

# The toy industry: mattel and hasbro



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During the 1700s, a business would produce toys as a secondary product line – for example, cobblers would whittle wooden toys in their downtime.

However, as the country moved into the 19th century, companies were formed expressly for the manufacture and sale of toys. Manufacturers started to experiment with different mediums such as tin and rubber – the mid-1800s saw a surge in new and innovative ideas, such as the classic rocking horse. By 1900, there were over 500 toy manufacturers in the United States, which collectively employed over 4, 000 workers.

The early 20th century and the Great Depression had a major impact on the toy industry. Hundreds of manufacturers went out of business, and those that survived did so by manufacturing cheaper toys and accepting a lower profit margin. Toys were designed and marketed to appeal to a less affluent market and the toy soldier was extremely popular, in part due to the looming war ahead. Two of today's largest and most popular brands, Fisher-Price and Playskool, survived this era by focusing their attention on educational toys for the infant, toddler and pre-school (ITP) market.

The toy industry began to flourish after the end of WW II, which coincided with the advent of television. The television effect had an enormous impact in the demand for toys because companies would now be able to appeal directly to their target market – the child. No longer did the company have to appeal to the parent by marketing educational or career-minded toys (such as Happy Homemaker dolls for young girls). Now companies could reach their target customers through two mediums: 1 – Advertising through commercials during television programs and 2 – Licensing the rights to produce toys based on popular television shows, such as the Mickey Mouse

Show. It was during the 1950s that Mattel Inc. broke the mold in terms of advertising – traditionally, toy companies purchased advertising spots during the Christmas season only. In an aggressive move, Mattel bought one years worth of advertising spots on the Mickey Mouse Show, which proved to be a very successful investment as the advertising improved their sales by 52%, comparatively. After seeing Mattel’s success with this type of campaign, other toy companies quickly followed suit. Children responded extremely well to this type of advertising, and parents wanted to make their children happy.

During the later half of the 20th century, angry parents began to push back against the toy companies. The toy industry was essentially unregulated and many toys were unsafe and promoted violence and aggression. In the overall war against the toy industry, these angry parents won one battle (safety), but lost another (advertising.) In a response to the lobbying by concerned parents, the Federal Government passed the Consumer Product Safety Act in 1972 and updated this act via the Consumer Product Safety Improvement act of 2008. One of the main tenets of the original act was to require toy companies to submit batches of their products to independent laboratories for testing. The Act also established a Consumer Product Safety Commission which retained the authority to pursue recalls on products that were deemed to be unsafe. The Improvement Act of 2008 posed stricter testing requirements and defined new “ unacceptable” levels of certain substances, specifically lead and phthalates. Many industry players considered the Improvement Act to be controversial because it affected many companies and the costs of implementing the increased testing were enough to force

smaller retailers out of business. While an exact number of impacted businesses has not yet been calculated, it is estimated to be in the thousands. The parents had won the safety battle, but they ultimately lost the advertising battle. In 1980, Congress sided with the toy industry and allowed companies the right to freely advertise their products directly to children.

### Current State of the Toy Industry

Mattel, Inc. (Mattel) and Hasbro, Inc. (Hasbro) have emerged as the #1 and #2 players in today's competitive toy industry. Today's toy landscape is extremely competitive and does not suffer from a high level of company/competitor concentration. Per the most recent available data from the U. S Economic Census, the Concentration Ratios for the toy industry have ranged from 35-44 (for the 4 largest companies) over the past 20 years. The Herfindahl-Hirshman Index for the same time period also reflects this level of competition, ranging from 410-527 for the same time period. (See Exhibit 3)

### 5-Forces Analysis

I – Rivalry among established firms: According to the economic data as supplied by the US Census, the toy industry is an extremely competitive market. The industry contains a relatively high number of companies and the four largest companies historically have controlled less than 40% of the market. Due to the fact that there is such a high number of companies, rivalry among competitors is intense – many companies are competing for the same target consumer, whether it be the parent or the child.

Mattel has emerged as the leading manufacturer of children's toys, capturing 12% market share in 2009. Mattel is behind some of the most popular toy brand on today's market - Barbie, American Girl, Fisher-Price, Hot Wheels, and Matchbox. The management of Mattel is fully aware of the intense rivalry of this changing market place, as noted in the 2009 Annual Report, "Competition among the above companies is intensifying due to recent trends towards shorter life cycles for individual toy products, the phenomenon of children outgrowing toys at younger ages, and an increasing use of high technology in toys. In addition, a small number of retailers account for a large portion of all toy sales, control the shelf space from which toys are viewed, and have direct contact with parents and children through in-store purchases, coupons, and print advertisements. Such retailers can and do promote their own private-label toys, facilitate the sale of competitors' toys, and allocate shelf space to one type of toys over another."

II - Risk of entry by potential competitors: The risk of entry by potential competitors is moderate. The toy industry has several barriers to entry - economies of scale, high fixed costs, slow market growth, and a concentration of demanding retailers. However, there is little in the way of government regulations, specific patents, or proprietary knowledge. There are many opportunities for niche markets and with the ability to sell toys via the Internet, access to distribution channels is not an obstacle.

III - Threat of substitutes: The very nature of the toy industry's target market (which is now the child, rather than the parent) has minimized the impact of the threat of substitutes. Anyone with a young child can tell an economist that the threat of substitutes for most toys is low - when a child wants a

particular doll that looks like their favorite Sesame Street character, no substitute on the market will suffice. Parents, in turn, have high demand for educational and developmental toys for which they are not willing to accept substitutes.

IV – Bargaining power of buyers: Toys are generally sold to retailers, who in turn, sell them to the end customer. In the current economic environment, there is a small group of retailers that currently influence the toy market – Walmart, Target, and Toys R Us. For example, these three retailers accounted for 40% of Mattel’s 2009 revenue. This level of buyer concentration means that significant control can be exercised by buyers when price setting. In times of economic recessions, when consumers are spending less of their discretionary income on non-essentials, such as toys, the large retail chains must lower their prices to compete. And the toy industry has no choice but to acquiesce to the buyer power if they want to maintain positive relationship.

V – Bargaining power of suppliers: Raw materials for the toy industry are available from a variety of sources, none of which are particularly concentrated. However, during the past few years, there has been an increase in the use of plastic resin in the toy manufacturing process. A key chemical component of plastic resin is petroleum, therefore oil prices have a direct impact on profits).

Market Leaders – Mattel and Hasbro

The undisputed leaders of today’s toy industry are Mattel (#1) and Hasbro (#2). The two toy giants collectively owned 23% market share, based on <https://assignbuster.com/the-toy-industry-mattel-and-hasbro/>

2009 sales. In the mid 90's, Mattel attempted to purchase Hasbro but was met with resistance from Hasbro's senior management and eventually Mattel's bid was dropped. More rumors of a possible merger circulated in 2005 when both companies experienced significant discounting threats from their major customers, Walmart and Target. However, the rumors and speculation were never founded, and the two toy giants continue to compete against each other.

### Mattel, Inception To Current State

Mattel was started in 1945 by Harold Mattson and Eliot Handler. The company was primarily focused on manufacturing doll-house furniture. Mattson eventually sold his ownership share to Handler and the company went on to manufacture a wide variety of toys. In addition to manufacturing toys, Mattel decided to sponsor the Walt Disney Mickey Mouse Club in 1955, which was a pioneering and very successful marketing step which provided direct access to millions of young potential customers.

The famous Barbie (named after Eliot Handler's daughter) was brought to market in 1959 and the company went public in 1960. After going public, gross sales increased to \$75 million and the famous Hot Wheels line was launched in 1968. Over the next 20 years, there was a series of management and changes in strategy - the Handlers were forcibly removed from management in 1974 and the company proceeded to acquire non-toy business, such as publishing and entertainment (Barnum & Bailey circus). By the 1980s, the company had revenues in excess of \$1 billion, but a net loss of \$93 million. In an effort to recapitalize and avoid bankruptcy, new

management sold all of Mattel's non-toy interests, cut manufacturing capacity by 40% and terminated 22% of its corporate staff.

In 1991, Mattel acquired Fisher-Price, which proved to be instrumental to the success of the company today. The 1990's also brought changes to top management – Jill Barad took over as CEO, ousting John Amerman and his 10 year tenure. Ms. Barad's focus was to add new life to the Barbie brand. Additional key acquisitions during this time were the acquisition of Tyco Toys in 1997 (Matchbox cars and Tickle Me Elmo) and the Pleasant Company, which is now known as American Girl, one of Mattel's most successful brands. Ms. Barad also attempted to streamline operations via a 1999 restructuring, closing several plants and laying off 3,000 employees. d restructuring Mattel in 1999, closing plants and laying off 3,000 workers.

After an unsuccessful journey into the software business, Ms. Barad resigned as CEO and was replaced by Bob Eckert, who is still currently in this position. Under Mr. Eckert's leadership, in 2000 the Fisher-Price subsidiary began to capitalize on its well-known name and announced that it would begin to sell children's apparel and toys on the internet and through direct-mail catalogs. In addition, at this time Mattel began to expand their licensing programs, signing an especially lucrative deal for toys and games based on Barney, TV's most loveable purple dinosaur.

2007 was a challenging year for Mattel as the company was under fire for a series of recalls related to high levels of lead in toys manufactured in China and potentially hazardous small magnets in certain toys. After learning that certain Chinese-made Fisher-Price toys may contain hazardous levels of lead



paint, Mattel recalled one million toys, which included some of Mattel's most popular characters, such as Dora the Explorer, Elmo, and Big Bird. The second recall included 440, 000 die cast toys from the Cars movie and 18 million toys due to potentially

hazardous small magnets included in Polly Pocket, Barbie dolls, and Batman action figures. The third recall, in September 2009, pertained to 775, 000 Barbie accessories that were believed to contain unsafe levels of lead paint. The financial toll of these recalls was extensive - the company estimates the impact related to these recalls to be \$50 million in product returns and related expenses. Additionally, Mattel is anticipating higher legal bills related to class-action suits filed against the company on behalf of parents seeking payment for medical testing for their children. In 2009, Mattel paid a \$2. 3 million civil penalty to settle allegations that they knowingly imported and sold toys that violated a Federal lead paint ban. In a response to the concern and litigation over the lead content in toys, Mattel has agreed to lower the acceptable level of lead in imported toys to 90 parts per million. 600 parts per million is the current Federal standard.

2009 marked Barbie's 50th birthday, an event that Mattel marked with a yearlong celebration. However, Mattel lost its Sesame Street licensing business to Hasbro the same year. As a result of recent financial events - regulatory fines, higher legal bills, increased expenses for product testing, higher materials and labor costs - Mattel raised their prices in June 2009. Management also cut 1, 000 jobs, effectively reducing professional employees by 10%.

In 2009, the company employed 27, 000 employees worldwide and reported gross sales of \$5. 4 billion (see Exhibit 1). Mattel’s major and most recognizable brands are:

1 – Barbie: fashion doll and accessories, Barbie is the figurehead brand for Mattel and one of the most recognizable and controversial brands in the world.

2 – Fisher Price: educational toys for infants and pre-school age children.

3 – American Girl: line of dolls, books, and accessories targeted towards pre-teen girls

#### Hasbro, Inception To Current State

Hasbro was founded in 1923 as by two brothers – Henry and Helal Hassenfeld. The company, then named Hassenfeld Brothers, was originally founded to distribute fabric remnants, but by 1926 they were manufacturing and distributing fabric-covered pencil boxes and pencils. In the 1940s, they branched into the toy industry by introducing fabric-covered boxes that contained nurse and doctor kits. The success of this venture enabled the Hassenfeld Brothers to start a toy division, which made history when it was the first company to use television to promote a toy – Mr. Potato Head, in 1952.

Hassenfeld Brothers quickly expanded and in the early 1960s, it introduced the GI Joe doll, which quickly became it’s best seller. In 1968, the company went public and changed it’s name to Hasbro Industries. The toy division and the pencil division were headed by different family members, who had

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different company visions. These differences caused the company to split in 1980 - the toy division continued to operate under the Hasbro name and the pencil division became a separate corporation.

Stephen Hassenfeld became CEO in 1980 and Hasbro expanded quickly under his management. Mr. S Hassenfeld wanted to pare down the toy offerings, preferring to concentrate efforts on developing a line of toys aimed at specific markets. In order to do this, he made the bold move of reducing the number of product offerings by one-third. During this decade, Hasbro made two key acquisitions - Milton Bradley (a major board game manufacturer) and PlaySkool (a major preschool toy manufacturer); additionally the wildly successful Transformer line of toys was released. Mr. S Hassenfeld died in 1989 and was succeeded as CEO by his brother, Alan Hassenfeld.

In 1996, Hasbro successfully blocked a hostile takeover attempt by Mattel and in 1997 was able to secure an exclusive four year deal to produce all NLF-related toys and games. In an effort to expand it's presences in the high-tech toys niche, Hasbro made several high tech acquisitions in 1998 - Tiger Electronics, rights to 75 Atari home console game titles, MicroProse, and Galoob Toys. Tiger Electronics proved to be a very successful acquisition because is had the " it" toy of the 1998 season - an interactive talking doll named Furby. Hasbro also executed restructuring plans, cutting 20% of it's workforce (2, 400 jobs).

Hasbro has been very successful in it's licensing ventures for movies and other forms of media. The company paid \$600 million for the right to make

the toys for the Star Wars prequels. The return on investment was quite positive, as the sales of Star Wars products contributed almost 20% of Hasbro's 2005 revenue, or \$700 million. One of Hasbro's major competitive hurdles is how to compete with Mattel's Barbie franchise. In order to do so, Hasbro has been licensing additional superheroes – the company has rights to more than 5, 000 Marvel characters, such as Fantastic Four, X-Men, and Captain America. The licensing agreement between Hasbro and Marvel Comics is in effect until 2017. The company also had rights to toy sales for major theater blockbusters, such as Ironman and Transformers, Revenge of the Fallen.

Hasbro scored a major coup by signing a deal with Sesame Workshop to make Sesame Street toys and games for such characters as Elmo, Big Bird, and Cookie Monster. This licensing agreement had been with Mattel for the previous decade. Hasbro plans to bring these new products to market in 2011 through the Playskool unit. Hasbro is also focusing on the digital world of gamers, partnering with Electronic Arts to create video game versions of some of its classic board games. Titles are starting to become available on major platforms, such as gaming consoles (Wii, GameBoy), mobile phones, and PCs.

In 2009, the company employed 5, 800 employees worldwide and reported gross sales of \$4. 1 billion (see Exhibit 2). Hasbro's major and most recognizable brands are:

1 – PlaySkool – infant and preschool

2 – Board Games – classics such as Monopoly, Twister, Battleship, Yahtzee, etc.

3 – Boys/Girls toys – Transformers, GI Joe, My Little Pony, Play-Doh, Nerf

### Advertising and Marketing Strategy

Mattel and Hasbro support their product lines with extensive advertising and consumer promotions, including television and radio commercials, print and internet ads, in-store displays, sweepstakes, and major events focusing on tie-ins with major media events, such as movies. In years that the either Mattel or Hasbro would generate a significant portion of its revenue from products related to a major motion picture release, advertising expense as a percentage of revenue generally decreases, because it does not take the same level of advertising expenses to support these products.

During 2009, 2008, and 2007, Mattel incurred expenses of \$609.8 million (11.2% of net sales), \$719.2 million (12.2% of net sales), and \$708.8 million (11.9% of net sales), respectively, for advertising and promotion. During 2009, 2008, and 2007, Hasbro incurred expenses of \$412.6 million (10.1% of net sales), \$454.6 million (11.3% of net sales), and \$434.7 million (11.3% of net sales), respectively, for advertising and promotion.

Exhibit 1: Mattel Income Statements

Exhibit \_\_\_: Hasbro Financial Statements

Exhibit 2: US Economic Census Industry Concentration Ratios; NAICS Code 339931, Doll and Toy Manufacturing

Year

# of companies

Value of Shipments

Concentration Ratios

Herfindahl-Hirshman Index for 50 largest companies

4 largest companies

8 largest companies

20 largest companies

50 largest companies

2002

865

\$4.05B

36

45

59

75

419

1997

995

\$4. 76B

40

50

62

76

496

1992

894

\$4. 18B

44

56

69

80

612

1987

698

\$3. 38B

43

55

71

84

618

1982

732

\$4. 48B

41

58

76

87

527

1977

754



\$2. 72B

34

47

66

82

Not Avail

1972

618

\$1. 73B

35

49

65

80

Not Avail

Concentration Ratio = percentage of market share owned by the largest 4 (generally accepted) firms in the industry. If the CR is less than 40 (i. e. the top 4 firms own less than 40% of the market), the industry is considered to be very competitive. Conversely, if the CR is higher than 90, this signifies

that one firm controls more than 90% of the market, which is effectively a monopoly.

Herfindahl - Hirschman Index = provides an additional measure of industry concentration. An HHI of less than 1000 signifies a relatively unconcentrated market; between 1000-1800 signifies a moderately concentrated market and above 1800 signifies a highly concentrated market.

Exhibit 3: Mattel, Worldwide Sales of Barbie franchise

<http://online.wsj.com/article/SB125607851547797455.html>

Exhibit 4: Mattel and Hasbro stock price history

Source: yahoo.finance.com