Hornby Hobbies

A Management Case Study

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HORNBY HOBBIES

Abstract

Hornby, the company that systematically gave the world Meccano, Hornby Dublo electric trains, Dinky Toys and Scalextric, remains an independent British company a century after it was started by entrepreneur Frank Hornby in Liverpool. This is something of a rarity in the UK toy industry, which has seen many brands disappear in the face of global competition and many businesses either close or be sold to foreign ownership. During the last forty years Hornby has been continually swimming against the tide. Strategies have changed. Innovation, new products and diversification have been important - so too have divestments. There have been different owners and several changes of strategic leadership. But recently the company’s prospects have been transformed. Production has been moved to China, enabling the company to provide more detail without increasing prices. Pre-tax profits more than doubled between 2001 and 2002 and the latest interim results show a further doubling. Hornby’s survival is testimony to the importance of branding and reputation.

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HORNBY HOBBIES

A new public company was launched in February 2002. Flying Scotsman plc had been formed to use the expensively restored and world-famous green steam engine for special excursions. The Flying Scotsman was, of course, the first steam engine to officially break the 100 mph speed barrier in 1934. The shares, like the locomotive, would prove attractive to enthusiasts who enjoyed the glorious days of steam trains, even if they were sometimes too young to remember them personally. The special long-distance excursions are a significant alternative to the continually popular, but much shorter, trips on the various restored steam railways operating in various parts of the UK. The engine itself had first taken to the rails in 1923, three years after Frank Hornby launched his first model train. Hornby is the UK brand leader in the field of model railways, and today a replica scale model of the Flying Scotsman is an important member of the Hornby range of electric trains, which continue to be popular with adults as well as children. At the same time, special ‘Thomas the Tank Engine’ events at restored steam railways up and down the country are also incredibly popular with children. Here plastic faces, based on the various engine characters, are attached to the front of renovated steam engines, transforming them. In part it is the smell, in part it is the noise, but nevertheless children of all ages, let alone their parents, continue to enjoy a ride in a railway carriage pulled by a steam engine, years after they have ceased to be used for any regular service.

Hornby now has an estimated 70% of the UK market for model electric railways and, with its Scalextric products, an estimated 75% of the UK market for slot-car racing systems. In the context of the fortunes of the UK toy industry overall, the fact that Hornby is still in existence almost eighty years after its first model electric train and a century after it started is quite remarkable. Without very strong brands, innovation and the exploitation of new opportunities as they arose this would not have happened. Other Hornby brands, such as Meccano and Dinky, have either disappeared altogether or fallen to overseas ownership. Airfix (model kits), Corgi and Matchbox (model cars), once leading UK toy companies and brands, are no longer British. The 1980s, with its economic recession accompanied by a strong pound, saw many surviving businesses go into either receivership or liquidation. Hornby has been swimming against the tide for forty years - and at times that tide must have seemed unstoppable.

The UK toy industry

In 2000 the sales value of toys and games in the UK passed the £1.75 billion threshold for the first time. Recent sales and predictions for the early years of the twenty-first century are provided in Table 1. Although Pokémon games, based on the Japanese characters, were instrumental in increased sales at the time, the last quarter of the twentieth century had seen a major shift of taste in the industry. Whilst cuddly toys remained the most popular, with a 20% share, video and computer games had
risen to 19%. ‘Vehicles’, which is the sector where Hornby competes with both electric train sets and Scalextric, now varies between 7 and 8% annually, whereas at one time it was much more significant. However, this still implies a market overall of some £130 million per year. In a survey of adult purchasing behaviour over a six month period in 2000 - incorporating the Christmas period - 3% had apparently bought a train set or motor racing game.

Arguably children ‘grow older younger’, affecting their choice of games. They switch from ‘traditional’ toys and games to music, video and computer games at relatively young ages.

<table>
<thead>
<tr>
<th>YEAR</th>
<th>SALES VALUE (£ billion)</th>
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<tr>
<td>1996</td>
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<td>2004</td>
<td>1.84</td>
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<td>2005</td>
<td>1.86</td>
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Table 1. Sales value of toys and games in the UK. Figures in italics are projections rather than actuals. 
*Source: Mintel*

Overall, more women than men buy toys and their preferred outlets are Argos, Woolworth’s and Toys R Us. Table 2 provides relative market shares of different types of outlet in 2001.

<table>
<thead>
<tr>
<th>TYPE OF OUTLET</th>
<th>RELATIVE SHARE - %</th>
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<tr>
<td>Toy shops</td>
<td>28</td>
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<tr>
<td>Mixed retailers</td>
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<tr>
<td>Catalogue showrooms</td>
<td>22</td>
</tr>
<tr>
<td>Mail order</td>
<td>7</td>
</tr>
<tr>
<td>Superstores</td>
<td>6</td>
</tr>
<tr>
<td>Department stores</td>
<td>5</td>
</tr>
<tr>
<td>Others</td>
<td>8</td>
</tr>
</tbody>
</table>

Table 2. Sales of toys and games in different outlets in the UK, 2001. 
*Source: Mintel*
At this time, a year that sales were rising after a period of relative stability, the only sector to experience a fall was mail order. Every other sector grew.

Hornby’s main channels are independent retailers, which are most important for Hornby trains - it sells to some 800 independent hobby and toy shops - and the major retail chains, which are more important for Scalextric. Toys R Us, Argos, Index and Woolworth’s are the leading distributors. Concession outlets are being increased, and they are particularly important for Scalextric.

Frank Hornby

Frank Hornby (1863-1936) entered the toy industry at the beginning of the twentieth century when he invented Meccano construction sets, an early fore-runner of Lego. Meccano used metal pieces punched with holes which children could screw and bolt together into elaborate models of buildings, bridges and motor vehicles, for which they would later be able to buy small engines. Meccano was an educational toy that helped teach construction and mechanics, but its uses and appeal spread way beyond this. A number of the pioneer computers were actually build out of Meccano. During the 1930s the ‘Meccano Magazine’, which had grown out of the instruction guides that explained how to build various models, was the most popular boy’s magazine of the age.

Frank Hornby was born in Liverpool, the sixth child in a family of seven. His father was a self-employed wholesaler/porter who transferred goods from the very busy Liverpool Docks to various shopkeepers in the area. The family was ‘comfortable’ but not wealthy. Frank was reputedly ‘bored at school’ but was determined and enjoyed a challenge. He secured a job as a book-keeper and clerk for a meat importer, David Elliott. Married in his early 20s he had two sons, Roland and Douglas, who were born in 1889 and 1890 respectively. Inspired by earlier inventors and a book entitled ‘Self Help’ Frank Hornby tinkered in his shed and built models for his sons to play with. His tools were relatively unsophisticated but he continued to experiment. The inspiration for Meccano was a large crane.

Frank patented the design for Meccano - although at this time the Meccano name did not exist - in 1901, borrowing the £5 fee from David Elliott. At the outset production was sub-contracted, but this was never wholly satisfactory. There were too many quality problems. Hornby and Elliott formed a partnership and leased the premises next door to Elliott’s meat business. For both of them Meccano was a part-time activity, and it continued this way until 1906. By this time this business was profitable. Hornby had proved himself to be a businessman and entrepreneur. He had secured retail outlets and actively marketed the product. Particularly successful were competitions through the Model Engineer magazine, which attracted more adults than children. Elliott began to withdraw his capital and, having secured a lease on larger premises, Hornby devoted all his time to the business. He spent money defending his patent and he travelled abroad extensively, setting up agency agreements. In 1910 Hornby recruited two key people who would stay with the business for the whole of their working lives. One, named Beardsley, was an expert in operations; the other, George Jones, was a salesman.
By 1914 the business, known as Meccano Ltd., was relocated in Binns Road, Liverpool, where it would stay for many years. Frank Hornby had borrowed money from a number of financial partners to fund the expansion.

**The growth of the Meccano business**

Not long after this, of course, the factory was commandeered for wartime production - something that would happen again in the 1940s. Once the war was over Frank Hornby saw an opportunity in model trains. Before World War I German producers had successfully exported to the UK, but after 1918 there was naturally some resistance to this. Hornby was not the only manufacturer to see the opportunity, but he would be the one to champion the development of the market. Hornby’s first model steam train (in 1920) was constructed in metal and powered by clockwork. Although these would continue to be available throughout the twentieth century, their popularity would systematically decline once electric trains were introduced and improved. From the outset the trains were branded Hornby.

The products were instantly popular and soon 1200 people were employed at Binns Road. At this time the factory became known as ‘Meccanoland’ and enthusiasts were encouraged to visit and look at Meccano constructions and, as time went on, railway layouts. Meccano and later Hornby enthusiasts clubs were soon beginning to spawn.

In 1925 Hornby launched an electric train powered directly from the mains; four years later he had launched the first version of the models that still prevail today. His safer system utilised just 6 volts via a transformer connected to the mains electricity supply. The first sets provided an engine and a number of freight trucks or passenger carriages together with a circular rail track. Point systems allowed more complex layouts and enthusiasts designed their own systems. Model stations, railway personnel, level crossings, signals and signal boxes were all introduced to add to the authenticity - but many people preferred to construct their own infrastructure out of materials they acquired. The first Hornby electric train sets were 0 gauge, to a scale of 1/43 - or 7 mm to 1 foot. Hornby train sets were smaller than most of their Continental rivals simply because European railway engines, carriages and trucks have long been wider and higher. Simply the UK size restrictions are tighter. Consequently a scaled down 0 gauge version of a European train will be bigger. The smaller 00 gauge trains came when it became possible to design electric motors that were small enough.

By 1930 Hornby train sets were outselling Meccano in the UK for the first time. However, Hornby never had the export potential that Meccano did.

**Dinky toys**

Dinky Toys were a range of zinc-based pressure die-cast model vehicles first introduced by Hornby in the early 1930s. He saw these as complementary to the die-cast figures and station accessories that he was already producing, but of course they found their own market as well. As with trains and carriages there are two key stages
to the process - and Hornby did both of them, as well as producing its own dies. The first stage of the process is the production of die-cast parts, which is followed by painting and plating. Assembly and packaging comprises the second stage. No longer owned by Hornby, Dinky Toys remain highly collectable and the value of mint-condition models, especially if they are in their original boxes, continues to rise. The vehicles were again 1/43 scale, designed to look realistic alongside the trains. During the early years of World War II, before Binns Road was given over to wartime production, military vehicles were added to the range of cars, trucks and buses. After the war the range amounted to some 300 vehicles.

During the 1950s Mettoy’s Corgi brand grew as a leading competitor for 1/43 scale die-cast models and in the 1960s the real growth story was Lesney’s Matchbox toys, smaller 1/72 scale model vehicles which were cheaper and available through outlets other than toy shops. Mettoy also marketed Playcraft model railways. For a time Lesney was one of the fastest growing companies in the UK, but its fortunes were hit when American rival Mattel launched its rival Hot Wheels with plastic, friction-free wheels. Hot Wheels would run more freely and were, therefore, clearly toys as well as models.

### Changing fortunes

During the 1930s Frank Hornby’s company, still called Meccano, mastered the technology for producing a smaller electric train. By 1938 it had developed a 00 gauge model, 1/76 scale. It was this new version that would be known as Hornby Dublo. Because of the intervention of World War II it was 1947 before the new model was available on the market. It’s success was instant. Demand for 00 gauge was there. Trix branded systems – from a company with German parentage and know-how – had begun to develop the market in the mid-1930s.

Hornby’s first 0 gauge electric trains were freelance design models. They clearly looked like the steam trains that ran the length and breadth of the country, but they were not exact replicas of the actual engines. Hornby Dublo 00 gauge would be different in this important respect, which gave an added realism to the products. Once replicas are made of actual engines the issue of licensing has to be dealt with. If an engine has been in production and use for over 25 years then no license fee is necessary, but within this time period some agreement has to be reached with the owners of the design. The other licensing issue concerns engine names. All railway engines have unique numbers and many have names. Famous names like ‘Flying Scotsman’ and ‘Mallard’ amount to brands and it has been obvious over time that different customers prefer certain names to others. To this day Hornby offers up to five differently named versions of the same basic locomotive design. Colours can be different and some models are available with a duller, weathered finish.

From the beginning, though, Frank Hornby would write to other businesses and ask if they would like to advertise their logo on his freight wagons! He implied they might wish to pay a fee for this.

Summary details of the current product range can be found in Appendix 1.
In 1958 the company also launched a series of Dinky Dublo cars in 00 gauge to accompany the new trains, but these never caught on and were withdrawn after a few years.

Meanwhile an important new competitor was emerging. Rovex Plastics was started in 1946 by Alexander Venetian to make and supply plastic toys to the growing Marks and Spencer. In 1949, at the request of M & S, Rovex launched a revolutionary range of trains made out of cheaper plastic moulded bodies but powered in the same way that Hornby Dublo was. They looked and felt different, and, of course, today, plastic has replaced metal as the material of choice for model trains. The Rovex system also used a 2 rather than a 3 rail track. Meccano and Hornby Dublo would later respond by copying Rovex, but a number of important years would be lost.

Rovex was acquired by another toy company, Lines, in 1951 and the range of trains was re-branded Tri-ang. Production was moved to a brand-new factory in Margate, Kent in 1954.

Founder and entrepreneur Frank Hornby died in 1936. Between 1931 and 1935 he was Conservative MP for the Liverpool Everton constituency, returning to Binns Road every Friday afternoon to check on the business. At this time George Jones effectively ran the business on a day-to-day basis. Already a diabetic, Frank Hornby retired as Managing Director in 1935. Meccano was floated as a public company in 1932 and Frank had become a wealthy man.

After his death he was replaced as Chairman of Meccano by his son, Roland. George Jones was now Managing Director and he continued to strengthen the marketing of Hornby, Dinky and Meccano products. He was behind the successful development of Hornby Dublo. But Jones also died in the 1940s and was in turn replaced by Beardsley, the other manager recruited in 1910 by Frank Hornby. During his period in charge operations was, perhaps inevitably, seen as more important than marketing.

New products were trialled, including Dolly Varden dolls houses - the first Hornby products specifically for girls. These were extremely high quality but they effectively disappeared after World War II. Those remaining are collectors’ items.

By the 1950s Meccano Ltd. was experiencing competition on a scale it had never faced before. Tri-ang competed with Hornby Dublo; Corgi competed with Dinky; and Lego competed with Meccano. Three important products from three significant - and different - manufacturers. The company struggled and by the early 1960s it was trading at a loss with a substantial overdraft. The owners of Meccano agreed to a take-over by Lines. The valuation price was £781,000. Roland Hornby was removed from the Board. In one respect there was a sense of irony. During the Depression of the early 1930s Walter Lines had asked Frank Hornby to buy his company, but Hornby had refused.

**Acquisition**
Lines, then the largest UK toy manufacturer, thus acquired Meccano and the Hornby brand name in 1964. Hornby and Tri-ang trains were amalgamated and produced alongside the other important Rovex product, Scalextric slot-car racing games. Lines moved Hornby Dublo production to Margate, but left Meccano and Dinky at Binns Road. In 1971 these two brands would be sold to Airfix. Meccano would later be transferred to France, where it had been popular for many years. It remains to this day, a niche product owned by Nikko of Japan. Dinky would disappear with the closure of the Liverpool factory in 1979. At this time over 1000 different models would have been produced. Today the brand is owned by Mattel, but it not used for new models.

Hornby Dublo and Tri-ang were different products and used different tooling. The staff at Margate, experienced in one, struggled with the other. As a consequence Lines decided to rationalise the business. In 1966 the Hornby Dublo tooling was switched to another Lines business, G & R Wrenn in Basildon, Essex. Wrenn’s had been started by two brothers in the 1950s to manufacture tracks for electric train systems and was later acquired by Lines. It also had its own slot-car racing system. The original Hornby products were now made at Basildon and marketed as Tri-ang Wrenn. In 1971 George Wrenn bought his business back from the Lines Bros. receivers and renamed the products Wrenn Railways. Production continued until 1992, when Wrenn retired and sold his business to Dapol, which had been established to market the former Airfix railway construction kits and spare parts. Since 1992 there have been no new railway models.

The Hornby name and brand was retained at Margate but the train systems that were marketed with the Hornby name were in reality Tri-ang systems. The brand was more important than the technology.

**Independence**

In 1971 Lines went into liquidation and was broken up. At the time it comprised some forty companies world-wide. The Hornby business at Margate was acquired by yet another toy company, Dunbee-Combex-Marx (DCM), which did not acquire the Tri-ang name - which went with another part of the business to a different owner. The Margate business was renamed Hornby Railways but by the late 1970s this had been changed to Hornby Hobbies. DCM itself collapsed in 1981. The receivers of DCM transferred the Hornby, Tri-ang and Scalextric activities into a new company still called Hornby Hobbies, and still based at the Margate factory - where its headquarters remain today - and this company was bought out by its managers in 1982. The buy-out cost £5.5 million but took some twelve months to arrange because prospective institutional backers were reluctant to commit funds to an industry in trouble. Until the buy-out the business was run by the receiver.

Throughout the 1960s and 1970s Hornby enjoyed something of a revival. The train products were popular. So too were Scalextric racing cars.

**Scalextric**
Scalextric is the oldest and arguably most popular slot car racing system. Scalextric was invented and launched by Minimodels, a company which began life in Mill Hill, England, in 1947, producing scale models. Scalex model cars, moved by a keyless clockwork mechanism, were introduced in 1952. They were 1/32 scale. Made from metal, they were quickly successful - and Minimodels relocated to larger premises in Havant, Hampshire. The owner of Minimodels, Fred Frances, went to the London Toy Fair in 1955 and was introduced to a new racing system produced by VIP. Model cars were raced around a two slot track; players had a separate control box at the side of the track for each car. Frances saw the potential and was able to modify his Scalex cars to take a small electric motor. Replicating VIP’s system, Scalextric was launched in 1957. Demand built quickly and Minimodels struggled to cope. The company was sold to the much larger Lines Bros. in 1958.

In 1960 Lines replaced the metal Scalex cars with plastic bodies and also changed the Scalextric track to plastic from rubber. The basic track design of twin slots in small straight and curved pieces with a specially designed attachment system remains today, although banked curves can now be built in. Owners design their own tracks and they can add grandstands, bridges and other accessories. It has always been straightforward to make four-track racing circuits by buying and piecing together the right pieces.

Motor bikes with sidecars and Go-karts were soon added to the existing range of racing cars. Owners today choose the type of car they race - options include Formula One, European rally cars and various American racing systems. See Appendix 1. Naturally they can race different cars on different days; and a policy of new models and model withdrawals has encouraged enthusiasts to continue updating their system. In the real world of Formula One, for example, basic designs change every year and looks alter as new sponsor logos are added. There is an active secondary market on the Internet for obsolete and collectable models in both the Scalextric and Hornby ranges, which Hornby observes but does not enter.

Slot car racing has long been popular across Europe and in America, as well as in Australia and New Zealand, and so it was inevitable that competition world-wide would be strong. Clubs were formed where people could compete - they remain popular today in various parts of the UK and the world. However the main UK market is, and always has been, home-based. By contrast when the market grew in America it was through clubs open to the public. People simply went along and paid to race on complex, sophisticated, state-of-the-art circuits. Enthusiasts customised their own cars, sometimes rebuilding the engines to make them more powerful. The adult market was just as important, if not more important, than children. But the concept was over-exploited and it died away as quickly as it grew. As a consequence America is now a potential opportunity as the popularity of home-based slot-car racing is behind demand in Europe. Hornby Hobbies has a dedicated Scalextric distribution business in America, where it is the biggest brand in an under-exploited market.

At one time larger 1/24 scale models on 3-slot tracks were very popular amongst racers and Scalextric experimented with these in the late 1960s. It proved harder to keep the cars firmly in the slots and Scalextric abandoned this larger size. Another innovation (in 1970) was a car which could be moved from side to side in a 2 cms. arc whilst remaining in its slot - via a wheel on the control box. This was also abandoned.
Retrenchment and turnaround

In 1982 the demand for traditional toys and games was hit by the growing popularity of electronic toys and home computers. Hornby’s turnover fell from £13 million in 1981 to £10 million in 1982. By 1984 it would fall to a low of £7.6 million. The popularity of slot car racing in the UK and elsewhere fell in the 1980s, and it would be the late 1990s before it truly revived. Some competitors disappeared, only to be replaced by new entrants such as Ninco (complete systems) and Fly (cars). They are both Spanish companies. Per capita, Spain is the world’s biggest market for slot-car racing products. The other main competitor for Scalextric are an ex-Lines company based in Spain and Carrera in Germany. The main competitor to Hornby trains in the UK is Bachmann. Originally an American company formed in 1935, Bachmann was bought out by the Shanghai-based Kader business in 1987. Kader already manufactured trains for Palitoy. The imported products offer good designs, good quality and very competitive prices.

The newly-independent Hornby managers were soon forced to retrench, cutting costs and overheads. Computer-based video games were beginning to take off. Existing lines were clearly in decline at this time. When DCM went into receivership in 1981, 1300 people were employed at Margate. At its peak 2000 had worked at the factory. By 1995 the numbers were reduced to 735.

A strategy of diversification was begun in 1983 with Flower Fingers - making flowers from kits. Hornby opted for some toys with relatively short lives, as a contrast to trains and cars which have more of a collectable appeal. There was also a deliberate attempt to widen the company’s appeal to girls as well as boys. Other new products launched in the 1980s included Flower Fairies (toy dolls and accessories), Pound Puppies (soft toys), Boo Boos Care (a baby doll), Gro-Toys and Tendertoyos (for pre-school toys) and LA Gear (a range of aerobic exercise toys for girls). Most of the products, in particular the soft toys, were manufactured by sub-contractors in Hong Kong and imported. By 1986 some 40% of turnover was contributed by the diversified products, and this percentage continued to grow. To all intents and purposes Hornby had become more of a toy company and less of a model business.

During this period several of the buy-out directors left the business, under pressure from the institutional investors who had funded the buy-out. The new Managing Director (in 1983) was Keith Ness, who had joined the company from outside as Sales Director. Ness had previously worked for Pedigree Dolls, another DCM business.

The trains were, however, given a boost in 1985 with the launch of models based on Thomas the Tank Engine and Friends, characters created years ago by the Reverend W.H. Awdry. These were variants of the existing models and they were manufactured in Margate to identical quality standards. A year earlier, television film producer and entrepreneur, Britt Allcroft, had acquired the merchandising rights to Thomas and she had instigated a real revival in its popularity. A series of short films was narrated by ex-Beatle Ringo Starr and a whole host of toy products would succeed on the back of this revival.
In December 1986 Hornby sought a flotation on the Unlisted Securities Market, offering 61% of the equity at a price which represented 11 times current earnings per share. After losing money in 1982 Hornby had been consistently profitable at an operational level. However, 1985 was the first year since the buy-out when a pre-tax profit - after interest charges - was recorded. Hornby was wanting to raise £5 million to reduce its debt, which stood at £6 million. The flotation was successful.

Turnover continued to rise in the 1980s to a high of £40 million in 1990, with record pre-tax profits of £3.8 million. Earnings per share of 30 pence were treble those of 1986.

In 1988 Hornby had diversified out of toys with the acquisition of Fletcher Sports, the UK market leader for speedboats.

**Renewed difficulties**

Unfortunately, another economic recession caught up with Hornby in 1991 and turnover fell back to £32 million, with pre-tax profits of £2 million. Within the context of the still-troubled toy industry, Hornby remained relatively successful. Demand for its core products, electric trains and Scalextric, continued to hold up.

But Hornby’s managers were not deterred from further diversification in the toy industry. In the autumn of 1991 they launched a new product range, plastic American wrestler figures. Commentators found this strange - new toys are typically launched in the spring, when retailers begin ordering in advance of the following Christmas, their main selling season. In 1992, after lengthy development, Hornby launched Cassy, a fashion doll, which, at 7 inches tall, was 5 inches shorter than the two well-known market leaders, Barbie and Sindy. Various outfits and accessories were available. There was also an open-fronted country house, which was built from a standard base and a variety of individual rooms. The rooms came in the form of two packs, each the size of a video cassette box, which opened up to provide two room corners. Children could customise the house and place the rooms where they wanted them. A stable block was an optional extra.

For a period of years Hornby had been searching for a new winning toy. Investment in the original core model products had been reduced.

**A change of leadership - and a change of strategy**

In 1995 revenues had fallen from a high of £40 million (1990) to £31 million. A year later they would rise again to £33 million - but a 1995 profit of £0.6 million would decline to a loss of £4.3 million. Ness had been promising profits, and, despite the underlying support for the strategies he had followed, the institutional investors looked for a replacement.
A new Chief Executive, Peter Newey, replaced Keith Ness in 1995. Newey was already a non-executive director of the business and widely respected as a strategist. His background was in Merchant Banking. He recognised that without diversification in the 1980s the Hornby Hobbies business would not have survived. However, he was concerned about the consequent loss of focus on the core model products, especially as the recession in the early 1990s had intensified the competition for Hornby’s train and slot-car products. In recent years the company had rather taken these for granted and now it was essential to refocus attention on them - especially as traditional toys were regaining some of their earlier popularity. Newey did not believe Hornby had the capability to cope with the constant innovation demands of the wide and diversified range of products it now had. It was his view that Hornby’s future lay in refocusing on models and exploiting its valuable brands, but others still questioned whether children were still really interested in model trains.

Newey - and Hornby’s management team - believed the market was still there if buyers had good opportunities to develop and personalise track layouts. Newey believed that Hornby should focus on the adult market as well as children. Evidence confirms that young children remain interested up to their teens, and then there is a dip in interest. This recovers with parenthood and continues through to grandparenthood. It is apparent that parents buy the train sets for their children and build a large proportion of the layouts. If the layouts can be made more sophisticated and exciting, children will retain an interest into adulthood and then continue when they have children of their own. On the other hand, adults can be persuaded by the collectable theme, and buy model engines, especially steam engines, if the scaled-down authenticity and manufacturing quality is good enough.

At the same time, there was clear evidence that children continued to enjoy racing model cars on ever-sophisticated tracks. The competition for Scalextric, though, had intensified with smaller, rival products from America and Japan, which featured more innovative loop and cross-over possibilities. Scalextric was no longer seen as the market leader - rather, it had some catching up to do.

Another growing problem was the cost base in the UK. Soft toy production in Hong Kong had shown what was possible without sacrificing quality. If production was to be maintained in the UK there would soon need to be some serious investment in new technologies and new processes.

Newey meanwhile completed the sale of Fletcher Sports and another subsidiary business, San Francisco Toymakers, in 1996. The company had to accept exceptional write-offs in both cases.

In 1997 Hornby Hobbies received the Toys R Us ‘Supplier of the Year’ award. Also in 1997 Hornby Hobbies started to sponsor two Collectors Clubs, one for Hornby trains and the other for Scalextric. Members receive six colour magazines every year, and these are filled with news and profiles, as well as access to special collectors’ models. Given the popularity of general magazines for model enthusiasts, there is an argument that this should have happened sooner.
New opportunities

Two major events transformed the UK railway industry in the mid-1990s. First, and most significantly, the industry was privatised. Second, the Channel Tunnel opened to rail traffic. Privatisation meant the disappearance of the name and the livery of British Railways. Locomotives and carriages, passenger and freight, would be re-branded and repainted with the name of the rail company with the relevant franchise. For long journeys, two old pre-Nationalisation names were revived - GNER (Great North Eastern Railways) and Great Western - and two new ones appeared - Virgin Railways and Midland Mainline. They all had distinctive liveries and there were some variations in train systems. This was a golden opportunity for Hornby, which brought out a whole new range of different sets. In addition Hornby introduced a model of the Eurostar Channel Tunnel train in 1996.

Whilst the train services were provided by a number of new operating companies, the infrastructure was the responsibility of Railtrack. New station liveries and new staff uniforms provided yet another opportunity for Hornby and its enthusiastic collectors.

Whilst all this was happening, Scalextric was not neglected. Product improvements were supported by the acquisition of Hornby’s existing Scalextric distribution business in America, a market where the product was gaining ground and popularity.

Despite all these opportunities and changes, in 2000 Hornby put itself up for sale. Newey no longer believed it could enjoy a prosperous future as an independent company. Recorded sales at this time were £21.5 million with pre-tax profits of £1.4 million. The business was capitalised at £13 million. But no suitable buyer emerged. As a consequence, and as his last major contribution, Newey switched all remaining manufacturing from Margate to two Chinese factories close to Hong Kong. This would almost certainly have happened with a new owner. Sanda Kan, which is ultimately owned by American financiers, handles 90% of the business; the other possesses special electrical skills. The production of Hornby’s products is labour-intensive and costs in the UK were no longer tenable if quality products were to be produced within acceptable price points. It soon became clear that the new factory could produce high quality products with considerable attention to detail and at a lower hourly wage cost. In effect 550 UK production workers have been replaced by 1200 Chinese employees for roughly the same cost. Hence twice as many hours are dedicated to each model, and hence the quality has been improved markedly. To the customer, prices have not changed, but the product looks more authentic.

Further changes

At the beginning of 2001 Newey left and was replaced by a new Chief Executive, Frank Martin, who inherited cash reserves of around £4 million from his predecessor. He quickly used £1.6 million to buy back 13% of the shares.

Newey had always preferred to work from his office in London rather than relocate to the factory in Margate. He was, therefore, not close to the management team and Hornby now needed someone who was more hands-on. In addition profits had
stabilised with the disruption of moving production overseas. Yet again the institutional investors were anxious for improvement if a buyer for the business could not be found. Figures for the last five years are provided in Appendix 2.

Frank Martin had a marketing background and his previous senior management roles had been with Humbrol/Airfix, Denby Potteries and Hasbro. Following his appointment - and the cessation of manufacturing in the UK - the business was restructured. The main plc Board now has four members - Martin, Hornby’s Finance Director and two non-executive directors. There is a management board at Margate, chaired by Martin, and also comprising four directors. The Chief Executive looks after sales and marketing - the 33 staff in the section include 9 who have responsibility for research and development. 8 people work for the Finance Director. The International Sales Director (14 staff) looks after the 12 people employed by Scalextric USA. The final 74 people report to the Operations Director who looks after warehousing, distribution and technical support - and liaises with China.

Of the £28.5 million revenues generated in 2001-2, some £10 million was committed to the Chinese suppliers, leaving £18.5 million as value generated by the 121 employees in the UK. Production may have been relocated but the brands remain under British ownership and control.

At this time Hornby was advancing with both trains and cars. A new engine, manufactured in China, the Merchant Navy Class, available in five different finishes, notched up sales of 25000 units in its first year, a significant number when annual sales overall hovered around 70000 units. Adult collectors were now buying more Hornby products than children. New personal computer software - The Virtual Railway - allowed enthusiasts to model track layouts and enjoy a virtual view from the cab of their chosen engine. In the past they had designed their layouts on graph paper, using track guides.

Software to support Scalextric was also making an impression. Owners could now race their cars around the track, but by connecting the track system to their PC they could receive constant updates on tyre wear and fuel. The Scalextric Race Management system (RMS) brings together the core elements of motor racing, facilitating practice laps, pit stops and proper starts and finishes. Cars are required to stop for refuelling. As well as a gaming element it acts as a database and enthusiasts who are on-line can compare their race data and times with other competitors. There is perhaps no equivalent opportunity for Hornby - model railways, by their nature, are more personal.

In 2001 sales climbed back to £24.6 million and pre-tax profits rose to £1.5 million, after a £0.8 million exceptional charge. US sales had risen from £1 million to £2.3 million, a major contribution. Hornby was increasingly focusing on specialist hobby shops and in-store concessions as opposed to mass toy retailers - to coincide with the growing adult appeal; and Martin believed there was again real growth potential in Western Europe and the US. Hornby already exports to France, Italy, Switzerland, Norway, America and Canada.
Towards the end of 2001 another wonderful opportunity presented itself. November marked the launch of the first Harry Potter film, and pretty well everyone knows about the Hogwarts Express steam train. Hornby’s initial run of the replica model was 10000 and, with sets priced at £89.99, they ‘flew off the shelves’. The set comprises the engine, one composite coach, one brake coach and Hogsmeade Station Halt. A special collector’s edition, with 18-carat gold plated wheels and connecting rods, sold well at £125. The Hogwarts Express is being relaunched in new packaging to coincide with the release of the second film, just before Christmas 2002.

Early in 2002 a new Scalextric ‘Sport’ track was added to the existing ‘Classic’ system. The two are compatible, but the new system, moulded from linear low-density polyethylene keeps the track free of modulations and bumps - unless they are put there deliberately. There is a deeper groove between the conductive rails to help the cars stay on the track. New curves and chicanes can be built and up to 8 cars can be raced together if people wish. A brochure featuring the parts make-up of 27 different layouts, including some notable Grand Prix circuits, is available from Hornby.

Also available now are ‘My First Scalextric’, a smaller electric version - 1/64 scale - designed for very young children, and Micro Mania Scalextric. The latter comprise concept car sets – smaller in size than the normal Scalextric - with names including Demon Flyers and Thunderbugs and a series of loop tracks where the cars go round in vertical circles.

By 2002 electric trains comprised some 44% of the business and Scalextric 56%. 79% of revenues are generated in the UK. The Rest of Europe contributes a further 9% and America 10%. Most of the non-UK revenues come from Scalextric. Profits more than doubled to £3.5 million on sales approaching £30 million; the shares were trading at their highest ever price. Spending on new product development to fuel long-term growth is £1.2 million.

At the moment Hornby Hobbies remains in its 240,000 square foot building on an industrial estate between Margate and Ramsgate. Used for offices and warehousing, much of the building is now unused. Around it a retail park has grown up - next door is a 40,000 square foot B&Q do-it-yourself outlet, which is proving too small for that company in 2002. An agreement has been reached between the two businesses. B&Q will move into the Hornby factory and expand. Hornby will move and build new premises, acquiring the existing B&Q, part of which will be developed as the Hornby Heritage Centre, featuring, amongst other things, a museum, interactive layouts and a store.

Might Frank Martin be justified if he thought that once more Hornby was swimming with the tide rather than against it? And is so, where next? At its height Meccano Ltd featured three winning products - Meccano sets, Dinky toys and Hornby Dublo trains. Would another product range be appropriate or a risky and unnecessary diversification?

Appendix 1 - Hornby Hobbies main product range, 2002

HORNBY ELECTRIC TRAINS
Complete sets (including tracks and train systems) - 8 alternatives
Locomotive and carriages/trucks sets - 10 alternatives
Steam locomotives - 70 alternatives

**Including:**
*Merchant Navy Class* - 5 engines - Brocklebank Line, Port Line, Bibby Line, Clan Line and Canadian Pacific
*9F* 2-10-0 locomotives - 3
*Princess Coronation Class* - 4 streamlined, 2 non-streamlined
*A4 locomotives* - 2 - Silver Fox and Mallard
*West Country Class* - 3
*Battle of Britain Class* - 3
*The Flying Scotsman*

*plus some 50 more including tank engines*

Diesel and electric locomotives - 20 alternatives
Passenger rolling stock
Freight rolling stock
Tracks
Buildings
Landscaping materials
Harry Potter train sets
Thomas the Tank Engine sets
The Virtual Railway CD

**SCALEXTRIC**

Sets and multiple car designs in the following series:
Road and Rally - old and modern
Endurance Racing - such as Le Mans cars
American Classic cars
NASCAR - National Association for Stock Car Auto Racing, USA
Formula One
Single Seaters
Touring Cars

*Plus:*
Tracks
Bridges and other circuit features
Grandstands and other circuit buildings
Figures.
Appendix 2

Five year financial summary - selected data for year ending 31 March - most figures in £'000s

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<td><strong>Turnover</strong></td>
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<td>– before exceptionals</td>
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<td></td>
<td>3,722</td>
<td>1,500</td>
<td>1,200</td>
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<tr>
<td><strong>Pre-tax profit</strong></td>
<td></td>
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<td>– after exceptionals</td>
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<td><strong>Net assets</strong></td>
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<td>13,271</td>
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<td><strong>Earnings per Share – pence</strong></td>
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<td>11.3p</td>
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<td><strong>Shareholders Funds</strong></td>
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