

Assignment Number 1-3

External Analysis

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Doing business in the world of toys and games is anything but child's play. The industry as a whole generated \$21.47 billion in 2009 and \$21.65 billion in 2008 (Riley, 2010). The industry is also fiercely competitive. Any new kid on the block can ride the wave of a fad to riches and fame. The Zhu Zhu Pets were the hot toy of the 2009 Christmas season and filled toymaker Cepia llc.'s stocking with \$70 million in revenue (Kumar, 2010). Toys and games also compete with a very important commodity: attention span. Today's children are spending less time with toys and games. Playthings need to work harder than ever before to fascinate children who are used to being entertained by television and mobile electronic devices like the iPad. To say the least, there are many pressures on companies in the toy business, so how do the top dogs stay on top?

Macro External Environment for the Toy Industry.

Social

Children and "tweens" are spending more time on the internet and social media sites as high-speed internet and mobile devices enter more and more homes. A study released in January 2010 by the Henry J. Kaiser Family Foundation found that young people, aged 8-18, spent seven and a half hours seven days a week consuming media (Music, videos, blogs, social media, etc.) While consuming, they are also multitasking. So they can fit almost eleven hours of media into that seven and a half hours (Rideout, Foehr, & Roberts, 2010). This leaves no time in the day for imagination play with traditional toys and games. The 8-12 consumers constitute approximately 31% of the market (Riley, 2010). Children are also growing up faster as high technology gadgets become commonplace.

Legal

Loose safety standards in Chinese factories caused the massive toy recall of 2007 which involved over 10 million toys that contained unsafe levels of lead and small magnets which, if swallowed, could cause serious injury or even death. This recall not only cost millions of dollars but severely damaged consumer confidence. A problem like this looms over every toy company that uses manufacturing plants in China.

Toy companies fiercely protect their copyrights and patents. This is illustrated in an ongoing court case between Mattel, maker of Barbie dolls, and one of their former toy designers Carter Bryant. In 2008, the Mattel sued a Bryant for selling a doll design, now marketed under the name Bratz, to their rival company MGA. In a long and presumably expensive court case, Mattel was first awarded the rights to the Bratz dolls only to have them taken away in a recent 9th circuit court overturning of the previous judgment. MGA made an estimated \$1 Billion from the Bratz toys in 2005, but in 2009 the toy line only generated \$300 million. Legal fees for MGA are estimated to be around \$100 million dollars and the fight is far from over. Hasbro recently filed suit against Buzz Bee Toys Inc. and Lanyard Toys Inc. to stop them infringing on Nerf and Super Soaker patents. "Hasbro aggressively protects its brands and products and the action we have taken today is part of Hasbro's plans to vigorously pursue companies who misappropriate our intellectual property for their own profit," said Wayne Charness, senior vice president of corporate communications (Chang, 2010).

Sometimes companies can be too aggressive about protecting their copyright. In an interesting and complicated example both Mattel and Hasbro have the rights to the board game Scrabble (Hasbro has rights in North America, Mattel has them everywhere else.) Two India-based brothers and programmers created a free-to-play version of Scrabble on Facebook called

Scrabulous. At the height of its popularity, Scrabulous attracted a half-million players a day. Mattel and Hasbro both sued the Argawalla brothers and forced them to remove the game from Facebook. Hasbro then made a slow and clunky official version bemoaned by fans of Scrabulous. The official version now draws 90,000 players daily. Instead of working with the creators of the knock-off and bringing the game into the fold of officially licensed content, Mattel and Hasbro caused resentment and hard feelings in customers on the world's most popular social network.

Economic

For many years, toy companies have used Chinese factories to manufacture their products. The combination of cheap labor and undervalued currency has been a very attractive recipe for keeping production costs as low as possible. Although as this arrangement as been profitable, it has also made toy companies very susceptible to problems within China itself.

China's up and coming working class is demanding more pay and benefits as China's economy grows. Sometimes these changes are explosive. In November, 2008, a worker riot broke out at a Hasbro factory in Dongguan, China (Foreman, 2008). 80 senior migrant workers, who felt they were being jilted by management on their severance pay, quickly organized a mob of 500 people that overturned a police car, stormed the factory offices, and damaged computers.

Political

China's undervalued currency is a target of U.S. policymakers. Recently, the U.S. House of Representatives Speaker Nancy Pelosi brought up the possibility of a new China currency bill that would give the "... the [Obama] administration leverage in its bilateral and multilateral negotiations with the Chinese government -- so that U.S. businesses and workers have a more

level playing field in world trade.” No one really knows how much this would affect export prices from China, but it is an issue that should remain on the radar.

Technical

Fad toys come and go often and quickly in the marketplace. This cuts into the sales of larger toy companies with legacy toy lines that have been around for years. Toy fads like the Pet Rock, Tamagotchi, Furby, Tickle-Me-Elmo, and Zhu Zhu Pets can be all the rage one Christmas then disappear as quickly as they arrived. Toy companies need to innovate continuously hoping to find that next big breakthrough. At the same time, corporate espionage is widespread in the industry. Company secrets are even more important because you only get one chance to come out with the first “Pet Rock.”

Micro External Environment for the Toy Industry.

Risk of Entry

The toy and game industries are fiercely competitive. The barrier to entry is very low. This allows many new companies, and entrepreneurs, to create products that vie for children’s attention. Also, many well-known brands invest a lot of resources into research and development which allows them to introduce new products all the time. Hasbro, Mattel, BanDai and others compete with each other for product licenses to characters from movies, TV shows, and video games among other media.

Power of Buyers

Toy outlets are very concentrated. For example, five stores, including Wal-Mart, Target, and Toys “R” Us make up 54% of Hasbro’s net revenues (Hasbro inc., 2009). Wal-Mart, Target, and Toys “R” Us also made up 43% of Mattel’s net sales (Datamonitor, 2007). This leaves toy

manufacturers in a very weak bargaining position with its customers. The rise of online sales opens the door for manufacturers to sell directly to the public, but for now retail stores rule.

Power of Suppliers

Most of Hasbro's products rely on basic materials like plastic, paper, and cardboard. Although these commodities are available from a wide range of suppliers, they are susceptible to market prices. Some of these materials contain chemicals (like phthalates and BPA) that might be subject to new federal regulations.

Substitute Products

Because younger and younger children are using high-technology gadgets, toy companies need to compete by making toys with more technology in them. High-tech toys now compete directly with non-toy items such as cell phones, mp3 players, and tablet computers. Diane Debrovner, health and psychology editor of Parents magazine said, "Increasingly, kids in sixth and seventh grade have cell phones, and your child might, depending on your community, be in the minority not to have one." (Flam, 2008) The risk posed to the toy industry by these devices is high. As prices continue to drop on cell phones, and other gadgets, children are adopting them earlier in their lives. These devices offer new games and forms of entertainment sometimes at little or no cost. To create more traditional toys with enough bells and whistles to compete with digital devices costs significantly more to invent and manufacture. As a result, these toys have a much smaller profit margin and need to sell more units to make a profit. Children at different ages have shifted preferences. Young children are expecting more stimulation from their playthings than before to capture and hold their attention. Hasbro calls this phenomenon of kids "Getting older, younger." This threatens everyone in the toy industry because the window toys and games have to make their way into children's lives keeps shrinking.

Toy companies rely on their intellectual properties which they may not be able to protect in countries with loose copyright laws. While not as big of a problem in the United States, piracy is rampant in the emerging economy of China where action figures, toys and DVDs can be easily duplicated and sold at a fraction of the retail price. This poses a great threat to toy companies looking to soften domestic revenue losses by expanding into China.

Rivalry

Respectively, Mattel and Hasbro are the number one and number two, toy and game companies in the United States. Mattel owns the licenses for Barbie, He-Man, Hot Wheels, Matchbox, many Disney properties, Batman and Fisher-Price among others. Hasbro's properties include Star Wars, Mr. Potato Head, Transformers, G.I. Joe, Battleship, Monopoly and more. Both companies fight for shelf space, with each other and every company that makes toys and games, at all of the same stores. Jockeying for position has lowered the profits all of the companies as they compete with each other using lower prices, offer exclusives, and unique feature sets.

Because most toy companies have the majority of its manufacturing done in China, it can only stock as much shelf space as there is available space on large cargo container ships. In 2007, Mattel was number 28, out of the top 50 U.S. importers, with 48,900 TEUs (Twenty-Foot Equivalent Units) (Manufacturing News, 2008). According to The Journal of Commerce's ranking of Top 100 container importers in 2009, Hasbro was number 46 with 24,800 TEUs (Journal of Commerce, 2010). With many companies fighting for the space, especially just before the holiday season, the price per TEU may go up. Shipping costs are also very vulnerable to changes in fuel prices.

Complementors

As toys become more technologically advanced, they use more batteries. According to Energizer Battery, December 21st through the 24th are the biggest days for battery sales of the year (Energizer, 2004). In England, consumers purchase 13 million batteries on those days to power their gifts.

In Role-Playing Games (RPG), a micro-niche of the toys and games industry, many complementors exist. Dungeons and Dragons release a line of books that outlines the rules and basic concepts of the game, lists monsters and gives players a sample adventure to play. As players expand their game they purchase all kinds of items to use during gaming sessions like dice, adventures, miniatures, maps and terrain. Miniatures lead to even more complementors as players purchase paint and brushes to enhance them.

In collectable card games, such as Magic: The Gathering and Pokemon, companies make products similar to those made for baseball cards. Plastic sheets to keep the cards in mint condition or so the cards can be displayed in a collector's album and boxes so the cards can be transported to tournaments.

Toy companies have their work cut out for them. Every facet of their business highlights something to keep their CEO awake at night. Lots of factors could take them off the map from Innovations, big competitors, and inventors tinkering around with the world's next big toy in their garage to people just being bored with their product.

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