Hasbro Second Quarter 2010 Financial Results Conference Call

Management Remarks

July 19, 2010

Debbie Hancock, Vice President, Investor Relations:

Thank you and good morning everyone. Joining me today are Brian Goldner, President and Chief Executive Officer; David Hargreaves, Chief Operating Officer and Deb Thomas, Chief Financial Officer.

To better understand our results, it would be helpful to have the press release and financial tables available that we issued earlier today.

The press release includes information regarding non-GAAP financial measures discussed on today's call and it is available on our website at hasbro.com.

We would also like to point out that on this call, whenever we discuss earnings per share or EPS, we are referring to earnings per diluted share.

During the call this morning Brian will discuss key factors impacting our results and Deb will review the financials. We will then open the call to your questions.

Before we begin, let me note 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 forward-looking statements may include comments concerning our product and entertainment plans, anticipated product performance, business opportunities and strategies, costs, financial goals and expectations for our future financial performance and achieving our objectives.

There are many factors that could cause actual results and experience 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, 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.

Now, I would like to introduce Brian Goldner.

Brian Goldner, Hasbro President and CEO:

Thank you, Debbie.

Good morning everyone and thank you for joining us today.

Our global teams continued to execute our long-term strategy through the second quarter. Heading into Q2, we knew it would be a challenging quarter as we faced difficult comparisons with the initial movie ship-ins last year for both TRANSFORMERS and G.I. JOE. In fact, the revenue decline from these two brands combined was $174 million in the quarter. This decline was partially offset by gains of $120 million across the remainder of our brand portfolio and backed by strong execution of our team globally. Overall, revenue declined 7 percent in the quarter as several of our brands and product categories grew. I will provide more insight on this performance in a moment.

Despite lower year-over-year revenues, we increased operating profit 9% from the second quarter last year. Our ability to improve operating profit clearly illustrates the operating leverage we are unlocking in our business.

We continue to expect our revenue to be more heavily weighted to the back half of the year as our major initiatives are beginning to launch. For the full year 2010, we still believe we should be able to grow revenues and earnings per share, including the dilution from our television investments and barring a further decline in foreign exchange, consumer spending or global economic conditions.

Reviewing our second quarter performance, the Games & Puzzles category, up 22%, and Preschool, up 32%, both posted strong growth as did several of our mega-brands, including:

- MAGIC: THE GATHERING - which continues to perform extremely well;

- MONOPOLY – celebrating its 75th anniversary this year;

- NERF – showing strong growth both in the U.S. and through international expansion; and

- PLAYSKOOL – which is seeing growth across a number of initiatives including infant, learning and Mr. & MRS. POTATO HEAD, who are leading characters in Toy Story 3.

- Other brands contributing to growth include FURREAL FRIENDS, PLAY-DOH, OPERATION, BABY ALIVE, STRAWBERRY SHORTCAKE, TONKA and IRON MAN.

We have said this year would be about “singles and doubles” – meaning it would be a year when we are driving growth across the breadth of our portfolio. Year-to-date, revenue is down just $3 million versus a year ago.

Over the coming months, we have a number of initiatives launching.

- In the Boys category, BEYBLADE is off to a promising early start in Canada, and is just starting to hit shelves in the U.S. Programming is on the air in both markets. Programming and product are also scheduled for major European markets, Mexico, Australia and New Zealand this year. NERF and the newly rebranded NERF SUPER SOAKER have been strong contributors to growth in the first half of the year and in the second half we have major new product launches slated;

- In Girls, LITTLEST PET SHOP is adding an exciting new play pattern inspired by our consumer insight work with BLYTHE LOVES LITTLEST PET SHOP. Also, FURRY FRENZIES, within our FURREAL FRIENDS line, will be hitting retail this fall;

- In Preschool, our entrance into the electronic learning aid category with ALPHIE is off to a good start. PLAYDOH is adding SESAME STREET to its line and CHUCK MY TALKING TRUCK will get additional support from new programming on THE HUB.

- Finally, in Games and Puzzles, we continue to innovate our evergreen brands with creative play while introducing exciting new brands. CUPONK, our new themed ball and cup game, is off to a good start. SCRABBLE FLASH, MONOPOLY REVOLUTION and our new line of construction games under the U-BUILD brand are just a few additional highlights for the second half of the year. We will support these initiatives with the continuation of our successful, global Family Game Night initiative including a new marketing campaign this fall.

We also feel very positive about our new network. This fall, the HUB, our children's television network with Discovery, is on schedule to launch on 10-10-10. At this point, Margaret Loesch and her team have announced much of the programming, completed all its acquisition deals for the fall launch, and continue to finalize the schedule. As part of these announcements, Hasbro Studios has seven shows announced to be on THE HUB. These include: *Transformers Prime; G.I. Joe Renegades; My Little Pony Friendship is Magic; The Adventures of Chuck and Friends; Pound Puppies; Pictureka* and *Family Game Night*. Additionally, several of our partners have programs slated for the network including *Strawberry Shortcake* from American Greetings, *In the Night Garden* from the BBC and *The WotWots* from Weta Workshop.   More programming announcements are expected from THE HUB in early August during the TCAs – a major press event for the Television Critics Association.

From a product standpoint, in addition to product already available in the market, we have a number of new product initiatives which will tie to our new programming on THE HUB. The majority of new product tied to programming is scheduled to launch in fall 2011. MY LITTLE PONY is undergoing a reinvention along with the new animation. A sneak peak of the new look will hit retail shelves this fall to coincide with THE HUB launch, with the whole new look for MY LITTLE PONY coming in 2011.

From an advertising perspective, Margaret and THE HUB's ad sales team have had many one-on-one meetings with potential advertisers. As a result, blue-chip advertisers are getting on board with THE HUB and its programming for kids and their families. They are enthusiastic about the mission of the network, and it provides them with an opportunity to reach a wide cross-section of viewers, including adults, moms, families and kids.

Prior to the launch of the network THE HUB will kick off a concentrated high impact marketing campaign. This campaign will have additional support in the late November/early December time period as well as in early 2011.

Turning to our movie pipeline, production is underway for TRANSFORMERS 3 which is scheduled for release on July 1, 2011. This year, TRANSFORMERS shipments are showing a more typical post-movie decline than the smaller decline we saw in 2008 when we had television to support the brand throughout the year. In 2011, we will have the support of both a major theatrical release and television behind the brand.

I started today's call reiterating that Hasbro's global teams are executing our long-term strategy -- a strategy built on a number of core elements designed to guide our business for years to come. Our brands – including Hasbro's core brands and our vast portfolio of active and vault brands - remain at the center of this strategy and guide the direction and decisions we are making globally in toys and games and immersive brand experiences.

We add to our efforts through alliances with marquee partners who are also re-imagining their brands, including:

- Marvel and its expansive universe of characters;
- Star Wars from Lucasfilm;
- And our newest partner Sesame Workshop.

Finally, we are working with the industry's best creative stewards at Paramount, Dreamworks, Universal, Sony, Discovery, THE HUB, Electronic Arts and Activision who are actively developing Hasbro brands into immersive experiences through movies, television and digital gaming.

Our global Hasbro teams are activating the elements of our strategy each and every day as we re-imagine, re-invent and re-ignite our brands today and for years to come.

I will now turn the call over to Deb.

Deb.

Deb Thomas, Hasbro CFO

Thank you, Brian and good morning.

The continued execution of our strategy and our attention to costs has enabled us to deliver improved profitability and maintain our strong balance sheet despite the revenue challenges in the quarter.

For the second quarter worldwide net revenues were $737.8 million compared to $792.2 million last year, a decline of 7%. Foreign exchange had a positive impact of $1.6 million to revenues in the quarter.

While revenue was down from last year as expected, operating profit of $79.7 million or 10.8% of revenue increased 9% or $6.6 million compared to $73.1 million or 9.2% of revenue last year.

Looking at our second quarter segment results:

U.S. and Canada segment net revenues were $444.5 million, a decrease of 9% compared to $490.9 million last year. The results reflect growth in the Games & Puzzles, Girls and Preschool categories, offset by a decline in the Boys category primarily due to lower TRANSFORMERS and G.I. JOE shipments.

U.S. and Canada operating profit for the quarter increased 4% to $58.7 million, or 13.2% of revenues, compared to $56.3 million or 11.5% of revenues last year. Operating profit increased despite lower revenue primarily due to lower royalty and amortization expense.

Net revenues in the International segment decreased 5% to $261.4 million compared to $276.2 million a year ago. Foreign exchange had a negative $800 thousand impact on revenue in the quarter. The results reflect growth in the Games & Puzzles and Preschool categories offset by declines in the Boys and Girls product categories.

The International segment reported an operating profit of $11.6 million compared to an operating profit of $16.5 million last year. The year-over-year decrease was primarily the result of lower revenues.

The Entertainment and Licensing segment net revenues increased 26% to $30.5 million compared to $24.2 million a year ago. This is primarily due to an increase in movie related revenues.

The Entertainment and Licensing segment operating profit increased to $13.0 million compared to $2.9 million last year reflecting higher revenue as well as the fact that the second quarter 2009 included $7.2 million in one-time advisory fees and deal costs associated with our investment in the joint venture television network. While we continue to have costs associated with our television initiatives, our current run rate of expenses is lower than last year’s one-time fees and costs.

Now let’s look at earnings:

For the quarter, we reported net earnings of $43.6 million or twenty nine cents per diluted share, compared to $39.3 million or twenty six cents per diluted share a year ago. The second quarter 2010 includes a negative five cent per share impact from our television related activities, while our second quarter 2009 included a negative six cent per diluted share impact.

Cost of sales in the quarter was $300.3 million, or 40.7% of revenues, versus $319.5 million or 40.3% of revenues in 2009.

During the past quarter there has been a great deal of discussion around input cost trends and I want to take a minute to discuss how these impact Hasbro.

Hasbro outsources between 80 and 85% of its manufacturing to vendors in China. We purchase this product in Hong Kong dollars, a currency which is pegged to the U.S. dollar. The costs we agree to with our vendors are based on the estimated market level of input costs, which includes commodities and labor, during the delivery stage of the product. As a general rule, once we agree on a cost with a vendor, we expect the cost to remain in place for the next 12 to 15 months.

As a result, the impact we experience from input cost increases and decreases would be primarily reflected in 2011 and beyond. For these products, we take into account the current cost environment as we design, engineer and price our product with an objective to maintain our desired level of profitability on the products sale. There have been instances when we have accepted higher prices from our vendors despite having agreements in place, but this is during periods of extraordinary inflationary pressure and is not our general practice. While costs had been rising in the first quarter, currently several input costs appear to have peaked and are now coming down in selected areas, including resins and paperboard.

Overall, operating margin increased to 10.8% from 9.2% last year. Operating profit improved despite lower revenue primarily due to lower royalties and amortization.

Royalties declined due to lower entertainment based revenue, including the decline in Transformers and G.I. Joe.

Amortization is down as the intangible assets associated with the Wizards of the Coast and Larami acquisitions have been fully amortized.

We continue to invest in our business including our television initiative, our emerging markets business as well as product development which has grown this year in support of major product initiatives planned for 2011.

Our investment in television programming is reflected in our balance sheet within other current assets. As we begin to generate revenue associated with our programs, programming costs will be expensed over the revenue curve of the program. No programming costs have been expensed on our P&L to date and we do not anticipate these costs to be significant in 2010.

Below the operating profit line:

Interest expense increased by $4.4 million to $21.9 million primarily due to the debt offering we completed in March 2010.

Other income, net, totaled $3.2 million compared to $1.3 million a year ago. Our 50% share of the joint venture results is included in this line on the P&L. This quarter, our share of the earnings in the joint venture, inclusive of amortization expense, was a loss of $76 thousand. In the second quarter 2009, our share of the earnings in the joint venture was a positive $1.0 million.

In the second quarter 2010, our underlying tax rate was 28.5% compared to 29.5% last year.

Now let's turn to the balance sheet:

At quarter end, cash totaled $872.3 million compared to $392.0 million a year ago. Over the past twelve months we have generated over $600 million in cash from operations. Our cash generation is healthy and we continue investing in our business. This includes approximately $19 million in television programming costs and a $25 million royalty advance to THE HUB. Our next $25 million royalty payment to the network is due in the fourth quarter 2010.

In March 2010, we raised $500 million through a debt offering. On March 29 we called our outstanding two and three quarter percent convertible debt. Prior to the end of the call period, substantially all the debentures were converted into 11.6 million shares.

In the second quarter we repurchased 6.7 million shares of common stock at a total cost of $271.4 million and an average price of $40.49 per share. In the first two quarters of 2010, we have repurchased 9.5 million shares of common stock at a total cost of $369.1 million and an average price of $38.99 per share. At the end of the second quarter, there was $417.5 million remaining in our current share repurchase authorization.

The quality of our receivables portfolio remains good and receivables at quarter end were $663.5 million up $10.9 million from $652.6 million last year. In the second quarter of 2010, we did not utilize our securitization facility; however, in the second quarter 2009 we securitized $85.1 million of receivables. As we mentioned previously, given the changing environment and government regulations impacting the securitization market, it’s likely we will not securitize receivables as actively in the future and we have not securitized receivables since the second quarter 2009.

Absent the impact of securitization in 2009, DSO’s decreased 3 days to 81 days due to the timing of sales and collections in the quarter compared with a year ago.

Inventories at $342.1 million in the quarter compared to $346.8 million a year ago.

In closing, there are a number of factors we are watching over the remainder of the year – namely foreign exchange, consumer spending and global economic conditions. In particular, foreign exchange rates continue to be very volatile and difficult to predict, and they do affect our reported revenues. Our largest currency impact is the Euro, followed by the British Pound, the Canadian Dollar, the Mexican Peso and the Australian Dollar.

What we are certain about is the breadth of our brand portfolio. Brian outlined a number of exciting initiatives launching in the coming months that will help drive our business for the rest of the year. In 2010 and beyond, the global Hasbro teams will remain committed to the execution of our strategy and the investment in our business for the long term.

We look forward to keeping you updated.