

# What Happened in Samsung?: An Asian Management Perspective



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# Samsung ( ) Story

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



# Samsung History

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- ❑ 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

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- ❑ 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: 21<sup>st</sup>)
- ❑ 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

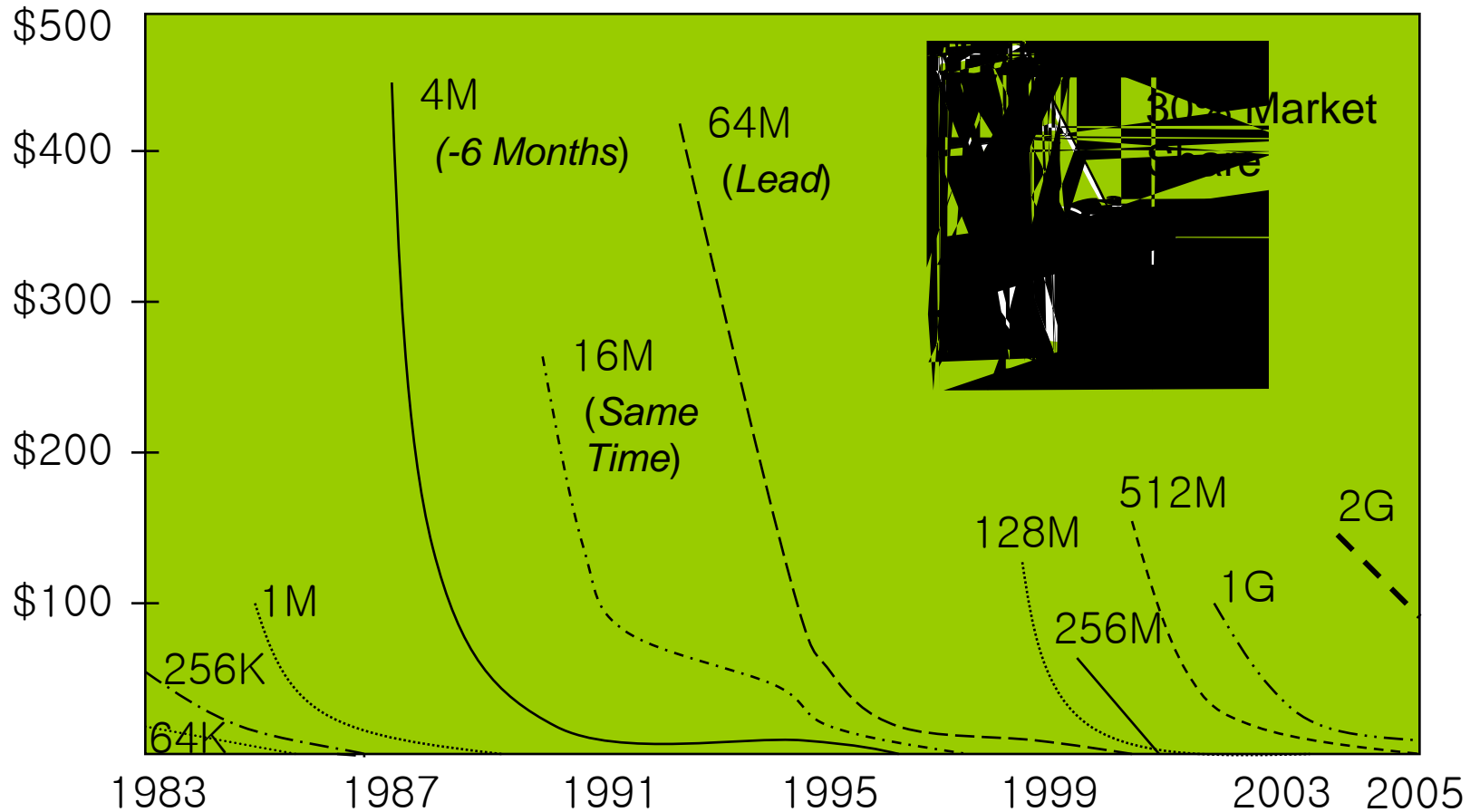
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- ❑ Flagship Company of Samsung Group: Established in 1969
  - \$89.5 Billion Revenues, \$8.3 Billion Profits in 2007
  - Global Ranking 46, Top in Semiconductor & LCD, 2<sup>nd</sup> in Cell-phone
  - About 70% of Group in Market Cap & Over 40% Revenue
- ❑ 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:

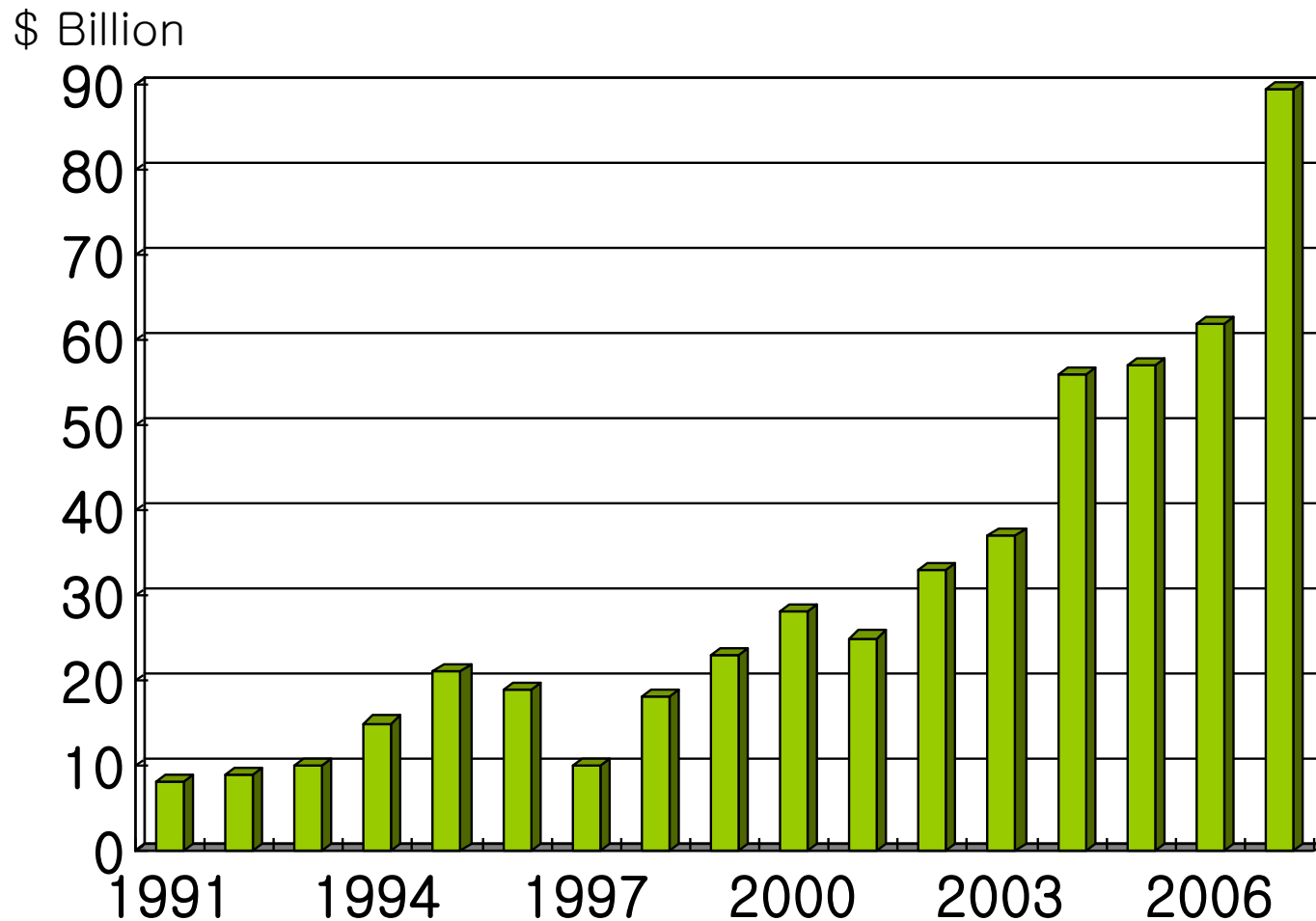
## Price of DRAM

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# Revenue of Samsung Electronics

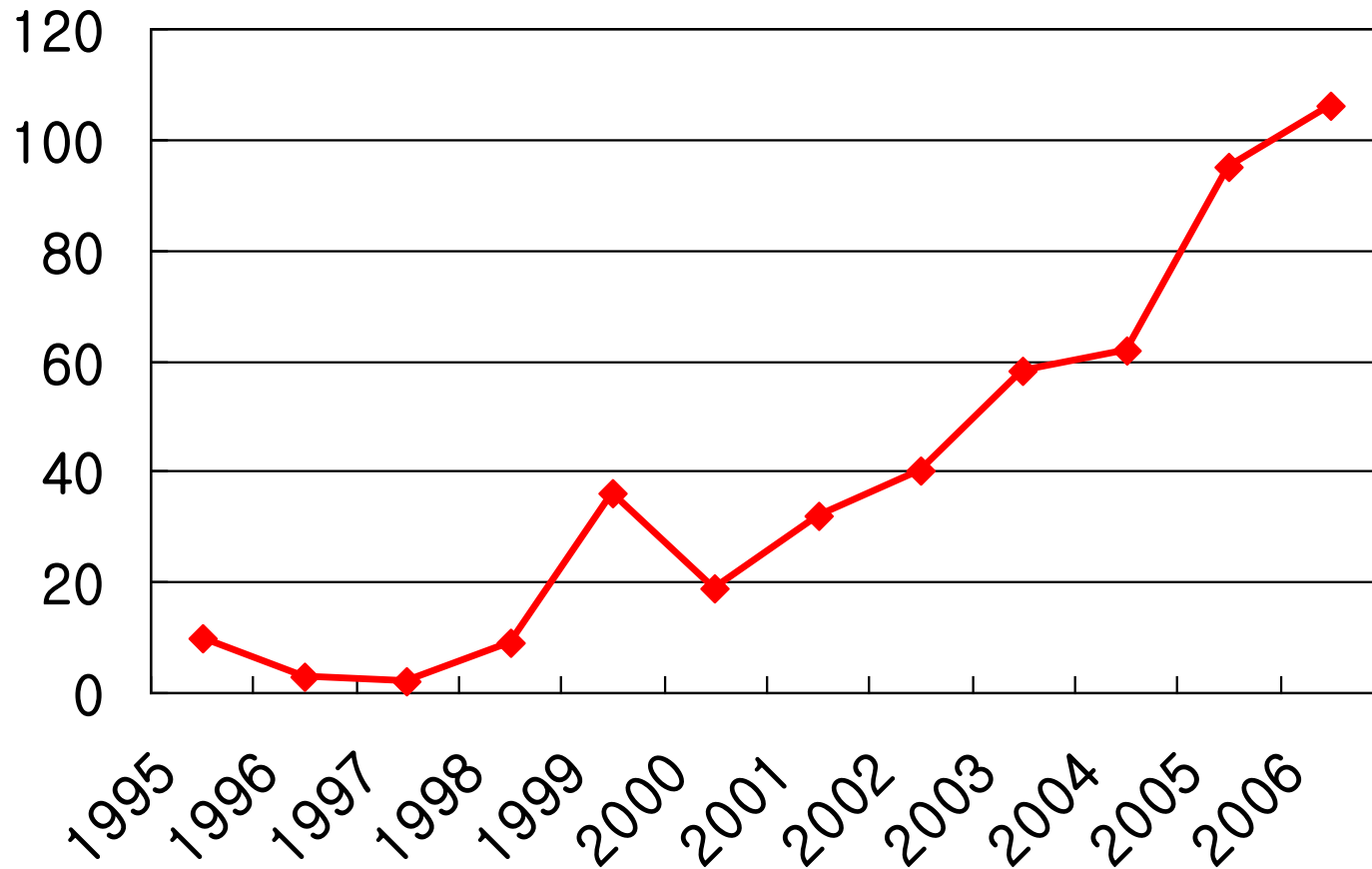
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# Market Capitalization of Samsung Electronics

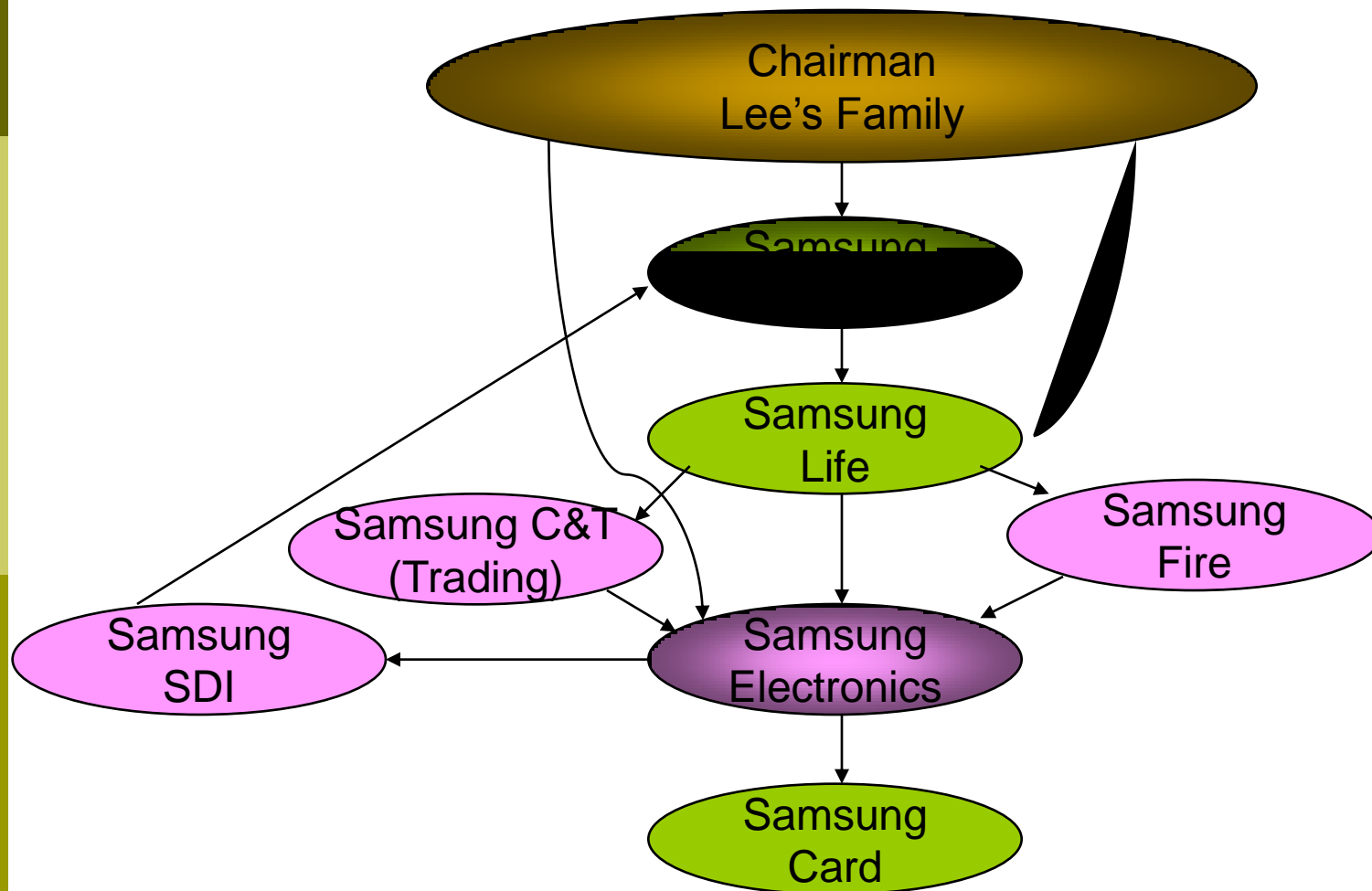
\$ Billion



More than  
Double of  
Sony, Philips

# Governing Structure of Samsung: Pyramid Structure

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# Samsung's Management System

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- ❑ 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 (      )
- ❑ Motivation
  - More Extrinsic Factors (Wages, Working Conditions, Job Security) than Intrinsic Factors (Creativity, Achievement)
  - Strict Discipline (                      ) and Loyalty
  - Incentive Bonus: Profit Sharing System
- ❑ Communication: Vertical Communication

# Chairman Lee's 'New Management' ( )

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- ❑ 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 ( )
  - 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)

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- 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 ( ): Mix All Needs in One Place
- Global Marketing: Brand, Sports (Olympic) Marketing

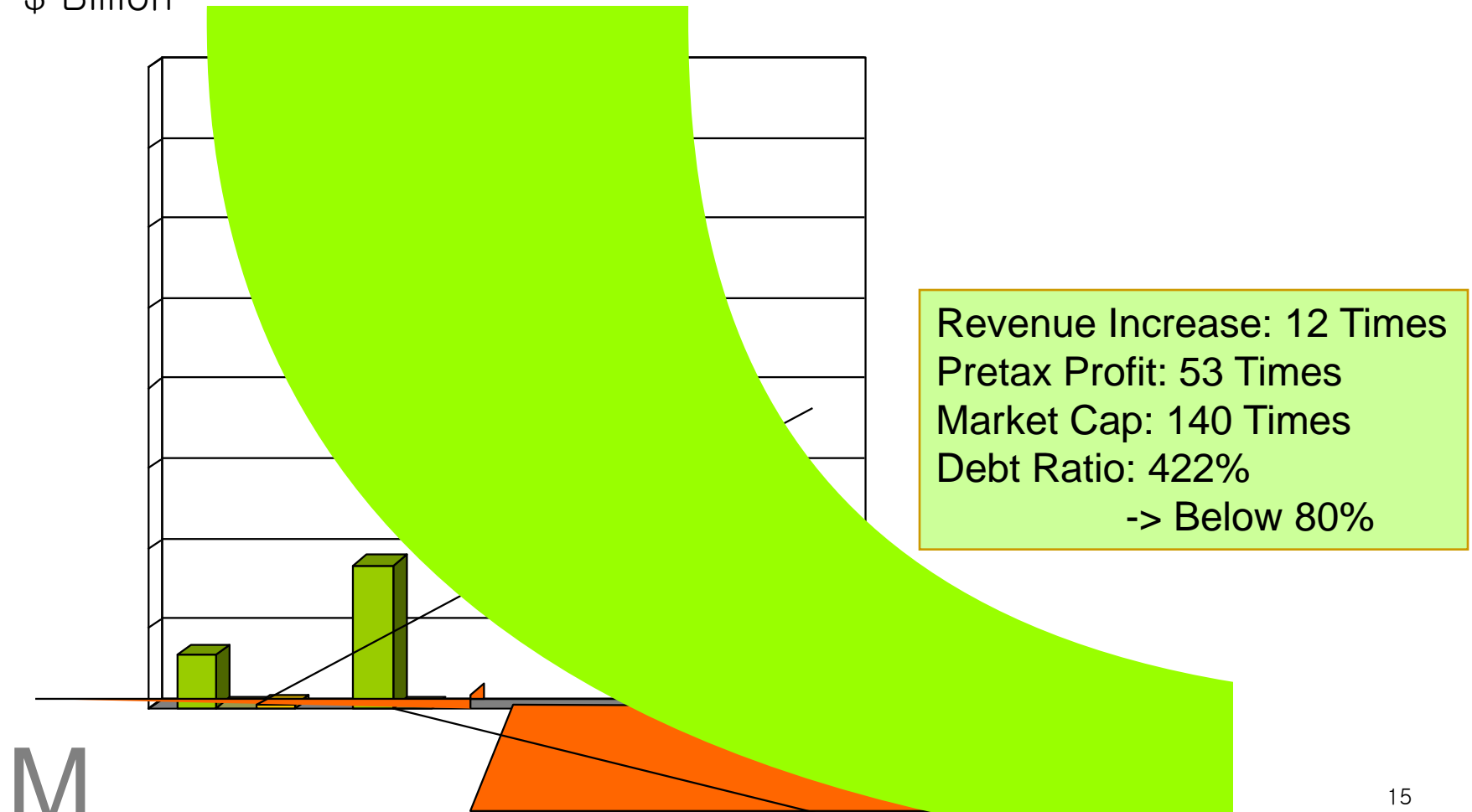
# Chairman Lee's Leadership

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- ❑ Hermit King (Newsweek, 2003)
  - Invisible Man
  - Mixed Evaluation: Reclusive Nerd vs. Outstanding Genius
- ❑ Charismatic Leadership: Autocratic Delegation/Entrust
  - Big Picture and Key Decisions
  - Empowerment: “
    - ❑ “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



# Samsung Scandal

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





# Samsung Scandal: Facts

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- ❑ 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?

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- ❑ 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 3<sup>rd</sup> 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 ( )

# Inheritance Issue

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## ❑ 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

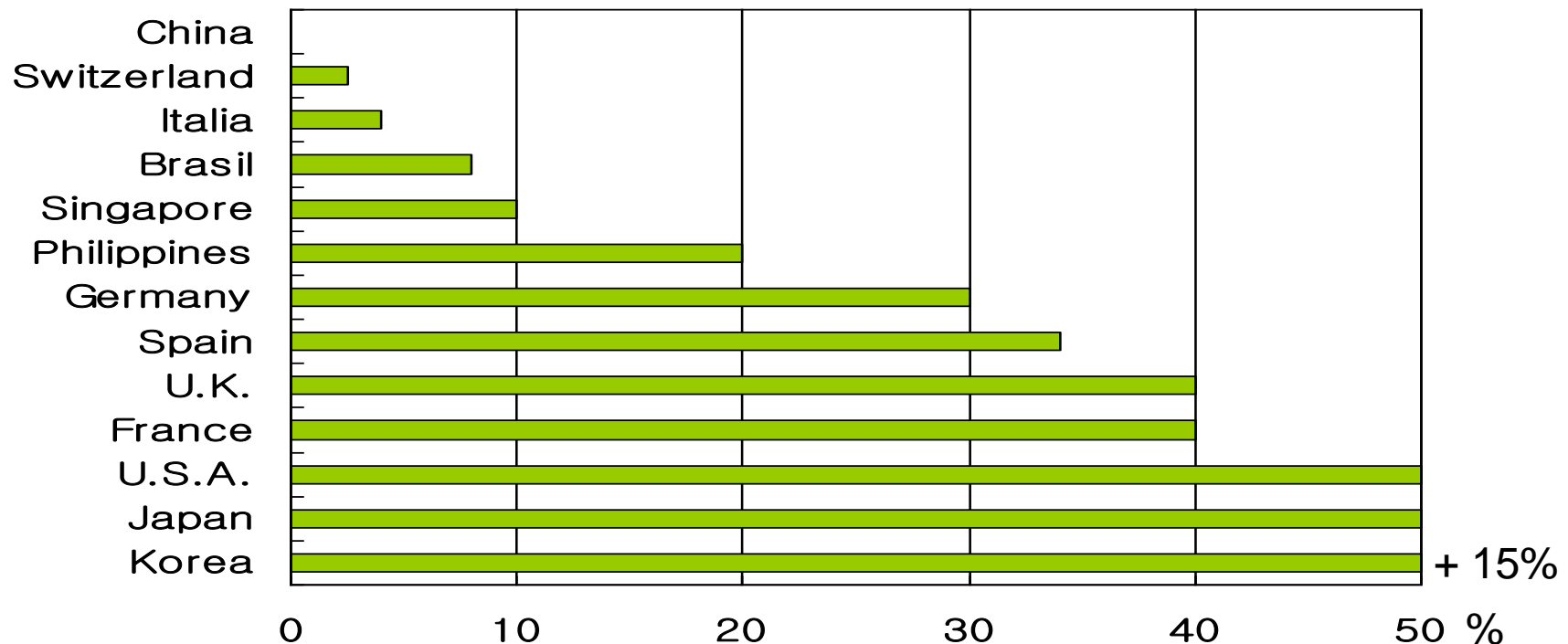
- ❑ Establish an unlisted company
- ❑ Give one-sided unfair favor such as supply of parts, logistics, sales, etc. to build a seed money
- ❑ Buy stock of major company to control

## ❑ 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, ...



+ 15%

# Arguments on Inheritance Tax

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## □ 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 Conflicts with The Western Management Practices

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- ❑ 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

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- ❑ 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

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- ❖ 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?

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- ❑ 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

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- ❑ 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

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- 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

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	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

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

# Experiments of Asian Management

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- ❑ 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 ( ) Model of Owner Management: Samsung
    - ❑ Leave what professional manager can do better but make key decisions
  - Almighty Emperor ( ) 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

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- ❑ 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

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



# Additional Considerations: Family Business

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- ❑ 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 (3<sup>rd</sup> Generation) is expected to succeed
    - ❑ No Public Resistance: Why?
      - Capability Proof Process, Pro-Corporation Sentiment ( )

# Collective Relationships in East Asian Countries

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- ❑ China: Guanxi-Oriented
- ❑ Korea: Personal Relationship-Oriented
  - Blood ( ) > School ( ) > Home Region ( )
- ❑ Japan: Organization-Oriented
  - Succession of Ownership by Blood or Adoption
  - High Survivability of Companies
    - ❑ World's Oldest Company: Kongogumi ( ) 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

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- ❑ 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

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



# Towards Global Management

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- ❑ 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 ( )
- ❑ 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





# Final Thoughts

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- ❑ 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
- ❑

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***Thank you!***

**!!**