Knockoffs for the Toy Box?

By Dina ElBoghdady
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For the holidays, Michele Hobson wants to buy "fun" and "catchy" toys for her two girls. But the last thing Hobson cares about is the brand name of those toys. After all, her 21/2-year-old daughter can't tell the difference between Barbie and any other fashion doll.

"Even my 9-year-old isn't picky," Hobson said as she strolled the toy aisles of the Wal-Mart in Alexandria. "And for me, as long as the kids like a toy and it keeps them busy, the brand doesn't matter at all."

The nation's largest toy retailers are hoping -- even betting -- that lots of shoppers feel the same way. Lining their shelves more and more are lower-cost versions of heavily advertised brand-name toys, versions that they expect will put more profit into the cut- throat business that toy retailing has become.

Shoppers may well reap the benefit of these lower-cost dolls and toy cars and such, and so might the retailers' bottom lines, at least in the short term. What some industry observers are saying, though, is that the retailers' strategy may ultimately backfire on them and their customers.

The toy business isn't going at it alone. The same strategy has been embraced by many industries for decades, most notably supermarket chains. Even private label toys are not a novelty. Some retailers, such as FAO Schwarz, have offered them for years.

Still, in modern, brand-crazy America, such toys were the exception up until five years ago. But today, they take up about 15 percent of shelf space on average at the nation's top five retail chains -- Wal-Mart, Toys R Us, Target, Kmart and KB Toys, according to a study released this month by the New York investment firm Harris Nesbitt Gerard.

The big five toy chains are going directly to toy factories overseas and ordering custom-designed toys. Some of those toys complement major brand offerings (such as a PT Cruiser car for a Mattel Barbie doll) while others compete (for instance, Wal-Mart's Kid Connection preschool products look like LeapFrog brand items), the study found after scouring the merchandise at different chains.

Because retailers have eliminated the middlemen by dealing directly with factories, they have also eliminated paying for the advertising, research and other costs included in the wholesale price charged by a Mattel or LeapFrog. End result: They build more profit margin into their store-brand toys even though those toys sell at a lower price.

But the more shelf space retailers devote to their own brands, the less space they have left for the better-known manufacturers, said Sean P. McGowan, a managing director at Harris Nesbitt Gerard.

"The retailers are pretty clearly skimming sales from their brand- name suppliers," said McGowan.

Jim Silver, co-publisher of Toy Wishes, describes the situation as "industry Armageddon."

If this trend continues, he said, consumers can expect to see less innovative toys in the future. The in-house brands will cut into the famous makers' sales, forcing manufacturers to cut back on research and development.

"All the retailers do is copy toys that are already out there," Silver said. "They might save consumers 10 cents, but they're killing innovation."

Retailers rarely go head-to-head with big manufacturers on "hot" toys that people ask for by name. Those toys are the most heavily advertised because they attract shoppers. But they also command the lowest retail markups, said John G. Taylor, an industry analyst with Arcadia Investment Corp.

Instead, retailers increasingly rely on selling in-house versions of generic board games -- such as checkers -- or stuffed animals to make up for those lost margins. That's how chains such as Toys R Us stay competitive with discounters such as Wal-Mart, Taylor said. "Without [store brands], a Toys R Us wouldn't be able to compete on price because they wouldn't make money on anything," he said.

But even Wal-Mart is getting aggressive about offering its own toys. Wal-Mart's toy vehicles -- marketed under the Kid Connection name -- take up more shelf space than Mattel's brand, according to a recent study by Funosophy Inc. in Long Beach, Calif. The study also found that private-label toys accounted for 50 percent of total shelf space set aside for large dolls at Wal-Mart, Toys R Us and Target.

Karen Burk, a Wal-Mart spokeswoman, said her company offers 300 Kid Connection toys, not all of them in every store. Burk declined to say how much of Wal-Mart's toy sales are generated by Kid Connection and other Wal-Mart toys, though many analysts estimate it is close to 20 percent.

"Wal-Mart is a brand-oriented company first, and we built the trust of our customers by offering quality well-known brands at everyday low prices," Burk said. But "we do use private-label toys to fill a void in pricing or value."

This week, Toys R Us executives said 20 percent of their U.S. toy sales come from "exclusive" products, compared with 5 percent about five years ago. The company declined to break down how much of that is private-label and how much is well-known merchandise sold only at Toys R Us, such as Cabbage Patch dolls. But the Harris Nesbitt Gerard study estimates the private-label sales at about half.

"We have been upfront with our manufacturers," said Richard Markee, president of Toys R Us Inc. "We don't look at [in-store brands] as taking away opportunities from manufacturers to sell their products."

A decade ago, in-house toys made up about 5 to 10 percent of KB Toys' business, said Tom Alfonsi, the company's senior vice president of product development. Today, that number is closer to 20 percent. In September, KB introduced its own brand of board games, which take up about 20 percent of its games section.

The major toy manufacturers have little to say publicly about the proliferation of in-store brands. But one executive with a major manufacturer called the trend "frustrating."

"Are they our partners, or are they our competitors?" the executive said.

Of course, this kind of arrangement is not unique to the toy industry. One in five products sold today at supermarkets, drugstore chains and mass merchandisers such as Wal-Mart is an in-house brand, according to the Private Label Manufacturers Association.

Sears, Roebuck and Co. established private labels over 100 years ago and to this day relies on its in-house Kenmore and Craftsman labels. Department stores have bulked up their private-label offerings in a quest to differentiate themselves from rival specialty fashion retailers. Macy's, for instance, offers INC in addition to the Liz Claiborne and Jones New York lines most department stores carry.

But Toys R Us, starting in the 1970s, and Wal-Mart, Target and Kmart in the 1980s seemed to turn their backs on private-label toys, the Harris Nesbitt Gerard study said. The big brands, hawked on kiddie TV, were king.

"A significant part of the appeal of these chains, at least regarding toy sales, was that they offered the best-selling brands at lower prices," the study said. "These chains invited price comparisons, because that was one of their strongest advantages."

Once Wal-Mart grew to become the nation's largest toy retailer toward the late 1990s, bumping Toys R Us down to the second slot, some toy retailers tried to compete with it on price.

Today, many of these specialty chain retailers are still trying. Toys R Us, for instance, recently put out its "Big Toy Book" coupons, good through Nov. 22. It also offered a jumbo "Lion King" Simba or Nala (worth $29.99) free to customers who purchased $100 or more of merchandise. The company says the deals will keep coming.

And KB Toys is striving to at least keep pace.

"We do try to stay competitive," said Alfonsi. "But we're not matching price."

Meanwhile, they're all trying to capture market share in an industry that has shown little or no growth for many years. And prospects for the future don't look any better.

Juliet Tamaro of Springfield is largely unaware of this backdrop. All she knows is that she doesn't like to buy expensive baby dolls for her 21/2-year-old because "they end up getting dirty."

At the Alexandria Wal-Mart, where Tamaro is shopping with her daughter, she doesn't have to.

While Disney's "Water Babies Dress Up Snugglers" (a baby doll filled with warm water) sells for $14.96, Wal-Mart's own Li'l Precious "New Born Baby" sells for about half that: $7.47.

But for bigger toy purchases, Tamaro is generally wary of in- house brands. In front of her is the Little Tikes Tender Heart Kitchen for $48.83, and a few feet away is Wal-Mart's Kid Connection Kitchen for $29.88.

The price on the Wal-Mart brand is enticing, she said. "But I wish I could take it out of the box to feel how heavy the plastic is and how it puts up with wear and tear," Tamaro said. "Little Tikes tends to be high-quality." If she has a second child, she doesn't want to have to buy the same thing twice, Tamaro said.

The in-house brands don't even register with Mary Beatson of Potomac, mother of five children ages 5 to 13.

"My children picked out specific brands they want to have," said Beatson, who was shopping with sons Michael, 12, and Robert, 13, at the Toys R Us in Rockville. "So that's what I'm getting."

In the heap of toys she and her boys were carrying were the store's last two Legally Blonde Barbie dolls for two of her girls. She'll go searching for a third one, for her other daughter, soon.