
101 California Street, Suite 2725
San Francisco, California 94111

Stock Exchange Listings

Mattel, Inc. Common Stock and Mattel, Inc. Preference Share
Purchase Rights
New York Stock Exchange and Pacific Exchange, Inc.

Mattel, Inc. Depository Shares
New York Stock Exchange

Stockholder Administration

Inquiries relating to stockholder accounting records, stock transfer, dividends (including dividend reinvestment) and direct stock purchase should be directed to:
BankBoston, N.A.
c/o EquiServe Limited Partnership
P.O. Box 8040
Boston, Massachusetts 02266-8040
Telephone numbers:
888-909-9922 (DRIP information only)
800-730-4001 (stockholder information)
Website: www.equiserve.com

Common Stockholders

As of March 1, 1999, there were approximately 48,000 holders of record of Mattel, Inc. common stock.

Annual Meeting

The Annual Meeting of Stockholders will be held June 3, 1999 at 10:00 a.m. at the Manhattan Beach Marriott, Manhattan Beach, California.

Form 10-K


Mattel's Annual Report to the Securities and Exchange Commission on Form 10-K for the year ended December 31, 1998 is available upon request by writing to the Secretary of the Company, 333 Continental Boulevard, El Segundo, California 90245-5012.

Trademark Legends

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El Segundo, California 90245

