Hasbro Third Quarter 2021

Financial Results Conference Call Management Remarks

October 26, 2021

Debbie Hancock, Hasbro, Senior Vice President, Investor Relations:

Thank you and good morning, everyone.

Joining me today are Rich Stoddart, Hasbro's interim chief executive officer, and Deb Thomas, Hasbro's chief financial officer. Today, we will begin with Rich and Deb providing commentary on the Company's performance. 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.

Our discussion will be based on adjusted results which exclude several items associated with the eOne acquisition outlined in our release today.

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.

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 Rich Stoddart, Rich.

Rich Stoddart, Hasbro Interim CEO

Thank you, Debbie, and welcome to everyone joining us today. I'm Rich Stoddart, interim CEO at Hasbro. Before we officially begin the remarks on the call today, I want to take a moment to reflect on the passing of our beloved leader and friend, Brian Goldner. I know many of you share in our sadness for his untimely passing. Brian was not only an accomplished CEO, he was a true visionary who transformed an almost 100-year-old toy and game company into a leading global play and entertainment company. But his impact can be felt well beyond Hasbro. He changed the game completely. He believed in the power of a story, seeing the potential for omni-channel storytelling and content built on powerful brands. He architected a compelling roadmap for Hasbro's growth in the Brand Blueprint strategy and was so proud of where it has taken Hasbro but even more so in its power and future potential now with eOne as an integrated part of the family.

I had the privilege to work together with Brian and the Hasbro team for the last seven years and serve on the Company Board, most recently as Lead Independent Director. During that time, the Company transformed its talent, its culture, its brands and its potential as it executed the Brand Blueprint. In my new role as interim CEO, I will continue to work with the talented leadership team Brian put in place over the last 13 years, along with the powerful culture at Hasbro, to Supercharge the Blueprint and build on the Company's strong momentum.

Hasbro is performing at a high level, and with a clear, well understood strategy. To ensure our success continues, I will be focused on five key priorities:

- Supporting the amazing people at Hasbro, ensuring they have what they need to succeed, while advancing our purpose-driven culture.

- Executing the Brand Blueprint. This strategy is central to continuing Hasbro's transformation as a global play and entertainment company. We are beginning to see the full blueprint execution come to life, with significant potential to grow revenue and profit in the years ahead.
- Accelerating the growth of our entertainment and Wizards of the Coast businesses where we have unique and distinct advantages in the market, and a differentiated business model relative to our competitors.
- Delivering the guidance established for the year, while helping the organization manage through supply chain challenges; and
- Continuing to drive strong cash generation in the business to pay down debt and fund the dividend.

This should sound familiar to many of you, as it is what the leadership team has been focused on as well.

It's fitting that the strong third quarter results reflect the power of the blueprint – with significant growth in entertainment as it returns to pre-pandemic levels; with another strong quarter in both tabletop and digital gaming from Wizards of the Coast; and with only a small decline in our consumer products business as we work to meet robust demand for Hasbro brands despite supply chain disruption.

The diversification of the business enabled us to deliver a very strong quarter with 11% revenue growth; 6% adjusted operating profit growth; 5% gains in adjusted EBITDA and earnings, and to generate significant cash.

Deb will speak shortly in more detail to the third quarter performance.

A clear proof point of the Brand Blueprint strategy and the omni-channel storytelling opportunity for our brands, is in the success of the CGI animated feature, *My Little Pony: A New Generation*, which debuted on Netflix September 24. In its first weekend, the movie reached number one on Netflix in the Kids Top 10 across 86 countries. It also reached the number one spot for Movies – regardless of genre or target demo – in 20 countries including the U.K., Germany, Brazil and Mexico. The success of the film was made possible by the collaboration and partnership of the talented brand teams at Hasbro with the teams at eOne who together created a beautiful engaging film for fans around the world to enjoy. The film's success is also a testament to their agility to successfully market and launch a picture originally planned for theatrical release on a streaming platform.

The movie's success builds deeper connections with consumers, driving incredible engagement on social media, across Instagram and TikTok.

The brand's relaunch, powered by an all-new Mane 5 cast of ponies, drove revenue growth for the franchise for the second straight quarter, and the first positive quarters since the fourth quarter of 2017. Third quarter point of sale momentum began to rebound as the merchandise tied to the brand reintroduction and movie began to hit shelves. In the four weeks leading up to the movie, POS was up mid-single digits globally, and the week following the movie resulted in Global POS gains over more than 150%. This trend has remained very strong in the weeks following.

The movie launch was further supported with a robust licensing program, including a dedicated MY LITTLE PONY shop on Amazon and cross-category campaigns at several major global retailers.

We've seen a favorable response from retailers and consumers and the entertainment plan is only beginning as we are supporting the film with a robust content roadmap from eOne, including Netflix specials and new series as well as digital content in the coming year.

Another significant milestone this quarter was the launch of Hasbro's PEPPA PIG and PJ MASKS toy and games lines in markets around the world. Brought into the Hasbro portfolio via the eOne acquisition, these brands significantly strengthen Hasbro's presence in the preschool market. We developed deep lines for each brand as well as expanding their licensed consumer products presence.

Each of these launches are off to strong starts, and contributed to growth in the quarter, but they – among many other brand campaigns - were limited in their upside in the short term due to the supply chain challenges global companies are facing. In the third quarter we had orders for approximately $100 million which did not ship by quarter end. The vast majority of this has already been delivered in the fourth quarter.

These factors were more than offset by the contribution of our entertainment business – which is up substantially versus last year's third quarter and up versus 2019, as well as the continuing momentum in the Wizards of the Coast business. Through our differentiated strategy, they delivered the revenue and profit growth for the quarter.

As we look to the fourth quarter, and the holiday season, there is strong demand for Hasbro toys and games. We are expertly managing the supply chain to ensure the shelves will be filled with Hasbro products this holiday.

As a result, we believe we will grow revenue in the fourth quarter, through the combination of our three business segments, and deliver full-year double-digit revenue growth in the range of 13% to 16%, along with adjusted operating profit margins in line with last year's adjusted rate of approximately 15%.

Before turning the call to Deb, I want to touch briefly on the plan for naming a permanent CEO. Our board is and always has been actively engaged in succession planning for the CEO and other senior executive roles. This work provides a strong foundation for the naming of a new long-term leader for Hasbro and is well underway. Until that time I am working closely with the outstanding group of talented individuals making up our senior management team. In addition to Deb, joining me today for the Q&A portion we have Chris Cocks, President and COO of Wizards of the Coast and Digital Gaming, Eric Nyman, Chief Consumer Officer and COO of Hasbro Consumer Products, and Darren Throop, CEO of eOne.

Now I'll turn the call over to Deb.

Deb Thomas, Hasbro CFO

Good morning, everyone. On behalf of Hasbro employees globally, I would like to thank Rich for stepping up at this time for us, our board, our shareholders, and our Company. The past couple of weeks have been difficult for all of us at Hasbro. Brian is missed but the impact he made is unmistakable. We heard from so many of you remarking on Brian's leadership and your positive personal interactions with him. Thank you for sharing these memories with us. Brian empowered me and the executive team to run Hasbro and together we are – and will continue - doing that.

Brian was proud of our third quarter results. They showcase the strength of Hasbro's unique business model, with growth in entertainment and at Wizards in both tabletop and digital gaming. Our results also show the strength of our global teams as they expertly manage through supply chain disruptions and position us for growth in the fourth quarter and for the year.

Brian believed, as we do, in investing to grow, to unlock Hasbro's full potential and create value for our shareholders. Our priorities remain the same, and we are executing against those priorities.

The quarter highlighted our focus on de-levering our balance sheet, as we repaid an additional $400 million of debt, bringing our year-to-date total to $972.5 million of long-term debt retired. We also paid the dividend, which has been maintained following the eOne acquisition and throughout the pandemic. At quarter end, cash on hand was $1.2 billion and we continue to make significant progress toward our goal of returning to our target of 2.0-2.5X debt to EBITDA and maintaining our investment grade rating.

For the quarter, revenue grew 11% versus last year, and 6% versus pro-forma 2019. MAGIC: THE GATHERING, MY LITTLE PONY, PEPPA PIG and PJ MASKS were among our largest revenue gaining properties globally in the quarter, further supported by significant entertainment deliveries. These include *My Little Pony: A New Generation* for Netflix, *Yellowjackets* for Showtime; *Fear the Walking Dead* for international markets; *Come From Away* and *Finch* for Apple TV as well as *The Rookie* for ABC.

Entertainment segment revenues grew 76%, with gains in scripted and unscripted television, live action and animated film, and animated content. This performance has us well on the way to reach 2019 levels of Entertainment revenue for the full year, excluding the music business over the second half of the year. The segment delivered adjusted operating profit of $42.1 million, or 12.9% operating profit margin, up from an adjusted loss of $3.6 million last year.

We are developing over 200 projects across Film & TV including content for over 30 Hasbro brands for the coming years. Year to date through September, we have invested approximately $526 million in content development and continue to anticipate a full year spend range of $675 million to $750 million.

For the fourth quarter, we have significant deliveries planned including *Graymail*, a new scripted program for Netflix; additional episodes of *The Rookie* and *Yellowjackets*; and the films *Clifford the Big Red Dog* and *Mrs. Harris Goes to Paris*.

Wizards of the Coast and Digital Gaming segment revenues increased 32%. Wizards had a great third quarter and we expect the business to deliver its goal of doubling from its 2018 revenue by the end of 2021, two years ahead of plan.

MAGIC: THE GATHERING and DUNGEONS & DRAGONS led this growth both in the quarter and over the past few years, with gains in both tabletop and digital gaming revenues. It was the second largest quarter in Wizards' history, behind only Q2 of this year. Among the MAGIC releases in the quarter, our third quarter premier set, *Adventures in the Forgotten Realms*, launched July 23rd and became our first co-branded premiere set. Fans of both MAGIC and DUNGEONS & DRAGONS embraced the product, and it is on track to be our best-selling summer release of all time.

Importantly, our digital investments are driving revenue growth. *Magic: The Gathering Arena* mobile continues to grow. It is a meaningful source of new players, and our releases were bolstered by their engagement in the game. Our licensed digital gaming business also delivered strong growth in the quarter.

Operating profit in the segment increased on the higher revenues. Investments in future game development and support of new game launches, as well as increased digital gaming depreciation, reduced operating profit margin from last year.

Consumer Products revenue declined 3%. There is strong demand for our brands but we were unable to fulfill approximately $100 million of product we had orders for during the quarter. Including these missed shipments, revenue would have increased 5%. In September we shipped the most volume ever domestically in a single month, and through today, we have shipped the majority of what we didn't deliver in the third quarter. This achievement is remarkable given it was accomplished in the middle of a global pandemic with unprecedented supply chain challenges across the globe.

As we shared last quarter, we took steps early to mitigate risk, including activating alternate ports in China and the U.S., expanding our shipping capacity, working closely with customers to provide support where we can and prioritize supply based on inventory and customer needs, and in certain instances using air freight to ensure delivery. The team has done an amazing job and continues to work nonstop.

Global point of sale declined mid-single digits. As we improve our in stock levels, and see the effects of a significant increase in advertising spend and out of aisle execution, we expect significant improvement.

Within Consumer Products, Hasbro Gaming revenues grew in the quarter, led by demand across our gaming portfolio, and Emerging Brands revenue was up, fueled by our toy and game launches of PEPPA PIG and PJ MASKS.

In our Franchise Brands, Rich already spoke to the success of MY LITTLE PONY and how this positions us well in the relaunch of the brand.

TRANSFORMERS revenue increased in the quarter. The final chapter of the *War for Cybertron* Trilogy launched July 29th on Netflix driving continued demand in our Generations Fan product. We also celebrated a new milestone for the TRANSFORMERS Franchise, when Universal Studios Beijing opened *Transformers: Metrobase*, the first ever TRANSFORMERS-themed land. In partnership with Paramount, production on *Transformers: Rise of the Beasts* continues for theatrical release next summer.

Partner Brands revenue declined, but Hasbro products for the Marvel portfolio grew, including Marvel Legends and the new preschool product line launch supporting *Spidey and His Amazing Friends*. We also introduced new products to support Marvel Studios' Disney+ series and the theatrical release of Marvel Studios' *Shang-Chi and the Legend of the Ten Rings*.

Ghostbusters revenue increased with the primary launch of the toy line in August for the feature film *Ghostbusters: Afterlife* from Sony Pictures, coming to theatres November 19th.

Operating profit for the Consumer Products segment decreased $15.8 million reflecting the lower revenue and incremental expense for freight and related costs. Price increases to mitigate the higher expenses in shipping and input costs went into effect in most markets in August and will be fully implemented for the fourth quarter.

Looking at our overall Hasbro P&L, gross margin, including cost of sales and program amortization, declined 130 basis points. This reflected essentially flat cost of sales dollars. Given favorable mix and growth in entertainment, cost of sales declined 340 basis points as a percent of revenue. The robust entertainment revenue growth drove an associated increase in program amortization of 470 basis points.

Product development increased $17 million, led by incremental investments in future tabletop and digital games at Wizards and our ongoing commitment to innovation across the business.

Advertising expense increased $26 million including promotional activity in support of the *My Little Pony* movie and advertising behind new Wizards' game launches. We have aggressive advertising plans for this holiday season, shifting more dollars this year into the fourth quarter, to drive point of sale. We will, however, closely match this expense with inventory availability.

Adjusted SD&A increased $35 million and continues to reflect higher expenses as the business returns to pre-Covid levels. This includes higher freight costs, incremental marketing and sales expense, increased depreciation associated with capitalized digital games, and increased compensation. Despite these higher expenses, SD&A remained flat as a percentage of revenue.

The adjusted underlying tax rate for the quarter was 23.4% compared to 19.9% a year ago. The rate is mainly driven by a change in the mix of income. We continue to expect the full-year underlying rate to remain at approximately 21%.

Our balance sheet is strong. In addition to our cash position and lower debt, DSOs were 68 days, a reduction of 5 days compared to Q3 2020 reflecting both higher revenue and good collections, despite shipping a large volume of product late in the quarter.

Inventory increased slightly year-over-year but declined absent FX. At quarter end, we had less in finished goods on hand than typical, and significantly more in-transit inventory. In general, total transit times have nearly doubled across all lanes and, on certain lanes, transit times are as much as 50 days longer compared to pre-pandemic levels.

Our strong third quarter and year to date performance has us on track to meet our guidance for double-digit revenue growth, which we now are expecting in the range of 13% to 16% for the full-year and maintaining an adjusted operating margin of approximately 15%. We have orders to support the high end of the revenue growth range, but there are supply chain factors out of our control which could impact our ability to fully achieve the upside.

I am incredibly proud of how the organization has come together this year. Despite many obstacles our results showcase the strength of our business, our strategy, and our team.

Our leadership team is now happy to take your questions.