Hasbro First Quarter 2020
Financial Results Conference Call Management Remarks
April 29, 2020

Debbie Hancock, Hasbro, Senior 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 an update on the Company's response to the Covid-19 pandemic. Then we will take your questions.

Our earnings release and presentation slides for today's call are posted on our investor website.

The press release and presentation include information regarding Non-GAAP adjustments and Non-GAAP financial measures. Our call today will discuss certain Adjusted measures, which exclude these Non-GAAP Adjustments. A reconciliation of GAAP to non-GAAP measures is included in the press release and presentation.

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. These statements include, among others, the impact of the coronavirus on our business, financial results and liquidity; our efforts to protect the health and well-being of our workforce, customers, consumers, manufacturers and suppliers; our efforts to ensure we have adequate liquidity; and our initiatives to support our communities, including our global workforce, children and their families during these difficult times.

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.

These factors include those 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.

Every day I am inspired by the inventiveness and creativity of the global Hasbro team. We are finding new and ingenious ways to get product from production into cars and homes – safely and efficiently. They are finding new ways to create and deliver content as this year continues to evolve. Our people are supporting each other from our homes around the world. They are adapting to an ever-changing environment as they work tirelessly to minimize the impacts of COVID-19 on our business and our people.

We've focused Hasbro on four critical areas:

First, **demand:** Consumers want our products and experiences. They are looking for connections and engagement during this time. We are leveraging our extensive product portfolio and diverse retail network to connect global consumers with the product and experiences they want. We are offering compelling storytelling that continues to create strong viewership globally.

Second, **supply:** The Hasbro team is working to utilize our diverse manufacturing and supply chain network to ensure product is available for our customers and consumers.

Third, **liquidity:** We have substantial liquidity and we are taking prudent steps to ensure Hasbro remains in a strong financial position by aligning expenses to today's environment and preserving cash, while paying our dividend, meeting our debt commitments and making essential investments for the long term.

And, finally, **community:** This is a top priority. We are making decisions to protect our employees and stakeholders but also help where we can through this challenging time. I am so proud of the amazing work our teams have accomplished including to supply much-needed PPE for front-line medical workers, by producing 50,000 face shields per week that we'll be donating to local hospitals in Massachusetts and Rhode Island. The Wizards team in Renton is supporting Wizard Play Network member stores through its Mystery Booster Initiative and several eOne productions donated PPE to front line workers at Toronto General Hospital, UCLA and others. These are just a few examples of our commitment to our communities.

Our release today laid out extensive details in each of these areas – so my comments will focus on a few key topics.

The Hasbro management team has been together for more than a decade. We've recently added new expertise and experience. Together we are managing this new challenge – a challenge we are well equipped to successfully navigate. Over the past several years, we've invested to diversify our revenue and talent across play and entertainment – expanding our brand portfolio to reach more demographics and play patterns while building new businesses in entertainment and digital gaming. We realigned our commercial efforts to reach more consumers and built best in class online and omni-channel execution – as well as new channels such as drug, grocery, dollar, and value. These are strengths unique to Hasbro.

Our first quarter results were good – reflecting strong consumer demand and our ability to get product to customers and to consumers. Global point of sale increased in the mid-single digits, led by double-digit gains in the U.S.

E-commerce point of sale increased significantly as shoppers turned to online and curbside pick up to meet their needs. While point of sale is positive in April, continuing these positive trends will likely become increasingly difficult as more countries are practicing social distancing, including limiting production of product and entertainment, distribution activities and shopping. We are leveraging our global sourcing network to get product made and delivered to consumers, but we expect the second quarter may be more challenging than the first. This is due to several factors including that late in the first quarter and to start the second quarter, more stores and countries have shut down activities; entertainment properties where we are launching product have moved to later release dates in 2020 and into 2021 – and some have gone straight to PVOD; and our own live action TV and film entertainment production is limited. We have done extensive scenario planning to understand these impacts to our business for multiple different periods when the consumer economies could reopen. We are acting nimbly and creatively to address these factors throughout the business. Across our portfolio, we have innovative product and compelling entertainment to deliver a good second half of the year, including for the holiday. 2021 is also set up well given the shift of several entertainment initiatives to next year, in addition to our established plans for the year.

In the first quarter, consumers sought out several Hasbro brands and experiences – games, PLAY-DOH and content viewership were amongst the strongest. Face to face gaming demand stood out – in many Hasbro gaming brands. Demand is robust and we are working to continue meeting consumer purchase interest with games production from multiple locations, some of which have been closed in recent weeks, but we expect to reopen this summer.

First quarter results for MAGIC: THE GATHERING were above trend behind strong releases, but also due to steps we took. We adapted the physical release cadence of *Ikoria: Lair of Behemoths*, including pulling product shipments into the first quarter to support a rolling release plan with a global launch currently scheduled for most of the world on May 15th. The team cancelled physical events and developed new initiatives to keep our organized play engines operational by transitioning to digital play on *Arena* with Friday Night Magic at Home and MagicFest Online. Despite a decline in organized in person play events, this pivot drove an increase in new players across the brand. Upcoming expansions into mobile, China and Mac in 2020 will continue to expand the *Arena* audience. We are supporting Wizards Play Network stores through innovative programs to create revenue opportunities for the store owners in the absence of players physically in them.

Importantly, this was our first quarter with eOne as part of Hasbro. Integration between Hasbro and eOne is on schedule and the teams are actively engaged together, allowing us to create and uncover new revenue opportunities through entertainment and merchandise. We expect to deliver synergies in line with our plan for 2020 and are on track to deliver the $130 million in synergies we've communicated by year-end 2022.

We've transitioned eOne to lead our company-wide entertainment content efforts and we've integrated the creative teams including development on potential Hasbro brands for television and film. eOne's first quarter TV and Film results reflected a difficult comparison to the first quarter of last year when they delivered a high volume of programming. Revenue is tied to production deliveries and these will vary in timing each year. In 2020, this was slated to be later and is being pushed further as production activities have closed and the deliveries have been delayed. The team can do development work and virtual pitches, as well as animation production. Delivery of programs will happen – just later than initially planned.

First quarter licensing revenues for PEPPA PIG and PJ MASKS include the holiday 2019 sales. Strong demand for content across all platforms was offset by lower licensee shipments to retailers. PEPPA PIG is now the most viewed pre-school show in the world on the YouTube platform and PJ MASKS is one of the most streamed children's shows on Netflix in the U.K. and U.S. We have aligned the consumer products efforts for these brands, along with RICKY ZOOM, under Hasbro's consumer products team and are identifying opportunities for expansion. However, certain consumer products categories, in particular soft goods like apparel, are showing weakness within the industry and we expect this will be a challenging period for licensed categories.

Our teams have reacted creatively and constructively to identify a successful path forward during this unprecedented global pandemic. The underlying drivers for our business are sound and with great innovation, brands and storytelling we are well positioned to successfully execute in 2020 and beyond. The North Star of our company has not changed: Hasbro is creating play and entertainment experiences which are vital and desired by consumers and audiences this year and for years to come, delivering value for our stakeholders.

I will now turn the call over to Deb.

Deb Thomas, Hasbro CFO

Thank you, Brian and good morning everyone.

Hasbro is in a good financial position – consumers and audiences are engaging with our brands and content; we are profitable; we have substantial liquidity; and we continue to take the necessary steps to align our expenses and cash spend with the current environment.

We completed the eOne acquisition in early fiscal 2020 and performed our first quarter close as a combined company remotely. Globally, our combined finance and accounting team did outstanding work and we've provided 2019 quarterly historical results in accordance with U.S. GAAP for eOne in today's earnings release. We have booked opening amounts, and as we complete our valuations and purchase accounting over the coming year, there may be further items impacting our results which we'll highlight as we progress through 2020.

We continue to target synergies of $130 million by year end 2022. We slowed the pace of certain activities early in the year to reflect the current environment, but we remain on track to achieve the targets we have set, including 2020 cost savings of approximately $20 million, before one-time expenses.

My discussion today will be versus pro forma adjusted 2019 earnings and exclude eOne acquisition-related expenses and amortization. In our reported numbers, we reflected $147 million after tax of one-time expenses and acquisition amortization, or an impact of $1.07 per share.

As Brian highlighted, our organization is focused on four things.

I'll start with our top priority: **Community**. Our teams around the world have showcased tremendous ingenuity and resilience during 2020. Their health, safety and well-being guide our every decision. I'd like to reiterate what Brian said – I am tremendously proud of the work our teams are doing to support not only each other but the communities in which we are operating. It is a testament to their belief in our purpose of making the world a better place for children and their families.

Moving to **Liquidity:**

We ended the quarter with $1.2 billion in cash on the balance sheet, we have $1.5 billion available through a revolving credit facility and are well within our financial covenants. As a reminder, our low cash period traditionally occurs in the fourth quarter, in the October and November time frame. We have significant cash and liquidity and have also identified opportunities to reduce our expenses and our cash spend. These include pausing planned headcount additions and broad scale merit increases, reducing future travel expenses and moving planned live events to virtual. These are just a few of the actions we are taking. Our next major debt maturity of $300 million is due in May of 2021. The Board remains committed to our dividend and in February we paid the first dividend of the year, with the next payment already declared for May.

As Brian discussed, entertainment production at eOne is shut down for most areas of their business. This is driving a lower than planned cash spend for content in 2020. Assuming an early third quarter return to production, we expect to spend approximately $150 million less this year than originally planned and within a range of $500 to $600 million for the year.

We've also closely reviewed capital expenditures. About half of our capital spending is related to tooling for our product for future periods and the timing of that spend is weighted to the second half of the year. We've reviewed IT projects and facility renovations as well as investments in digital gaming development and reduced our 2020 spend expectation to $145 to $155 million.

Moving to the balance sheet, inventories declined overall and include approximately $7 million from eOne. Accounts Receivable increased $325 million, approximately $223 million of which relates to eOne. For the remainder, much of the increase is coming from the U.S. and is driven by the timing of sales in the quarter and the shift to more domestic revenues versus direct imports that we were seeing at the end of 2019. When we compare the March 2020 DSO to the comparable pro forma measure in 2019, we have increased DSO of 2 days.

We are closely monitoring credit for our customers, however, we should recognize our three largest customers remain Walmart, Target and Amazon.

Next, let's discuss **Demand:**

For the first quarter, revenues declined 7% absent FX.

20% growth in the U.S. and Canada segment, including growth in gaming such as MAGIC: THE GATHERING, MONOPOLY, DUNGEONS AND DRAGONS, THE GAME OF LIFE, JENGA, CONNECT 4 and others; and our product for Disney's *Frozen 2*, along with 8% growth in Europe was more than offset by the declines in eOne, including a slate which was planned for later deliveries this year versus last; in Asia Pacific – which was impacted by COVID-19 during the quarter; and Latin America - which is working through excess retail inventory.

We currently expect the impact of COVID-19 to be more significant in the second quarter due to retail store closures, supply chain disruption, live action production shutdowns and changing theatrical release schedules. However, consumer demand through April has continued to be up and we are working aggressively and creatively to meet that demand.

As Brian highlighted, we've seen high viewership for our content, which is driving brand engagement.

Finally, **Supply.** The Global Operations team is working to ensure we can make and deliver the product our customers and consumers are looking for. About 55% of our production is currently done in China and has returned to normal levels. In other states and countries, we have varying levels of supply chain operations, including some closed warehouses and factories. As outlined in our release, we expect to catch up on production over the coming months and be positioned to meet holiday demand. Should the facility closures last longer than anticipated, this would be more challenging. We've also recorded incremental shipping costs to support the movement of product across our global supply chain network.

For the eOne business, TV and film production teams are able to perform development and animation work, as well as pitch ideas. They are being incredibly creative on how to get work done, but the majority of production is not happening. As I mentioned earlier, our plans currently have us resuming live action production early in the third quarter.

Finally, let me touch on a few expense items on a pro forma basis:

Gross profit margin, including both cost of sales and program production cost amortization, increased 110 basis points, aided by favorable mix due to strong gaming, including MAGIC: THE GATHERING, and lower program amortization.

Cost of sales decreased 4%, due to the favorable product mix mentioned, partially offset by higher air freight costs associated with moving product out of China once the factories re-opened.

Program production cost amortization declined 21% on a pro forma basis on the lower entertainment deliveries in the quarter.

On the advertising line, the year-over-year rate was higher due to aligning eOne and Hasbro's accounting policies. We are reducing advertising levels while adjusting campaigns and their timing to reflect the current environment. This is one of our most variable line items and we are appropriately aligning the spend to both deliver top line and lower our cash outlay and will be well prepared to drive demand for the third and fourth quarters.

SD&A increased 2%. We are implementing cost savings activities related to compensation and hiring as well as professional services, travel and other discretionary areas, such as shifting live events to virtual ones. In the quarter, we aligned accounting policies on cost capitalization and stock compensation, which resulted in higher admin costs for eOne. We also experienced higher shipping expense due to the unplanned significant increase in games sales, which offset savings from a decline in warehousing expense.

We've done extensive scenario planning to understand the impact of COVID-19 on our business, mapping out the implications for various returns to more normalized activities, as well as the impact of operating in a global recession. Despite having a good understanding of the factors and how to manage them, the outcomes vary widely and that drove our decision to withdraw our full-year 2020 guidance. As we move toward reopening economies, we are planning for a good holiday season with great innovation and entertainment across our portfolio. We have confidence in the strategic advantages of our business model as a global play and entertainment company to both navigate the near-term and to drive long-term profitable growth.

Now, Brian and I are happy to take your questions.