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Doll Unit Avoids Growth Spurt

Mattel's American Girl, which will open a store in L.A., aims to keep its grip on the upscale niche partly by limiting its expansion.

By Abigail Goldman
Times Staff Writer

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American Girl doesn't have to look far for a reminder of how a top-tier toy name can fade.

The upscale doll unit of Mattel Inc. will open its third American Girl Place store this weekend at the Grove in Los Angeles. It is hoping to avoid the fate of the previous tenant, FAO Schwarz, whose parent company filed for bankruptcy protection after more than 100 years in business.

The challenge facing American Girl: how to maintain its cachet amid double-digit growth. It's a job made more difficult because of its position as one of the fastest-growing units of toy giant Mattel, which has suffered Wall Street's wrath over flat sales.

"When something's value is wrapped around its uniqueness, it's hard to exploit that in scale," said toy industry analyst Sean McGowan at Harris Nesbitt Corp. in New York. "The specialness of the product is a big part of its appeal — if it becomes available to everybody, it loses some of that."

No one has to tell that to Ellen Brothers, the American Girl president who has shepherded the company for the last six years.

"We've always been very careful not to turn our brand into a craze or a fad, where we would burn very brightly potentially and then burn out," said Brothers, who joined American Girl after serving as president at Pepperidge Farm Mail Order Co. "The goal here is not to be the biggest brand in the shortest amount of time. The goal is to provide a quality product and a great experience to girls and their parents."

That's been working like a charm for American Girl, which has the kind of sales growth — 15% last year — that would make long-suffering Barbie green with envy. It's a cautious approach that Mattel has never embraced for its ubiquitous beach blond.

The balance Brothers has to strike now is walking the fine line between being careful and being timid. It's a struggle that most niche luxury companies face: How does a brand that thrives on being special best leverage its success and continue to grow?

FAO had trouble finding the answer.

The 144-year-old company, pieces of which were bought out of bankruptcy by hedge fund D.E. Shaw for \$41 million in 2004, suffered primarily from overexpansion and poorly chosen acquisitions.

FAO went from presiding over a venerable New York store, where Tom Hanks' character in the 1988 movie "Big" danced on a giant piano's ivories, to operating a small chain of stores in malls and shopping districts around the country.

As it began to wane, FAO's best assets were purchased in 2002 by Right Start Inc., even as it was still digesting an earlier acquisition, toy chain Zany Brainy.

But unlike FAO, which started out as a seller of toys made by a variety of manufacturers, American Girl Place sells only its own products. The company has held fast to the notion of enticing girls with a store "experience."

At the center of that experience are the dolls themselves, a historical line including such characters as Kaya, an 18th century Nez Perce girl; Addy, a slavery escapee; Samantha, an early 20th century orphan; and Molly from the World War II era. Each of the dolls' lives and times are outlined in a series of books.

The lessons of patriotism and Americana don't come cheap. A starter package of a doll, a book, a basic outfit and an accessory kit costs about \$100.

Fancier furniture and doll toys are extra, such as Samantha's \$68 bicycle and colonial-era Felicity's \$78 stable set.

Despite questions from investors and others about opening more U.S. stores and expanding into international markets, Brothers said that there were no plans for either.

In fact, Brothers envisions having fewer than five stores total and could decide to hold the line at three. Company executives have talked about a smaller-format store focused on birthday parties or acting lessons or some other experience but have yet to formally explore any proposals, she said.

Nor is American Girl likely to take on any more licensees. So far, the company has paired only with Limited Brands Inc.'s Bath & Body Works for a line of preteen soaps, shampoos, lotions and perfume.

Instead, Brothers said American Girl would continue to work on entertainment properties, following up on television specials-turned-DVDs.

Like the American Girl Place stores in Chicago and New York, the 40,000-square-foot Los Angeles store will house the American Girl Bookstore, featuring the company's advice, fiction and activity titles; a doll hair salon, where professionals will restyle dolls' locks; a 133-seat theater featuring the musical American Girls Revue; a photo studio; a doll hospital and a cafe, where guests dine with their American Girl dolls seated next to them in specially designed chairs.

All of that is in addition to the walls full of products — matching outfits for girls and their dolls, doll jewelry, doll furniture, doll pets and, of course, the dolls.

Part of the company's success, industry experts say, is that it is alone in a very specific niche.

Other upscale dolls, such as Alexander Doll Co.'s long beloved Madame Alexander dolls, mostly target collectors — adults or children who would carefully display the expensive dolls on shelves in safekeeping for their own daughters one day.

And other companies that tried to build direct-market toy businesses weren't able to connect with consumers. Rumpus, for example, was a successful specialty toy company when founder Larry Schwarz in 2000 pulled its signature Gus Guts, Harry Hairball and other toys from stores and moved them to an online-only format.

Schwarz believed that on the Web he could leverage his creative and unique toys by featuring games, short movies and the like that would connect with children, much like American Girl. The online effort failed and Rumpus went out of business shortly thereafter.

"American Girl had done it strictly catalog and online, before they built the three stores," said Jim Silver, publisher of Toy Wishes magazine. "They developed this brand throughout the years. They have a loyal following, and it's very hard to do."

American Girl, founded by educator Pleasant Rowland in 1986 in Middleton, Wis., became part of Mattel with its 1998 purchase of Pleasant Co. for \$700 million. Although Mattel has used American Girl's distribution prowess to handle the mail-order arm of its Barbie collectibles, Hot Wheels and Fisher-Price businesses, analysts and others say the El Segundo giant has been most notable for what it has not done — tinker with a winning formula.

"Mattel has certainly understood that whatever American Girl is to girls in the U.S., it is not Mattel blazed on the side," said M. Eric Johnson, a professor of management at Tuck School of Business at Dartmouth College and an expert on the toy industry. "If you go on the website, you have to really dig around to even find a Mattel logo."

For that, Mattel has been rewarded. In 2005, while Barbie's sales slumped 13% worldwide, American Girl's revenue rose 15% to \$436 million. Oppenheimer & Co. analyst Linda Bolton Weiser pegged American Girl's operating profit at about \$100 million, meaning that the division accounted for 8% of Mattel's gross sales and about 15% of the parent company's operating profit.

Mark Greenberg, portfolio manager for the AIM Leisure Fund in Denver, said the company's caution probably made sense. Amvescap, parent of AIM, owned 2.5 million Mattel shares as of Dec. 31, the most recent period for which ownership information was available.

"Could they be a little more aggressive? Yes," Greenberg said. "Should they be a lot more aggressive? It's hard to say."

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