

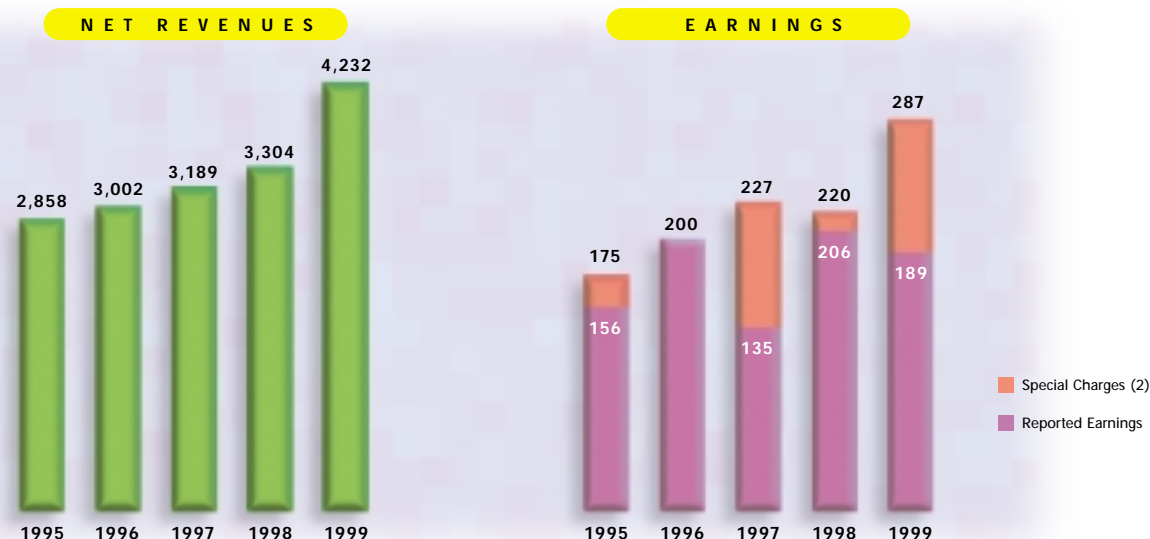


Hasbro



Financial Highlights

| (Thousands of Dollars and Shares Except Per Share Data) | 1999 | 1998 | 1997 | 1996 | 1995 |
|---------------------------------------------------------|-------------|-----------|-----------|-----------|-----------|
| FOR THE YEAR | | | | | |
| Net revenues | \$4,232,263 | 3,304,454 | 3,188,559 | 3,002,370 | 2,858,210 |
| Operating profit | \$ 327,569 | 324,882 | 235,108 | 332,267 | 273,572 |
| Earnings before income taxes | \$ 273,845 | 303,478 | 204,525 | 306,893 | 252,550 |
| Net earnings | \$ 188,953 | 206,365 | 134,986 | 199,912 | 155,571 |
| Cash provided by operating activities | \$ 391,512 | 126,587 | 543,841 | 279,993 | 227,400 |
| Cash utilized by investing activities | \$ 429,092 | 792,700 | 269,277 | 127,286 | 209,331 |
| Weighted average number of common shares outstanding | | | | | |
| Basic | 194,917 | 197,927 | 193,089 | 195,061 | 197,272 |
| Diluted | 202,103 | 205,420 | 206,353 | 209,283 | 210,075 |
| EBITDA (1) | \$ 669,125 | 514,081 | 541,692 | 470,532 | 434,580 |
| PER COMMON SHARE | | | | | |
| Net earnings | | | | | |
| Basic | \$.97 | 1.04 | .70 | 1.02 | .79 |
| Diluted | \$.93 | 1.00 | .68 | .98 | .77 |
| Cash dividends declared | \$.24 | .21 | .21 | .18 | .14 |
| Shareholders' equity | \$ 9.74 | 9.91 | 9.18 | 8.55 | 7.76 |
| AT YEAR END | | | | | |
| Shareholders' equity | \$1,878,975 | 1,944,795 | 1,838,117 | 1,652,046 | 1,525,612 |
| Total assets | \$4,463,348 | 3,793,845 | 2,899,717 | 2,701,509 | 2,616,388 |
| Long-term debt | \$ 420,654 | 407,180 | — | 149,382 | 149,991 |
| Debt to capitalization ratio | .38 | .29 | .06 | .14 | .15 |



(1) EBITDA (earnings before interest, taxes, depreciation and amortization) represents operating profit plus acquired in-process research and development, restructuring and discontinued development project charges and depreciation and all amortization. EBITDA is not adjusted for all noncash expenses or for working capital, capital expenditures or other investment requirements and, accordingly, is not necessarily indicative of amounts that may be available for discretionary uses. Thus, EBITDA should not be considered in isolation or as a substitute for net earnings or cash provided by operating activities, each prepared in accordance with generally accepted accounting principles, when measuring Hasbro's profitability or liquidity as more fully discussed in Management's Review.

(2) Amounts shown on charts are in millions of dollars. Special charges include consolidation program in 1999, acquired in-process research and development in 1998, restructuring in 1997 and discontinued development project in 1995.

Dear Fellow Shareowners

Hasbro had its best year ever in 1999. Overall, we delivered record financial results and we met or exceeded our most ambitious business objectives.

Today's Hasbro is stronger than ever. The heart of our business is making great games, toys, lifestyle, and entertainment products that are enjoyed by people of all ages. Hasbro enters the 21st Century with a balanced and deep portfolio — from our popular classic board games to products with the latest technologies and everything in between. Hasbro has what it takes to succeed. In fact, more than half of the 66 most notable toys and games of the last century, which were identified by a leading trade publication, are ours. We believe this **unmatched content**, combined with our emphasis on **technology, toys, and game play**, will contribute to delivering the outstanding results you expect from Hasbro. Simply put, we intend to be the number one company in the toy and game industry, the leading provider of play and fun the world over.

Before sharing with you the strategic road map to our continued success, here is a recap of some of our major 1999 achievements:

- Record revenues of \$4.2 billion, up 28% on the strength of our balanced and diversified portfolio.
- Record earnings per share, up 33% to \$1.42, prior to charges associated with the 1999 Consolidation Program and the 1998 write-off of acquired in-process research and development.
- Our strategic acquisition of Wizards of the Coast enables us to expand in the growing games arena.
- We announced a Consolidation Program to help better leverage our revenue growth opportunities.
- We unveiled our initial plans for Games.com, which we expect will become the best online games portal, building on our tremendous content.
- We formed the Hasbro Properties Group to maximize the value and profit potential of our vast intellectual properties in a wide range of consumer products and entertainment categories, including television, publishing, and live entertainment.
- Plus, we made many other moves to help secure an even brighter future for our shareowners in 2000 and beyond.

These outstanding results and strategic moves to secure our future were not reflected in our stock price performance. As we write this annual report, we believe that our shares are significantly undervalued. We believe in

our future, and are investing in it. We will continue to work hard to try to add value for our shareowners, and we are confident that we are on the right track. Our job is to help you share and understand our vision. First, let's celebrate our 1999 performance, followed by our winning formula for the future.

WINNING FINANCIAL RESULTS

Net revenues climbed to record levels in every quarter of 1999, and increased 28% for the year to a record \$4.2 billion. This reflected balanced growth in core brands and key licenses in the U.S. and internationally, led by STAR WARS, FURBY, hand-held electronic games, plus a wide range of new POKEMON toys and games. We are especially pleased with the outstanding performance of our international businesses during 1999, where revenues increased 24% in local currencies and 19% in U.S. dollars.

STAR WARS: EPISODE I: THE PHANTOM MENACE is the second highest-grossing motion picture of all time. Retail sales of Hasbro's STAR WARS toys and games were approximately \$500 million (in wholesale dollars), the largest annual sales of any Hasbro product line in our history. STAR WARS is a powerful global brand with proven long-term appeal, and we are working hard with our partners to ensure its continued success for years to come.

The continuing phenomenal success of FURBY — including the introduction of five foreign-language editions, FURBY limited collector editions, plus adorable interactive FURBY BABIES — underscores the powerful combination of creativity and technology embodied by our 1998 acquisition of Tiger Electronics.



Alan G. Hassenfeld (right),
Chairman and Chief Executive Officer
and Herbert M. Baum (left),
President and Chief Operating Officer



Hasbro Interactive revenues increased from \$192 million in 1998 to \$229 million in 1999, which fell below our expectations in the fourth quarter. This was partly the result of the late introduction of new product, as well as significant industry-wide softening of the video and PC CD-ROM business and significant price erosion. This resulted in a full-year loss of approximately \$53 million after-tax, excluding Consolidation Program charges. However, this growing business remains strong. For example, we had 23 games that sold more than 100,000 units at retail in the U.S. during 1999 — a notable accomplishment. With the streamlining steps we have taken — including exiting the high end flight simulation game business and the closure of two development studios — we are forecasting a much improved performance from Hasbro Interactive in 2000.

Net earnings for the year 1999 increased 30% to \$286.6 million compared to \$220.0 million in 1998, and earnings per share increased 33% to \$1.42 per share compared to \$1.07 per share in 1998. These results include a loss of \$0.01 per share attributable to initial spending for Games.com, and exclude \$141.6 million of pre-tax charges (\$97.7 million after-tax) associated with the Consolidation Program in December 1999 and a \$20.0 million one-time pre-tax charge (\$13.6 million after-tax) in 1998 to write off acquired in-process research and development of MicroProse. Reported net earnings in 1999 were \$189.0 million or \$0.93 per share, compared to \$206.4 million or \$1.00 per share in 1998.

Hasbro remains a cash powerhouse. Earnings Before Interest, Taxes, Depreciation and Amortization increased 30% to \$669.1 million, more than double our net earnings. We maintain tight control over working capital and our strong balance sheet continues to provide financial flexibility.

We continued working hard to add value for our shareowners on the financial front in other ways, too:

- We aggressively repurchased our stock during 1999, investing over \$237 million to buy back almost nine million shares. Through mid-February of 2000, we had invested \$478 million under the \$500 million repurchase program approved in December 1997. On February 25, we announced a Modified Dutch Auction tender offer for up to 17.25 million shares. This offer is scheduled to expire on March 27, 2000. While we cannot predict the results, we expect this tender offer to utilize part of the additional \$500 million repurchase authorization of December 1999, and we plan to resume open market repurchases in April.
- The dividend was increased 13% to an annual rate of \$0.24 per share, effective May 1999.
- In June, we moved to the New York Stock Exchange, to help make Hasbro more visible and accessible to global investors.

Tiger Electronics brings a wide range of fun, technology-based products to the mass market. In 2000, "focus" on the YAHOO! CAM digital camera and POO-CHI, a canine with advanced bio-rhythmic technology.



SHELBY (top left), a new friend of FURBY, lives in a shell, so if he is scared or sleeping, he clams up! Hasbro Interactive invented the recipe for success with its line of CD-ROM Playsets, including the EASY-BAKE KITCHEN. Interactive YODA has a vocabulary of more than 800 words and guides his "apprentice" in the proper use of a lightsaber.



POKEMON'S popular PIKACHU is beloved around the world. MR. POTATO HEAD continues to appeal to all generations.



- To sharpen our focus on the bottom line, we realigned our organization into key business segments with profit and loss responsibility. In addition, we imposed a two-year freeze on senior management base compensation while increasing incentive pay based on performance.
- Under the Consolidation Program announced in December of 1999, we further realigned our business to support our greater commitment to game play and technology. For example, we announced the closure of two manufacturing facilities, streamlined aspects of our U.S. Toy business and are further consolidating European sales and marketing activities where the regional management structure we implemented in 1998 has proven very successful. Hasbro must be a low-cost operator to win and continue to grow profitably.

WINNING WITH CONTENT AND TECHNOLOGY

Hasbro has the winning formula. Our unmatched content and emphasis on technology will unlock new and exciting possibilities for everyone who enjoys play.

Technological advances are lowering the price points on smart toys to levels unimaginable even a few years ago. Today, toys and games deliver the power of play in so many different and engaging ways.

Plus, as kids "get older younger" and adults "stay younger older," Hasbro will win by shaping its powerful and versatile content beyond traditional toys and games into additional forms of leisure time play and entertainment.

WINNING WITH GAME PLAY AND TECHNOLOGY

Games are one of Hasbro's strongest core competencies. In recent years, we have been building and leveraging our games content on a variety of platforms, from core board games to hand-held electronic games, interactive games, trading card games and online games. Our worldwide games business represented over 50% of Hasbro's revenues in 1999, up from 37% just two years ago, and we expect continued growth.

We continue to enjoy success in the traditional board game category, thanks to great content and marketing initiatives such as our FAMILY GAME NIGHT and FIRST GAMES promotional programs. In fact, retail takeaway of our most popular classic board games was up over 6% in the U.S. in 1999.

Hand-held electronics are also growing, with best selling games including the BOP IT franchise we created. Add to that some incredible offerings from our highly innovative Tiger Electronics, a leader in youth electronics for the mass market. Tiger highlights for 2000 include SHELBY, a new friend of FURBY, who has a vocabulary of 80 words in a mixture of

Hasbro has a "game plan" for every member of the family. Our unmatched games content – combined with the latest technology – allows us to continually enhance the entertainment experience. From board games to online games and everything in between, Hasbro has what it takes to keep on winning!



FURBISH, English and his own special language...SHELBISH! Tiger has also teamed up with Yahoo! to manufacture and market a wide variety of Yahoo! branded electronic products, including the YAHOO! CAM, a palm-sized digital camera, and the YAHOO! HITCLIPS DOWNLOADER which records music and audio clips from the Internet.

Hasbro Interactive provides one more example of how technology has allowed us to unlock our games content into new forms of exciting entertainment. As an example, we had the number one U.S. interactive title in 1999 when measured by units sold — ROLLERCOASTER TYCOON. We see it as a long-term, extendable brand, and thanks to Hasbro's intellectual property portfolio, we are already making things happen. This year...MONOPOLY TYCOON.

We are now leaders in the fast-growing trading card game genre thanks to our acquisition of Wizards of the Coast and their incredibly popular POKÉMON trading card game. Yet they bring us so much more, including game centers and great content such as MAGIC: THE GATHERING, which is played by more than six million people worldwide. Wizards of the Coast has retained its hobby roots while simultaneously extending the reach and popularity of trading card games to the mass market.

Our recently-announced Games.com initiative — which we believe will be the ultimate online game experience when it launches in mid-2000 — unites Hasbro's content with our emphasis on game play and technology in an exciting new platform. Over time, Games.com will highlight Hasbro's powerful game content in six different channels: Family, Kids, Arcade, Game Shows, Sports, and Avid Gamer.

ACTION MAN (right), the number one boys action brand in Europe, lifts off in the U.S. later this year. With millions of players worldwide and growing, the MAGIC: THE GATHERING trading card game will add a number of new and innovative expansions in 2000.



The successful BEAST MACHINES television series on Fox Kids Network demonstrates how the Hasbro Properties Group is able to "transform" Hasbro content into family entertainment beyond traditional toys and games.

WINNING WITH TOYS AND TECHNOLOGY

Our goal is to be the world's leading toy developer and marketer. We will succeed by continually innovating, creating, and unlocking the value of our classic toy brands as well as creating new brands for all to enjoy.

Our toy chest currently includes classic brands such as MR. POTATO HEAD, G.I. JOE, ACTION MAN, EASY-BAKE OVEN, PLAY-DOH, PLAYSKOOL, LITE BRITE, TINKERTOY, NERF, and TONKA, to name only a few.

Hasbro's emphasis on toys that deliver great play, and our ability to enhance the "fun factor" of our content through technology, were clearly evident at Toy Fair. Highlights include TUCKER MY TALKIN' TRUCKBOT, an interactive, electronic robo-truck from Tonka; eSPECIALLY MY BARNEY, the only plush toy that parents can personalize, customize and update by downloading information from a specially created website (www.mybarney.com); and POKÉMON THINK CHIP FIGURES, "smart" action figures that allow kids to engage in electronic POKÉMON battles and then store the experience for future game encounters.

WINNING WITH THE HASBRO PROPERTIES GROUP (HPG)

HPG was formed in May of 1999 to profitably exploit Hasbro's new, classic and acquired content across a wide range of entertainment categories. By expanding the breadth of our content library, we are uncovering new opportunities outside of Hasbro's core toy and game businesses through our successful consumer products arm, 3-D Licensing. Our success in television programming is another example of HPG at work. This process starts with our in-house "fantasy factory," a talented group of producers and artists who develop the underlying fantasy of each Hasbro property. Then, the Visual Media Group, with offices in London and Los Angeles, prepares creative presentations for television, motion picture and video partners. The placement of the highly anticipated ACTION MAN programming, which will debut on the Fox Kids Network this fall, is a shining example of what HPG can accomplish by leveraging Hasbro's brand portfolio.

In closing, it is CONTENT that distinguishes Hasbro from the rest.

Today, more than ever, we are acting aggressively to leverage this unmatched content — through technology, continued success with classic toys and games, online game play, television programming, licensing, publishing, and other avenues.

Remember the friends who seemed to have all the best toys and games? You always wanted to go to their house and play, because your toy chest seemed empty in comparison. Hasbro has not only the biggest and best toy chest, we also have the content, strength, and balance to win today and in the future.

At Hasbro **We Play to Win**, and we want all of our shareowners to win, too.

Alan G. Hassenfeld
Chairman and Chief Executive Officer

Herbert M. Baum
President and Chief Operating Officer



Hasbro's winning combination: great content plus new technology equals innovative products like TONKA'S TUCKER MY TALKIN' TRUCKBOT and eSPECIALLY MY BARNEY.



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**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Summary

A percentage analysis of results of operations follows:

| | 1999 | 1998 | 1997 |
|--------------------------------------------------------------------------|--------|--------|--------|
| Net revenues | 100.0% | 100.0% | 100.0% |
| Cost of sales | 40.1 | 41.3 | 42.6 |
| Gross profit | 59.9 | 58.7 | 57.4 |
| Amortization | 4.1 | 2.2 | 1.7 |
| Royalties, research and development | 16.8 | 12.9 | 12.1 |
| Advertising | 10.8 | 13.3 | 12.9 |
| Selling, distribution and administration | 19.0 | 19.8 | 19.4 |
| Restructuring charge and acquired in-process research and development | 1.5 | .6 | 3.9 |
| Interest expense | 1.6 | 1.1 | .9 |
| Other (income) expense, net | (.4) | (.4) | .1 |
| Earnings before income taxes | 6.5 | 9.2 | 6.4 |
| Income taxes | 2.0 | 2.9 | 2.2 |
| Net earnings | 4.5% | 6.3% | 4.2% |

(Thousands of Dollars Except Share Data)

Results of Operations

Net earnings for the year ended December 26, 1999 were \$188,953 compared to \$206,365 and \$134,986 in 1998 and 1997, respectively. Diluted earnings per share was \$.93 in 1999, \$1.00 in 1998 and \$.68 in 1997. During 1999, the Company reorganized its business into segments. Net revenues and operating profits, excluding charges relating to the 1999 consolidation program, of the U.S. Toys, Games and International segments increased in 1999 over comparable 1998 levels. The operating loss in Operations, which is not intended to be a profit center, and the operating profit in the Company's Other segments decreased, all largely due to the reasons discussed below. The overall increase in operating profit of the Games segment was partially offset by the unfavorable impact of increased costs incurred to expand the Company's offering of interactive software games. Part of this increased cost resulted from escalating research and development costs, coupled with the unanticipated shortfall in fourth quarter revenues attributable to the late introduction of new product as well as a significant industry-wide softening of the video and personal computer CD-ROM business in the fourth quarter and price erosion. On an after-tax basis, excluding charges attributable to the 1999 consolidation program, this resulted in an approximate \$53 million dollar loss from interactive software games.

Net revenues for 1999 were \$4,232,263 compared to \$3,304,454 and \$3,188,559 for 1998 and 1997, respectively. This approximate 28% increase in revenues over 1998 levels was net of an approximate \$62,000 unfavorable impact of foreign currency translation rates. The Games segment led revenue growth during the year, accounting for approximately 71% of the increase, followed by U.S. Toys and International, contributing 18% and 13% of revenue growth, respectively. Increased Games segment revenue was primarily driven by FURBY, which accounted for 24% of segment revenue in 1999 compared to 7% in 1998. Revenues from Wizards of the Coast, Inc. (Wizards), acquired in the fourth quarter of 1999, accounted for 14% of Games segment revenues. Increased activity in hand-held electronic games utilizing Company and licensed brands, interactive CD-ROM games and traditional board games such as MONOPOLY and TRIVIAL PURSUIT also contributed to Games segment growth. U.S. Toy segment revenues were boosted by sales of STAR WARS product associated with the theatrical release of STAR WARS: EPISODE 1: THE PHANTOM MENACE. Revenues from this line accounted for 36% of segment revenues in 1999 compared to 13% in 1998. This, as well as the popular POKÉMON line, traditional toy offerings such as EASY BAKE and LITE BRITE and the full year inclusion of the MICRO MACHINES line acquired with Galoob Toys, Inc. (Galoob) in the fourth quarter of 1998, also contributed to revenue growth over 1998 by the U.S. Toy segment. The International segment contribution to revenue growth was primarily driven by sales of STAR WARS, POKÉMON, TELETUBBIES and FURBY and hand-held electronic products in certain markets, all partly offset by decreased volume in traditional board games and puzzles as well as the negative impact of foreign currency translation. The results of Other segments negatively affected revenue by approximately 3%, primarily due to decreased revenues of KOOSH and candy product.

The Company's gross profit margin increased to 59.9% from 58.7% in 1998, and 57.4% in 1997. The increase in margin from 1998 principally reflects the increased revenues in the Games segment, where many product lines carry a higher gross margin. The improvement in 1998 from 1997 is attributable to a lower cost structure resulting from the removal of excess capacity, the increased level of sales of interactive products, which have a higher gross margin, and overall favorable material prices. The improvement in the 1998 gross margin was moderated by the unanticipated shortfall in business with Toys 'R Us which resulted in lower than anticipated factory utilization.

Amortization expense of \$173,533 includes amortization of both property rights and cost in excess of net assets acquired. This compares with \$72,208 in 1998 and \$53,767 in 1997. During 1999, impairment charges of \$38,449, or 22% of amortization expense, were recognized, arising from the decision to discontinue or significantly reduce product line offerings as part of our 1999 consolidation program. The remaining increases in all years were attributable to the acquisitions made during the period.

Expenditures for royalties, research and development increased to \$711,790 from \$424,673 in 1998 and \$386,912 in 1997. Included in these amounts are expenditures for research and development of \$254,599 in 1999, \$184,962 in 1998 and \$154,710 in 1997. As percentages of net revenues, research and development was 6.0% in 1999, up from 5.6% in 1998 and 4.9% in 1997. Contractual development commitments recognized for discontinued product lines in connection with the 1999 consolidation program amounted to \$10,992. The remaining 1999 and the 1998 increases reflect the expenditures of the Company's 1998 acquisitions as well as the continuing investment to grow the Company's offering of interactive game titles. Revenues derived from entertainment based properties, such as STAR WARS and POKÉMON, and resultant royalties, while continuous over the life of a contract, are generally higher in amount in the year a theatrical release takes place. It is anticipated that operating profit will also generally be higher in these years. The degree to which revenues, royalties and operating profits fluctuate is dependent not only on theatrical release dates, but video release dates as well. Royalty expense increased in dollars and as a percent of net revenues from 1998. Royalty commitments on discontinued product lines recognized in connection with the 1999 consolidation program amounted to \$15,300. The remaining increase reflects the increased percentage of 1999 revenues obtained from licensed product carrying higher royalty rates, primarily STAR WARS. While royalties increased in dollars during 1998, they remained constant as a percentage of net revenues.

On December 15, 1999, the Company announced plans to launch Games.com in mid-2000. Games.com will be the Games segment's online internet portal, allowing users to play Company branded games, have online chats with fellow gamers, compete in tournaments and purchase games and related product from an online store. The Company has entered into a non-binding memorandum of understanding for a three-year licensing and distribution agreement with Go2Net, Inc. providing technology, engineering and software management support for this site. Revenue sources are expected to come from advertising, online game and related product sales and premium subscription services. The Company expects to spend approximately \$60 million during 2000 to develop and launch this site.

Advertising expense decreased to 10.8% of net revenues from the 1998 level of 13.3%, which compared to 12.9% in 1997. The decrease in 1999 primarily reflects the mix of more entertainment based properties, such as STAR WARS and POKÉMON, marketed throughout our segments, which tend to carry a lower advertising to revenue ratio. Increased revenues in our Games segment from the popular FURBY and trading card games also contributed to the decrease from 1998, as these lines do not carry as great of an advertising spend ratio as other products. The increase in 1998 from 1997 reflects the mix of more non-entertainment based product in 1998 and the absence of support from a major motion picture release.

During 1999, selling, distribution and administration costs increased in dollars but decreased as a percentage of net revenues to \$799,919, or 19.0% of revenues, from \$655,938, or 19.9% in 1998 and \$617,140, or 19.4%, in 1997. Of the increase in dollars, approximately 25% of the increase reflects the Games segment's 1999 acquisition of Wizards and approximately 31% of the increase reflects higher performance based bonus accruals. The remainder of the increase in dollars primarily reflects costs associated with the higher level of activity in 1999. The decreased percentage reflects higher 1999 revenues as well as the Company's commitment to control these costs, and the benefit received from the 1997 global integration and profit enhancement program. In addition to normal inflationary trends, the 1998 increase over 1997 reflects the impact of the Company's acquisitions and new operations in those years. Also adversely affecting the 1998 rate was the unanticipated reduction in revenues resulting from the changes in inventory management policies at Toys 'R Us.

On December 7, 1999, the Company announced a program to further consolidate manufacturing and sourcing activities and product lines, as well as streamline and further regionalize marketing, sales and research and development activities worldwide. Costs associated with this consolidation program amounted to \$141,575, and were recorded in the fourth quarter as follows:

| | |
|-------------------------------------|------------------|
| Restructuring charge | <u>\$ 64,232</u> |
| Other operating expenses: | |
| Cost of sales | 8,740 |
| Amortization | 38,449 |
| Royalties, research and development | 26,292 |
| Advertising | <u>3,862</u> |
| | <u>77,343</u> |
| Total consolidation program costs | <u>\$141,575</u> |

The significant components of the restructuring charge were the planned closing of two factories, in Mexico and the United Kingdom, the reduction of capacity at the remaining three factories, the shift of production to third party manufacturers in the Far East and further consolidation and regionalization of the International marketing and sales structure. The plan anticipates the redundancy of approximately 2,200 employees, including 1,800 in manufacturing and sourcing activities and 400 worldwide in research and product development, marketing, sales and administration. The restructuring charge of \$64,232 represents approximately \$38,700 of cash charges for severance benefits which will be disbursed over the employee's entitlement period, \$14,300 of cash charges for lease and facility closing costs to be expended over the contractual lease term and closing process, and non-cash charges of \$11,200 for fixed asset write-offs, arising primarily in the manufacturing area. Of the cash amount, approximately \$4,700 has been paid for severance benefits relating to 193 employees terminated as of December 26, 1999. Non-cash charges relating to fixed asset write-offs have been credited to the respective line items in the balance sheet. The remaining amount of approximately \$48,000 is included in accrued liabilities. The restructuring plan is expected to be completed in fiscal 2000. The Company expects to generate pre-tax savings of approximately \$16,000 in 2000 and \$23,000 per year thereafter from these actions.

The components of the consolidation program included in other operating expenses represent costs associated with exiting certain product lines and reevaluating other product lines which resulted in reduced expectations. The product lines being exited were not, either individually or in the aggregate, material to the Company's revenues or operating results. Approximately \$12,000 represents cash charges that will be incurred on contractual royalty, product development and advertising commitments associated with the discontinued product lines. Non-cash charges of approximately \$65,000 relate to asset write-offs and write-downs of underutilized assets. This includes impairment of intangible assets arising from the decision to discontinue or significantly reduce product line offerings. The resulting sum of undiscounted future cash flows of these assets was not sufficient to cover the carrying amount of the assets, and as such, they were written down to their fair market value. Items relating to property rights and licenses, goodwill, inventory, prepaid and other current assets have been credited to the respective asset in the balance sheet.

During the third quarter of 1998, the Company incurred a one-time charge to write off the \$20,000 appraised value of acquired in-process research and development of MicroProse, Inc. (MicroProse), which was acquired for a total purchase price of approximately \$70,000 on September 14, 1998.

Late in the fourth quarter of 1997, the Company announced a global integration and profit enhancement program which included the redundancy of approximately 2,500 employees, principally in manufacturing, and provided for actions in three principal areas: a continued consolidation of the Company's manufacturing operations; the streamlining of marketing and sales, while exiting from certain underperforming markets and product lines; and the further leveraging of overheads. Of the \$140,000 estimated costs related to these actions, \$125,000 was reported as a restructuring charge and \$15,000 was reflected in cost of sales. Of the restructuring amount, approximately \$54,000 related to severance and people costs, \$52,000 to property, plant and equipment and leases and \$19,000 to product line related costs. During 1998, the employment of all employees planned for redundancy was terminated. The program has been completed. The Company had initially estimated its pretax cost savings from this initiative to be \$40,000 in 1998 and \$70,000 per year thereafter. Because of the unanticipated shortfall in sales to Toys 'R Us during 1998 and changes in product mix, factory utilization rates were not as high as initially anticipated, which resulted in below target savings during 1998. The Company estimated pretax savings of approximately \$30,000 during 1998. During 1999, the Company estimates that it has realized planned pretax savings of approximately \$70,000. The positive cash flow impact from this program has and will occur largely in the form of reduced outflows for payment of costs associated with the manufacture and sourcing of products.

Interest expense was \$69,340 in 1999 compared to \$36,111 during 1998 and \$27,486 during 1997. The increase during the current year largely reflects the costs associated with funding the Company's 1998 acquisitions, the 1999 acquisition of Wizards and the Company's stock repurchase program, all partially offset by the availability of funds generated during 1999 and 1998. Due to additional debt incurred during 1999, interest expense in 2000 is expected to increase.

Other income of \$15,616 in 1999 compares with \$14,707 in 1998 and expense of \$3,097 in 1997. While 1999 and 1998 were essentially flat, the change between 1998 and 1997 primarily reflects the larger benefits to Hasbro from its consolidated and unconsolidated operations in which it either is, or has, a minority partner, increased interest income and a decrease in foreign currency transactional losses.

Income tax expense as a percentage of pretax earnings in 1999 decreased to 31.0% from 32.0% and 34.0% in 1998 and 1997, respectively. The decrease in all periods reflects the downward trend of the tax on international earnings due to the reorganization of the Company's global business.

Liquidity and Capital Resources

The Company continued to have a strong and liquid balance sheet with cash and cash equivalents of \$280,159 at December 26, 1999. Cash and cash equivalents were \$177,748 and \$361,785 at December 27, 1998 and December 28, 1997, respectively.

Hasbro generated approximately \$392,000 of net cash from its operating activities in 1999, compared with approximately \$127,000 in 1998 and \$544,000 in 1997. The significant change between the 1999 and 1998 amounts results from a combination of factors. Included in the 1999 amount was \$38,361 utilized by changes in operating assets and liabilities, compared with \$267,231 utilized in 1998 and \$273,344 provided in 1997. Full year accounts receivable for 1999 increased at a rate significantly below that of the increase in fourth quarter revenues. Reflecting the acquisition of Wizards made during the fourth quarter and growth in inventory levels in the International segment for 2000 product introduction, inventories increased over prior year levels. Prepaid and other current assets also increased from the prior year, in part due to the acquisition of Wizards and the increased spending on product development. Reflecting amounts due for the Wizards acquisition, the remaining unpaid amounts from the 1999 consolidation program and increased bonus accruals in high performing segments, accounts payable and accrued liabilities increased by 35% over prior year levels. Royalty advances made in connection with the STAR WARS license that apply to future years have been included in long-term assets.

During 1998, \$267,231 was utilized by changes in operating assets and liabilities. With the \$170,723 increase in fourth quarter revenues from the comparable period of 1997, most of which, under Hasbro's normal trading terms, became due after the end of the Company's fiscal year, accounts receivable increased. Inventories also increased, in part reflecting acquisitions made during the year, as did prepaid expenses and other current assets, largely reflecting higher advance royalty payments. Partially offsetting these utilizations of funds was a small increase in accounts payable and other accrued liabilities. During 1997, \$273,344 was provided by changes in operating assets and liabilities. Contributing to this were reductions in accounts receivable, inventories and prepaid expenses and other current assets and an increase in trade payables and accrued liabilities, reflecting the unpaid portion of the costs associated with the Company's global integration and profit enhancement program.

Cash flows from investing activities were a net utilization of \$429,092, \$792,700 and \$269,277 in 1999, 1998 and 1997, respectively. During 1999, the Company expended approximately \$107,000 on additions to its property, plant and equipment while during 1998 and 1997 it expended approximately \$142,000 and \$100,000, respectively. Of these amounts, 53% in 1999, 38% in 1998 and 51% in 1997 were for purchases of tools, dies and molds related to the Company's products. The 1998 additions also include the expenditures associated with the consolidation of its Spanish manufacturing and marketing operations into one facility. During the three years, depreciation and amortization of plant and equipment was \$103,791, \$96,991 and \$112,817, respectively.

On September 30, 1999, the Company acquired the outstanding shares of Wizards, for an initial purchase price of \$325,000, subject to additional payments based upon the closing balance sheet and future payments contingent upon achieving certain operating objectives. The total acquisition cost to date amounts to \$412,769. The Company also made other smaller acquisitions and investments, none of which were significant. Hasbro made three major acquisitions during 1998, having an aggregate purchase price of \$669,737. On April 1, 1998, it acquired substantially all of the business and operating assets of Tiger Electronics, Inc. and certain affiliates. On September 14, 1998, it acquired the outstanding shares of MicroProse through a cash tender offer of \$6.00 for each outstanding share of MicroProse. On October 30, 1998, it acquired the outstanding shares of Galoob through a cash tender offer of \$12.00 for each outstanding share of Galoob. During 1997, Hasbro acquired certain assets of OddzOn Products, Inc. and Cap Toys, Inc., wholly owned subsidiaries of Russ Berrie and Company, Inc., for \$167,379.

As part of the traditional marketing strategies of the toy industry, many sales made early in the year are not due for payment until the fourth quarter or early in the first quarter of the subsequent year, thus making it necessary for the Company to borrow significant amounts pending these collections. During the year, the Company borrowed through the issuance of commercial paper and short-term lines of credit to fund its seasonal working capital requirements in excess of funds available from operations and the issuance of long-term debt. During 2000, the Company expects to fund these needs in a similar manner and believes that the funds available to it are adequate to meet its needs. At March 5, 2000, the Company's unused committed and uncommitted lines of credit, including revolving credit agreements for \$350,000 (long-term) and \$350,000 (short-term), were in excess of \$1,300,000.

During 1999, net financing activities provided approximately \$145,000 of funds to the Company, primarily through the use of short-term borrowings. Net financing activities during 1998 provided approximately \$490,000, principally through the issuance of \$100,000 of 5.60% notes due November 1, 2005, \$150,000 of 6.15% notes due July 15, 2008 and \$150,000 of 6.60% debentures due July 15, 2028. In 1997, net financing activities utilized approximately \$125,000 of Hasbro's funds. During 1999, the Company also invested approximately \$240,000 to repurchase its common stock in the open market. This compares with approximately \$180,000 and \$135,000 repurchased in the open market in 1998 and 1997, respectively.

During October 1997, the Company called its 6% Convertible Subordinated Notes Due 1998 for redemption. Substantially all of these notes were converted into approximately 11.4 million shares of Hasbro common stock.

On December 9, 1997, the Board of Directors (the Board) canceled all prior share repurchase authorizations and authorized the purchase of up to an additional \$500,000 of the Company's common stock. At December 26, 1999, \$72,008 remained under this authorization. In addition to the remaining amount under this repurchase authorization, on December 6, 1999 the Board authorized an additional common share repurchase program up to \$500,000. The Company anticipates that it will continue to repurchase its shares in the future, when it deems conditions to be favorable (see discussion of the Dutch Auction Tender Offer below), and will fund such purchases from working capital or available lines of credit. The shares acquired under these programs are being used for corporate purposes including issuance upon the exercise of stock options and warrants.

Financial Risk Management

The Company is exposed to market risks attributable to fluctuations in foreign currency exchange rates primarily as a result of sourcing products in four currencies while marketing those products in more than thirty currencies. Results of operations will be affected primarily by changes in the value of the U.S. dollar, Hong Kong dollar, British pound, Euro and Mexican peso versus other currencies, principally in Europe and the United States.

To manage this exposure, as of December 26, 1999, Hasbro has hedged a portion of its estimated fiscal 2000 foreign currency transactions using a combination of forward foreign exchange contracts and purchased foreign currency options. The Company estimates that a hypothetical immediate 10% unfavorable movement in the currencies involved could result in an approximate \$4.7 million decrease in the fair value of these instruments. The Company is also exposed to foreign currency risk with respect to its net cash and cash equivalents or short-term borrowing positions in other than the U.S. dollar. Hasbro believes, however, that the risk on this net exposure would not be material to its financial condition. In addition, the Company's revenues and costs have been and will likely continue to be affected by changes in foreign currency rates. The Company does not speculate in and other than set forth above, the Company does not hedge foreign currencies.

At December 26, 1999, the Company had fixed rate long-term debt of \$420,654. Interest rate changes affect the fair value of this fixed rate debt but do not impact earnings or cash flows. The Company estimates that a hypothetical one percentage point decrease or increase in interest rates would increase or decrease the fair value of this debt by approximately \$27,000 or \$24,000, respectively.

The Economy and Inflation

The Company continued to experience difficult economic environments in some parts of the world during 1999. The principal market for the Company's products is the retail sector where certain customers have experienced economic difficulty. The Company closely monitors the creditworthiness of its customers and adjusts credit policies and limits as it deems appropriate.

The effect of inflation on the Company's operations during 1999 was not significant and the Company will continue its policy of monitoring costs and adjusting prices accordingly.

Year 2000

During 1999, the Company concluded its efforts to address the Year 2000 issue. A planned global 'enterprise' system became operational at many of the Company's major units replacing a number of older non-compliant systems and modifications or replacements were made of other non-compliant systems. Readiness reviews were completed on customers, vendors and service providers. Contingency plans were expanded to include potential Year 2000 related failures. Excluding costs related to the enterprise system, the Company's out of pocket costs associated with becoming Year 2000 compliant were approximately \$2,500. These costs were expensed as incurred, and the Company does not anticipate any additional material expenditure as a result of Year 2000 issues.

Based on operations since January 1, 2000, including the leap year date of February 29, 2000, the Company has not experienced any significant disruption or change, and does not expect any significant impact to its ongoing business as a result of the Year 2000 issue. Additionally, the Company is not aware of any significant Year 2000 issues or problems that have arisen for its significant customers, vendors or service providers. As there can be no assurance that the Company's efforts to achieve Year 2000 readiness have been completely successful or that customers, vendors and service providers will not experience Year 2000 related failures in the future, the Company will continue to monitor its exposure to Year 2000 issues and will leave its contingency plans in place in the event that any significant Year 2000 related issues arise.

Euro Conversion

Certain member countries of the European Union established fixed conversion rates between their existing currencies and the European Economic Monetary Union common currency, or Euro. While the Euro was introduced on January 1, 1999, member countries will continue to use their existing currencies through January 1, 2002, with the transition period for full conversion to the Euro ending June 30, 2002. Transition to the Euro creates certain issues for the Company with respect to upgrading information technology systems for 2002 full use requirements, reassessing currency risk, product pricing, amending business and financial contracts as well as processing tax and accounting records. The Company has and will continue to address these transition issues and does not expect the Euro to have a material effect on the results of operations or financial condition of the Company.

Forward-Looking Statements

This discussion contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These statements may be identified by the use of forward-looking words or phrases such as “anticipate,” “believe,” “expect,” “intend,” “may,” “planned,” “potential,” “should,” “will,” and “would.” These forward-looking statements are inherently subject to known and unknown risks and uncertainties. A variety of factors could cause actual results and experience to differ materially from the anticipated results or other expectations expressed in the forward-looking statements. These factors include, but are not limited to market conditions, third party actions or approvals and the impact of competition that could delay or increase the cost of implementation of our consolidation program or alter our actions and reduce actual results, and with respect to our on-line gaming site initiative, technical difficulties in adapting games to on-line format and establishing the on-line game site that could delay or increase the cost of the site becoming operational; the acceptance by customers of the games and other products and services to be offered at our on-line game site; and competition from other on-line game sites and other game playing formats as well as competition from other internet companies in recruiting and retaining talented employees. We undertake no obligation to revise the forward-looking statements contained in this discussion or to update the forward-looking statements to reflect events or circumstances occurring after the date of this discussion.

Other Information

The Company’s revenue pattern continues to show the second half of the year more significant to its overall business and within that half, the fourth quarter most prominent. The first half of 1999 represented a greater proportion of full year revenues than the first half of 1998, principally because of the May 19, 1999 theatrical release of STAR WARS: EPISODE 1: THE PHANTOM MENACE. The trend of retailers over the past few years has been to make a higher percentage of their purchases within or close to the fourth quarter holiday consumer selling season, which includes Christmas.

The Company is not aware of any material amounts of potential exposure relating to environmental matters and does not believe its compliance costs or liabilities to be material to its operating results or financial position.

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133). SFAS 133 was amended during 1999, requiring the Company to adopt SFAS 133 effective January 1, 2001. SFAS 133 will require that the Company record all derivatives, such as foreign exchange contracts, in the balance sheet at fair value. Changes in derivative fair values will either be recognized in earnings as an offset to the changes in the fair value of the related hedged assets, liabilities and firm commitments or, for forecasted transactions, deferred and recorded as a component of other shareholders’ equity until the hedged transactions occur and are recognized in earnings. The ineffective portion of a hedging derivative’s change in fair value will be immediately recognized in earnings. The impact of SFAS 133 on the Company’s financial statements will depend on several factors, including interpretive guidance issued from the FASB, the extent of the Company’s hedging activities and use of equity and other financial derivatives, the Company’s ability to forecast foreign currency transactions compared to actual results and the effectiveness of the hedging instruments used. However, the Company does not believe adoption of SFAS 133 will have a material impact on either the Company’s financial condition or its results of operations.

On February 25, 2000, the Company announced plans to repurchase up to 17.25 million shares of its common stock at a purchase price between \$15.25 and \$17.50 per share through a Modified Dutch Auction Tender Offer, commencing February 29 and expiring on March 27, 2000, unless extended by the Company. The Modified Dutch Auction tender procedure allows shareholders to select the price within the specified range at which each shareholder is willing to sell all or a portion of his or her shares to the Company. This repurchase will complete the repurchase authorization of 1997 and utilize part of the additional \$500 million share repurchase authorization of December 1999.

On March 15, 2000 the Company issued \$750 million of debt securities in the form of \$550 million of notes at 7.95% due March 15, 2003 and \$200 million notes at 8.50% due March 15, 2006. The Company intends to use the proceeds of these notes to pay down short term debt primarily incurred in connection with the acquisition of Wizards and the repurchase of shares of its common stock, including repurchases of shares under the Modified Dutch Auction Tender Offer.

CONSOLIDATED STATEMENTS OF EARNINGS

| Fiscal Years Ended in December (Thousands of Dollars Except Share Data) | 1999 | 1998 | 1997 |
|-------------------------------------------------------------------------|--------------------|-----------|-----------|
| Net revenues | \$4,232,263 | 3,304,454 | 3,188,559 |
| Cost of sales | 1,698,242 | 1,366,061 | 1,359,058 |
| Gross profit | 2,534,021 | 1,938,393 | 1,829,501 |
| Expenses | | | |
| Amortization | 173,533 | 72,208 | 53,767 |
| Royalties, research and development | 711,790 | 424,673 | 386,912 |
| Advertising | 456,978 | 440,692 | 411,574 |
| Selling, distribution and administration | 799,919 | 655,938 | 617,140 |
| Restructuring charge | 64,232 | — | 125,000 |
| Acquired in-process research and development | — | 20,000 | — |
| Total expenses | 2,206,452 | 1,613,511 | 1,594,393 |
| Operating profit | 327,569 | 324,882 | 235,108 |
| Nonoperating (income) expense | | | |
| Interest expense | 69,340 | 36,111 | 27,486 |
| Other (income) expense, net | (15,616) | (14,707) | 3,097 |
| Total nonoperating expense | 53,724 | 21,404 | 30,583 |
| Earnings before income taxes | 273,845 | 303,478 | 204,525 |
| Income taxes | 84,892 | 97,113 | 69,539 |
| Net earnings | \$ 188,953 | 206,365 | 134,986 |
| Per common share | | | |
| Net earnings | | | |
| Basic | \$.97 | 1.04 | .70 |
| Diluted | \$.93 | 1.00 | .68 |
| Cash dividends declared | \$.24 | .21 | .21 |

See accompanying notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

| December 26, 1999 and December 27, 1998 (Thousands of Dollars Except Share Data) | 1999 | 1998 |
|-------------------------------------------------------------------------------------------------------------------------------------|--------------------|------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 280,159 | 177,748 |
| Accounts receivable, less allowance for doubtful accounts of \$65,000 in 1999 and \$64,400 in 1998 | 1,084,118 | 958,826 |
| Inventories | 408,571 | 334,801 |
| Prepaid expenses and other current assets | 358,804 | 318,611 |
| Total current assets | 2,131,652 | 1,789,986 |
| Property, plant and equipment, net | 318,825 | 330,355 |
| Other assets | | |
| Cost in excess of acquired net assets, less accumulated amortization of \$193,947 in 1999 and \$152,008 in 1998 | 806,092 | 704,282 |
| Other intangibles, less accumulated amortization of \$300,632 in 1999 and \$192,268 in 1998 | 949,789 | 837,899 |
| Other | 256,990 | 131,323 |
| Total other assets | 2,012,871 | 1,673,504 |
| Total assets | \$4,463,348 | 3,793,845 |
| Liabilities and Shareholders' Equity | | |
| Current liabilities | | |
| Short-term borrowings | \$ 714,669 | 372,249 |
| Trade payables | 284,772 | 209,119 |
| Accrued liabilities | 983,280 | 729,605 |
| Income taxes | 88,606 | 55,327 |
| Total current liabilities | 2,071,327 | 1,366,300 |
| Long-term debt | 420,654 | 407,180 |
| Deferred liabilities | 92,392 | 75,570 |
| Total liabilities | 2,584,373 | 1,849,050 |
| Shareholders' equity | | |
| Preference stock of \$2.50 par value. Authorized 5,000,000 shares; none issued | — | — |
| Common stock of \$.50 par value. Authorized 300,000,000 shares; issued 209,694,630 shares in 1999 and 209,698,516 shares in 1998 | 104,847 | 104,849 |
| Additional paid-in capital | 468,329 | 521,316 |
| Retained earnings | 1,764,110 | 1,621,799 |
| Accumulated other comprehensive earnings | (32,982) | (9,625) |
| Treasury stock, at cost, 16,710,620 shares in 1999 and 13,523,983 shares in 1998 | (425,329) | (293,544) |
| Total shareholders' equity | 1,878,975 | 1,944,795 |
| Total liabilities and shareholders' equity | \$4,463,348 | 3,793,845 |

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

| Fiscal Years Ended in December (Thousands of Dollars) | 1999 | 1998 | 1997 |
|----------------------------------------------------------------------------------------|------------------|------------------|------------------|
| Cash flows from operating activities | | | |
| Net earnings | \$188,953 | 206,365 | 134,986 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | | |
| Depreciation and amortization of plant and equipment | 103,791 | 96,991 | 112,817 |
| Other amortization | 173,533 | 72,208 | 53,767 |
| Deferred income taxes | (38,675) | 1,679 | (40,555) |
| Acquired in-process research and development | — | 20,000 | — |
| Change in operating assets and liabilities (other than cash and cash equivalents): | | | |
| (Increase) decrease in accounts receivable | (11,248) | (126,842) | 11,920 |
| (Increase) decrease in inventories | (44,212) | (44,606) | 40,739 |
| (Increase) decrease in prepaid expenses and other current assets | (26,527) | (113,451) | 20,326 |
| Long-term royalty advance | (150,000) | — | — |
| Increase in trade payables and other current liabilities | 193,626 | 17,668 | 200,359 |
| Other | 2,271 | (3,425) | 9,482 |
| Net cash provided by operating activities | 391,512 | 126,587 | 543,841 |
| Cash flows from investing activities | | | |
| Additions to property, plant and equipment | (107,468) | (141,950) | (99,356) |
| Investments and acquisitions, net of cash acquired | (352,417) | (667,736) | (172,116) |
| Other | 30,793 | 16,986 | 2,195 |
| Net cash utilized by investing activities | (429,092) | (792,700) | (269,277) |
| Cash flows from financing activities | | | |
| Proceeds from borrowings with original maturities of more than three months | 460,333 | 407,377 | 295,132 |
| Repayments of borrowings with original maturities of more than three months | (308,128) | (24,925) | (304,927) |
| Net proceeds (payments) of other short-term borrowings | 226,103 | 271,895 | 21,599 |
| Purchase of common stock | (237,532) | (178,917) | (134,880) |
| Stock option and warrant transactions | 50,358 | 58,493 | 37,258 |
| Dividends paid | (45,526) | (42,277) | (39,694) |
| Net cash provided (utilized) by financing activities | 145,608 | 491,646 | (125,512) |
| Effect of exchange rate changes on cash | (5,617) | (9,570) | (6,238) |
| Increase (decrease) in cash and cash equivalents | 102,411 | (184,037) | 142,814 |
| Cash and cash equivalents at beginning of year | 177,748 | 361,785 | 218,971 |
| Cash and cash equivalents at end of year | \$280,159 | 177,748 | 361,785 |
| Supplemental information | | | |
| Cash paid during the year for | | | |
| Interest | \$ 64,861 | 25,135 | 23,480 |
| Income taxes | \$108,342 | 128,436 | 135,446 |
| Non-cash financing activities | | | |
| 6% Convertible Subordinated Notes Due 1998, converted into common stock | \$ — | — | 149,354 |

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

| (Thousands of Dollars) | Common Stock | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Earnings | Treasury Stock | Total Shareholders' Equity |
|--------------------------------------------------------------------|-------------------|----------------------------------|----------------------|---------------------------------------------------|-------------------|----------------------------------|
| Balance, December 29, 1996 | \$ 66,080 | 282,922 | 1,364,285 | 19,993 | (81,234) | 1,652,046 |
| Three-for-two stock split | 33,039 | (33,039) | — | — | — | — |
| Balance, December 29, 1996, as restated for stock split | 99,119 | 249,883 | 1,364,285 | 19,993 | (81,234) | 1,652,046 |
| Net earnings | — | — | 134,986 | — | — | 134,986 |
| Other comprehensive earnings | — | — | — | (23,896) | — | (23,896) |
| Comprehensive earnings | — | — | — | — | — | 111,090 |
| Purchase of treasury stock | — | — | — | — | (134,880) | (134,880) |
| Stock option and warrant transactions | — | 57,378 | — | — | 41,287 | 98,665 |
| Dividends declared | — | — | (41,783) | — | — | (41,783) |
| Conversion of 6% debt | 5,730 | 147,354 | — | — | — | 153,084 |
| Other | — | (117) | 7 | — | 5 | (105) |
| Balance, December 28, 1997 | 104,849 | 454,498 | 1,457,495 | (3,903) | (174,822) | 1,838,117 |
| Net earnings | — | — | 206,365 | — | — | 206,365 |
| Other comprehensive earnings | — | — | — | (5,722) | — | (5,722) |
| Comprehensive earnings | — | — | — | — | — | 200,643 |
| Purchase of treasury stock | — | — | — | — | (178,917) | (178,917) |
| Stock option and warrant transactions | — | 66,818 | — | — | 60,195 | 127,013 |
| Dividends declared | — | — | (42,061) | — | — | (42,061) |
| Balance, December 27, 1998 | 104,849 | 521,316 | 1,621,799 | (9,625) | (293,544) | 1,944,795 |
| Net earnings | — | — | 188,953 | — | — | 188,953 |
| Other comprehensive earnings | — | — | — | (23,357) | — | (23,357) |
| Comprehensive earnings | — | — | — | — | — | 165,596 |
| Purchase of treasury stock | — | — | — | — | (237,532) | (237,532) |
| Stock option and warrant transactions | — | (52,892) | — | — | 105,747 | 52,855 |
| Dividends declared | — | — | (46,642) | — | — | (46,642) |
| Other | (2) | (95) | — | — | — | (97) |
| Balance, December 26, 1999 | <u>\$ 104,847</u> | <u>468,329</u> | <u>1,764,110</u> | <u>(32,982)</u> | <u>(425,329)</u> | <u>1,878,975</u> |

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Thousands of Dollars Except Share Data)

(1) Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of Hasbro, Inc. and all significant majority-owned subsidiaries (Hasbro or the Company). Investments in affiliates representing 20% to 50% ownership interest are accounted for using the equity method. All significant intercompany balances and transactions have been eliminated.

Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and notes thereto. Actual results could differ from those estimates.

Fiscal Year

Hasbro's fiscal years end on the last Sunday in December. Each of the reported three fiscal years are fifty-two week periods.

Cash and Cash Equivalents

Cash and cash equivalents include all cash balances and highly liquid investments purchased with a maturity to the Company of three months or less.

Inventories

Inventories are valued at the lower of cost (first-in, first-out) or market.

Long-Lived Assets

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. Recoverability is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets were considered to be impaired, the impairment to be recognized would be measured by the amount by which the carrying value of the assets exceed their fair value. Fair value is determined based on discounted cash flows or appraised values, depending on the nature of the asset. Assets to be disposed of are carried at the lower of the carrying amount or their fair value less disposal costs.

Cost in Excess of Net Assets Acquired and Other Intangibles

Approximately 45% of Hasbro's goodwill results from the 1984 acquisition of Milton Bradley Company (Milton Bradley), including its Playskool and international units, and the 1991 acquisition of Tonka Corporation (Tonka), including its Kenner, Parker Brothers and international units. Approximately 29% results from the Company's 1998 acquisitions of Tiger Electronics, Inc., MicroProse, Inc. and Galoob Toys, Inc. An additional approximate 15% results from the Company's 1999 acquisition of Wizards of the Coast, Inc. Goodwill is being amortized on the straight-line basis over lives ranging from seven to forty years.

Substantially all of the other intangibles consist of the cost of acquired product rights. In establishing the value of such rights, the Company considers, but does not individually value, existing copyrights, trademarks, patents, license agreements and other product-related rights. Approximately 61% of these other intangibles relate to rights acquired in the acquisitions noted above. These rights, which were valued at their acquisition date based on the anticipated future cash flows from the underlying product lines, are being amortized over three to twenty-five years using the straight-line method. An additional approximate 12% of these other intangibles relate to rights acquired from a major motion picture studio and are being amortized over the contract life, in proportion to projected sales of the licensed products during the same period.

Depreciation and Amortization

Depreciation and amortization are computed using accelerated and straight-line methods to amortize the cost of property, plant and equipment over their estimated useful lives. The principal lives, in years, used in determining depreciation rates of various assets are: land improvements 15 to 19, buildings and improvements 15 to 25 and machinery and equipment 3 to 12.

Tools, dies and molds are amortized over a three year period or their useful lives, whichever is less, using an accelerated method.

Revenue Recognition

Revenue from product sales is recognized upon shipment to customers. Provisions for discounts, rebates and returns are made when the related revenues are recognized.

Research and Development

Research and product development costs for 1999, 1998 and 1997 were \$254,599, \$184,962 and \$154,710, respectively.

Advertising

Production costs of commercials and programming are charged to operations in the fiscal year during which the production is first aired. The costs of other advertising, promotion and marketing programs are charged to operations in the fiscal year incurred.

Income Taxes

Hasbro uses the asset and liability approach for financial accounting and reporting for income taxes. Deferred income taxes have not been provided on undistributed earnings of international subsidiaries as substantially all of such earnings are indefinitely reinvested by the Company.

Comprehensive Income

Comprehensive income is comprised primarily of gains and losses on the translation of foreign currency financial statements and also includes unrealized gains and losses on certain investment securities, net of tax. The related tax (benefit) expense of other comprehensive income items was \$(3,187), \$(1,684) and \$1,005 for the years 1999, 1998 and 1997, respectively. Reclassification adjustments were not material for all years presented.

Foreign Currency Translation

Foreign currency assets and liabilities are translated into dollars at current rates, and revenues, costs and expenses are translated at average rates during each reporting period. Current earnings include gains or losses resulting from foreign currency transactions as well as translation gains and losses resulting from the use of the U.S. dollar as the functional currency in highly inflationary economies. Other gains and losses resulting from translation of financial statements are the principal component of other comprehensive earnings.

Pension Plans, Postretirement and Postemployment Benefits

Hasbro, except for certain international subsidiaries, has pension plans covering substantially all of its full-time employees. Pension expense is based on actuarial computations of current and future benefits. The Company's policy is to fund amounts which are required by applicable regulations and which are tax deductible. The estimated amounts of future payments to be made under other retirement programs are being accrued currently over the period of active employment and are also included in pension expense.

Hasbro has a contributory postretirement health and life insurance plan covering substantially all employees who retire under any of its United States defined benefit pension plans and meet certain age and length of service requirements. It also has several plans covering certain groups of employees which may provide benefits to such employees following their period of employment but prior to their retirement.

Risk Management Contracts

Hasbro does not enter into derivative financial instruments for speculative purposes. The Company enters into foreign currency forward and option contracts to mitigate its exposure to foreign currency exchange rate fluctuations. This exposure relates to future purchases of inventory not denominated in the functional currency of the unit purchasing the inventory as well as other cross-border currency requirements. Premiums on option contracts are amortized over their term and if such contract is terminated before its maturity, the unamortized premium is expensed and included in other expense, net. The carrying value of options is included in prepaid expenses and other current assets. Gains and losses on forward and option contracts meeting hedge accounting requirements are deferred and recognized as adjustments to the carrying value of the related transactions. In the event hedge accounting requirements are not met, gains and losses on such instruments are included currently in the statements of earnings.

Earnings Per Common Share

Basic earnings per share is computed by dividing net earnings by the weighted average number of shares outstanding for the year. Diluted earnings per share is similar except that the weighted average number of shares outstanding is increased by shares issuable upon exercise of stock options and warrants for which market price exceeds exercise price, less shares which could have been purchased by the Company with the related proceeds.

A reconciliation of earnings per share for the three fiscal years ended December 26, 1999 is as follows:

| | 1999 | | 1998 | | 1997 | |
|----------------------------------------------|-----------|---------|---------|---------|---------|---------|
| | Basic | Diluted | Basic | Diluted | Basic | Diluted |
| Net earnings | \$188,953 | 188,953 | 206,365 | 206,365 | 134,986 | 134,986 |
| Effect of dilutive securities: | | | | | | |
| 6% Convertible Notes due 1998 | — | — | — | — | — | 4,782 |
| Adjusted net earnings | \$188,953 | 188,953 | 206,365 | 206,365 | 134,986 | 139,768 |
| Average shares outstanding (in thousands) | 194,917 | 194,917 | 197,927 | 197,927 | 193,089 | 193,089 |
| Effect of dilutive securities: | | | | | | |
| 6% Convertible Notes due 1998 | — | — | — | — | — | 9,428 |
| Options and warrants | — | 7,186 | — | 7,493 | — | 3,836 |
| Equivalent shares | 194,917 | 202,103 | 197,927 | 205,420 | 193,089 | 206,353 |
| Earnings per share | \$.97 | .93 | 1.04 | 1.00 | .70 | .68 |

(2) Acquisitions

On September 30, 1999, Hasbro acquired Wizards of the Coast, Inc. for an initial purchase price of \$325,000 subject to additional payments based upon the closing balance sheet and future payments contingent upon achieving certain operating objectives. The total acquisition cost to date amounts to \$412,769 and has been accounted for using the purchase method. Based upon estimates of fair market value, \$77,039 has been allocated to net tangible assets, \$214,700 has been allocated to property and related rights and \$121,030 to goodwill.

Hasbro made three major acquisitions during 1998, having an aggregate purchase price of \$669,737. On April 1, it acquired substantially all of the business and operating assets of Tiger Electronics, Inc. and certain affiliates (Tiger). On September 14, 1998, it acquired MicroProse, Inc. (MicroProse) through a cash tender offer of \$6.00 for each outstanding share of MicroProse. Upon completion of a short-form merger, MicroProse became a wholly owned subsidiary of the Company and each untendered share was converted into the right to receive \$6.00 in cash. On October 30, 1998, it acquired Galoob Toys, Inc. (Galoob) through a cash tender offer of \$12.00 for each outstanding share of Galoob. Upon completion of a short-form merger, Galoob became a wholly owned subsidiary of the Company and each untendered share was converted into the right to receive \$12.00 in cash.

These three acquisitions were accounted for using the purchase method, and accordingly, the net assets acquired have been recorded at their fair value and the results of their operations included from the dates of acquisition. Based on fair market value, \$86,926 has been allocated to net tangible assets, \$301,100 to product rights, \$261,711 to goodwill and \$20,000 to acquired in-process research and development. The appraised fair value of this acquired in-process research and development (interactive game software projects under development at the date of acquisition) was determined using the discounted cash flow approach, considered the percentage of completion at the date of acquisition and was expensed at acquisition.

On a pro forma basis, reflecting the acquisitions described above as if they had taken place at the beginning of each period and after giving effect to adjustments recording the acquisitions, and excluding the charge for in-process research and development, unaudited net revenues, net earnings and basic and diluted earnings per share for the year ended December 26, 1999 would have been \$4,630,368, \$270,386, \$1.39 and \$1.34, respectively, and for the year ended December 27, 1998 would have been \$3,685,696, \$143,205, \$.72 and \$.70, respectively. These pro forma results are not indicative of either future performance or actual results which would have occurred had the acquisitions taken place at the beginning of the respective periods.

(3) Inventories

| | 1999 | 1998 |
|-------------------|-----------|---------|
| Finished products | \$348,058 | 283,160 |
| Work in process | 13,470 | 12,698 |
| Raw materials | 47,043 | 38,943 |
| | \$408,571 | 334,801 |

(4) Property, Plant and Equipment

| | 1999 | 1998 |
|--------------------------------------------|------------------|----------------|
| Land and improvements | \$ 16,323 | 14,748 |
| Buildings and improvements | 199,713 | 197,295 |
| Machinery and equipment | 355,958 | 295,810 |
| | 571,994 | 507,853 |
| Less accumulated depreciation | 298,766 | 227,820 |
| | 273,228 | 280,033 |
| Tools, dies and molds, net of amortization | 45,597 | 50,322 |
| | <u>\$318,825</u> | <u>330,355</u> |

Expenditures for maintenance and repairs which do not materially extend the life of the assets are charged to operations.

(5) Short-Term Borrowings

Hasbro has available unsecured committed and uncommitted lines of credit from various banks approximating \$760,000 and \$645,000, respectively. Substantially all of the short-term borrowings outstanding at the end of 1999 and 1998 represent borrowings made under, or supported by, these lines of credit and the weighted average interest rates of the outstanding borrowings were 6.4% and 6.0%, respectively. Hasbro's working capital needs were fulfilled by borrowing under these lines of credit and through the issuance of commercial paper, both of which were on terms and at interest rates generally extended to companies of comparable creditworthiness. The committed lines include \$350,000 and \$350,000 available under long-term and short-term revolving credit agreements, respectively. These agreements contain certain restrictive covenants with which the Company is in compliance. Compensating balances and facility fees were not material.

(6) Accrued Liabilities

| | 1999 | 1998 |
|-----------------------------------|------------------|----------------|
| Royalties | \$178,211 | 116,603 |
| Advertising | 140,129 | 172,621 |
| Payroll and management incentives | 114,852 | 54,622 |
| Other | 550,088 | 385,759 |
| | <u>\$983,280</u> | <u>729,605</u> |

(7) Long-Term Debt

| | 1999 | 1998 |
|---------------------------|------------------|----------------|
| 5.60% Notes Due 2005 | \$100,000 | 100,000 |
| 6.15% Notes Due 2008 | 150,000 | 150,000 |
| 6.60% Debentures Due 2028 | 150,000 | 150,000 |
| Other | 20,654 | 7,180 |
| | <u>\$420,654</u> | <u>407,180</u> |

Current installments of \$4,142 in 1999 and \$260 in 1998 are aggregated with short-term borrowings. The maturities of long-term debt in 2001 and in the succeeding three years are \$2,007, \$1,041, \$1,076 and \$1,112.

(8) Income Taxes

Income taxes attributable to earnings before income taxes are:

| | 1999 | 1998 | 1997 |
|-----------------|------------------|---------------|-----------------|
| Current | | | |
| United States | \$ 77,512 | 40,256 | 62,042 |
| State and local | 5,566 | 5,226 | 8,296 |
| International | 40,489 | 49,952 | 39,756 |
| | <u>123,567</u> | <u>95,434</u> | <u>110,094</u> |
| Deferred | | | |
| United States | (40,131) | (6,458) | (31,533) |
| State and local | (3,440) | (554) | (2,793) |
| International | 4,896 | 8,691 | (6,229) |
| | <u>(38,675)</u> | <u>1,679</u> | <u>(40,555)</u> |
| | <u>\$ 84,892</u> | <u>97,113</u> | <u>69,539</u> |

Certain tax benefits are not reflected in income taxes in the statements of earnings. Such benefits of \$16,735 in 1999, \$14,377 in 1998 and \$4,036 in 1997, relate primarily to stock options.

A reconciliation of the statutory United States federal income tax rate to Hasbro's effective income tax rate is as follows:

| | 1999 | 1998 | 1997 |
|-----------------------------------|--------------|--------------|--------------|
| Statutory income tax rate | 35.0% | 35.0% | 35.0% |
| State and local income taxes, net | .5 | 1.0 | 1.7 |
| Goodwill amortization | 3.3 | 1.8 | 2.4 |
| Tax on international earnings | (7.9) | (5.4) | (4.9) |
| Other, net | .1 | (.4) | (.2) |
| | <u>31.0%</u> | <u>32.0%</u> | <u>34.0%</u> |

The components of earnings before income taxes, determined by tax jurisdiction, are as follows:

| | 1999 | 1998 | 1997 |
|---------------|------------------|----------------|----------------|
| United States | \$ 79,519 | 123,969 | 157,987 |
| International | 194,326 | 179,509 | 46,538 |
| | <u>\$273,845</u> | <u>303,478</u> | <u>204,525</u> |

The components of deferred income tax expense arise from various temporary differences and relate to items included in the statements of earnings.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at December 26, 1999 and December 27, 1998 are:

| | 1999 | 1998 |
|-------------------------------|------------------|----------------|
| Deferred tax assets: | | |
| Accounts receivable | \$ 36,696 | 27,556 |
| Inventories | 26,205 | 14,718 |
| Net operating loss carryovers | 28,930 | 31,608 |
| Operating expenses | 39,512 | 44,491 |
| Postretirement benefits | 12,243 | 12,269 |
| Other | 99,143 | 74,955 |
| Gross deferred tax assets | 242,729 | 205,597 |
| Valuation allowance | (15,146) | (13,261) |
| Net deferred tax assets | <u>227,583</u> | <u>192,336</u> |
| Deferred tax liabilities | 100,820 | 46,174 |
| Net deferred income taxes | <u>\$126,763</u> | <u>146,162</u> |

Hasbro has a valuation allowance for deferred tax assets at December 26, 1999 of \$15,146, which is an increase of \$1,885 from the \$13,261 at December 27, 1998. The allowance pertains to United States and international operating loss carryforwards, some of which have no expiration and others that would expire beginning in 2002. If fully realized, \$9,672 will reduce goodwill and the balance will reduce future income tax expense. Deferred tax liabilities relate primarily to property rights.

Based on Hasbro's history of taxable income and the anticipation of sufficient taxable income in years when the temporary differences are expected to become tax deductions, it believes that it will realize the benefit of the deferred tax assets, net of the existing valuation allowance.

Deferred income taxes of \$115,646 and \$100,332 at the end of 1999 and 1998, respectively, are included as a component of prepaid expenses and other current assets, and \$19,592 and \$53,331, respectively, are included as a component of other assets. At the same dates, deferred income taxes of \$1,236 and \$491, respectively, are included as a component of accrued liabilities, and \$7,239 and \$7,010, respectively, are included as a component of deferred liabilities.

The cumulative amount of undistributed earnings of Hasbro's international subsidiaries held for reinvestment is approximately \$347,000 at December 26, 1999. In the event that all international undistributed earnings were remitted to the United States, the amount of incremental taxes would be approximately \$48,000.

(9) Capital Stock

Preference Share Purchase Rights

Hasbro maintains a Preference Share Purchase Rights plan (the Rights Plan). Under the terms of the Rights Plan, each share of common stock is accompanied by a Preference Share Purchase Right. Each Right is only exercisable under certain circumstances and, until exercisable, the Rights are not transferable apart from Hasbro's common stock. When exercisable, each Right will entitle its holder to purchase until June 30, 2009, in certain merger or other business combination or recapitalization transactions, at the Right's then current exercise price, a number of the acquiring company's or Hasbro's, as the case may be, common shares having a market value at that time of twice the Right's exercise price. Under certain circumstances, the Company may substitute cash, other assets, equity securities or debt securities for the common stock. At the option of the Board of Directors of Hasbro (the Board), the rightholder may, under certain circumstances, receive shares of Hasbro's stock in exchange for Rights.

Prior to the acquisition by the person or group of beneficial ownership of a certain percentage of Hasbro's common stock, the Rights are redeemable for \$.01 per Right. The Rights Plan contains certain exceptions with respect to the Hassenfeld family and related entities.

Common Stock

On December 9, 1997, the Board canceled all prior share repurchase authorizations and authorized the purchase of up to an additional \$500,000 of the Company's common stock. At December 26, 1999, \$72,008 remained under this authorization. In addition to the remaining amount under this repurchase authorization, on December 6, 1999, the Board authorized an additional common share repurchase program up to \$500,000.

On February 19, 1999, the Board declared a three-for-two stock split, payable in the form of a 50% stock dividend, on March 15, 1999 to shareholders of record on March 1, 1999. All earnings per common share amounts, references to common stock and shareholders' equity amounts have been restated as if the stock split had occurred as of the earliest period presented.

(10) Stock Options and Warrants

Hasbro has various stock option plans for employees as well as a plan for non-employee members of the Board (collectively, the plans) and has reserved 31,771,373 shares of its common stock for issuance upon exercise of options granted or to be granted under the plans. These options generally vest in equal annual amounts over three to five years. The plans provide that options be granted at exercise prices not less than market value on the date the option is granted and options are adjusted for such changes as stock splits and stock dividends. No options are exercisable for periods of more than ten years after date of grant. Certain of the plans permit the granting of awards in the form of stock options, stock appreciation rights, stock awards and cash awards. At December 26, 1999, awards made under these plans have been in the form of stock options.

As permitted by Statement of Financial Accounting Standards No. 123 (SFAS 123), Hasbro continues to apply Accounting Principles Board Opinion No. 25 (APB 25) in accounting for the plans under which no compensation cost is recognized. Had compensation expense been recorded under the provisions of SFAS 123, the impact on the Company's net earnings and earnings per share would have been:

| | 1999 | 1998 | 1997 |
|--------------------------------------------|-----------|----------|---------|
| Reported net earnings | \$188,953 | 206,365 | 134,986 |
| Pro forma compensation expense, net of tax | (18,335) | (10,339) | (5,880) |
| Pro forma net earnings | \$170,618 | 196,026 | 129,106 |
| Pro forma earnings per share | | | |
| Basic | \$.88 | .99 | .67 |
| Diluted | \$.84 | .95 | .65 |

The weighted average fair value of options granted in 1999, 1998 and 1997 were \$12.13, \$8.66 and \$5.76, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 1999, 1998 and 1997, respectively: risk-free interest rates of 5.60%, 5.70% and 6.20%; expected dividend yields of 0.78%, 0.85% and 1.12% and expected volatility of approximately 34%, 26% and 21%, and expected lives of approximately 6 years.

Additionally, the Company has reserved 16,762,500 shares of its common stock for issuance upon exercise of outstanding warrants. During 1999, 5,737,500 warrants were exercised at an exercise price of \$14.00. During 1998, warrants to purchase 6,000,000 shares at an exercise price of \$23.3333 per share were issued in connection with the acquisition of certain rights. The fair value of these warrants was \$11.42 each on the date of grant.

Information with respect to options and warrants, in thousands of shares, for the three years ended December 26, 1999 is as follows:

| | 1999 | 1998 | 1997 |
|----------------------------------|----------|---------|---------|
| Number of shares: | | | |
| Outstanding at beginning of year | 36,361 | 31,424 | 20,452 |
| Granted | 7,168 | 8,639 | 14,191 |
| Exercised | (8,313) | (3,468) | (2,651) |
| Expired or canceled | (1,440) | (234) | (568) |
| Outstanding at end of year | 33,776 | 36,361 | 31,424 |
| Exercisable at end of year | 23,456 | 11,673 | 11,090 |
| Weighted average exercise price: | | | |
| Granted | \$ 31.32 | 23.86 | 18.77 |
| Exercised | \$ 14.51 | 13.34 | 12.30 |
| Expired or canceled | \$ 27.43 | 18.75 | 15.80 |
| Outstanding at end of year | \$ 21.46 | 18.17 | 16.08 |
| Exercisable at end of year | \$ 19.09 | 14.43 | 13.46 |

Information, in thousands of shares, with respect to the 33,776 options and warrants outstanding and the 23,456 exercisable at December 26, 1999, is as follows:

| Range of Exercise Prices | Shares | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price |
|--------------------------|--------|---------------------------------------------|---------------------------------|
| Outstanding | | | |
| \$ 4.56 – \$13.86 | 1,531 | 3.1 years | \$10.67 |
| \$14.00 – \$16.64 | 4,924 | 4.3 years | \$15.25 |
| \$18.67 – \$23.27 | 13,347 | 8.8 years | \$18.93 |
| \$23.33 – \$36.27 | 13,974 | 9.6 years | \$27.25 |
| Exercisable | | | |
| \$ 4.56 – \$13.86 | 1,531 | | \$10.67 |
| \$14.00 – \$16.64 | 3,719 | | \$15.57 |
| \$18.67 – \$23.27 | 11,379 | | \$18.72 |
| \$23.33 – \$36.27 | 6,827 | | \$23.52 |

(11) Pension, Postretirement and Postemployment Benefits

Pension and Postretirement Benefits

Hasbro's net pension and profit sharing cost for 1999, 1998 and 1997 was approximately \$12,600, \$12,900 and \$13,400, respectively.

United States Plans

Substantially all United States employees are covered under at least one of several non-contributory defined benefit pension plans maintained by the Company. Benefits under the two major plans, principally covering non-union employees, are based primarily on salary and years of service. One of these plans is funded. Benefits under the remaining plans are based primarily on fixed amounts for specified years of service. One of these plans is also funded. At December 26, 1999, the two funded plans have plan assets of \$242,889 and accumulated benefit obligations of \$137,828. The unfunded plans have accumulated benefit obligations of \$16,878.

Hasbro also provides certain postretirement health care and life insurance benefits to eligible employees who retire and have either attained age 65 with 5 years of service or age 55 with 10 years of service. The cost of providing these benefits on behalf of employees who retired prior to 1993 is and will continue to be substantially borne by the Company. The cost of providing benefits on behalf of employees who retire after 1992 is shared, with the employee contributing an increasing percentage of the cost, resulting in an employee-paid plan after the year 2002. The plan is not funded.

| | Pension | | Postretirement | |
|---------------------------------------------------|-------------|----------|----------------|----------|
| | 1999 | 1998 | 1999 | 1998 |
| Change in projected benefit obligation | | | | |
| Projected benefit obligation at beginning of year | \$207,063 | 184,589 | \$ 28,428 | 28,885 |
| Service cost | 9,356 | 9,362 | 227 | 224 |
| Interest cost | 13,670 | 12,798 | 1,775 | 1,893 |
| Plan amendments | (2,298) | — | — | — |
| Actuarial (gain) loss | (32,438) | 6,468 | (3,263) | (271) |
| Benefits paid | (6,305) | (5,539) | (2,484) | (2,303) |
| Expenses paid | (730) | (615) | — | — |
| Projected benefit obligation at end of year | \$188,318 | 207,063 | \$ 24,683 | 28,428 |
| Change in plan assets | | | | |
| Fair value of plan assets at beginning of year | \$219,410 | 196,634 | \$ — | — |
| Actual return on plan assets | 30,061 | 28,522 | — | — |
| Employer contribution | 453 | 408 | — | — |
| Benefits paid | (6,305) | (5,539) | — | — |
| Expenses paid | (730) | (615) | — | — |
| Fair value of plan assets at end of year | \$242,889 | 219,410 | \$ — | — |
| Funded status | \$ 54,571 | 12,347 | \$ (24,683) | (28,428) |
| Unrecognized net (gain) loss | (80,496) | (39,402) | (406) | 2,885 |
| Unrecognized prior service cost | 5,836 | 9,268 | — | — |
| Accrued benefit cost | \$ (20,089) | (17,787) | \$ (25,089) | (25,543) |

The assets of the funded plans are managed by investment advisors and consist primarily of pooled indexed and actively managed bond and stock funds. For measuring the expected pension accumulated benefit obligation, assumed discount rates of 7.75%, 6.75% and 7.00% were used for 1999, 1998 and 1997, respectively; assumed long-term rates of compensation increase of 4.50% in 1999 and 1998 and 5.00% in 1997, and an assumed long-term rate of return on plan assets of 9.00% in all years.

For measuring the expected postretirement benefit obligation, an 7.25%, 7.50% and 8.00% annual rate of increase in the per capita cost of covered health care benefits was assumed for 1999, 1998 and 1997, respectively. The 1999 and 1998 rates were further assumed to decrease gradually to 4.50% in 2012, while the 1997 rate was assumed to decrease to 5.00% over this same period. All were assumed to remain constant after 2012. The discount rates used in the pension calculation were also used for the postretirement calculation.

| | 1999 | 1998 | 1997 |
|---------------------------------|----------|----------|----------|
| Components of net periodic cost | | | |
| Pension | | | |
| Service cost | \$ 9,356 | 9,362 | 8,022 |
| Interest cost | 13,670 | 12,798 | 11,451 |
| Expected return on assets | (19,484) | (17,465) | (14,517) |
| Net amortization and deferrals | (786) | (448) | (465) |
| Net periodic benefit cost | \$ 2,756 | 4,247 | 4,491 |
| Postretirement | | | |
| Service cost | \$ 227 | 224 | 205 |
| Interest cost | 1,775 | 1,893 | 2,039 |
| Net amortization and deferrals | 27 | 57 | 22 |
| Net periodic benefit cost | \$ 2,029 | 2,174 | 2,266 |

If the health care cost trend rate were increased one percentage point in each year, the accumulated postretirement benefit obligation at December 26, 1999 and the aggregate of the benefits earned during the period and the interest cost would have each increased by approximately 10%.

Hasbro also has a profit sharing plan covering substantially all of its United States non-union employees. The plan provides for an annual discretionary contribution by the Company which for 1999, 1998 and 1997 was approximately \$4,900, \$5,000 and \$5,100, respectively.

International Plans

Pension coverage for employees of Hasbro's international subsidiaries is provided, to the extent deemed appropriate, through separate defined benefit and defined contribution plans. These plans were neither significant individually nor in the aggregate.

Postemployment Benefits

Hasbro has several plans covering certain groups of employees which may provide benefits to such employees following their period of active employment but prior to their retirement. These plans include certain severance plans which provide benefits to employees involuntarily terminated and certain plans which continue the Company's health and life insurance contributions for employees who have left Hasbro's employ under terms of its long-term disability plan.

(12) Leases

Hasbro occupies certain manufacturing facilities and sales offices and uses certain equipment under various operating lease arrangements. The rent expense under such arrangements, net of sublease income which is not material, for 1999, 1998 and 1997 amounted to \$56,072, \$50,932 and \$48,090, respectively.

Minimum rentals, net of minimum sublease income which is not material, under long-term operating leases for the five years subsequent to 1999 and in the aggregate are as follows:

| | |
|-------------|------------------|
| 2000 | \$ 40,084 |
| 2001 | 33,976 |
| 2002 | 26,274 |
| 2003 | 22,834 |
| 2004 | 20,451 |
| Later years | 107,623 |
| | <u>\$251,242</u> |

All leases expire prior to 2015. Real estate taxes, insurance and maintenance expenses are generally obligations of the Company. It is expected that in the normal course of business, leases that expire will be renewed or replaced by leases on other properties; thus, it is anticipated that future minimum lease commitments will not be less than the amounts shown for 1999.

In addition, Hasbro leases certain facilities which, as a result of restructurings, are no longer in use. Future costs relating to such facilities were included as a component of the restructuring charge and are not included in the table above.

(13) Consolidation Program and Restructuring Charge

On December 7, 1999, the Company announced a program to further consolidate manufacturing and sourcing activities and product lines, as well as streamline and further regionalize marketing, sales and research and development activities worldwide. Costs associated with this consolidation program amounted to \$141,575, and were recorded in the fourth quarter as follows:

| | |
|-------------------------------------|------------------|
| Restructuring charge | \$ 64,232 |
| Other operating expenses: | |
| Cost of sales | 8,740 |
| Amortization | 38,449 |
| Royalties, research and development | 26,292 |
| Advertising | 3,862 |
| | <u>77,343</u> |
| Total consolidation program costs | <u>\$141,575</u> |

The significant components of the restructuring plan include the closing of two factories in Mexico and the United Kingdom, reducing capacity at the remaining three factories, shifting production to third party manufacturers in the Far East and further consolidation and regionalization of the International marketing and sales structure. This plan anticipates the redundancy of approximately 2,200 employees, including 1,800 in manufacturing and sourcing activities and 400 worldwide in research and product development, marketing, sales and administration. The restructuring charge of \$64,232 represents approximately \$38,700 of cash charges for severance benefits which will be disbursed over the employee's entitlement period, \$14,300 of cash charges for lease and facility closing costs to be expended over the contractual lease term and closing process and non-cash charges of \$11,200 for fixed asset write-offs arising primarily in the manufacturing area. Of the cash amount, approximately \$4,700 has been paid for severance benefits relating to 193 employees terminated as of December 26, 1999. Non-cash charges relating to fixed asset write-offs have been credited to the respective line items on the balance sheet. The remaining amount of approximately \$48,000 is included in accrued liabilities. The restructuring plan is expected to be completed in fiscal 2000.

The components of the consolidation program included in other operating expenses represent costs associated with exiting certain product lines and reevaluating other product lines resulting in reduced expectations. The product lines being exited were not, either individually or in the aggregate, material to the Company's revenues or operating results. Approximately \$12,000 represents cash charges which will be incurred on contractual royalty, product development and advertising commitments associated with the discontinued product lines. Non-cash charges of approximately \$65,000 relate to asset write-offs and write-downs of underutilized assets. This includes impairment of intangible assets arising from the decision to discontinue or significantly reduce product line offerings. The resulting sum of undiscounted future cash flows of these assets was not sufficient to cover the carrying amount of the assets, and as such, they were written down to their fair market value. Items relating to property rights and licenses, goodwill, inventory, prepaid and other current assets have been credited to the respective asset in the balance sheet.

Late in the fourth quarter of 1997, the Company announced a global integration and profit enhancement program which anticipated the redundancy of approximately 2,500 employees, principally in manufacturing, and provided for actions in three principal areas: a continued consolidation of the Company's manufacturing operations; the streamlining of marketing and sales, while exiting from certain underperforming markets and product lines; and the further leveraging of overheads. Of the \$140,000 estimated costs related to these actions, \$125,000 was reported as a restructuring charge and \$15,000 was reflected in cost of sales. Of the restructuring amount, approximately \$54,000 related to severance and people costs, \$52,000 to property, plant and equipment and leases and \$19,000 to product line related costs. During 1998, the employment of all employees planned for redundancy was terminated. This program has been completed.

(14) Financial Instruments

Hasbro's financial instruments include cash and cash equivalents, accounts receivable, short- and long-term borrowings, accounts payable and accrued liabilities. At December 26, 1999, the carrying cost of these instruments approximated their fair value. Its financial instruments also include foreign currency forwards and options. At December 26, 1999, the carrying value of these instruments approximated their fair value based on quoted or publicly available market information.

Hasbro uses foreign currency forwards and options, generally purchased for terms of not more than twelve months, to protect itself from adverse currency rate fluctuations on firmly committed and anticipated foreign currency transactions. These over-the-counter contracts, which hedge future purchases of inventory and other cross-border currency requirements, are primarily denominated in United States and Hong Kong dollars and Irish punts and entered into with counterparties who are major financial institutions with which Hasbro also has other financial relationships. The Company believes any risk related to default by a counterparty to be remote.

The Company had the equivalent of approximately \$85,000 and \$130,000 of foreign currency forwards outstanding at December 26, 1999 and December 27, 1998, respectively, and approximately \$132,000 of foreign currency options outstanding at December 26, 1999. Gains and losses deferred under hedge accounting provisions are subsequently included in the measurement of the related foreign currency transaction. Gains and losses on contracts not meeting hedge accounting provisions are included currently in earnings. The aggregate amount of gains and losses resulting from all foreign currency transactions was not material.

(15) Commitments and Contingencies

Hasbro had unused open letters of credit of approximately \$15,000 and \$20,000 at December 26, 1999 and December 27, 1998, respectively.

The Company routinely enters into license agreements with inventors, designers and others for the use of intellectual properties in its products. Certain of these agreements contain provisions for the payment of guaranteed or minimum royalty amounts. Under terms of currently existing agreements, in certain circumstances the Company may become liable for remaining guaranteed minimum royalties of up to \$665,000 between 2000 and 2007. Of this amount, approximately \$233,000 has been paid. Approximately \$83,000 is included in the \$111,523 of prepaid royalties which are a component of prepaid expenses and other current assets in the balance sheet. Included in other assets is \$150,000 representing the long-term portion of the amount paid in 1999. Of the remaining unpaid minimum guaranty, Hasbro may be required to pay amounts as follows:

| | |
|------|------------------|
| 2000 | \$ 88,000 |
| 2001 | 84,000 |
| 2002 | 130,000 |
| 2003 | 6,000 |
| 2004 | 2,000 |
| 2005 | <u>122,000</u> |
| | <u>\$432,000</u> |

Such payments are related to royalties which are expected to be incurred on anticipated revenues in the years 2000 through 2007.

Hasbro is party to certain legal proceedings, substantially involving routine litigation incidental to the Company's business, none of which, individually or in the aggregate, is deemed to be material to the financial condition of the Company.

(16) Segment Reporting

Segment and Geographic Information

Hasbro is a worldwide marketer and distributor of children's and family entertainment products, principally engaged in the design, manufacture and marketing of games and toys ranging from traditional to high-tech. During the second quarter of 1999, the Company redefined its focus and method of managing its business into two major areas, Toys and Games. Following this organizational adjustment, within its two key areas, under the provisions of Statement of Financial Accounting Standards No. 131, Disclosures about Segments of an Enterprise and Related Information, the Company's reportable segments are U.S. Toys, Games, International and Global Operations. Prior year amounts have been reclassified to reflect the Company's current focus.

In the United States, the U.S. Toy segment includes the design, marketing and selling of boys action figures, vehicles and playsets, girls toys, preschool toys and infant products and creative play products. The Games segment includes the development, marketing and selling of traditional board games and puzzles, handheld electronic games, electronic interactive plush, children's consumer electronics, electronic learning aids, trading card and role-playing games and interactive software games based on the Company's owned and licensed brands. Within the International segment, the Company develops, markets and sells both toy and game products in non-U.S. markets. Global Operations manufactures and sources product for the majority of the Company's segments. The Company also has other segments which license certain toy properties and which develop and market non-traditional toy and game based product realizing more than half of their revenues and the majority of their operating profit in the first half of the year, which is contra-seasonal to the rest of the Company's business. These other segments do not meet the quantitative thresholds for reportable segments and have been combined for reporting purposes.

Segment performance is measured at the operating profit level, prior to certain charges. In 1999, segment profitability was measured prior to \$141,575 in charges incurred in connection with the 1999 consolidation program. For 1998, operating profits are reflected prior to the \$20,000 charge incurred to write-off acquired in-process research and development arising on the MicroProse acquisition. For 1997, operating profit is reflected prior to \$140,000 of restructuring charges. Included in Corporate and eliminations are general corporate expenses, the elimination of intersegment transactions and assets not identified with a specific segment. Intersegment sales and transfers are reflected in management reports at amounts approximating cost.

As a result of the complexity of the Company's organizational changes, it currently is unable to segregate assets and related expenses between the U.S. Toys and Games segments, and thus they are currently reported as one. It is anticipated that such items will be segregated in the future and will then be separately reported. Certain asset related expense items including depreciation and amortization of intangibles have been allocated to segments based upon estimates in order to arrive at segment operating profit. During 1999, the Company's Games segment acquired Wizards of the Coast, Inc. During 1998, the Company's present U.S. Toys segment acquired Galoob and the present Games segment acquired Tiger and MicroProse.

The accounting policies of the segments are the same as those described in note 1 to the consolidated financial statements.

Information by segment and a reconciliation to reported amounts are as follows.

| | Revenues from External Customers | Affiliate Revenues | Operating Profit | Depreciation and Amortization | Capital Additions | Total Assets |
|-------------------------------------------------|-------------------------------------------|-----------------------|---------------------|-------------------------------------|----------------------|-----------------|
| 1999 | | | | | | |
| U.S. Toys (a) | \$1,056,700 | — | 91,588 | | | |
| Games (a) | 1,703,216 | 81,948 | 259,314 | | | |
| U.S. Toys and Games (a) | 2,759,916 | 81,948 | 350,902 | 109,250 | 12,077 | 3,588,994 |
| International | 1,227,949 | 6,403 | 140,567 | 34,150 | 9,539 | 1,285,342 |
| Global Operations (b) | 24,923 | 1,030,028 | (1,878) | 61,175 | 67,644 | 572,454 |
| Other segments | 219,475 | 18,988 | 5,777 | 22,517 | 4,301 | 269,435 |
| Corporate and eliminations | — | (1,137,367) | (26,224) | 11,783 | 13,907 | (1,252,877) |
| Segment total | 4,232,263 | — | 469,144 | 238,875 | 107,468 | 4,463,348 |
| Consolidation program (c) | — | — | (141,575) | 38,449 | — | — |
| Consolidated Total | \$4,232,263 | — | 327,569 | 277,324 | 107,468 | 4,463,348 |
| 1998 | | | | | | |
| U.S. Toys (a) | \$ 894,279 | 61 | 55,103 | | | |
| Games (a) | 1,043,623 | 1,019 | 143,216 | | | |
| U.S. Toys and Games (a) | 1,937,902 | 1,080 | 198,319 | 54,543 | 12,739 | 2,390,147 |
| International | 1,106,565 | (174) | 130,232 | 23,905 | 34,480 | 840,246 |
| Global Operations (b) | 6,453 | 935,683 | (6,560) | 62,397 | 71,585 | 415,872 |
| Other segments | 253,534 | 8,992 | 35,565 | 19,106 | 4,925 | 354,717 |
| Corporate and eliminations | — | (945,581) | (12,674) | 9,248 | 18,221 | (207,137) |
| Segment total | 3,304,454 | — | 344,882 | 169,199 | 141,950 | 3,793,845 |
| Acquired in-process research and development | — | — | (20,000) | — | — | — |
| Consolidated Total | \$3,304,454 | — | 324,882 | 169,199 | 141,950 | 3,793,845 |

| | Revenues from External Customers | Affiliate Revenues | Operating Profit | Depreciation and Amortization | Capital Additions | Total Assets |
|----------------------------|-------------------------------------------|-----------------------|---------------------|-------------------------------------|----------------------|-----------------|
| 1997 | | | | | | |
| U.S. Toys (a) | \$1,068,736 | — | 59,354 | | | |
| Games (a) | 725,683 | 3,151 | 151,352 | | | |
| U.S. Toys and Games (a) | 1,794,419 | 3,151 | 210,706 | 45,381 | 13,604 | 1,676,254 |
| International | 1,212,811 | 24,616 | 133,374 | 25,153 | 6,976 | 887,256 |
| Global Operations (b) | 8,108 | 1,117,281 | 5,061 | 74,153 | 60,821 | 714,656 |
| Other segments | 173,221 | 3,148 | 8,586 | 14,045 | 2,222 | 267,756 |
| Corporate and eliminations | — | (1,148,196) | 17,381 | 7,852 | 15,733 | (646,205) |
| Segment total | 3,188,559 | — | 375,108 | 166,584 | 99,356 | 2,899,717 |
| Restructuring | — | — | (140,000) | — | — | — |
| Consolidated Total | \$3,188,559 | — | 235,108 | 166,584 | 99,356 | 2,899,717 |

(a) As a result of the complexity of the Company's organizational changes, it currently is unable to segregate assets and related expenses between the U.S. Toys and Games segments, and thus they are currently reported as one. It is anticipated that such items will be segregated beginning in fiscal 2000 and will then be separately reported. Certain asset related expense items including depreciation and amortization of intangibles have been allocated to segments based upon estimates in order to arrive at segment operating profit.

(b) The Global Operations segment derives substantially all of its revenues, and thus its operating results, from intersegment activities.

(c) The impact of the consolidation program to operating profit by segment was \$16,150 to U.S. Toys, \$35,732 to Games, \$23,044 to International, \$44,324 to Global Operations and \$22,325 to Other segments.

The following table presents consolidated net revenues by classes of principal products for the years ended in December:

| | 1999 | 1998 | 1997 |
|----------------------------|-------------|-----------|-----------|
| Boys toys | \$1,232,300 | 891,600 | 1,152,900 |
| Games and puzzles | 1,936,100 | 1,268,700 | 1,093,700 |
| Interactive software games | 229,400 | 192,300 | 87,000 |
| Preschool toys | 273,600 | 341,600 | 317,200 |
| Other | 560,863 | 610,254 | 537,759 |
| Net revenues | \$4,232,263 | 3,304,454 | 3,188,559 |

Information as to Hasbro's operations in different geographical areas is presented below on the basis the Company uses to manage its business. Net revenues and the related pretax earnings are categorized based on location of the customer, while long-lived assets (property, plant and equipment, cost in excess of acquired net assets and other intangibles) are categorized based on their location:

| | 1999 | 1998 | 1997 |
|--------------------|--------------------|------------------|------------------|
| Net revenues: | | | |
| United States | \$2,818,837 | 2,113,057 | 1,947,824 |
| International | 1,413,426 | 1,191,397 | 1,240,735 |
| | <u>\$4,232,263</u> | <u>3,304,454</u> | <u>3,188,559</u> |
| Pretax earnings: | | | |
| United States | \$ 158,834 | 194,050 | 117,436 |
| International | 115,011 | 109,428 | 87,089 |
| | <u>\$ 273,845</u> | <u>303,478</u> | <u>204,525</u> |
| Long-lived assets: | | | |
| United States | \$1,880,029 | 1,694,967 | 1,119,836 |
| International | 194,677 | 177,569 | 126,067 |
| | <u>\$2,074,706</u> | <u>1,872,536</u> | <u>1,245,903</u> |

Principal international markets include Western Europe, Canada, Mexico, Australia, New Zealand and Hong Kong.

Other Information

Hasbro markets its products primarily to customers in the retail sector. Although the Company closely monitors the creditworthiness of its customers, adjusting credit policies and limits as deemed appropriate, a substantial portion of its customers' ability to discharge amounts owed is dependent upon the overall retail economic environment.

Sales to the Company's two largest customers, Wal-Mart Stores, Inc. and Toys 'R Us, Inc., amounted to 16% each of consolidated net revenues during 1999, 18% and 17%, respectively, during 1998 and 15% and 22%, respectively, during 1997.

Hasbro purchases certain components and accessories used in its manufacturing process and certain finished products from manufacturers in the Far East. The Company's reliance on external sources of manufacturing can be shifted, over a period of time, to alternative sources of supply for products it sells, should such changes be necessary. However, if Hasbro were prevented from obtaining products from a substantial number of its current Far East suppliers due to political, labor or other factors beyond its control, the Company's operations would be disrupted while alternative sources of product were secured. The imposition of trade sanctions by the United States or the European Union against a class of products imported by Hasbro from, or the loss of "most favored nation" trading status by, the Peoples Republic of China could significantly increase the cost of the Company's products imported into the United States or Europe from China.

(17) Quarterly Financial Data (Unaudited)

| | Quarter | | | | |
|------------------------------|-------------------------------------|---------------------------------|----------------------------------|---------------------------------|---------------------------------|
| | First | Second | Third | Fourth | Full Year |
| 1999 | | | | | |
| Net revenues | \$668,398 | 874,574 | 1,098,179 | 1,591,112 | 4,232,263 |
| Gross profit | \$411,881 | 529,548 | 654,166 | 938,426 | 2,534,021 |
| Earnings before income taxes | \$ 19,993 | 46,796 | 123,434 | 83,622(a) | 273,845 |
| Net earnings | <u>\$ 13,795</u> | <u>32,289</u> | <u>85,170</u> | <u>57,699</u> | <u>188,953</u> |
| Per common share | | | | | |
| Earnings | | | | | |
| Basic | \$.07 | .17 | .44 | .30 | .97 |
| Diluted | \$.07 | .16 | .43 | .29 | .93 |
| Market price | | | | | |
| High | \$ 30 ¹ / ₈ | 37 | 28 ⁵ / ₈ | 24 ¹ / ₄ | 37 |
| Low | \$ 21 ¹³ / ₁₆ | 27 | 21 ¹⁵ / ₁₆ | 16 ⁷ / ₈ | 16 ⁷ / ₈ |
| Cash dividends declared | <u>\$.06</u> | <u>.06</u> | <u>.06</u> | <u>.06</u> | <u>.24</u> |
| 1998 | | | | | |
| Net revenues | \$482,820 | 572,057 | 945,498 | 1,304,079 | 3,304,454 |
| Gross profit | \$278,508 | 324,962 | 543,129 | 791,794 | 1,938,393 |
| Earnings before income taxes | \$ 11,808 | 8,262 | 89,601(a) | 193,807 | 303,478 |
| Net earnings | <u>\$ 7,793</u> | <u>5,453</u> | <u>61,330</u> | <u>131,789</u> | <u>206,365</u> |
| Per common share | | | | | |
| Earnings | | | | | |
| Basic | \$.04 | .03 | .31 | .67 | 1.04 |
| Diluted | \$.04 | .03 | .30 | .65 | 1.00 |
| Market price | | | | | |
| High | \$ 25 ³ / ₄ | 27 ¹ / ₁₆ | 27 ¹ / ₄ | 25 ⁷ / ₁₆ | 27 ¹ / ₄ |
| Low | \$ 19 ⁷ / ₈ | 23 ¹ / ₈ | 19 ⁵ / ₈ | 18 ⁵ / ₈ | 18 ⁵ / ₈ |
| Cash dividends declared | <u>\$.05</u> | <u>.05</u> | <u>.05</u> | <u>.05</u> | <u>.21</u> |
| 1997 | | | | | |
| Net revenues | \$555,784 | 583,886 | 915,533 | 1,133,356 | 3,188,559 |
| Gross profit | \$320,413 | 330,969 | 512,506 | 665,613 | 1,829,501 |
| Earnings before income taxes | \$ 40,147 | 20,283 | 115,441 | 28,654(a) | 204,525 |
| Net earnings | <u>\$ 25,694</u> | <u>12,981</u> | <u>77,400</u> | <u>18,911</u> | <u>134,986</u> |
| Per common share | | | | | |
| Earnings | | | | | |
| Basic | \$.13 | .07 | .41 | .10 | .70 |
| Diluted | \$.13 | .07 | .38 | .09 | .68 |
| Market price | | | | | |
| High | \$ 19 ³ / ₄ | 19 ⁵ / ₈ | 20 ³ / ₄ | 24 ⁵ / ₁₆ | 24 ⁵ / ₁₆ |
| Low | \$ 16 ¹ / ₁₆ | 15 ¹ / ₄ | 17 ⁵ / ₈ | 17 ¹ / ₈ | 15 ¹ / ₄ |
| Cash dividends declared | <u>\$.05</u> | <u>.05</u> | <u>.05</u> | <u>.05</u> | <u>.21</u> |

(a) In 1999 and 1997, includes \$64,232 and \$125,000, respectively relating to restructuring of operations and, in 1998, includes the expense impact of \$20,000 relating to acquired in-process research and development.

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Shareholders
Hasbro, Inc.:

We have audited the accompanying consolidated balance sheets of Hasbro, Inc. and subsidiaries as of December 26, 1999 and December 27, 1998 and the related consolidated statements of earnings, shareholders' equity and cash flows for each of the fiscal years in the three-year period ended December 26, 1999. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Hasbro, Inc. and subsidiaries as of December 26, 1999 and December 27, 1998 and the results of their operations and their cash flows for each of the fiscal years in the three-year period ended December 26, 1999 in conformity with generally accepted accounting principles.

KPMG LLP

Providence, Rhode Island
February 7, 2000

FIVE-YEAR SUMMARY SELECTED FINANCIAL INFORMATION

| (Thousands of Dollars Except Share Data) | 1999 | 1998 | 1997 | 1996 | 1995 |
|-----------------------------------------------------------------------------------------------------------|-----------------------------------|--------------------------------|--------------------------------|-----------|--------------------------------|
| Operating information | | | | | |
| Net revenues | \$4,232,263 | 3,304,454 | 3,188,559 | 3,002,370 | 2,858,210 |
| Cost of sales | \$1,698,242 | 1,366,061 | 1,359,058 | 1,328,897 | 1,237,197 |
| Amortization | \$ 173,533 | 72,208 | 53,767 | 40,064 | 38,471 |
| Royalties, research and development | \$ 711,790 | 424,673 | 386,912 | 319,494 | 304,704 |
| Advertising | \$ 456,978 | 440,692 | 411,574 | 418,003 | 417,886 |
| Selling, distribution and administration | \$ 799,919 | 655,938 | 617,140 | 563,645 | 555,280 |
| Restructuring, acquired in-process research and development, and discontinued development project charges | \$ 64,232 | 20,000 | 125,000 | — | 31,100 |
| Nonoperating expense | \$ 53,724 | 21,404 | 30,583 | 25,374 | 21,022 |
| Earnings before income taxes | \$ 273,845 | 303,478 | 204,525 | 306,893 | 252,550 |
| Net earnings | \$ 188,953 | 206,365 | 134,986 | 199,912 | 155,571 |
| Common share data | | | | | |
| Price at year end | \$ 18 ¹ / ₈ | 22 ¹ / ₄ | 20 ³ / ₈ | 17 | 13 ³ / ₄ |
| Earnings per share | | | | | |
| Basic | \$.97 | 1.04 | .70 | 1.02 | .79 |
| Diluted | \$.93 | 1.00 | .68 | .98 | .77 |
| Book value per share | \$ 9.74 | 9.91 | 9.18 | 8.55 | 7.76 |
| Price/earnings ratio | 19.49 | 22.25 | 29.96 | 17.35 | 17.86 |
| Price/book value ratio | 1.86 | 2.25 | 2.22 | 1.99 | 1.77 |
| Statistics and ratios | | | | | |
| Gross profit margin | 59.9% | 58.7% | 57.4% | 55.7% | 56.7% |
| Operating profit margin | 7.7% | 9.8% | 7.4% | 11.1% | 9.6% |
| Net profit margin | 4.5% | 6.3% | 4.2% | 6.7% | 5.4% |
| Effective tax rate | 31.0% | 32.0% | 34.0% | 34.9% | 38.4% |
| Long-term debt to capitalization | 18.3% | 17.3% | — | 8.3% | 9.0% |
| Return on average assets | 7.2% | 6.5% | 4.9% | 7.4% | 6.0% |
| Ratio of earnings to fixed charges (1) | 4.10 | 6.70 | 5.66 | 7.51 | 5.82 |
| Supplementary data | | | | | |
| Capital expenditures | \$ 107,468 | 141,950 | 99,356 | 101,946 | 100,639 |
| Depreciation and all amortization | \$ 277,324 | 169,199 | 166,584 | 138,265 | 129,908 |
| Property, plant and equipment, net | \$ 318,825 | 330,355 | 280,603 | 313,545 | 313,240 |
| Cash dividends declared | \$ 46,642 | 42,061 | 41,783 | 34,559 | 28,050 |
| Number of employees | 9,500 | 10,000 | 12,000 | 13,000 | 13,000 |

(1) For purposes of calculating the ratio of earnings to fixed charges, fixed charges include interest, amortization of debt expense and one-third of rentals; earnings available for fixed charges represent earnings before fixed charges and income taxes.

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Chief Executive Officer

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Vice Chairman
Kissinger Associates

Herbert M. Baum
President and Chief Operating Officer

E. Gordon Gee
Chancellor-Elect
Vanderbilt University

Harold P. Gordon
Vice Chairman

Alex Grass
Private Investor

Sylvia Hassenfeld
Former Chairman of the Board
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Committee, Inc.

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Senior Fellow
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Norma T. Pace
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Paper Analytics Associates

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Chairman and Chief Executive Officer
Carl Spielvogel Associates, Inc.

Preston Robert Tisch
Co-Chairman of the Board
Loews Corporation

Alfred J. Verrecchia
Executive Vice President
Global Operations and
Chief Financial Officer

Paul Wolfowitz
Dean, Paul H. Nitze School of Advanced
International Studies
The Johns Hopkins University

EXECUTIVE OFFICERS

Alan G. Hassenfeld
Chairman of the Board and
Chief Executive Officer

Herbert M. Baum
President and
Chief Operating Officer

Harold P. Gordon
Vice Chairman

Alfred J. Verrecchia
Executive Vice President
Global Operations and
Chief Financial Officer

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George B. Volanakis
Sector Head and General Manager,
International Businesses

E. David Wilson
Sector Head and General Manager,
U. S. Games

David D. R. Hargreaves
Senior Vice President and
Deputy Chief Financial Officer

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Senior Vice President and Controller

Barry Nagler
Senior Vice President and General Counsel

Douglas J. Schwinn
Senior Vice President and
Chief Information Officer

Martin R. Trueb
Senior Vice President and Treasurer

Phillip H. Waldoks
Senior Vice President
Corporate Legal Affairs and Secretary

Shareowner Information

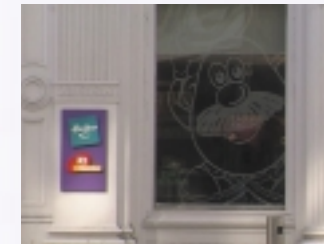
Stock Exchange Information

The Common Stock of Hasbro, Inc. is listed on the New York Stock Exchange and the London Stock Exchange under the symbol HAS.



Annual Meeting

The annual meeting of shareowners will be held at 10:00 A.M. on Wednesday, May 17, 2000 at:
Hasbro, Inc.
32 West 23rd Street
New York, New York 10010



Dividend Reinvestment and Cash Stock Purchase Program

Under this plan, Hasbro shareowners may reinvest their dividends or make optional cash payments towards the purchase of additional shares of common stock. Shareowners wishing information about this plan should contact the Transfer Agent and Registrar.

Transfer Agent and Registrar

Shareowners who wish to change the name or address on their record of stock ownership, report lost certificates, consolidate accounts or make other inquiries relating to stock certificates or the Dividend Reinvestment and Cash Stock Purchase Program should contact:

Fleet National Bank
c/o EquiServe Limited Partnership
Boston Division
Shareholder Services
P.O. Box 8040
Boston, Massachusetts 02266-8040
(781) 575-3400 or (800) 733-5001

Shareowners

As of February 29, 2000, there were approximately 7,800 shareowners of record of Hasbro's common stock.

Investor Information

Securities analysts, investors and others who wish information about Hasbro are invited to contact:

Investor Relations
1027 Newport Avenue
P.O. Box 1059
Pawtucket, Rhode Island 02862-1059
(401) 431-8697
Internet address: <http://www.hasbro.com>



Form 10-K

Hasbro's Annual Report on Form 10-K to the Securities and Exchange Commission provides certain additional information. Shareowners may obtain a copy without charge by writing:

Barry Nagler
Senior Vice President and General Counsel
1027 Newport Avenue
P.O. Box 1059
Pawtucket, Rhode Island 02862-1059



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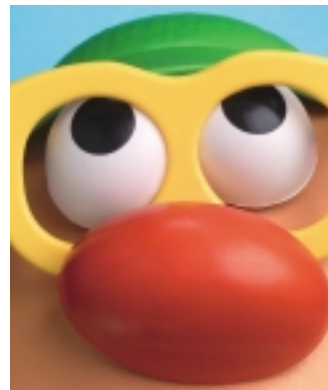
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MAKING THE WORLD SMILE