Illustration 14.1
What Is the Definition of the Toy Market?

While the answer to this question doesn't seem important, it was quite important in early 1996 in a $5.2 billion bid by the largest toy maker, Mattel, for the second-largest toy maker, Hasbro. Hasbro, fearful of costly legal battles to win government approval of the merger, was hesitant about making the deal.

According to ***The Wall Street Journal,*** Mattel, attempting to convince Hasbro that the FTC and the Justice Department would not find the merger to be anticompetitive, relied heavily on "cutting edge legal theories [that] . . . advocated a broader than traditional definition of the 'toy market,' assumed relative ease of entry for new industry competitors and generally claimed the existence of intense competition despite the huge gap between the second and third largest toy companies."*

Mattel's analysis predicted that the merger would create a firm with a 28 percent share of the $16.3 billion toy market. Hasbro worried that the proposed new firm would have a much larger share and would therefore be blocked by federal antitrust enforcement agencies. According to some observers, Hasbro was walking away from the deal because the company disagreed with Mattel's legal and political risk analysis. Several leading antitrust specialists agreed with Mattel's definition of the toy market. According to them, Mattel was relying "on the claim that video games, children's books and even some sporting goods should be included in any antitrust analysis." Under this scenario, the new company would have a share of 20 percent or less of such an expanded "toy" market. Antitrust experts also said that Mattel could argue that the industry offers relatively easy entry to new competitors. They pointed out that independents are often the ones that come up with surprise hits such as Cabbage Patch Kids. These analysts argued that the new company would have less market power under the expanded market definition, because of more intense competition, than would be the case under the more narrowly defined market.

A former top antitrust enforcer at the Justice Department, who wasn't working for either party, focused on a more reliable indicator of market power than share of the market. Noting that Mattel's expanded market definition seemed to track some of the more recent analyses of some federal antitrust regulators, he said, "To a certain extent there is some substitutability among traditional toys, some electronic games and perhaps other products designed for children of the same age . . . [which] should keep a lid on price increases." He asked rhetorically, "If the price of a particular doll or toy goes up 5 percent, for example, would consumers start buying other things?" Thus his focus was on elasticity and cross-price elasticity as being more reliable indicators of market power than share of a narrowly defined market.

This story illustrates three points. First, in practice, it is often difficult to define a firm's market, especially within a legal framework. Second, a firm's share of a narrowly defined market is generally not a good indicator of its market power. Third, elasticity and cross-price elasticity are better indicators of market power than is market share. It is, after all, the effect of price changes on sales that determines market power.

As a footnote, Hasbro's board rejected the offer and Mattel dropped it on February 2, 1996. Don't feel too sorry for Mattel's top executives, however. The ***WSJ*** noted that Mattel's top four executives "marched off with profits" after they sold stock in their company with an estimated value of $23.9 million.[†]

*"Mattel Practices Theories Preached in Attempt to Secure Bid," ***The Wall Street Journal,*** Jan. 30, 1996.
[†]"Mattel Officers Sold Stock after Hasbro Bid Ended," ***The Wall Street Journal,*** Mar. 6, 1996.