Hasbro Third Quarter 2017
Financial Results Conference Call Management Remarks
October 23, 2017

Debbie Hancock, Hasbro, Vice President, Investor Relations:

Thank you and good morning everyone.

Joining me this morning are Brian Goldner, Hasbro's Chairman and Chief Executive Officer, and Deb Thomas, Hasbro's Chief Financial Officer. Today, we will begin with Brian and Deb providing commentary on the Company's performance and then we will take your questions.

Our third quarter earnings release was issued this morning and is available on our website. Additionally, presentation slides containing information covered in today's earnings release and call are also available on our site. The press release and presentation include information regarding Non-GAAP financial measures. Please note that whenever we discuss earnings per share or EPS, we are referring to earnings per diluted share.

Before we begin, I would like to remind you that during this call and the question and answer session that follows, members of Hasbro management may make forward-looking statements concerning management's expectations, goals, objectives and similar matters.

There are many factors that could cause actual results or events to differ materially from the anticipated results or other expectations expressed in these forward-looking statements.

Some of those factors are set forth in our annual report on form 10-K, our most recent 10-Q, in today's press release and in our other public disclosures.

We undertake no obligation to update any forward-looking statements made today to reflect events or circumstances occurring after the date of this call.

I would now like to introduce Brian Goldner.

Brian Goldner, Hasbro Chairman and CEO:

Thank you, Debbie. Good morning everyone and thank you for joining us today.

The Hasbro team delivered a very good third quarter – the highest revenue and earnings quarter in our history.

We have positioned Hasbro to unlock the full potential of our brands, investing significantly across the Brand Blueprint. We are still in the early stages of realizing our ambition. During this quarter we demonstrated our strategy's ability to deliver growth amid challenging conditions, across a number of dimensions.

- Revenues grew in each operating segment with double-digit consumer takeaway globally at retail;
- Franchise Brands, Hasbro Gaming and Emerging Brands revenues increased led by growth in NERF, TRANSFORMERS, MY LITTLE PONY, MONOPOLY, BABY ALIVE, FURREAL FRIENDS, SPEAK OUT and TWISTER;
- Our commercial and finance teams are effectively managing the short-term disruption from the Toys"R"Us restructuring and bankruptcy filing in the U.S. and Canada, as well as ongoing softness in the UK and Brazil;
- And our investments in our multi-screen content to commerce and omni-channel retail strategies are building deeper consumer

engagement across multiple brand experiences as evidenced by the growth in TRANSFORMERS and MY LITTLE PONY.

The industry data supports our success, and through August, Hasbro ranked first in the G11 toy and game markets, according to industry sources.

Hasbro revenues grew in developed economies including the U.S, Canada, France, Germany, Mexico and Australia. Emerging market revenues increased 8%, with growth in China and Russia, as well as from our new operations in India.

As we discussed last quarter, the UK and Brazil continue to face tough economic conditions, and we forecast that to continue in the near term. Our diverse geographic and brand portfolio positions us to overcome these challenges with strength in other major markets.

In addition, over the past several years, our global commercial teams have invested in an omni-channel retail strategy which puts Hasbro where consumers are shopping - not just at mass and toy specialty, but importantly in e-commerce, where consumer takeaway continues to outpace total point of sale; as well as in emerging channels including value, grocery and drug, new feature shops at retailers, fan and specialty retail.

While the near term impact of Toys“R”Us is disruptive, and we paused shipments for a short period as we gained clarity on the situation, we are working with them as we enter the holiday period. This doesn’t impact our outlook for overall consumer takeaway, which has continued to be strong, but does introduce higher uncertainty as to the level of shipments to them in the fourth quarter.

Importantly, we are also well positioned in new and growing channels. With the wealth of retail options, in store, online and omni channel, we are confident in the collective long-term outlook for the retail landscape.

For the third quarter, Hasbro’s Franchise Brand revenues increased 7%, with growth in NERF, TRANSFORMERS, MY LITTLE PONY and MONOPOLY. Hasbro Gaming increased 22% and Emerging Brands were up 9%.

NERF has posted double-digit growth throughout 2017 and Q3 was no exception. Global POS was up in the mid-to-high teens for the quarter, increasing in all regions. NERF Nitro launched and is off to a good start.

TRANSFORMERS multi-screen entertainment continued to drive revenue growth in the franchise. Point of sale is up versus last year and up versus the last movie year. This fall we continue with new entertainment initiatives to engage our fans. The global home entertainment release of *TRANSFORMERS: THE LAST KNIGHT* took place on Sept 28th and all-new episodes of *ROBOTS IN DISGUISE* and *RESCUE BOTS* are running on linear and streamed services. In addition, in partnership with Machinima, in November we are debuting the second chapter of the critically acclaimed Digital Animated series Prime Wars Trilogy…*TITANS RETURN*.

We see every day that brands backed by multi-format stories, combined with merchandise based on a robust investment in innovation, deliver engaging experiences for consumers, fans and audiences. Consumer insights, storytelling and content remain an integral part of creating successful sustainable brand franchises, and Hasbro is building industry-leading expertise.

My Little Pony revenue increased behind the release of *MY LITTLE PONY THE MOVIE* and successfully drove point of sale gains around the movie debut. Our content to commerce model delivers multiple revenue streams, including entertainment and merchandise, and we are well positioned in our investment. The film was successful in reinvigorating and energizing our core consumer base <u>and</u> our fanbase, while inviting new fans into the brand. The film is yet to be released in a number of international markets and will be followed by the home entertainment window, an important element of expanding the audience.

MONOPOLY revenues were up, with several new games including the Token Madness Edition as well as MONOPOLY GAMER featuring Nintendo characters and new game play.

As expected, MAGIC: THE GATHERING revenues declined in the quarter, while play numbers remain high, and sentiment from players and stores is positive. Our new digital gaming initiative, *Magic: The Gathering Arena,* was announced on September 7th and will go into closed Beta in November. The MAGIC: THE GATHERING franchise remains strong and our investments in its content, storytelling and digital platform will continue as we believe there remains significant future potential for the franchise.

Hasbro Gaming revenues grew 22% and consumer takeaway increased at a similar level. Gaming growth continued across multiple formats and our expertise in gaming coupled with our ability to translate social trends into commercial gaming experiences is driving growth around the world.

Partner Brand revenues decreased, led by declines in YOKAI WATCH as well as DREAMWORKS' TROLLS, which was down versus last year's third quarter's launch of the movie product. Point of sale for the category was up, including gains in MARVEL, DISNEY PRINCESS and DISNEY DESCENDANTS, DREAMWORKS' TROLLS and SESAME STREET.

TROLLS is performing well this year and we look forward to the upcoming entertainment, *DreamWorks' Trolls Holiday*, airing November 24 on NBC.

STAR WARS revenue increased in the quarter, with robust global retail support of *Star Wars: The Last Jedi* merchandise released on September 1. We anticipate consumer interest building as promotional activities increase and we get closer to the film launch date. The multi-year entertainment slate for STAR WARS has created a larger, more sustainable level of business for this top industry property. Today's entertainment cadence enables a higher, more repeatable level of sales versus historical periods when revenues would decline significantly in years without theatrical entertainment.

BEYBLADE is now available in all regions and contributing to year-over-year revenue gains. Europe and Latin America launched in the quarter and both are off to a good start. We continue to release new waves of BEYBLADE tops supporting ongoing innovation in the line.

Hasbro's portfolio of Marvel toy lines saw consumer momentum in the third quarter behind the theatrical release of Marvel Studios *Spider-Man: Homecoming*, as well as the home entertainment release of *Guardians of the Galaxy: Vol. 2*, with especially strong brand momentum in our Marvel Legends segment across Marvel franchises, as well as SPIDER-MAN role play items. We also have a new line supporting the November 3rd theatrical release of *Thor: Ragnarok.* In 2018, Marvel has eight theatrical films including Marvel Studios *Black Panther* in February and Marvel Studios *Avengers: Infinity War* slated for release in May.

Disney Princess and Disney Descendants consumer takeaway increased, behind strength in Moana and new Descendants 2 entertainment. In addition, Hasbro's new line in support of Disney's new holiday featurette "*Olaf's Frozen Adventure*" is now at retail ahead of the limited theatrical release in front of Disney/Pixar's *Coco* on November 22.

Finally, from September 8-10th, we hosted our first-ever HASCON in Providence - three days of hands-on brand experiences, meet-and-greets, sneak peaks, and fan-centric events for families and fans of all ages. This first of a kind event is emblematic of our journey from a toy and game company to a global play and entertainment leader, delivering immersive entertainment experiences around our brands, for fans of all ages.

To conclude, I want to reassure you that our brands and global POS are strong through today. Our growth plans for the holiday have been impacted by recent events at Toys"R"Us, as well as the economic outlook in certain countries. As a result, we currently expect fourth quarter revenue growth in the range of 4% to 7% year-over-year. This is a shift from our prior expectation, but reflects our current shipment plans for the next sixty days.

Consumer momentum continues to drive our business and we are well positioned with a diverse, in-demand brand portfolio to deliver growth for 2017 and beyond.

I'd now like to turn the call over to Deb.

Deb Thomas, Hasbro CFO

Thank you, Brian and good morning everyone.

The third quarter presented economic and retailer challenges, yet the Hasbro team delivered revenue and earnings growth while returning $164 million to shareholders through our dividend and repurchase program. We ended the quarter with $1.2 billion in cash, and are well positioned to capitalize on the innovation we have in the market place this holiday season.

As Brian mentioned, the Toys“R”Us bankruptcy filing in the U.S. and Canada negatively impacted our third quarter revenue and operating profit, including incremental bad debt expense associated with the bankruptcy. Excluding the incremental expense, total company operating profit would have been approximately 100 basis points higher in the quarter. While this event has also negatively impacted our initial growth outlook for the fourth quarter, we continue to work closely with Toys“R”Us to be able to deliver the right products to consumers for a successful holiday season.

For the third quarter, revenues in the U.S. and Canada segment increased 7% and grew in all product categories, including Franchise Brands, Partner Brands, Hasbro Gaming and Emerging Brands.

In total, U.S. and Canada point of sale increased double digits for the quarter and the first nine months of the year. Retail inventory remains of good quality.

Operating profit in the U.S. and Canada segment declined 5% to $217.3 million or 21.9% of net revenues. The year-over-year decline was the result of a shift in product mix, including the decline in quarterly MAGIC: THE GATHERING revenues, the revenue impact from ceasing shipments to Toys“R”Us for a short period and incremental bad debt expense. Excluding the bad debt expense, operating profit margin in the segment was down slightly.

International segment revenues increased 7%, including a favorable $27.9 million impact from foreign exchange.

Within the International segment, Franchise Brand and Hasbro Gaming revenue growth offset a decline in Partner Brand and Emerging Brand revenues.

Revenues increased across all three regions, Europe, Latin America and Asia Pacific, although Europe declined 1% on a constant currency basis. Point of sale increased in all three regions for the quarter and over the first nine months. The challenges we saw emerging in the second quarter have continued in the UK and Brazil, and we anticipate this will continue for the remainder of the year.

We ended the quarter with good quality inventory at retail, having addressed the pockets of inventory we previously discussed.

Operating profit in the International segment declined $1.1 million, or 1%, to $132.0 million, or 17.9% of net revenues. The decrease was primarily the result of a less favorable product mix.

Entertainment and Licensing segment revenues increased 4%. Growth was the result of higher consumer product revenues associated with our entertainment initiatives as well as a contribution from Boulder Media.

Segment operating profit increased 20% to $16.9 million, or 28.9% of revenue, on the higher revenues and expense leverage.

Overall Hasbro operating profit dollars were essentially flat, and operating margin declined to 20.1% versus 21.6% in 2016. As previously mentioned, operating profit margin would have been approximately 100 basis points higher excluding the bad debt expense.

Cost of sales increased 11% to 40.8% of revenues. The primary driver of the increase was a less favorable product mix, including the expected decline in MAGIC: THE GATHERING revenues and slightly lower Partner Brand revenues.

Royalty expense decreased 20 basis points to 7.8% of revenue, on the small decline in Partner Brand revenues partially offset by the continued growth from *Transformers: The Last Knight* movie product, which carries some external royalties.

Our investment in product development was essentially flat year-over-year but declined as a percentage of revenues due primarily to lower expenses at Backflip Studios. Our investment in innovation remains a point of differentiation and a high priority for our teams.

Program production amortization declined slightly in the quarter, but will increase in the fourth quarter as we begin to amortize our investment in the MY LITTLE PONY movie.

SD&A increased as a percentage of revenue to 17.4%. The percent increase over 2016 is the result of higher bad debt expense associated with Toys“R”Us. SD&A declined as a percent of revenue absent this expense.

We remain focused on the most efficient cost structure for our Company. Given the current environment, changing revenue expectations may slightly impact our operating profit margin outlook for the year.

Turning to our results below operating profit:

Other income was $14.0 million versus income of $8.5 million last year. Consistent with prior quarters, the biggest components of this line are higher interest income and our share of the earnings from the Discovery Family Channel.

During the quarter, we refinanced $350 million of 6.3% maturing debt by issuing $500 million of new 10-year 3.5% debt. We took advantage of the low interest rate environment to raise an additional $150 million to use for general corporate purposes. We are pleased with this result and expect this transaction to provide a very low cost of capital over the next 10 years. Going forward this will have a favorable impact of approximately $4 million per year to interest expense.

The underlying tax rate was 23.5%, down from 26.0% last year and versus the 24.5% for the full year 2016. The quarter included an approximate $0.04 benefit from our adoption of the new accounting standard governing stock compensation. This is consistent with our forecast from August and we continue to expect the fourth quarter's favorable impact to be in the range of $0.11 to $0.13. Our underlying tax rate is trending to the lower end of our estimated range. Based on our projected mix of revenue and earnings for the remainder of the year, we expect this trend to continue.

Diluted earnings per share for the quarter were $2.09.

Hasbro is in a strong financial position including a healthy balance sheet and good cash generation. We generated $823.6 million in operating cash flow over the trailing twelve-month period, ending the quarter with $1.2 billion in cash.

During the quarter we paid out $71.4 million in dividends and repurchased $92.9 million worth of common stock. We continue to target approximately $150 million in share repurchase this year and had $216.5 million available in our authorization at quarter end.

Receivables increased 14% and days sales outstanding increased 5 days to 83 days. The increase was due primarily to the mix of revenues as well as the timing of collections. Our accounts receivable are in good condition and collections continue to be strong. However, we expect the timing impact of ultimate collection from our Toys“R”Us receivables could add an incremental 2 days on our year end receivables compared to the end of 2016.

Inventories are in good shape, increasing 4% versus revenue growth of 7% and essentially flat absent the impact of foreign exchange. Inventories both at Hasbro and at retail are well positioned and of good quality to support our growth expectations for the holiday season.

In closing, despite a dynamic environment which has impacted our initial estimates for the year, we now expect our fourth quarter revenues to grow year-over-year in the range of 4% to 7%. Consumer trends remain positive through today, but there is higher near-term uncertainty with

Toys“R”Us as we see how they will begin to execute their plan to emerge from Chapter 11. Our global teams are effectively executing our strategy, with the industry’s best brands and strong commercial programs heading into the holiday season, while profitably driving our business both in the fourth quarter and beyond.

Brian and I are now happy to take your questions.