

What Happened in Samsung?: An Asian Management Perspective



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Samsung (三星) Story

- ❖ Samsung History
- ❖ Economic Power
- ❖ Samsung Electronics
- ❖ Governing Structure
- ❖ Management System
- ❖ Samsung Under Chairman Lee, Kun-hee (李健熙)



Samsung History

- ❑ 1938: Small rice trading outfit in Daegu
 - Founder: Lee, Byung Chul
- ❑ 1950's: Sugar, Textile, Retail
- ❑ 1960's: Electronics, Fertilizer, Paper
- ❑ 1970's: Construction, Electronic Components, Heavy Industry, Synthetic textiles, Petrochemicals, Shipbuilding
- ❑ 1980's: Aircrafts, Bioengineering, Semiconductors
- ❑ Present: Conglomerate (Chaebol) with 59 Corporations
 - 70 Years Old
 - Amusement Park, Information Systems, Security, Insurance, Hotel, Hospital, Baseball, ...

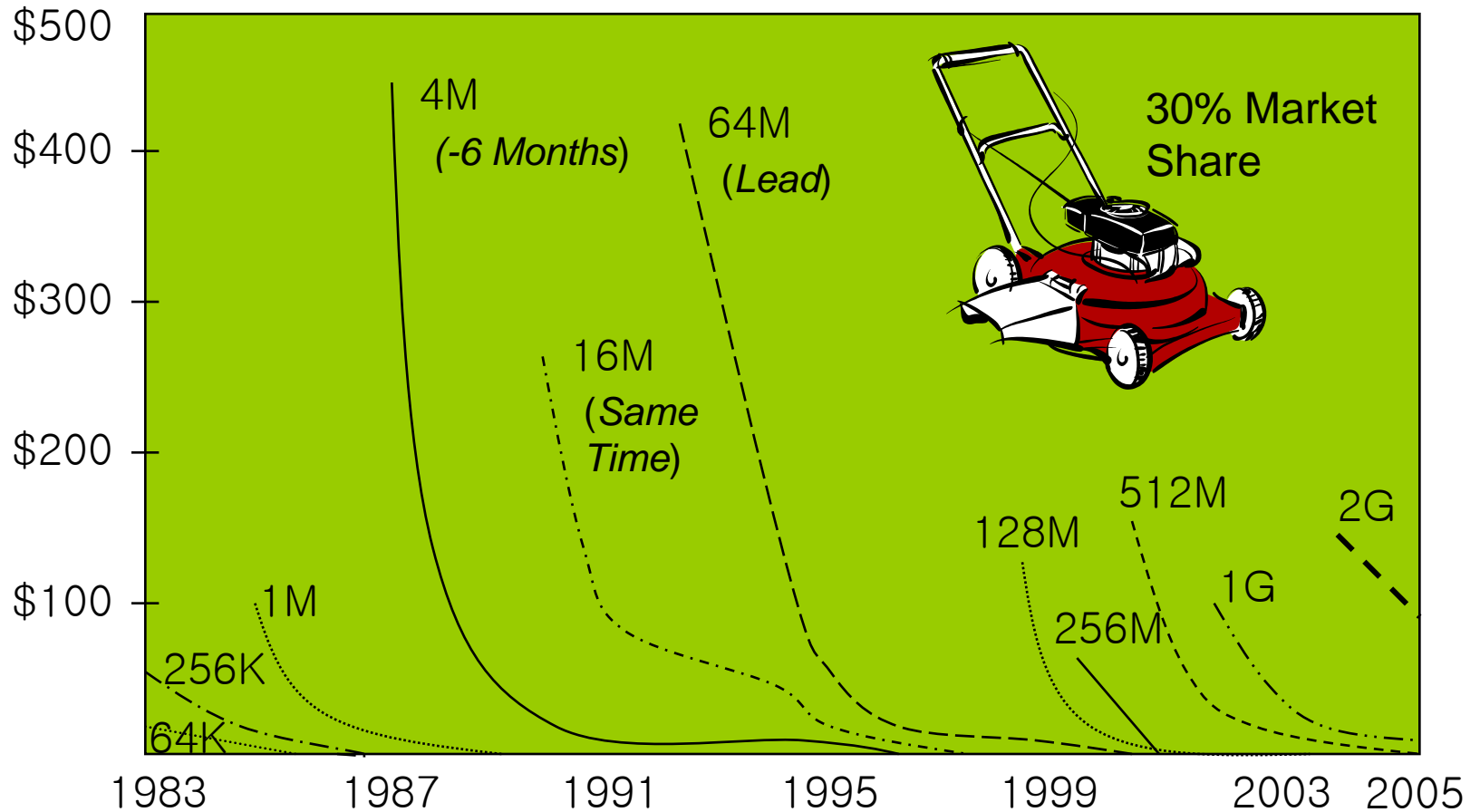
Samsung's Economic Power

- Total Revenue: \$160 Billion (17.3% of GDP)
 - About the Same Size of Singapore's GDP
- Export: \$70 Billion (20.4% of National Exports)
- Brand Value: \$17 Billion (Global Ranking: 21st)
- Market Capitalization of Listed Companies: \$140 Billion (14% of the Total KOSPI)
- Proportion of Corporate Tax in Korea: 25%
- Employment: 261,000 (169,000 in Korea)

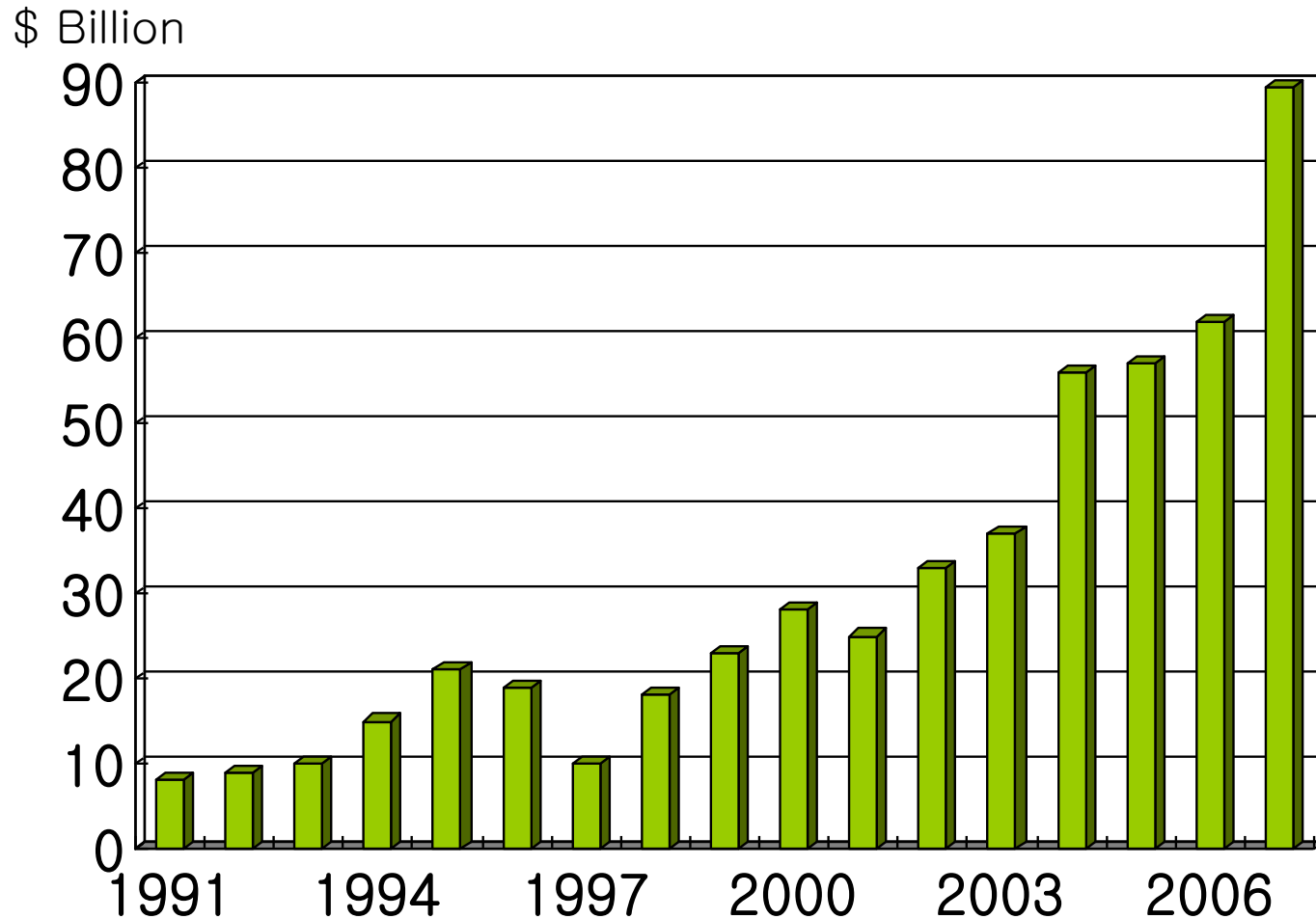
Samsung Electronic's Success

- Flagship Company of Samsung Group: Established in 1969
 - \$89.5 Billion Revenues, \$8.3 Billion Profits in 2007
 - Global Ranking 46, Top in Semiconductor & LCD, 2nd in Cell-phone
 - About 70% of Group in Market Cap & Over 40% Revenue
- Keys for the Success of Samsung Electronics
 - Speed and Efficiency
 - Production Efficiency (Commodity): Yield Management, ERP
 - Heavy Investment in R&D: 40% of Employees & 3,200 Ph.Ds
 - Speed: Grass-Cutter Strategy (High Risk High Return)
 - Owner Leadership
 - Supported by Strategic Planning Office (SPO)
 - Bold Investment Decision
 - Decisive Coordination Among Group Businesses
 - LCD: SDI -> Samsung Electronics (SE)
 - Digital Camera: Samsung Techwin -> SE

Product Characteristics: Price of DRAM

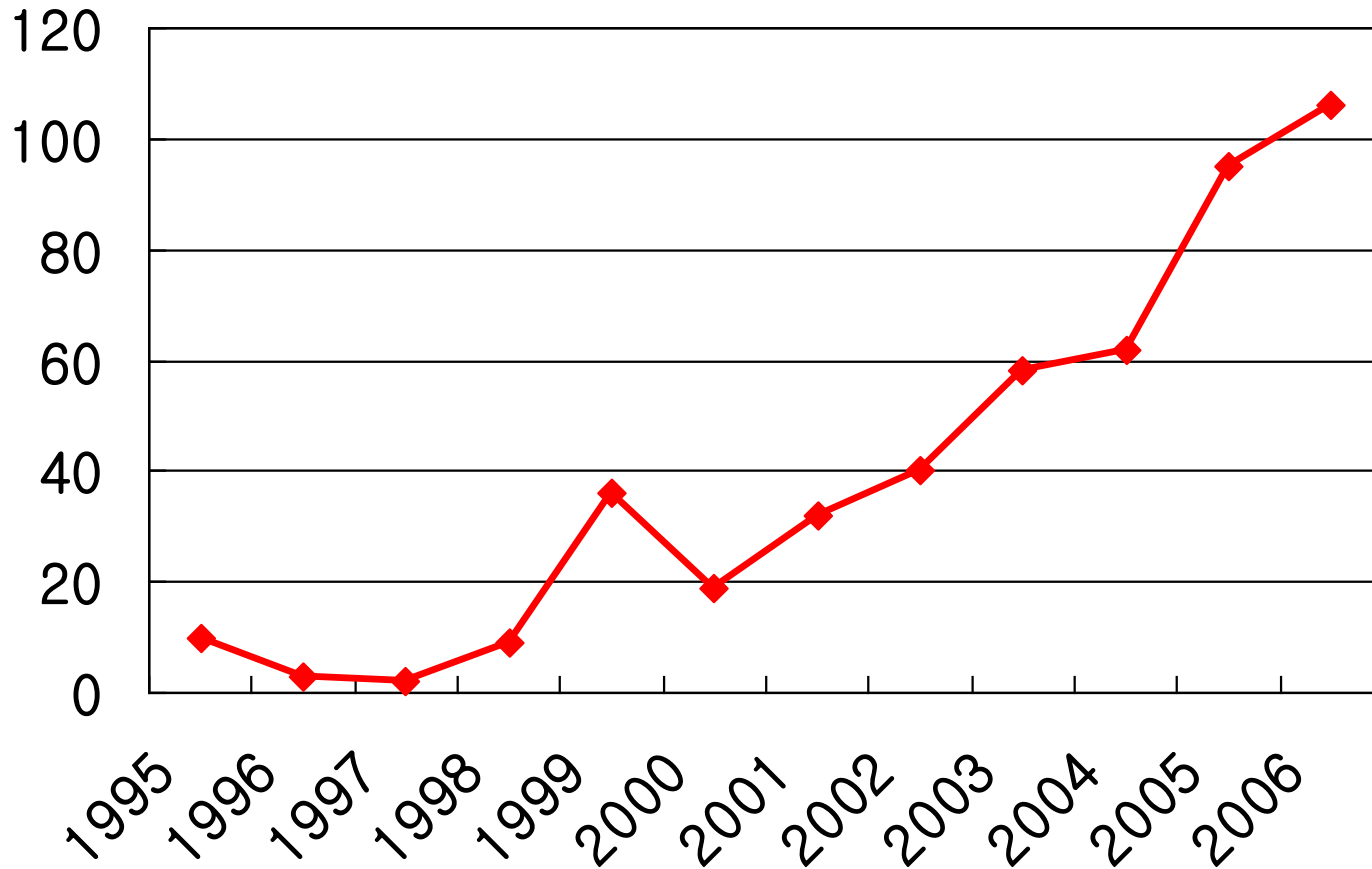


Revenue of Samsung Electronics



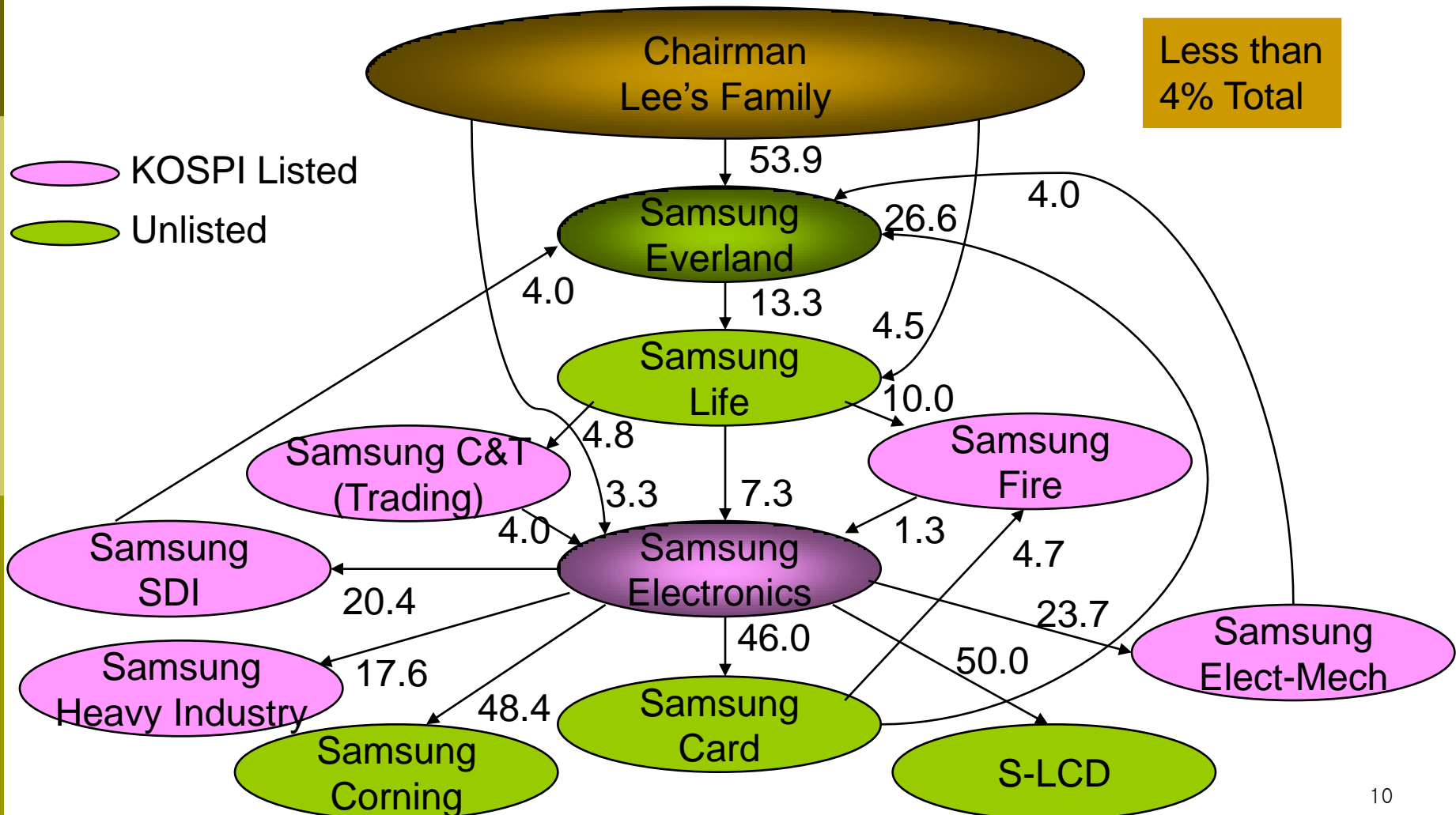
Market Capitalization of Samsung Electronics

\$ Billion



More than
Double of
Sony, Philips

Governing Structure of Samsung: Pyramid Structure



Samsung's Management System

- Organizational Structure
 - High Degree of Centralization & Formalization
 - Business Unit & Team Organization
- Leadership: Strong Authoritarian Style of Superiors
 - Top-down Decision Making
 - Personal harmony among Superiors-Followers: Inhwa (人和)
- Motivation
 - More Extrinsic Factors (Wages, Working Conditions, Job Security) than Intrinsic Factors (Creativity, Achievement)
 - Strict Discipline (管理 三星) and Loyalty
 - Incentive Bonus: Profit Sharing System
- Communication: Vertical Communication

Chairman Lee's 'New Management' (新經營)

- Frankfurt Declaration of 'New Management' in 1993
 - CHANGE: "Change everything except for your wife and children!"
- 7-4 System: Start work at 7 a.m. and finish at 4 p.m.
 - Killing 5 Birds with One Stone: '*Wake-Up Effect*'
 - Get up early to raise the consciousness of crisis
 - Raise the quality of life by having personal time for retraining or hobby
 - Contribute to alleviate the traffic congestion during rush hour
 - Reduce the logistic cost and raise the efficiency of work
 - More time with family: Peace and happiness at home
- World Best Samsung (超一流 三星)
 - Quality Not Quantity
 - Bonfire 150,000 Units of Low Quality Mobile Phones (Worth \$15 Million)
 - Ethics Focus: Only ethical company can make good products
 - CEO: Chief Ethics Officer

'New Management' (continued)

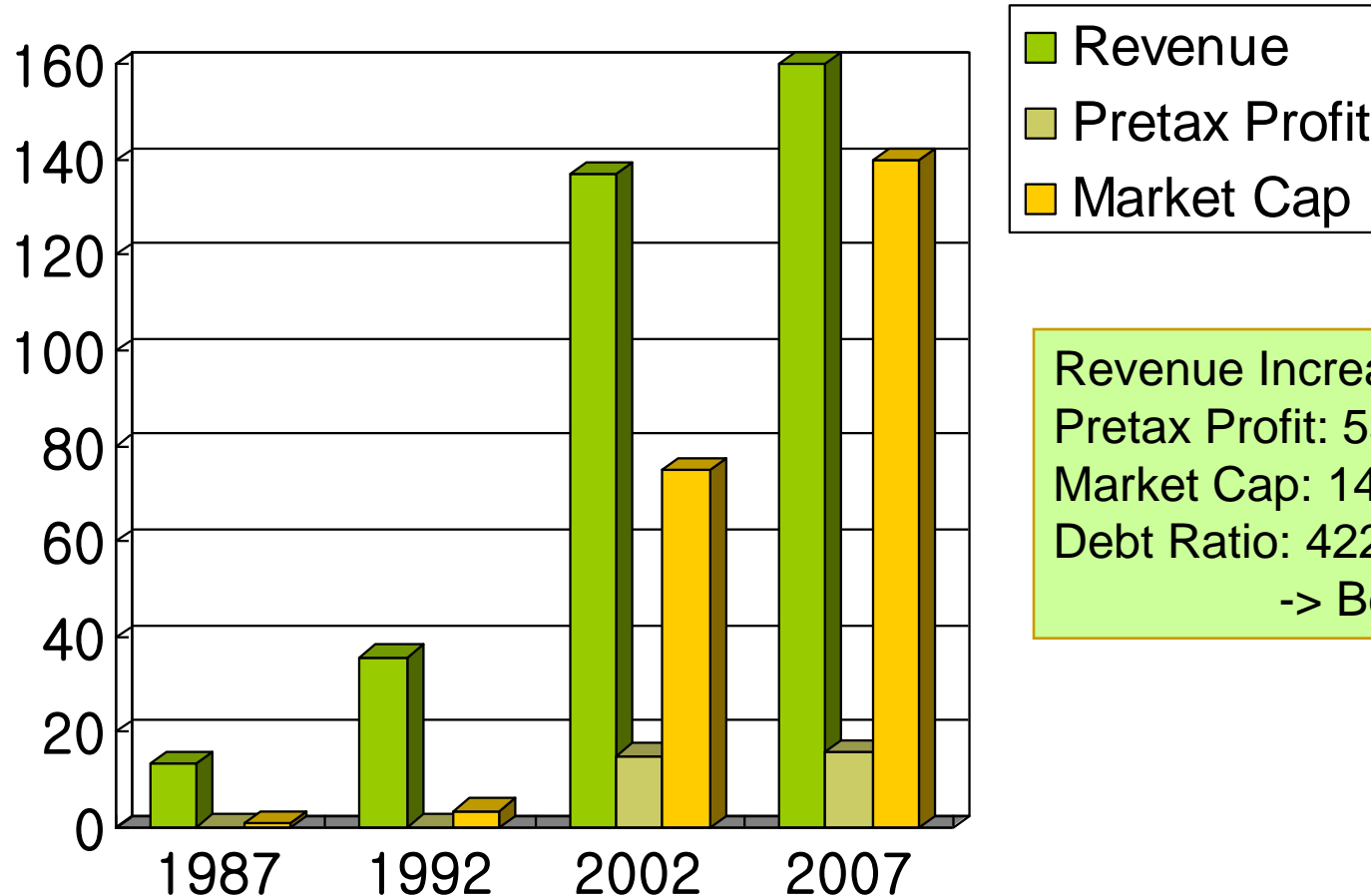
- Cultivation of Top Manpower
 - Techno-MBA at KAIST: 2 Year Full-time (1995-)
 - Regional Specialist: Spend free 1 Year in a foreign country
- Information Infra & Process Innovation
 - ERP: Reduction of Inventory (1/2), Insolvent Obligation (1/2)
 - CRM, SCM, KMS
- Design Innovation
 - Samsung Identity
- Complex (複合化): Mix All Needs in One Place
- Global Marketing: Brand, Sports (Olympic) Marketing
- Emphasis on Technology
 - Cell-phone: Chairman's Design (Nitty-gritty details of gadgets)
- Genius Management (天才經營): Creativity
 - Manpower: S(uper), A(ce), H(igh Potential)

Chairman Lee's Leadership

- Hermit King (Newsweek, 2003)
 - Invisible Man
 - Mixed Evaluation: Reclusive Nerd vs. Outstanding Genius
- Charismatic Leadership: Autocratic Delegation/Entrust
 - Big Picture and Key Decisions
 - Empowerment: “疑人不用 用人不疑”
 - “If you don't believe one, don't use. If you use, believe in him or her”
 - Management by Un-management for Normal Business
- Execution Orientation
 - Decisive Actions
 - Detailed Follow-up: Cell-phone Development
 - Speed in Key Decisions
- Consistency & Long-termism
 - Evaluation, HRM
 - Longer tenure for CEOs: More than 10 years, e.g., Vice Chairman Yoon J.Y.

Samsung's Performance Under Chairman Lee K.H.(1987-2007)

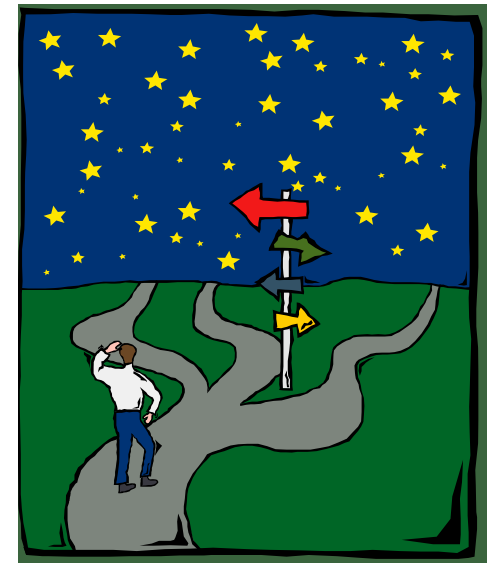
\$ Billion



Revenue Increase: 12 Times
Pretax Profit: 53 Times
Market Cap: 140 Times
Debt Ratio: 422%
-> Below 80%

Samsung Scandal

- ❖ Samsung Scandal: Facts
- ❖ Why It Happened?
- ❖ Inheritance Issue
- ❖ Samsung's Hubris
- ❖ Conflicts with Western Management
- ❖ Samsung's Reform



Samsung Scandal: Facts



- Lee Kun-hee, Chairman of Samsung Group: Charged with *tax-evasion* and *breach-of-trust* in April 2008
 - \$4.5 Billion secret funds in 1,200 false-name bank accounts: \$110 Million tax evasion
 - Breach fiduciary duty: Letting his children buy (convertible) bonds of Samsung's affiliate companies through irregular financial transactions, incurring losses at the companies
 - Cleared bribery charge: due to lack of evidence

Why Samsung Scandal Happened?

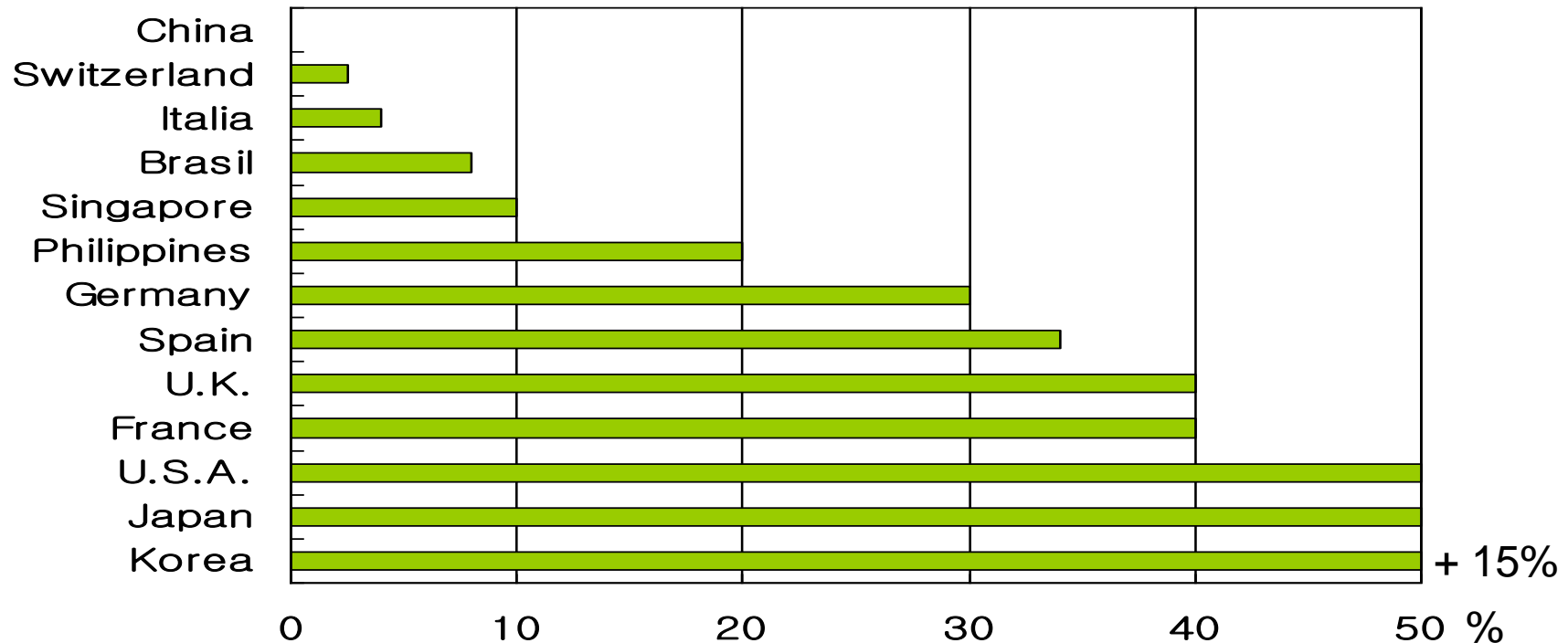
- Inheritance of Ownership
 - Tradition of Owner-management
 - Phenomenal achievement under Chairman Lee
 - Strong Preference of Blood-relationship
 - Insufficient Proof of Heir Son's Capability: Weak Public Acceptance
 - The 3rd Generation Syndrome
- Paradox of Success
 - Hubris: A Natural Law
 - Excessive 'Can-Do' Spirit
 - Excessive Confidence and Influence to the Whole Country
- Conflicts between Global & Korean/Asian Managements
 - Traditional value of Korean/Asian management
 - Rule Changes: The Real-name Financing Transaction System (1993)
 - Public awareness of global standards and Anti-Corporation Sentiment (反企業情緒)

Inheritance Issue

- Two (Ab)Normal Practices
 - Convertible Bond: Samsung
 - Buy convertible bond of unlisted company at a substantially low price (1/11 of Market Value)
 - Realize the Convertible Bond to build a seed money
 - Buy stock of holding-like company
 - Control through pyramid-structure of cross shareholding
 - Unfair Favor: Hyundai Motors
 - Establish an unlisted company
 - Give one-sided unfair favor such as supply of parts, logistics, sales, etc. to build a seed money
 - Buy stock of major company to control
- Legal but Unethical Practice: Board of Trustees
 - Groups tend to act in their common interest: Not True
 - Role of External Independent Board Member is very limited

Inheritance Tax

- 71 Countries have zero inheritance tax
 - China, Canada, Australia, New Zealand, Russia, Sweden, Malaysia, Mexico, India, Thailand, Portugal, Hong Kong, ...



Arguments on Inheritance Tax

□ Pros

- Inequality Solution
- Protect Excessive Accumulation of Wealth
- Contribution to Tax Revenues

□ Cons

- Prohibit Capital Accumulation and Economic Growth
- Against the Entrepreneurship
- Unethical Tax: Milton Friedman
 - Encourage Spending than Saving
- Inequality of Consumption: Joseph Stiglitz
- Harmful to Labor: Gregory Mankiw
 - Decreased accumulation of capital may lead to the increased inequality of wealth

Samsung's Hubris

- ❑ Success of Samsung Electronics
 - Became the National Pride as a World Top Class Company
 - 59 Companies in the Group closely collaborate to become the biggest group
- ❑ Influence to Every Part of Country
 - Administration/Politics
 - ❑ Recruit Retired and/or Influential High-ranking Officials
 - ❑ Token of Good-will (Pseudo Bribery)
 - Media
 - ❑ Control by Advertising Contract
 - Academics
 - ❑ Influential Group in the Society
- ❑ Republic of Samsung: Public Resistance

Samsung's Conflicts with The Western Management Practices

- Key is Corporate Governance
 - Owner Management
 - Independence of Board of Trustees: Transparency
- Other Asian Management Practices
 - Stakeholder Idealism, Autocratic Leadership, Seniority-based Promotion, (Semi-)Lifetime Employment, Hierarchical Organization, ...
- Are these all bad? Outcome tells!
- But *Corporate Governance* issue will remain.

Samsung's Reform

- ❑ Chairman Step Down
 - Accountability: Leader takes the responsibility
 - Top executives also quit
- ❑ Reform Corporate Governance
 - Change and Strengthen Independent Directors in the Board
- ❑ Dismantle Strategic Planning Office
 - Powerful central control across the whole Group
- ❑ Sell Samsung Card's 24% stake in Everland
 - To reduce cross-shareholdings
- ❑ No Banking nor Holding Company



Efforts towards More Transparency,
More Autonomy, No Cross-sharing

Roots of the Issue

- ❖ What is Company?
- ❖ What is Management?
- ❖ Western and Eastern Way of Thinking
- ❖ Asian and Western Management
- ❖ Experiments of Asian and Global Management



What is Company?

- Ideas of Modern Company
 - Artificial Person: Same ability to do business
 - Issue tradable shares to any number of investors
 - Investors could have limited liability
- The Companies Act of 1862 (Britain)
 - Limited-Liability Joint-Stock Company
 - No special sanction from parliament for limited and specific worthy aim: Chartered corporations, e.g., Railway, Harvard, ...
 - Copied to other European Countries and America
 - “The greatest single discovery of modern times” N. M. Butler
- Success in America
 - Competition Among the States: Favorable conditions, corporate tax

Issues of Company

- A Legal Entity
- Historical Concerns
 - Less efficient than sole traders: Adam Smith
 - Agency problem: Hired managers would not bring the same “anxious vigilance” to their firm’s interest as owner-managers
- Ownership
 - Shareholder Ideal: Anglo-Saxon Model
 - Stakeholder Ideal: German-Japan Model
- Social Responsibility
 - A Franchise from Society
 - Company is an organ of society and exists for the sake of society
 - Cum + panis: Breaking bread together

What is Management?: Drucker's View

- Management is about *human beings*.
 - It's task is to make people capable of joint performance, to make their strengths effective and their weakness irrelevant.
- Management is deeply *embedded in culture*.
 - What managers do is exactly the same but How they do it may be quite different.
- Management must also enable the enterprise and each of its *members to grow and develop* as needs and opportunities change.
- The results of enterprise exist *only in the outside*.

Fundamental Question (R.E. Nisbett): Western vs. Eastern Way of Thinking

	West <i>Individualism</i>	East <i>Collectivism</i>
Agency	Personal Agency	Collective Agency
Happiness	Liberty	Harmony
Rights	Individual Rights	Community Rights
Focus	Object	Relationship
Social Norm	Diversity	Unity
World View	Reductionism Static View	Holism, Ying-Yang Dynamic View

Asian Cultural Traits

- Collectivist Norms
 - High Family Values
 - Hierarchy-Sensitive
 - Equality of Result
 - Consensus Formation
 - Relationship Orientation
- Education Emphasis
- Strong Work Ethics
- Pragmatism & Thriftiness
- Cooperation
- Long-termism
- Heavy Government Involvement

Asian vs. Western Management

	Asia	West (U.S.)
Corporate Governance	Owner Management	Professional Management
Board of Trustees	Internal Execution & Supervision	Separate Execution & Supervision
Idealism	Stakeholder	Shareholder
Focus	People	Work Task
Leadership	Autocratic	Democratic
Promotion/Pay	Seniority-based	Performance-based
Employment	Lifetime	Contract
Orientation	Group/Society & Relationship	Individual
Trust	Human Relationship	Social Contract
Time Frame	Long Term	Short Term
Organization	Hierarchical	Horizontal

Experiments of Asian Management

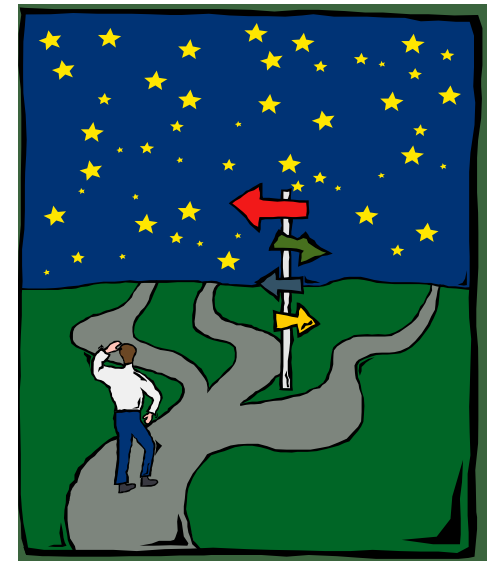
- Corporate Governance: POSCO and KT
 - Active Role of Independent (External) Directors
 - Stakeholder Model
- Owner Management: Toyota, LG, Samsung, Daewoo
 - Society Accepted Succession of Family Member: Toyota
 - Holding Company with Owner-Control: LG
 - Wise King (賢帝) Model of Owner Management: Samsung
 - Leave what professional manager can do better but make key decisions
 - Almighty Emperor (皇帝) Model: Daewoo
 - Do everything by the owner: High Risk led to Failure
- Performance-based Pay System: Fujitsu, Nikko Securities
 - Failure in Fujitsu, Success in Nikko Securities
- Lifetime Employment: Toyota, Cannon
 - Performance-based Lifetime Employment: Cannon
 - Combination of Performance based merit system and stability of employment
- Hierarchical Organization: Toyota
 - Switch back to hierarchical structure after experimenting horizontal structure

Experiment of Global Management: Sony Story

- ❑ Adopt a US-style Management Structure (2003)
 - Abolish Japanese-style audit system
 - Create a committee structure with a majority of independent directors
- ❑ Change of Top Management (2005)
 - CEO Idei Nobuyuki: World's Best Manager (1997) -> Worst Manager (2004)
 - Chairman & CEO: Howard Stringer (British)
- ❑ Difficulties of Sony
 - Revenue \$70 Billion, Profits \$1 Billion in 2007
 - Profit Rate: 8% (97) -> 1.4% (07)
 - Market Capitalization: \$80 Billion (00) -> \$53 Billion (07)
- ❑ Reasons of the Difficulties
 - Hubris: Technical Prowess, First Global Company in Japan
 - ❑ Legacy: Huge Success of Analog led Missing to Catch On Digital Trend
 - Confusion of Japanese/Asian and Global Management
 - ❑ Short-termism
 - ❑ Either Not-Ready Or Not-Fit: Externally Global But Internally Japanese

Additional Considerations

- ❖ Family Business
- ❖ Collective Relationships in East Asian Countries
- ❖ Corporate Governance in Korea: A Survey



Additional Considerations: Family Business

- Is family-owned or -controlled business bad?
 - More than 50% of GDP in U.S.A.
 - More than 80% in Europe
- Ford
 - Ford Family control the Ford Company with 1% of share but more than 40% (discriminated) voting rights
- Toyota
 - The biggest family(-controlled) business in Japan
 - Similar governance structure with Samsung
 - Toyota Akio (3rd Generation) is expected to succeed
 - No Public Resistance: Why?
 - Capability Proof Process, Pro-Corporation Sentiment (親企業情緒)

Collective Relationships in East Asian Countries

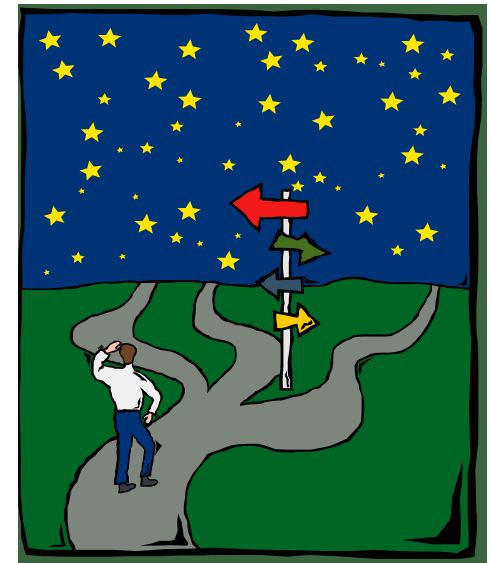
- China: Guanxi-Oriented
- Korea: Personal Relationship-Oriented
 - Blood (血緣) > School (學緣) > Home Region (地緣)
- Japan: Organization-Oriented
 - Succession of Ownership by Blood or Adoption
 - High Survivability of Companies
 - World's Oldest Company: Kongogumi (金剛組) Construction Company (578 A.D., 1430 Years Old)
 - Over 50% of the 200+ Years Old Companies in the World (3146/5586)
 - Korea: Only 2 Over 100 Years Old Companies

Corporate Governance in Korea: A Survey

- Korean CEO Survey (Forbes Korea, 2008)
 - Shareholder Capitalism: 11%
 - Stakeholder Capitalism 52%
 - Customer(9.8), Employee(9.2), Shareholder(8.3)
- Owner Management vs. Professional Management
 - Which Fits Korean Business?
 - No One Solution: 58%
 - Professional: 22%, Owner: 19%
 - Owner Management: Manufacturing
 - Professional Management: Finance, Service, Construction, Retail/Distribution

Conclusions

- ❖ Towards Global Management
- ❖ Study of Asian Management
- ❖ Final Thoughts



Towards Global Management

- Convergence or Cross-verging Trend
 - Westernization of Asian Management
 - Asia Eclipse after Financial Crisis: Cronyism, Favoritism, Corruption, ...
 - Towards Transparency, Shareholder Value, Rational Decision Making, ..
 - Asianization of Western Management
 - Disadvantages: Short-termism, Systemic Irresponsibility, ...
 - Towards Human-Centered, Social Responsibility, Sustainability, ...
 - Sub-prime Financial Crisis and Questions on Market Capitalism :
 - Creative Capitalism, Value-based Capitalism, ...
 - From Maximization of Profit to Maximization of Society's Good (社會善)
- There is no single model of global management
 - A myth: There is the one best global (western) management system
 - Superficial Globalization: Difficult to change the inside of Human
- Success of Asian economy will depend on the success of finding Asian management fit to culture and global business

Study of Asian Management

□ Need Systematic and Extensive Study of Asian Management

- Past Studies: Analysis Given I & S -> O
- Future Studies: Design Given I & O -> S
 - To Find Cultural-Fit Model



Final Thoughts

- ❑ Hubris is the Cancer of Successful Companies
- ❑ There is no Unilateral Model of Management
- ❑ There are strengths and weaknesses in both Western management and Asian management systems
- ❑ An Extravaganza of Management Experiments is going on in Asia
- ❑ Management system that doesn't fit to it's culture will be doomed to fail
- ❑ Right management system will be the definite competitive advantage
- ❑ We need an extensive and systematic study on the Asian management not only for Asian companies but also for global companies
- ❑ Values of Transparency, Accountability, Social Responsibility and Sustainability will continue to be the Global Norm for Business
- ❑ The 21st Century can be 'the Asian Century' only if we can find Asian management models fit to it's culture and global business

Thank you!

謝! 謝!