

## CASE ANALYSIS

### Brick by Brick: Inside LEGO

#### Toy Industry

For starters, what is a “toy” in this analysis? Solely for the sake of consistency, a “toy” is defined as a “an object for a child to play with, typically a model or miniature replica of something,” according to Google Definitions. Thus, technology, games, and electronics will not be categorized into the definition of “toy” for this paper. Outside sports will be omitted as well. This analysis will focus on the U.S. market.

In order to decipher where the toy industry is headed in the future, its past must be analyzed first. There are archeological treasures that historians have found of pictographs, artifacts, and written records of children making and playing with their own toys whether it was a horse with a chariot carved out of wood and a wooden spinning top. Next, the present-day toy industry is now described as a growing pure competition industry with high saturation in competition, low barriers to entry, and low barriers to exit.

The toy industry has key competitors and conglomerates like Lego, Mattel, and Hasbro, but because oftentimes toys can be replaced with other toys, there is a low barrier to entry. To further explain this point, a high barrier to the entry industry is the gas and oil industry. Many of these companies have solidified their relationship with their customers centuries ago, and the industry is an oligopoly because few firms own the majority of the percentage within the industry. There are many legal regulations, capital investment, and labor investment that need to be done to enter the market or to exit. Toys will be toys, and the demand continues to be there. Thus, any company could easily enter the toy industry, even small business owners.

Seasonality tends to peak during the holiday season during November and December and have a slight decline in January and the rest of Q1 of each year according to Statista.com. The data was between 2017 and February 2024 on a month-to-month basis to analyze the seasonality of the toy industry. This aligns with the socioeconomic standpoint of the U.S. population; most individuals do not have work off until the holidays, so it is a very important time of year. Parents buy gifts during the holiday season, so the uptick in sales during that time of year makes a logical sense.

Technology has changed the way customers interact with toys as well as expanded the toy industry to electronics. Still, for the sake of consistency, that aspect of toys will not be elaborated. Technology like the internet, social media, and the converging of consumer needs cause toys to trend or go viral to shorten the products’ lifespan, but to bring in a massive amount of revenue. Additionally, technology like ecommerce and online shopping also have completely changed the way consumers purchase things in general, including the toy industry.

The U.S. market size for the total toy industry for 2024 was about \$42.0 billion, according to Circana. From 2019 to 2024, it grew 26% according to Circana. Based off the data that Statista.com, the compound annual growth rate is a 3.47% increase. Thus, the industry will most likely increase due to the positive annual growth rate, but also due to the timelessness of toys and entertainment as mentioned before in the beginning of this industry analysis.

Several factors are fueling this growth. In Q3 2023, four major trends stood out: Kidults, nostalgia, social responsibility, and education. The term “Kidult” refers to an adult who buys and plays with toys. Ever since the COVID-19 pandemic, mental health awareness has skyrocketed, and the stigma around adults playing with toys has significantly decreased. Parents found themselves reconnecting with the toys they loved as kids and sharing them with their own children during lockdowns. With more disposable income, collectibles and nostalgic toys—like Squishmallows, Pokémon trading cards, Legos, and blind boxes—have become insanely popular. According to the Toy Association, during the 2024 holiday season, 89% of adults bought a toy for another adult, while 43% purchased one for themselves. On top of that, adults aged 18 and up spent \$1.5 billion on toy-related purchases in Q1 2024, officially making them a bigger consumer group than the three-to-five-year-old demographic, according to a Cirana report. Gen Z and Millennials are driving this trend.

Social responsibility is another major factor shaping the industry. Consumers today care more about the ethical impact of their purchases, and the toy industry is no exception. The Toy Association’s holiday survey found that people are prioritizing diversity, equity, inclusion, and sustainability when buying toys. A Deloitte report also revealed that 58% of consumers prefer eco-friendly toys. Meanwhile, educational toys continue to be a big deal. Many parents actively seek out toys that offer developmental benefits. According to the Toy Association, 81% of parents say they are likely to purchase at least one toy with educational value. This has led to a rise in STEM-based toys and other products designed to encourage cognitive growth and problem-solving skills.

All in all, the toy industry is highly competitive but continues to thrive as a fragmented industry. With low barriers to entry, constantly shifting trends, and strong consumer demand, it’s a market that keeps evolving. While competition is fierce, companies that stay ahead of trends and cater to changing consumer values will continue to succeed. Given the industry’s adaptability and timeless appeal, the toy market is expected to keep growing in the coming years.

#### **Firm: Lego**

Founded in Denmark in 1932 by Christiansen, Lego began as a company that sold wooden toys. The word Lego comes from the Danish work “leg godt”, which means play well. However, one day the wooden toys caught on fire. Thus, the company pivoted to making them out of plastic. Later, they brought the original idea of the Lego brick in 1949, but they were hollow, meaning they would not stick together. Thus, a few years later they solved this problem by adding three small holes under the brick. They garnered immense success, and so much so that it soon was an international name.

During the early 2000s, the company began to lose sight of what was most important to them as well as who they were as a whole. They expanded into amusement parks, clothing, video games, books, and so much more. Soon, they were losing \$1 million per day. That was when the company hired outside of the family for once and brought in Knubstorp. It was a great strategic decision because on top of being an external hire who brought in a new perspective to the company, he was only 36-years-old, had two master degrees (one in business administration and the other in economics), and had previous experience at McKinsey.

When he began his work as CEO, the first thing he did was discover the cause of their crisis. The company revealed that their processes and operations were not in place at all. They did not know where they were losing or making money, nor did they not know where to invest. They lacked management between forecast and manufacturing. There was limited sharing of data. In fact, they did not even know who their customers were. Lego was so lost to the point that they forgot who they were at the core.

Nonetheless, Knubstorp began to decrease costs by pulling out from amusement parks, clothing stores, bookstores, and ectara—all until they came down to the very start of the company: the brick. Next, Lego went out to the actual real world to interact with their customers and understand why they buy their products, who they are, what their characteristics are, and better understand their buying behaviors. At Brickfest, 100,000 Lego fans came to show off their creations, and that was where Lego realized who they were. They were a very simple thing—the brick—but with it, unimaginative and endless heights of creativity could be reached.

Lego leaned forward into that creativity by starting AFOLS, a robotic group for Lego fans, expanding into franchises like Harry Potter, world architecture, Friends line that focuses on young girls, and so much more to have a family be a lifelong customer, either as a child or as an adult. They constantly were and even now are constantly talking to their customers to make them more a part of the Lego development process like even hiring fans into Lego corporate or allowing their fans to submit ideas to evolve into real life Lego sets. On the production side of things, Lego utilized machinery and automation to keep labor and production costs low. As early as 2013, they were using robots in their warehouses to organize each piece of a Lego set. They additionally streamlined all their processes and packaging to ensure that quality control for their customers.

The initial strategy was causing their problems primarily due to lack thereof. The strategic solution was first understanding who they were at the core, excelling in their comparative advantage, and driving cost strategy. Lego was not perceived by the public as anything extravagant like Louis Viton when they were back on the rise in the early 2000s. They focused on cutting costs as much as possible and increasing loyalty with their customers.

### SWOT Analysis

Lego's strengths are their distinctive competency of the brick, their global brand, their loyal customers, and licensing agreements. For starters, the invention of the Lego brick was so unique and revolutionary that now anything that is like it cannot replace it. They were the first to do anything similar to it, which naturally keeps them now at a competitive edge. While utilizing the VRIO framework, the brick provides value and a competitive advantage, no other competitor possesses it, and the firm can exploit the resource e (although it is inexpensive to be produced. In the weaknesses aspect of the SWOT analysis, this will be expanded upon.) Lego's strong global brand is truly impeccable—their sales hitting \$13 billion dollars in 2023 alone in 140 countries with 100 branded stores. This naturally leads to a loyal fanbase that as Knudstop envisioned now grows up with Lego as a child up into adulthood. Lastly, Lego partners up with large entertainment companies like Disney, Marvel, Harry Potter, and Star Wars to make Lego sets, which bring in other communities of fanatics into the Lego space.

On the other hand, their weaknesses are high prices, dependency on plastic, and research cost. In 2022, Lego increased their prices on average at 24%, according to Business Insider, and continues to do so. It is primarily since they know they can increase the prices, and their adult fans will continue to purchase these sets. Additionally, according to the Business Insider, Lego increases their prices based on the Lego set piece count, so the more pieces and the more complicated a set is then naturally the more expensive it is. This naturally aligns with their adult fans since many of them tend to be more interested in Harry Potter, Star Wars, architecture, or Black Box series. Second, the dependency on plastic comes from the ongoing trend of sustainability and social responsibilities businesses now have to making a profit in ethical standards to the people, government, and the earth. Third, although Lego is dedicated to their customers, the constant research and innovation that Lego invests is extremely expensive.

Still, there are many opportunities for Lego like exploring sustainable materials, entering new markets, emerging technology like AR/VR, the growing Kidult community, and even subscription services. By 2030, Lego has a goal to switch to more sustainable materials than plastic, which would appeal more to environmentally conscious millennials and Gen Z as their disposable income continues to grow. According to Statista, there has been an increase in the Americas as well as Europe, the Middle East, and Africa (although those three are not broken down), but there was a slight decrease in 2023 compared to 2022 in Asia. However, in 2024 for China alone, sales surged by 14% according to China Daily, a Chinese newspaper, and now current CEO Niels B. Christiansen is investing more into the Asian market. Also, technology like AR/VR are being explored for more Lego media and video games. The Kidult community is continuing to grow within the toy industry and within Lego customer base. Lego can continue to invest into the community. On top of that, adults may be interested in purchasing a subscription to either buy specific Lego pieces they may need for their collection, specific sets they are interested in at a lower cost, or whatever it may be since nowadays subscriptions are a great way to increase brand loyalty.

Lastly, Lego has a few threats. The list is most definitely not limited to the following: intense competition, changing consumer preferences, counterfeit products, supply chain disruptions, and the rise of data security and concern. The toy industry is fragmented with low barriers to entry and low barriers to exit, meaning there is high competition—both old and new, large and small, online and retail. Next, consumers are always changing, so Lego is always researching what their current customers want as well as what their potential customers and their competitors' customers want. Third, the threat of counterfeit products and substitutes is significant to Lego. It does not cost a lot of money to produce an interlocking plastic block, so there are many suppliers that will do such a thing and sell it at a cheaper price, especially now that Lego prices continue to increase. Production disruptions with any product or finished good will be a concern. Now, there is a continuous rise in customer data security since businesses and companies have been caught doing unethical things in the past. Keeping their customers safe continue to be a concern.

### Where Lego is Headed

All in all, Lego will continue to grow in the upcoming five to seven years due to the fact that the toy industry is timeless and is forecasted to grow in the future at least at 3.47% annual rate. Also, Lego is so valuable, rare, and organized as a distinctive product and concept. Kidults in general is a growing demographic, and in 2024, their CEO announced that they are more focusing on

their 18+ demographic due to their sales. They will most likely continue to expand into other regions like Asia and Africa. The increase in new technological innovations and subscriptions can be an opportunity for Lego to explore as well. Lego without a doubt will grow in the upcoming years.

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