Richard Ivey School of Business
The University of Western Ontario

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THE LEGO GROUP: BUILDING STRATEGY

Paul Bigus wrote this case under the supervision of Professor Darren Meister solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

On February 15, 2011, world-famous toy maker the LEGO Group (LEGO) assembled an internal management team to create a strategic report on LEGO's different product lines and business operations. Over the past two years, numerous threats had emerged against LEGO in the toy industry: the acquisition of Marvel Entertainment by The Walt Disney Company created major implications for valuable toy license agreements; LEGO had lost a long legal battle with major competitor MEGA Brands — maker of MEGA Bloks — with a European Union court decision that removed the LEGO brick trademark; new competition was preparing to enter the marketplace from Hasbro — the second-largest toy maker in the world — with the company launching a new rival product line called Kre-O. It was critical for the management team to identify where to expand LEGO's product lines and business operations in order to develop a competitive strategy to continue the organization's financial success and dominance in the building toy market.

COMPANY HISTORY[1]

LEGO first began during the Great Depression in 1932, when Danish carpenter Ole Kirk Kristiansen and his sons started making wooden toys after the demand for building houses and furniture declined. Some of the first toys they made included yo-yos, wooden blocks, pull-along animals and wooden vehicles. Kristiansen believed that "only the best is good enough" in manufacturing children's toys; this motto was so important to him that it was carved on a sign and hung on the workshop wall to serve as a reminder to always produce top-quality products. He used the highest quality materials and workmanship to produce toys that were designed to last through years of play. In 1934, the company name LEGO was created when Kristiansen held a friendly competition among the workshop employees to help name the company, with a bottle of wine as the prize. Kristiansen won the competition himself by creatively combining the first two letters of the Danish words *leg* and *godt*, meaning "play well," to form the name LEGO, which also meant "I put together" in Latin. In 1942, disaster hit the small company of only 12 employees as the entire workshop burned to the ground. Not willing to quit, Kristiansen rebuilt the factory and painstakingly remade all of the lost designs from memory in order to keep the company going.

[1] *Daniel Lipkowitz, The LEGO Book, Dorling Kindersley Publishing, New York, 2009, pp.10-49.*

Following the end of World War II, LEGO became the first company in Denmark to purchase a plastic-injection molding machine in 1947; however, the new machine came at a high cost, requiring the company to risk a large portion of revenues and face the additional financial risk of plastic toys being expensive to manufacture. With the acquisition of the new machine, one of the first plastic toys to be created by LEGO was a baby rattle that was shaped like a fish. It did not take long before the investment in the machine proved to be a success, as LEGO quickly expanded its business operations to produce over 200 varieties of plastic and wooden toys. Using the new technology, the first plastic LEGO bricks — named Automatic Binding Bricks — were created and sold in sets in 1949; however, this name did not last long as it was changed to LEGO Bricks in 1953, with the addition of the LEGO name being molded onto every brick manufactured.

Godtfred Kirk Christiansen, one of Kristiansen's sons, had grown up with the family company and eventually became the junior managing director of LEGO. Upon returning from a toy fair in 1954, Godtfred and a co-worker had a conversation during which they realized that no system existed to connect different products or items in the toy industry. To Godtfred this represented a key opportunity to design a new structured system of toy products, selecting the LEGO brick as the best company product with which to create what he referred to as the "LEGO System of Play." The idea behind the LEGO System of Play was that each and every LEGO brick should connect to each other — not just within one set but across multiple sets. A 'Town Plan' series with 28 building sets and eight vehicle sets was developed and released. The strategy was simple but important: each additional LEGO set obtained by a child increased the amount of LEGO bricks that the child had available to build with, thus more sets equalled more creative opportunities. The different Town Plan models included LEGO bricks as well as various plastic people, trees, vehicles and road signs. In order to help market the product to children and parents, the sets were creatively designed in collaboration with the Danish Road Safety Council to help teach children about traffic safety. Godtfred commented on the LEGO System of Play: "Our idea is to create a toy that prepares the child for life, appeals to the imagination and develops the creative urge and joy of creation that are the driving force in every human being."[2]

The development of the LEGO System of Play lead Godtfred to realize that improvements were needed to the LEGO brick design so that bricks could lock together firmly yet come apart easily: he referred to this as the brick's 'clutch power.' Finding the correct clutch power would allow for more stable and secure LEGO brick models that would not easily fall apart. With such a brick design and building capability, Godtfred believed that it would be possible to create anything out of LEGO bricks. In attempting to find such a design, LEGO experimented with different plastic-injection molding designs that included various shapes and connection methods before finally selecting a brick design that added hollow connection tubes to the bottom of the existing LEGO brick design. With the improved design, when two bricks were placed directly on top of each other, the hollow tubes on the underside of the top brick connected firmly between the existing circular studs on the top of the bottom brick, providing the perfect amount of clutch power. Pleased with the results, Godtfred submitted an application in Denmark on January 28, 1958, to officially patent the improved LEGO brick design. The year signified a historical event for LEGO; unfortunately, it also represented a major loss with the death of LEGO founder Kristiansen. This left Godtfred in charge of the company, which had grown to 140 employees.

The 1960s

During the 1960s, LEGO had experienced rapid success with the new brick design, expanding sales to many European countries as well as new markets in the United States, Canada, Japan and Australia. After

[2] *Daniel Lipkowitz, The LEGO Book, Dorling Kindersley Publishing, New York, 2009, pp.18.*

another fire destroyed the workshop where LEGO wooden toys were made, the company decided to stop selling wooden toys altogether and focus completely on the LEGO brick and System of Play. By 1967, more than 18 million LEGO sets had been sold in 42 different countries, with LEGO employing over 600 people. The company had also expanded the LEGO brick design to include over 200 different shapes such as wheels, flat bricks, train tracks, windows, doors and flags; this added further detail and allowed more creative possibilities to the System of Play sets. In an effort to help children and parents with the variety of bricks and the increased complexity of building sets, LEGO introduced building instructions as a standard feature of each building set. The increased success and popularity of LEGO around the world lead to the development of the first LEGOLAND theme park, opening in LEGO's home country of Denmark in 1968. During the same year, LEGO continued to experiment with new products, introducing a brick called DUPLO which was eight times the size of an original LEGO brick and safe for children under five.

The 1970s

By 1975, LEGO had grown to over 2,500 employees and continued to develop new innovative sets that included a series for girls involving doll houses and furniture, ships made out of LEGO that could float in water and a LEGO Technic series which created models with mechanical moving parts. In 1978, LEGO continued to transform the building toy industry by introducing the first miniature figures with painted faces and movable arms and legs. LEGO incorporated the mini-figures into the launch of three new play themes: LEGO Castle featuring medieval knights and castle sets, LEGO Town featuring city characters and modern buildings and LEGO Space featuring astronauts and spacecraft. The company changed leadership again in 1979, when third-generation Kjeld Kirk Kristiansen, Godtfred's son, became president and chief executive officer (CEO) of LEGO.

The 1980s

With LEGO celebrating its 50th anniversary in 1982, the company continued to expand operations, launching an educational line for schools as well as a DUPLO Baby series. Over the years, LEGO continued to experiment by combining LEGO bricks with technology, introducing a Light & Sound series in addition to a LEGO Technic series — that allowed motors to be controlled by a computer — in 1986. Success of the LEGO play themes continued with new Castle, City and Space sets being released each year, in addition to a new LEGO Pirates theme being launched. With many children building their own LEGO creations without instructions, buckets full of assorted LEGO bricks were also made available to purchase for creative building. LEGO had become established around the world as the building toy of choice, with many fan clubs being created and building competitions taking place. To stay connected to an ever-growing market, a LEGO magazine was also made available in many countries to keep members up to date on new product information and creative building ideas.

The 1990s

LEGO had grown to become one of the top 10 largest toy manufactures in the world by 1990. Global operations employed over 7,000 people and included over 1,000 injection molding machines in five LEGO factories. LEGO utilized its strong brand image by opening LEGO stores to exclusively sell LEGO products and merchandise. The use of television advertising also helped the company to build a familiar "LEGO Maniac" slogan. With the increase of home computer use and the rise of the Internet, LEGO launched the official LEGO website (www.LEGO.com) in 1996. Following soon after in 1997,

LEGO expanded into a new business area with the release the first-ever LEGO computer game. The combination of LEGO and computers continued with the LEGO MINDSTORMS line, which allowed users to build and control complex sets with the use of desktop computers and remote controls.

LEGO also diversified its product line by launching many new creative play themes such as LEGO Western, LEGO Adventurers, LEGO Aquazone, LEGO Iceplanet, LEGO Time Cruisers and LEGO Space Insectoids. The company had even created a LEGO brick vacuum device to help children do their least-favourite LEGO activity — picking up the bricks. LEGO advanced again in 1999, as for the first time the company acquired the licensed rights to famous movies and children themes, which lead to the launch of LEGO Star Wars and DUPLO Winnie the Pooh product lines. Combining Star Wars licensed property with LEGO bricks allowed for constructible sets to be created, featuring various well-known characters and vehicles from the widely-popular franchise films. The LEGO Star Wars theme was a huge success, quickly developing into one of LEGO's most profitable product lines.

2000 and Beyond

Following the success of LEGO Star Wars, other popular licensed rights were obtained for new product lines. Harry Potter, Spiderman, Batman, Indiana Jones and SpongeBob SquarePants were all developed into LEGO series sets. Licensed rights were also obtained for DUPLO sets including Bob the Builder, Dora the Explorer and Disney themes. The licensed agreements did not stop there as LEGO viewed professional sports as new opportunities, subsequently launching series sets with LEGO NBA Basketball, LEGO NHL Hockey and LEGO Soccer. Lego also continued to develop products internally, offering new play themes such as LEGO Knights' Kingdom, LEGO Alpha Team, LEGO Bionicle, LEGO Discovery, LEGO Clikits Jewelry, LEGO Studios, LEGO Mars Mission and LEGO Exo-Force. As LEGO was also popular with many adults, special edition sets were created for advanced LEGO builders and collectors, featuring such famous structures as the Statue of Liberty, Taj Mahal, Eiffel Tower and the Star Wars Death Star. Some sets proved to be more successful than others; as a result, some product lines were only sold for a few years before being discontinued in order to free valuable shelf space, production and advertising resources to produce LEGO sets that were in high demand.

With the successful acquisition of many licensed rights, LEGO partnered with video game design companies to develop video games for both computers and video game consoles: this resulted in over 30 LEGO video games being released between 1997 and 2009, featuring the popular LEGO licensed product lines of Harry Potter, Batman, Indiana Jones and Star Wars. LEGO had also developed video games based on its own successful product lines and themes. Overall, many of the video games were highly popular with both children and adult age groups, as they featured LEGO characters and famous movie storylines to play and explore in LEGO-designed environments. At a time when many video games were seen as too violent — with content inappropriate for children — LEGO provided non-violent video games with content that parents could trust.

LEGO continued to expand beyond traditional video games to develop a virtual online LEGO Universe in 2010. After paying online to register, players could design their own personalized LEGO mini-figures to be used to explore online environments and interact with other online players. LEGO was also constantly updating and improving the LEGO website, which was receiving over four million visitors per month from over 200 countries by 2003. All LEGO items were made available to purchase online, and the website also provided interactive games, animated videos and comics. One of the most popular additions to the LEGO website was the introduction of software called LEGO Digital Designer: this allowed a user to design a LEGO set online, using the enormous catalog of LEGO bricks available. After users finished building their own personal designs, the site would automatically calculate the cost for the materials,

providing users with the option to buy their unique creations. If purchased, LEGO would package the physical bricks needed to build the online design and ship them directly to the user's home. Users could also share their designs online, with contests taking place from which winning designs were turned into official LEGO sets.

THE FIRST TIME MANAGEMENT SAVED THE COMPANY[3]

The threats in the toy industry did not represent the first time LEGO management had faced serious issues. Between 1998 and 2004, the company had lost money four out of seven years. Revenues had dropped 30 per cent in 2003, and continued to fall another 10 per cent in 2004. Problems existed not with the LEGO products but behind the scenes in how the company manufactured and distributed LEGO around the world. Years of continuous growth added layers of complexity to LEGO's operations. Knowing that the company needed to change directions, Kjeld stepped down as company CEO in 2004. He was replaced by Jorgen Vig Knudstorp, who had started at LEGO as the director of strategic development in 2001. In his first actions as CEO, Knudstorp assembled a leadership team of senior executives and managers to start analyzing every part of LEGO's supply chain operations as a whole: this included everything from new product development to materials sourcing, production and distribution.

The leadership team discovered that over the years, as new products represented a larger amount of annual revenues, newer-generation LEGO sets had become more elaborate while providing less profit in return. Product designers were creating new sets without giving full consideration to the costs of materials or production: this resulted in LEGO dealing with over 11,000 suppliers, as designers often selected their own vendors. Not considering production costs resulted in serious waste. If a designer created a new brick or selected a rare colour, manufacturing would often be left with extra materials or costly resin colours that would never be used again. Inefficiencies were also revealed from the poor organization of LEGO's plastic-injection molding machines, with each one capable of producing every type of LEGO brick: this required costly retooling and created long downtimes, translating into production facilities only operating at 70 per cent of capacity. Upon producing a finished product, the leadership team traced additional high costs to distribution operations. Logistics represented a web of 26 different providers that shipped products from multi-levelled distribution networks: this created a backlog of orders and inefficiencies in inventory levels. The leadership team continued to uncover damaging business practices at the final retail level. Overall, LEGO was spending the same amount of time dealing with thousands of smaller independent stores that represented one-third of revenues as it did with 200 larger chain and big box stores that generated two-thirds of revenues. Smaller stores also added extra costs for LEGO in shipping, labour and inventory, as they often ordered less than a full carton of product. In turn, the disproportionate amount of time with chain and big box stores equalled inaccurate forecasting and inventory shortages that decreased sales.

In order to make LEGO profitable again, the leadership team introduced numerous changes across the organization. Cost-saving measures were found by cutting the selection of LEGO brick colours in half, while also reducing the number of different mini-figures available. The production cost for each individual LEGO brick shape helped identify and reduce expensive items: this resulted in an 80 per cent reduction in the amount of suppliers needed. With better production costs, designers could be shown the impact of using existing brick shapes compared to creating new molds and colours. Further down the supply chain, the leadership team increased production capacity by assigning certain machines to make only specific LEGO bricks on scheduled production cycles: this reduced the amount of downtime and

[3] *Keith Oliver, Edouard Samakh and Peter Heckmann, "Rebuilding Lego, Brick by Brick," Strategy and Business, August 29, 2007, www.strategy-business.com/article/07306?gko=99ab7, accessed on August 27, 2011.*

costly retooling for each machine. The leadership team also realized that revenue could increase by moving more inventory; therefore, using greater economies of scale they reduced the number of logistic suppliers from 26 to four, improving structure and communication. Smaller distribution centres were replaced by larger hub centres that were strategically located closer to retailers, providing better control over inventory and fewer stock shortages. Due to the contrast in revenue between small and large retailers, changes were introduced to create value and optimize sales: discounts were offered to smaller stores in exchange for placing orders early, and LEGO would no longer ship cartons that were not full. In order to maximize business opportunities with large chain stores and big box retailers, LEGO worked closely to provide joint forecasting, inventory management and marketing support.

The significant changes to design, production, distribution and sales resulted in LEGO increasing its inventory turnover by 12 per cent in 2005, earning a profit of $72 million. This continued with an inventory turnover increase of 11 per cent in 2006, as well as profits increasing by 240 per cent. Knudstorp's leadership had successfully modernized LEGO's business operations while placing his mark on the company. He commented on the company's progress: "It has allowed us to again focus on developing the business."

LEGO IN 2010

As of 2010, LEGO remained a privately-held company by the Kirk Kristiansen family. Annual sales reached an all-time high at DKK16.014 billion (Danish kroner), equaling over US$3.7 billion (see Exhibit 1).[4] Overall, the company's strongest-selling product lines were LEGO Star Wars, LEGO City and LEGO DUPLO. The high sales figures translated into seven LEGO sets being sold each second around the world.

With over 9,000 employees, LEGO had grown to become the fourth-largest toy manufacturer in the world.[5] The company had developed a global brand that spread across numerous business operations (see Exhibit 2). As a household name and icon in the toy industry, LEGO had received the distinction of being named 'Toy of the Century' by the British Association for Toy Retailers.[6] Since first starting to manufacture LEGO bricks back in 1949, the company had produced over 400 billion bricks, with 19 billion new bricks being made each year — translating to over two million bricks made every hour, or 36,000 each minute.[7] Starting with one patented brick design in 1958, over the span of 50 years LEGO had developed over 2,400 different brick shapes, which were available in 53 different colors.

The LEGO mission stated, "Our ultimate purpose is to inspire and develop children to think creatively, reason systematically and release the potential to shape their own future — experiencing the endless human possibility"[8], such a vision could be started with a handful of LEGO, requiring just six original shaped LEGO bricks to build over 915 million different creations.[9]

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[4] *Andrew Couts, "Lego Systems' sales surpassed $1 billion mark in 2010," Digital Trends, February 14, 2011, www.digitaltrends.com/gaming/lego-systems-sales-surpassed-1-billion-mark-in-2010/, accessed on August 27, 2011.*

[5] *"LEGO 2010 Annual Report," LEGO, 2011, http://cache.lego.com/upload/contentTemplating/AboutUsFactsAndFiguresContent/otherfiles/downloadE994290D230BFB0E2A914F4DC3B6531C.pdf, accessed on August 27, 2011*

[6] *Daniel Lipkowitz, The LEGO Book, Dorling Kindersley Publishing, New York, 2009, pp.30.*

[7] *Jesus Diaz, "LEGO Brick Timeline: 50 Years of Building Frenzy and Curiosities," Gizmodo, January 28, 2008, http://gizmodo.com/349509/lego-brick-timeline-50-years-of-building-frenzy-and-curiosities, accessed on August 27, 2011.*

[8] *"Mission and Vision," LEGO, 2011, http://aboutus.lego.com/en-us/group/vision.aspx, accessed on August 27,2011.*

[9] *Daniel Lipkowitz, The LEGO Book, Dorling Kindersley Publishing, New York, 2009, pp.7.*

COMPETITION

Over a span of 50 years selling plastic bricks LEGO had faced a variety of competitors, as other companies entered the building toy market hoping to capitalize on LEGO's success. Some companies introduced products based on their own unique design: one example was introduced by toy company Fisher Price, with a plastic construction toy called Construx. It used plastic beams and connector nuts to form different structures, but only lasted in production from 1983-1988.[10] Another attempt was seen as a new company entered the building toy market in 1992, introducing a product called K'NEX that used flat plastic gear shapes and thin straw-shaped beams to build different designs.[11]

Some companies introduced plastic brick products that were compatible with the LEGO brick design: this meant that competitors' bricks fit together and could be built with LEGO bricks. Toy manufacturer TYCO introduced TYCO Super Blocks in 1984, with a plastic brick design that was almost identical to LEGO bricks.[12] In addition, TYCO also made reference to LEGO in its advertising, communicating to consumers that TYCO Super Blocks connected to LEGO, providing slogans such as, "If you can't tell the difference, why pay the difference."[13] In response, LEGO launched a lawsuit that lasted four years (1984-1988); the outcome was LEGO being successful in forcing the removal of the advertisements and product reference; however, the U.S. Supreme Court denied LEGO's claim on the building block design as the LEGO patent expired in 1988.[14]

Upon the LEGO plastic brick design patent expiring in 1988, the barriers of competition were lowered in the building toy market.[15] In 1991, Canadian toy manufacturer MEGA Brands, which had been selling plastic brick building products called MEGA Bloks since 1984, introduced a smaller-sized line of MEGA Bloks that were compatible with LEGO bricks.[16] By 2003, MEGA Bloks had seen 17 straight years of sales growth with annual revenue of over US$188 million to become the world's second-largest building toy producer behind LEGO.[17] MEGA Bloks continued to quickly expand to different countries around the world. In 2010, MEGA Bloks had developed successful product lines that included license agreements with the popular HALO video game franchise, Marvel Comics, Disney, Thomas the Train, Hello Kitty, Nickleodeon and Caterpillar Construction Equipment.[18] Although MEGA Bloks had significantly smaller sales with annual revenue of over US$368 million, it represented the largest competition to LEGO.[19] It had also proved that other companies could carve out a percentage of the building toy market, with

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[10] *"Construx Main Index," This Old Toy, 2007, www.thisoldtoy.com/fisher-price/dept-7-playsets/f-construx/a-construx-index.html, accessed on August 27, 2011.*
[11] *"About K'NEX," K'NEX, 2011, www.knex.com/About_KNEX/, accessed on August 27, 2011.*
[12] *"TYCO Super Blocks Resource," Tony Cook's HO-Scale Trains Resource, 2011, www.ho-scaletrains.net/tycosuperblocks/index.html, accessed on August 27, 2011.*
[13] *Barbara Demick, "Judge Blocks Tyco Ads Claiming Blicks Are Like Lego's," The Philadelphia Inquirer, September 2, 1987, http://articles.philly.com/1987-09-02/business/26207754_1_tyco-toys-lego-systems-plastic-bricks, accessed on August 27, 2011.*
[14] *"Tyco wins lawsuit over Lego," HighBeam Research, May 6, 1988, www.highbeam.com/doc/1G1-6653339.html, accessed on August 27, 2011.*
[15] *"Patents that changed the world: Lego," New Legal Review, June 23, 2010, www.cpaglobal.com/newlegalreview/widgets/notes_quotes/more/3123/patents_that_changed_the_world_lego, accessed on August 27, 2011.*
[16] *"Mega Bloks, Inc.," Funding Universe, 2011, www.fundinguniverse.com/company-histories/Mega-Bloks-Inc-Company-History.html, accessed on August 27, 2011.*
[17] *Ibid.*
[18] *"Shop," MEGA Bloks, 2011, www.megabloks.com/Shop/MEGA_Bloks/, accessed on August 27, 2011.*
[19] *"MEGA Brands Inc.: Consolidated Financial Statements December 31, 2010 and 2009," a PricewaterhouseCoopers report, March 16, 2011, MEGA Brands, www.megabrands.com/media/pdf/corpo/en/reports/Financial_Statements_2010-2009.pdf, accessed on August 27, 2011.*

MEGA Bloks management estimating that the company had a 25 per cent share of the North American building toy market and a 12 per cent share of the international building toy market.[20]

NEW BUSINESS THREATS

Over the past two years, LEGO had faced new threats emerging in the toy industry from company acquisitions, court battles and new product competition.

Company Acquisitions

In a strategic move to strengthen its position in the global entertainment industry, the Walt Disney Company (Disney) acquired Marvel Entertainment (Marvel) for US$4 billion in 2009.[21] This provided Disney with control over Marvel's vast catalogue of over 5,000 comic book characters to be used in future publishing, movie production and licensing operations. Movies based on comic book characters had proven to be extremely successful and profitable in the film industry, with Spider-Man earning over US$821 million in 2002,[22] and The Dark Knight earning over US$1 billion in 2008.[23] On top of producing massive movie revenues, comic book characters also generated huge revenues in the toy industry with the Spider-Man film generating over US$100 million in related toy sales in 2002.[24] Mattel and Hasbro were the two largest toy manufactures in the world. Mattel had the highest revenue of any toy company with US$5.8 billion in 2010.[25] It manufactured popular products such as Hot Wheels and Barbie, as well as a large selection of toys based on licensed rights. Behind Mattel but still significant in size, Hasbro operated as the world's second-largest toy maker with a revenue of US$4 billion in 2010.[26] The company produced many long-running successful toy products including Transformers, Mr. Potato Head, Play-Doh and Board Games, in addition to licensed toy products.

Although licensing arrangements often varied, many involved a foundation in which the licensee toy company paid the licensor a large advance of money. This advance guaranteed the licensor a large profit regardless of the licensee successfully selling its product; however, the licensee would often also be required to pay the licensor a percentage of the net sales for a licensed product, called a royalty. Licensing agreements also specified numerous details including the amount of time a licensee could produce a product, the type of products to be created and in which countries the products could be sold. The acquisition of Marvel by Disney represented a significant move, as it placed a large amount of entertainment licensing under the control of one organization.

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[20] *"MEGA Bloks Inc.," Industry Today, 2010, www.usitoday.com/article_view.asp?ArticleID=1495, accessed on August 27, 2011.*

[21] *"Disney Completes Marvel Acquisition," Marvel, December 31, 2009, http://marvel.com/news/story/10809/disney_completes_marvel_acquisition, accessed on August 27, 2011*

[22] *"Box Office History for Spider-Man Movies," The Numbers, 2011, http://www.the-numbers.com/movies/series/SpiderMan.php, accessed on August 27, 2011.*

[23] *"The Dark Knight," The Numbers, 2011, http://www.the-numbers.com/movies/2008/BATM2.php, accessed on August 27, 2011.*

[24] *"Box Office History for Spider-Man Movies," The Numbers, 2011, http://www.the-numbers.com/movies/series/SpiderMan.php, accessed on August 27, 2011.*

[25] *"Mattel 2010 Annual Report," Mattel, 2011,http://corporate.mattel.com/annualreport2010/pdfs/2010%20Mattel%20Annual%20Report(Bookmarked).pdf, accessed on August 27, 2011.*

[26] *"Hasbro Annual Report 2010," Hasbro, 2011,http://investor.hasbro.com/annuals.cfm, accessed on August 27, 2011.*

Mattel, Hasbro and LEGO all had individual licensing agreements with Disney to produce toys; however, Disney had a long and favourable history of licensing toys with Mattel. Hasbro on the other hand had an existing license agreement to produce Marvel toys and games until 2017.[27] This created speculation in the toy industry as to which direction Disney would proceed in with future toy licensing agreements. Disney Chief Financial Officer Tom Staggs commented on this topic to the media: "As many of these deals conclude over time, we will have the flexibility to either bring them in-house or pursue third-party licensing agreements depending on how we feel we can create the most value."[28]

Court Battle

LEGO had also been facing competition in the courtroom. In 1999, LEGO registered its classic eight-stud plastic brick shape as a trademark with the European Union, causing objection from rival competitor MEGA Brands. LEGO argued that its brick shape was distinctive and that consumers were often misled, believing that they were purchasing a LEGO product even when viewing a different company name on the box. The result was an 11-year court battle that came to a final decision in September 2010. The European Court of Justice ruled in favour of MEGA Brands, stating that shapes used for a technical result did not qualify for a trademark, thus revoking the LEGO brick trademark.[29] This decision represented a major loss for LEGO. The company still held trademarks with the LEGO logo and popular mini-figure, but opportunities and business conditions existed for competition to increase.

New Competition

In 2011, new competition was set to emerge as Hasbro was planning to launch a new building block line called Kre-O that would be compatible with LEGO bricks. Although many different plastic brick building toys had been launched to compete with LEGO over the past 50 years, most did not succeed and eventually became discontinued; however, this product had serious threat potential due to the size and brand power of Hasbro. The new Kre-O line was set to be released in the spring of 2011, with the introductory Kre-O product line featuring the popular Transformers characters. Each set would include two sets of instructions that would allow builders to create a vehicle and a robot with the same building pieces. The launch was designed to take advantage of the release of the third installment in the blockbuster Transformers movie franchise, *Transformers: Dark of the Moon*. Hasbro was hoping to tap into a licensed theme in the building toy market that had not been used before. The Transformers Kre-O line was scheduled to launch with 12 sets, with Hasbro planning to release additional product lines soon after.[30]

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[27] *Aarthi Sivaraman, "Disney-Marvel deal casts web of issues for toymakers," Reuters, August 31, 2009, www.reuters.com/article/2009/08/31/us-hasbro-analysis-sb-idUSTRE57U63C20090831, accessed on August 27, 2011.*

[28] *Ibid.*

[29] *Sean Farrell, "Lego loses 11-year trademark battle," The Telegraph, September 14, 2010, www.telegraph.co.uk/finance/newsbysector/retailandconsumer/8002268/Lego-loses-11-year-trademark-battle.html, accessed on August 27, 2011.*

[30] *Mark Lennihan, "Hasbro pushes into Lego's land with new blocks," USA TODAY, February 12, 2011, http://www.usatoday.com/money/companies/2011-02-12-hasbro-transformers_N.htm, accessed on August 27, 2011.*

FUTURE STRATEGY

Global toy sales represented over US$83.3 billion in 2010.[31] One of the fastest-growing categories was building sets, with an increase of 13 per cent in 2010.[32] The future in the building toy market held both opportunity and uncertainty, with new threats emerging from increased control over licensing agreements, loss of trademark protection and competition from new and existing sources. It was important for the LEGO management team to identify where to expand current product lines in order to help the company formulate a strategy to ensure that LEGO maintained market dominance in the building toy market and financial success in the years ahead.

[31] *"Global Toy Sales in 2010 Increased by Nearly 5%, NPD Reports," International Council of Toy industries, June 27, 2011. http://www.toy-icti.org/news/globaltoysalesin2010.html, accessed on August 27, 2011.*

[32] *Mae Anderson, "Hasbro to challenge Legos with 'Transformers,'" Msnbc.com, February 13, 2011, www.msnbc.msn.com/id/41561886/ns/business-consumer_news/t/hasbro-challenge-legos-transformers/, accessed on August 27, 2011.*

Exhibit 1

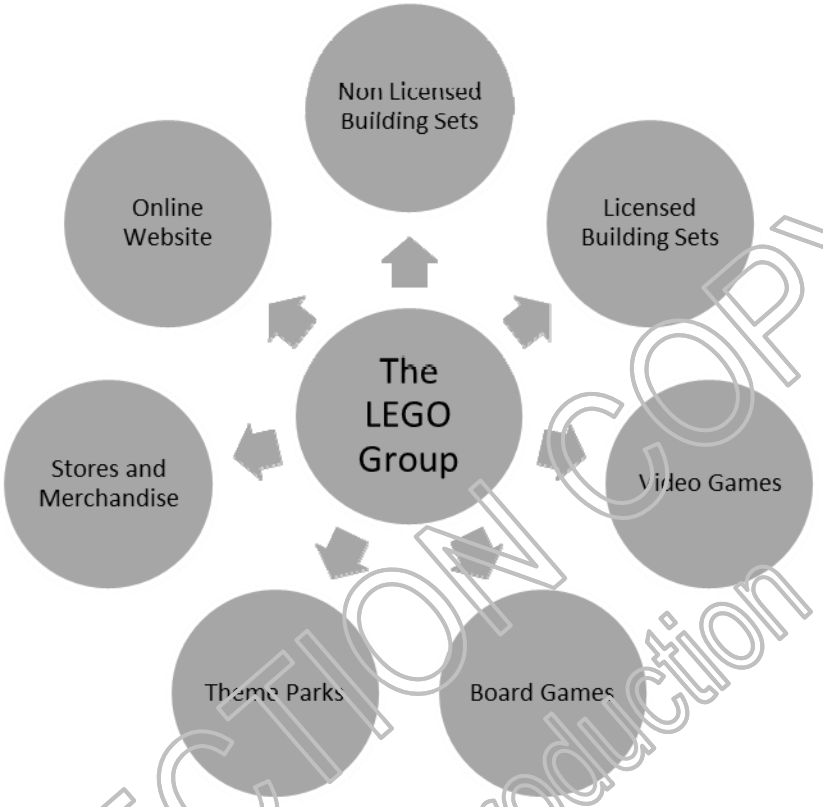
FINANCIAL HIGHLIGHTS
(in millions of DKK)

	2010	2009	2008	2007	2006
Income Statement:					
Revenue	16,014	11,661	9,526	8,027	7,798
Expenses	(10,899)	(8,659)	(7,522)	(6,556)	(6,393)
Operating profit before special items	5,115	3,002	2,004	1,471	1,405
Special items	(142)	(100)	96	(22)	(80)
Financial income and expenses	(84)	(15)	(248)	(35)	(44)
Profit before income tax	4,889	2,887	1,852	1,414	1,281
Net profit for the year	3,718	2,204	1,352	1,028	1,290
Balance Sheet:					
Total assets	10,972	7,788	6,496	6,009	6,907
Equity	5,473	3,291	2,066	1,679	1,191
Liabilities	5,499	4,497	4,430	4,330	5,716
Cash Flow Statement:					
Cash flows from operating activities	3,744	2,712	1,954	1,033	1,157
Investment in property, plant and equipment	1,077	1,042	368	399	316
Investment in intangible assets	123	216	75	34	-
Cash flows from financing activities	(3,477)	(906)	(1,682)	(467)	597
Total cash flows	(871)	558	128	592	1,925
Employees:					
Average number (full-time)	8,365	7,286	5,388	4,199	4,908
Financial ratios (in %):					
Gross margin	72.5	70.3	66.8	65.0	64.9
Operating margin (ROS)	31.1	24.9	22.0	18.1	17.0
Net profit margin	23.2	18.9	14.2	12.8	16.5
Return on equity (ROE)	84.8	82.3	72.2	71.6	147.1
Return on invested capital (ROIC I)	161.2	139.5	101.8	69.7	63.6
Return on invested capital (ROIC II)	157.9	138.0	113.8	77.1	67.4
Equity ratio	49.9	42.3	31.8	27.9	17.2
Equity ratio	49.9	42.3	39.5	46.2	33.2

Source: The Lego Group: Annual Report 2010," LEGO, 2011, http://cache.lego.com/upload/contentTemplating/AboutUsFactsAndFiguresContent/otherfiles/downloadE994290D230BFB0E2A914F4DC3B6531C.pdf, accessed on August 27, 2011.

Exhibit 2

BUSINESS OPERATIONS (2010)



Source: LEGO, 2011, http://www.lego.com/en-us/default.aspx, accessed on August 27, 2011.