Is Spin Master Corp. Headed South in 2017?

Description

The hottest toy this Christmas might have just gone off the rails, leaving **Spin Master Corp.** (TSX:TOY) investors pondering a speedy exit from its stock. How the company responds to this crisis will dictate the degree to which investors forgive Spin Master heading into 2017.

Should you stay or should go?

It's not a good thing when your star toy—Hatchimals—appears on the *Today Show* just three days after Christmas, and they're reporting on irate parents furious with the company for delivering a dud of a product.

Apparently, many of the eggs won't hatch, leaving children very distraught over the most highly anticipated gift of Christmas 2016. The runaway success story has caused people to pay as much as US$60,000 to acquire the toy at **eBay** and other online resale stores, well above the US$59.99 suggested retail price.

Now, all that consumer excitement appears ready to crumble. If Spin Master doesn't get this right, history has shown investors will show no mercy; the stocks of toy manufacturers are notoriously vulnerable to bad PR—and this is the worst.

Spin Master's **Facebook** page has been overwhelmed with comments—most of them negative—leaving the company's customer service team scrambling to respond to frustrated parents.

""Egg wouldn't do anything, no noises no lights. Did all tips and tricks, even watched the YouTube video. Had to manually hatch it," wrote one mother on Facebook. "Changed the batteries and it still won't do anything. Upset 6 year old on Christmas morning. Very very disappointed in this product."

The reaction on **Twitter** has been much the same.

"@SpinMaster I have been calling for 2 days, it keeps telling me to call back later, #Hatchimals is a dud and store won't take it back," Jessica Brown tweeted on December 27.

Spin Master has reacted to this problem in a timely manner, adding more staff to speak with upset parents.

“We have increased the number of customer case representatives, extended our hours and increased the capacity for callers in the queue to help prevent calls dropped due to the holiday volume,” a Spin Master spokesperson told *CNN* December 27. “We are reviewing each and every consumer inquiry.”

Interestingly, if you look at Spin Master’s stock movement year-to-date, you will see that most of its 56.9% gain came prior to Hatchimals being launched October 7. Spin Master closed October 6 at $32.29. As I write this, it’s down around 5% and is right back where it was prior to launch; it closed 2015 at $21.86.

The gains Spin Master stock has made this year have been gradual based primarily on three good quarterly reports—Q1 revenue up 52%, Q2 revenue up 41% and Q3 up 23%—with no mention of Hatchimals until the third quarter.

Here’s why Spin Master shareholders should be concerned.

“It’s not just hype,” toy analyst and CEO of Klosters Trading Corporation Lutz Muller told *BNN* in a phone interview. “Spin Master has been quite brilliant with this [...] it’s definitely going to last into next year.”

The company has been working feverishly in December to get more product to the stores, but with the latest blowback, how likely are toy buyers to commit to additional orders until Spin Master is able to assure the public that the toys aren’t defective?

Not very.

The toy business is a fickle one at the best of times. This might have been Spin Master’s 15 minutes of fame. If it doesn’t turn around the Hatchimals story in 2017, it doesn’t necessarily mean it won’t continue to grow revenues by double digits, but I wouldn’t count on its stock gaining 50% or more in 2017.

If I owned Spin Master stock and bought anywhere in mid to low $20s, I’d be inclined to sell half my position, take some profits, and wait for this situation to resolve itself. If I’d bought above $30, I’d be inclined to sell before a small gain becomes a loss.

Long term, I see Spin Master doing well, but 2017 might have just become a write-off for its stock.

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