

TOY MAKING

Smackdown in Toyland

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BERTRAND MAROTTE

With Indiana Jones and Star Wars in its war chest, Lego has made an impressive comeback. Meanwhile, Mega Brands has been forced to retreat after a series of safety-related recalls. Can the Canadian upstart mount a counterattack of its own?

MONTREAL -- It has the makings of a serious rumble in Toyland.

In one corner stands a resurgent Lego AS, blazing ahead with Indiana Jones and Star Wars on its side.

In the other is Canada's humbled but feisty Mega Brands Inc., attempting a comeback with a new line of magnet-based construction toy sets as a marquee product, and keen to return to the good old days when it wrenched market share away from dominant player Lego with its own line of colourful interlocking blocks.

After stumbling badly with major safety-related product recalls of its earlier-generation magnet construction kit, Montreal-based Mega Brands is betting big that its safer, more innovative MagNext line will help return it to profitable growth.

Despite the damage the company suffered as a result of the nightmare recalls of its earlier Magnetix toy - after one child died and others suffered internal injuries on ingesting magnets that came loose - Mega Brands has decided to stick with the magnetic construction toy category.

It's doing so at a particularly difficult time for toy makers: stagnant growth; increasing retailer clout; rising prices for raw materials; tech-savvy kids drawn to video games, the Web and electronic gadgets; not to mention an economic slump, which tends to tighten up spending on toys.

Unlike Lego, Mega Brands doesn't have any major licensed movie tie-ins this year but is counting on MagNext and two other new proprietary products to restart the fire: a giant-scale building toy called Struxx and a Legends of King Arthur construction set.

Danish giant Lego, on the other hand, is going gangbusters with hot-selling products based on the Star Wars and Indiana Jones franchises. In fact, it's one of the few toy makers to buck the flat market.

Last week, Lego posted stellar second-quarter results that reflected the payoff from a massive turnaround effort that included shedding non-core assets and implementing a sweeping efficiency plan.

In stark contrast, Mega Brands yesterday reported a loss of \$3.6-million

(U.S.) and said its revenue fell 12.4 per cent to \$106.4-million.

Mega Brands president and chief executive officer Marc Bertrand points out that the second quarter of this year included some fallout from the Magnetix recall and is disappointing compared with the same period last year when the company had two movie tie-ins - Spider-Man 3 and Pirates of the Caribbean.

The launch in the second half of this year of the three new proprietary product lines will be reflected in improved quarterly results, he said in an interview yesterday.

"Yes, Lego has Star Wars and Indiana Jones but - looking at retailer shelf space allocation going into the fall season - we're having excellent success," he said.

He says company research among consumers indicates that the magnet category is a reliable one that will continue to show strong growth.

"We think it's a great, magical play pattern. There's a very high rate of consumer interest," he said, adding that the new MagNext line is not only safer but also offers kids far greater scope and scale for building the wildest creations from their imaginations.

Soren Torp Laursen, the president of Lego's North American operations, isn't about to take a renewed Mega Brands offensive lying down.

Lego's slump began about 10 years ago when the company lost its way as it expanded into everything from apparel and video games to theme parks and retailing.

Mr. Laursen said those days are behind the company, and it's back in shape and prepared to take on all comers.

"I think it was relatively easy for Mega Brands to steal some of our market share in the past. Going forward, that's going to be a lot more difficult," he said in a recent interview.

"We got a wake-up call. We had become a little bit slow-moving after 50 years of success.

"The opportunity for any company to come in and take away from our share now is much more difficult than 10 years ago. Those days are gone."

The secret to Lego's reinvention was the return to its core, iconic building block - with improvements - and a massive streamlining operation, he added.

One toy industry expert says Lego has all the right things in its toy box to help it survive tough times, but Mega Brands has much work to do.

"The companies that are weathering these difficult times the best are those with consumer-driven brands," says Nancy Zwiers, head of Long Beach, Calif.-based Funosophy Inc., a product design and strategic marketing firm specializing in kids' products.

However, Mega Brands doesn't have Lego's oomph when it comes to brand identity, said Ms. Zwiers, a former Mattel executive who was responsible for the successful relaunch of Barbie in the 1990s.

"Mega Brands' biggest opportunity is to really start nurturing a more consumer-oriented brand. That can give them more insulation in times of trouble and also more leverage with retailers who have a lot more power these days."

Mega Brands' past success has been built on providing great value to the consumer in comparison with the established competition in the construction category, she said.

The Canadian upstart's strength has always been in its preschool offerings, with its oversized building blocks - a segment that it pioneered, Ms. Zwiers said.

MEGA BRANDS INC. (MB)

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