CASE STUDY 1-1 Lego

Lego has long been an industry leader in children's toys with its simple yet unique building block-style products. A Danish carpenter whose family still owns Lego today founded the privately held company in 1932. But by 2004, the company found itself close to extinction, losing $1 million a day. A new CEO was brought in, and within five years sales were strong, profits were up, and naysayers who felt the new strategy was going to fail were proved wrong. In fact, sales, revenues and profits continued to be strong. Revenues grew from 16 billion Danish krone (DKK) in 2010 to over 28 billion DKK in 2014, and in the same period, profit almost doubled from 3.7 billion DKK to 7 billion DKK. With the advent of high-tech forms of entertainment, such as the iPod and PlayStation, Lego found itself more antique than cutting edge in the toy world. When new CEO Jorgen Vig Knudstorp, a father and former McKinsey consultant, took over, the company was struggling with poor performance, missed deadlines, long development times, and a poor delivery record. The most popular toys frequently would be out of stock, and the company was unable to ship enough products or manage the production of its more complicated sets. Retail stores were frustrated, and that translated into reduced shelf space and ultimately to business losses. Knudstorp changed all of that. He reached out to top retailers, cut costs, and added missing links to the supply chain. For example, prior to the new strategy, 90% of the components were used in just one design. Designers were encouraged to reuse components in their new products, which resulted in a reduction from about 13,000 different Lego components to 7,000. Because each component's mold could cost up to 50,000 euros on average to create, this reduction saved significant expense. Lego was known for its traditional blocks and components that would allow children to build just about anything their imagination could create. The new strategy broadened the products, targeting new customer segments. Lego managers created products based on themes of popular movies, such as Star Wars and the Indiana Jones series. The company moved into video games, which featured animated Lego characters sometimes based on movies. The company created a product strategy for adults and engaged the communities who had already set up thousands of Web sites and blogs featuring Lego creations. It embraced the community who thought of Lego as a way to create art rather than simply as a building toy. And the company designed a line of Legos aimed at girls because the majority of its products had primarily targeted boys. The culture of Lego changed to one that refused to accept nonperformance. The company's past showed a tendency to focus on innovation and creativity, often at the expense of profits. But that changed. “Knudstorp … made it clear that results, not simply feeling good about making the best toys, would be essential if Lego was to succeed… . Its business may still be fun and games, but working here isn't,”20 describes the current culture at Lego. Some of the most drastic changes came from within the Lego organization structure. After its massive losses in 2004, Lego switched its employee pay structure, offering incentives for appropriate product innovation and sales. Key performance indicators encourage product innovation that catalyzes sales while decreasing costs. Development time dropped by 50%, and some manufacturing and distribution functions were moved to less expensive locations, but the focus on quality remained. The creation of reusable parts alleviated some of the strain on Lego's supply chain, which in turn helped its bottom line. Lego also expanded into the virtual world, extending into video gaming and virtual-interaction games on the Internet. Thinking outside the company's previous product concepts cut costs while encouraging real-time feedback from customers across a global market. Additionally, Lego created brand ambassadors who organized conventions across the world to discuss product innovation and to build communities of fellow customers. With increased revenue, Lego managers considered entering the movie-making business—a risky proposition for a toy company. However, Lego's success with Hollywood-type action figures fueled its interest in a movie-making endeavor. The growth put strains on the IS supporting the business. Order management and fulfillment were particularly affected, resulting in the inability to meet customer demand. Employee management systems were stretched as new employees were added to support the growth and additional locations. Product design and development, especially the virtual and video games, required new technology, too. To solve some of these problems, Lego managers used the same approach they used for their blocks. They created a modularized and standardized architecture for their IS, making it possible to expand more quickly and add capacity and functionality as it was needed. They implemented an integrated enterprise system that gave them new applications for human capital management, operations support, product life cycle management, and data management. The new systems and services, purchased from vendors such as SAP and IBM, simplified the IT architecture and the management processes needed to oversee the IS. One manager at Lego summed it up nicely, “The toy world moves onwards constantly, and Lego needs to re-invent itself continuously. Significant corporate re-shaping introduced new energy to the company.” 21 He went on to say that simplifying Lego's IT systems and implementing an efficient product development process that was able to maintain quality and cost favorably positioned Lego to respond to the fast changing pace of the toy industry.