



## Spin Master Corp.: A Cautionary Tale of Why the Devil Is in the Details

### Description

Let's play a little game of *Jeopardy!*. I'll be Alex Trebek. The category is "**Spin Master Corp.** ([TSX:TOY](#))."

If you're unfamiliar with the popular trivia game show, contestants provide answers in the form of questions, winning varying amounts of cash based on the level of difficulty. For example, if the category was "Investing," an appropriate answer might be "Warren Buffett" and the correct question, "Who is the world's greatest investor?"

I hope that makes sense. Now, let's get the show on the road.

Spin Master is a Toronto-based toy manufacturer whose 2015 revenue hit US\$879 million, a 23% increase over its 2014 results. It's the fourth-largest toy company behind just **Mattel**, **Hasbro**, and **Lego**. Earlier this year it made the news for its acquisition of Etch A Sketch from the **Ohio Art Company**. Like *Jeopardy!*, Etch A Sketch evokes fond memories from my childhood. It plans to reinvigorate the product just as it did with Meccano a couple of years ago.

With toy sales up 8% in 2015, Spin Master has lots of opportunities ahead of it, and its first-quarter numbers—net income of US\$9.9 million on revenue of US\$162 million, both well above the same quarter in fiscal 2015—suggest it's making hay while the sun shines.

But before you go ahead and buy Spin Master stock, it's important that we figure out what someone might pay to buy the company, lock, stock, and barrel.

Usually, a prospective buyer would pay an appropriate multiple based on its enterprise value, which is simply its market cap plus debt less cash on hand. One scenario might have Company A with a market cap of \$500 million, no debt and \$100 million in cash. Another could have it with \$400 million in market cap, \$200 million in debt and \$25 million in cash.

In the first version of its capital structure, Company A would have an enterprise value of \$400 million. In the second it would be \$575 million for the same exact revenue and income stream. Now, this is only a made-up example, but it demonstrates why investors need to look more closely at the financial

situation of prospective company investments.

Capital structure is a big deal. Our game of *Jeopardy!* will demonstrate why.

The *Final Jeopardy* answer: Spin Master's enterprise value.

The question: ?

Before you can fill in the question, you need the three financial numbers mentioned previously. The first is market cap, and here I get five different answers from five different websites: \$559.31 million, \$2.59 billion, \$556.62 million, \$2.60 billion, and \$548.23 million from Spin Master's own investor relations site.

The debt and cash parts of the equation aren't going to vary, and those can be found in its Q1 2016 report. To save you time, the debt is \$76.79 million and cash \$54.94 million.

Ready to provide the question? Well, we're getting closer. But first, we have to decide which market cap is the right one. If one assumes that Spin Master's investor relations number would most likely be the right one because it's their stock, then the question becomes "What is \$570.1 million?"

But, if you take the higher \$2.60 billion market cap number, the question becomes "What is \$2.62 billion?"

Huh! That's a \$2 billion difference. What gives?

The solution to this puzzle is all in how you calculate the market cap. Spin Master's site uses 21.3 million shares outstanding as its multiplier with its stock price. Those are the subordinate voting shares which carry one vote per share. The much higher \$2.6 billion figure includes almost 80 million multiple voting shares, which carry 10 votes each.

The mystery I'll leave you with is this: Why does Spin Master use 21.3 million shares to calculate market cap, but closer to 100 million for earnings per share? If you can answer this riddle, you're ready for the real *Jeopardy!*.

## CATEGORY

1. Investing

## POST TAG

1. Editor's Choice

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## Tags

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