A Comparative Study on Competitive Strategies of Foreign and Local Discount Stores in Korea

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Introduction
Since 1993 when the first discount store was introduced in Korea, the sector has grown dramatically with the deregulation of Korean distribution industry in 1996. The aggressive thrust of international players into the Korean retail market has set to motion a restructuring of the distribution industry. This thrust has brought leading international players in head-to-head competition with existing local discount stores such as E-Mart and Lotte Mart, although so far the clash has resulted in a surprising triumph of the local players. A more serious result, however, is the upsurge competition with other retail formats. As such, the advent of the discount store has had tremendous impact on inter- and intra-type competition, yielding both positive and negative consequences.

The current study delves into several issues regarding the discount store sector in Korea, with a comparative analysis of the international players and domestic ones. More specifically, this study aims to investigate:

1) how discount stores evolved,
2) how are they competing against each other and among other retailers in different formats,
3) what the major business strategies are,
4) what their effects on other retail formats are,
5) whether the international players are really competitive, and finally
6) what international and domestic players need to do in order to remain competitive.

The paper is organized into seven sections. The first section describes the discount store sector in Korea very briefly and defines the intent of this paper. The second section describes the current situation and characteristics of discount stores in Korea. The third section describes the competition in the market, focusing on similarities in organizational form and strategies. The fourth section selects five major discount stores and explains each company's business strategies briefly. The fifth section discusses the impact of discount stores on the Korean distribution industry and their effects on other retail formats. The sixth section centers on the international players' characteristics and attempts an explanation of their disappointing performance. Finally, strategic directions for the international players and domestic ones are discussed.

I. Discount Stores in Korea: Current Situation and Characteristics
The first discount store to provide service in Korea is E-Mart, which began operation in November 1993 in Chang-Dong, located in the North-eastern part of the Seoul Metropolitan area. In Korea, whose people experienced radical reduction of purchasing power in the aftermath of the 1997 Asian financial crisis, the discount store came to be recognized as a more attractive retailing format compared with other prevailing formats, including the department store and the supermarket. During this crisis, the discount store emerged as a formidable presence, as most small department stores in regional cities faced bankruptcy due to shortage of financial resources and recessions in the real estate market.

Discount stores in Korea share the following two characteristics: 1) huge potential for growth in a fast-growing market, and 2) intense competition among market players.

1. Market with Huge Potential
According to the report published by Korea Chainstores Association for the year 2001, the sales volume of discount stores was $11 billion US$ as of the end of December 2001, up 29% from $8.5 billion US$ in the year 2000. The figure amounts to 87.5% of the total sales volume of department stores, the largest sector in the overall retail market. Judging by the phenomenal growth rate of 33% in 2000, the discount store sector is expected to continue to grow rapidly for the time being. The sales volume of this
sector is projected to rise another 28.5% this year, reaching 14.8 billion US$ in 2002. Upon reaching this threshold number, the discount store sector will finally surpass the department store sector in terms of sales volume.

That discount stores are overtaking a market sector once occupied by several other retail sectors—department stores, supermarkets, and traditional local marketplaces—suggests that the entry patterns by which a discount store make its inroad are no different from that of other advanced countries. The rapid growth of discount stores has caused considerable change in the merchandising strategy of department stores, the current but insecure leaders in the retail market. In response to losing customers to discount stores, department stores are beginning to cater to changes in consumers’ needs by converting their floor space, once filled with food products and general household appliances, into a gallery of high margin goods such as internationally famous brands and luxurious clothing.

2. Intense Competition
The number of discount stores with a minimum floor space of 3,000m2 is soaring, as evidenced by the number of newly-opened stores in the past two years (47 in 2000 and 39 in 2001). The rapid growth in the number of stores implies intense competition among players, and there appears to be no letup in this expansion trend as this number is expected to increase continually until 2005. The forerunner, E-Mart, has 43 stores as of December 2001 and is planning to have 80 stores in operation by 2005. Lotte Mart, the runner up, is also going to run 80 stores by the same year (from 24 in 2001). Samsung Tesco (Homeplus), the third runner, plans to expand to 55 stores from the current 14, and Carrefour, the fourth company, with 22 stores in 2001 will be operating 40 stores by 2005. In addition, Hanaro Club, which has retailing as well as wholesaling operations, has been running 13 stores in 2001 and plans to increase its stores to 30. In total, the number of discount stores is expected to be doubled, up to 366 from the current 175 stores, operated by 11 different retailers.

As the number of discount stores grows continuously, the market will eventually be saturated. While the leader E-Mart will enjoy first-mover advantage of multiple stores and of established infrastructures, it will surely pay more and more attention to profitability, represented by the return on investment (ROI) indicator, as saturation days draw on. By the time of saturation, the market will be restructured into 2 tiers—a leader group consisting of 2 companies and a follower group of 3 or 4 retailers.

Competition among players is typically intense in Seoul, its suburbs, and regional major cities. Ilsan City, for instance, with only a population of 400 thousand is emerging as the most competitive region in the country as 10 discount stores and 4 department stores openly compete against each other, regardless of inter and intra format. Competition among discount stores is also very intense in major regional cities such as Daegu and Ulsan.

Table 1. The Number of Major Discount Stores by Year

<table>
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<tr>
<th>Classification</th>
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<th>1999</th>
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</table>
II. Competition among Discount Stores in Korea

Competition among discount stores in Korea shows the following characteristics.

1. Local Players’ Successful Operation

Business Week reported on January 21, 2002 that the world giants WALMART from the U.S.A. and Carrefour from France were struggling against a local rival, E-Mart. This amazing fact is underscored by the following: while WALMART recorded consecutive net losses for the last three years, the net income of domestic players, led by E-Mart and Lotte Mart, has grown by 20 times in the last four years. The domestic players’ share amounts to 77% of the total discount store market, a staggering figure if we take in the obvious calculation that international players like Carrefour, WALMART and Samsung Tesco account for only 23% of the market.

E-Mart, the forerunner, earned sales revenue of over 3.3 billion US$ in 2001 (an increase of 41% since the previous year) and accounted for 31% of the total Korean market. The disparity in sales revenue between the leader and the runner up in the market is becoming more and more obvious, as indicated by the fact that, while in the year 2000 E-Mart earned 1.58 billion US$ more than the runner up Carrefour in terms of sales revenue, it earned 2 billion US$ more than the new runner up Lotte Mart in 2001.

E-Mart’s operational practice is so successful that Japanese corporations Ito Yokado and Jasco are willing to benchmark the company in an effort to counterattack incoming international retailers. E-Mart’s success shows no sign of letting up, as its operational success continues even in China, where it made its entrance as the first Korean discount store in 1996 and recorded net income since 1998.

It was in 1996 when barriers were dismantled for the foreign retailers that international operators entered into Korean market. Interestingly, international players’ market share has been dwindling year by year. Macro and Continent, which advanced into this country at the outset of market opening, were acquired by WALMART and Carrefour respectively.

In 2001, Carrefour occupied 11.4% of total market share with 1.25 billion US$ in sales revenue, and WALMART occupied only 4.7%. In terms of sales ranking, Carrefour dropped to the 4th place from second, and WALMART to 8th from 4th, compared with the preceding year. Only two WALMART stores were in the top 30 sales revenue stores, and none of Carrefour stores was in the list.

Among international players, Samsung Tesco Co., LTD., a joint venture between Samsung Corporation and Tesco, is taking a firm hold in the market; in 2001 it marked 1.25 trillion won in sales revenue, making itself third runner up and showing an increase of 138% from the preceding year. The company is expected to rank 2nd overall in the market this year, overtaking Lotte Mart in the process.

2. Strategic Similarities

Generally, management practice of discount stores is strikingly different from that of department stores, supermarkets and convenience stores, while sharing some similar characteristics. One of its significant characteristics is the ELDP (Every Day Low Price) strategy. This ELDP strategy necessarily involves supplementary strategies such as low cost operations and low margin tactics. Furthermore, its strategy is perfectly implemented by subsequent techniques like 1) grand-scale multi stores, 2) IT-oriented management utilizing UPC, EDI, and WSN, 3) timely restructuring, and 4) the strengthening of relationship with suppliers. Such examples are evidenced by the strategic practice of world-class giant WALMART.

Domestic discount stores are not much different from their international competitors in the sense that they are pursuing 1) ELDP, replenishing quality items at a reasonable price, supplemented by low cost and low margin strategies, 2) multi-store strategy with large floor space, and 3) state-of-the-art management techniques. Furthermore, Korean firms are more aggressive than foreign firms in their pursuit of multi-store strategies.

As competition grows increasingly intense, each firm is implementing its indigenous strategies and tactics. Rather than simply selling products at a lower price, for example, E-Mart is making enormous efforts to become customer-friendly. Among the more visible changes is the expansion of the stores’ entrance for better access and better view. In addition, E-Mart is providing a variety of innovative services toward its customers. These services, introduced in Korea for the first time, include:
1) no-questions-asked 'exchange/reimbursement' in case of dissatisfaction,
2) 'double reward' for any item not purchased at the lowest price in the market,
3) 'miscalculation reward' of approximate 4 US$ for any payment error,
4) 'freshness-guarantee' if any item is not considered to be fresh, and
5) guide for parking.

However, as most store operations tactics are easily imitated by competitors, such competitive advantages are not expected to last long. Even now, the operation strategies of E-Mart and close-follower SamsungTesco are in many respects considerably similar to each other, especially with regard to customer service.

3. Free-form Corporation

Discount store business in Korea is run by free-form corporations—defined as corporations in pursuit of multi-channel businesses—whose aim is to serve heterogeneous market segments more effectively and simultaneously.

The major stockholder of the number one discount store brand in Korea, E-Mart, is Shinsegae, one of the leading department store corporations. Likewise, department store giant Lotte is the major investor into Lotte Mart. Carrefour and SamsungTesco are also free-form enterprises: Carrefour became a free-form corporation by entering into the supermarket business when international expansion into hypermarket business became unpopular in 1998. Buyout of Comptoirs Modernes and Promodes provided the momentum in Carrefour's rise to the rank of the world's second retailing conglomerate. As a free-form corporation, the company is operating hypermarket and supermarket businesses, along with electronic commerce ‘@Carrefour,’ founded in 2000.

Domestic discount stores are all striving to make their inroad to internet business. Compared with international players, they are much more enthusiastic about internet businesses and are planning to offer from 20 thousand to 30 thousand items, confident in the know-how accumulated by way of running off-line businesses. In contrast, international corporations are more cautious with regard to on-line business. Carrefour constructed the internet homepage in 2001 but provides only a brief introduction to the company and to the product items they are selling. While the SamsungTesco headquarters in England is successfully managing online business, it is only carefully reviewing the feasibility of online business in Korea.

III. Business Strategies of Major Discount Stores in Korea

As discussed in the preceding section, in addition to the characteristics that discount stores have in general, discount stores in Korea are each implementing a variety of strategies to cope with severe competition. The following examples describe the distinctive business strategies of major players in the Korean discount store market.

1. E-Mart

E-Mart keeps inventory turn-over ratio, the essential indicator for store management, 3 times as high as that of its international competitors. It also has a very low cost structure while maintaining high sales revenue. What are the contributing factors in maintaining this ideal mixture of low cost structure and high sales revenue? Business Week ascribes its competitiveness to:

1) customer-oriented store layout,
2) merchandising capability focusing on fresh food,
3) price-competitiveness made possible through purchasing power, and
4) aggressive multi-store strategy.

E-Mart has a better understanding of Korean customers' needs and its ability is well reflected in its visual merchandising strategy. Selling in units instead of bulk; bright illumination with luxurious interior design; displays similar to that of department stores; low shelves for customer comfort—these are some distinctive characteristics that differentiate E-Mart from its foreign competitors. Industry analysts point out that international discount stores are no match for E-Mart in their interior design and product display, which do not take the cultural and physical profiles of Korean customers into consideration.

More importantly, however, there are other reasons why E-Mart outperforms world giants like WALMART. Having developed on a thorough understanding of its customers' needs and wants, the company's customer service strategy takes maximum advantage of the massive infrastructure—IT, logistics, distribution centers, and superior site location. More importantly, the infrastructure
is already in place in most cases, for E-Mart developed this infrastructure well ahead of its competitors.

In addition, state-of-the-art business practices like:

1) the development and implementation of supply chain management (SCM),
2) the development of aggressive private brands in TVs, Kimchi refrigerators and outfits, and
3) reduction of intermediate processes through a direct transaction with producers, are contributing factors in the successful business operation of E-Mart.

The company is so far ahead of its competition that it now finds itself in a position to pay closer attention to corporate ethics and societal marketing, that is, in a position to consider the finer aspects of intangible marketing, a higher form of enhancing its corporate image. In principle, its transactions are conducted with transparency and fairness, and the company implements several community sponsorships and educational programs.

E-Mart’s success has increased its brand power to a great extent. It ranked top discount brand in 2001, its brand value alone assessed to be 130 million US$, according to a study conducted by The Institute of Industrial Policy Studies. According to a brand awareness survey jointly made by Maet Business Newspaper and Brandmajor, E-Mart was positioned as the representative discount store in Korea. Brand awareness level was 69%, which was strikingly high, as compared with the runner up Lotte Mart, whose level showed only 9%. Among several perceived attributes surveyed, price, quality, variety, convenience, familiarity, reliability, and symbol took the 1st ranking.

2. Lotte Mart
Lotte Mart was founded in 1998 by Lotte Group, a giant retailer. Following the multi-store strategy, it reached 16 outlets in an amazingly short span of time, with 833 million US$ in sales revenue at the end of 2000. As of June 2002, the number of stores has grown to 29, and it is expected to have 34 by the end of the year. Lotte Mart plans to have 80 stores in operation by the end of 2005, hoping to become a strong contender against E-Mart.

While it focuses on the multi-store strategy on the one hand, Lotte Mart is actively improving its basic infrastructure on the other. To that end, for example, it is trying to minimize logistical cost by introducing an automatic replenish system through state-of-the-art POS system.

Lotte Mart is actively developing a specialized food section that satisfies local customers’ needs. Customers not only come in to buy food products, but they also try them out during the many special “eating” events. In addition to the food section, introduction of several private brands makes it possible to provide quality items at a lower price. Lotte Mart contributes to national economy by hiring in-city residents, and by supporting and maintaining good relationships with local suppliers.

3. Carrefour
The French-based Carrefour’s interest in overseas business goes back to its early history. Domestic success was an impetus toward its first expansion into Belgium in 1969. Then it entered Spain, and the knowledge accumulated of its Spanish customers’ characteristics played an important role in its operational success in South-American countries. Carrefour’s success took it into South-Eastern Asian countries: first into Taiwan and Korea, and then into China and Japan.

Part of Carrefour’s active interest in overseas business may be attributed to its progressive corporate ethos of seeking new markets abroad, but it is also very much motivated by difficulties in the French domestic market. Ever since a law regulating large-store business was passed in 1973, Carrefour started actively to seek opportunities in international business.

Since the opening at Bucheon city’s Joongdong Branch in July 1996, Carrefour has been expanding businesses very rapidly. A total of 22 stores are in operation as of May 2002, and the number is still growing. When Carrefour’s headquarters acquired French-based Continent(Promodes) in 1999, Promodes’ Korea businesses were merged into and operated by Carrefour.

Because of its very aggressive multi-store strategy, Carrefour was once regarded as the most formidable rival against E-Mart. However, Carrefour has been falling far short of its objective, and this failure can be attributed to the Asian financial crisis of 1997, which occurred not long after the Joongdong Branch opening. The influx of IMF bailout funds was
conducted in such a way as to arouse Korean antipathy to foreign corporations, and this social environment became a major obstacle in Carrefour’s operations.

Nevertheless, Carrefour has begun to reinforce its organizational resources in Korea. Compared with that of South American or Southeast Asian countries, market potential in Korea is very strong: Korea’s lowest income-level class is very thin, which translates to a comparatively thicker middle-class tier, and Koreans prefer discount stores with luxurious atmosphere, which suggests higher margin of profit per units sold.

From its establishment, Carrefour has been pursuing two primary management principles: thorough localization and autonomous operation. In procurement all products are initially sought in the local markets, and importation is considered necessary only when local supply and purchase is unavailable. Taking Macro’s and Continent’s failure as instructive lessons, it shows flexibility in applying business strategies to local business. Its localization strategy is a major part of its global strategy. Through a strategy called glo-cal strategy, Carrefour does its best to accommodate the heterogeneous needs of the local market, provided they fall within the flexible standards set by its headquarters. In contrast to the traditionally divergent strategies of multinational corporations, where each local branch is considered merely an arm of a unilateral decision-making body, Carrefour’s is a convergent strategy, aiming to utilize the multiple resources made available by its glo-cal stores.

Carrefour’s localization strategy is benchmarked by Tesco. In as much as competition becomes more intense in Korea, Tesco tends to regard localization as being more important, and, therefore, its headquarters has delegated decision-making authority to Samsung Tesco to a large extent.

As the number of stores is growing, however, Carrefour is leaning more to global sourcing, which implies a significant shift in its glo-cal strategy. In addition, the ratio of joint-procurement with France headquarters has increased. In particular, global sourcing of products such as household items and liquors is evaluated to be very successful.

Carrefour’s merchandising efforts, including global sourcing, contribute to its price competitiveness and availability of a variety of products; they also give Carrefour an edge over its competitors in terms of profitability through low-cost operational know-how that is acquired in overseas countries.

In Korea Carrefour purchases processed food and clothes at reasonable prices and exports them to Central and South American countries. For this purpose, it plans to sign up over 10 export agents to its services.

Carrefour is also considering entrance into other retail formats such as supermarkets and convenience stores. More specifically, it is reportedly planning to open a convenience store with its own brand name Casino after acquiring a Korean business.

4. WAL-MART

WAL-MART came to Korea in July 1998 by way of acquiring Macro Korea, a Dutch and Korean joint venture Membership Wholesale Club (MWC), which had been operating 4 stores including the Incheon Branch since 1996. In addition to the 4 stores owned by Macro Korea, WAL-MART also acquired sites in various strategic locations for 6 additional discount stores. Currently, it operates a total of 9 stores, having added 5 more stores by acquisition or construction on the sites mentioned above.

WAL-MART’s core entry strategy into a new market is to acquire an existing player and to establish local partnerships during the process of acquisition. Generally, prior to full-scale expansion, WAL-MART tends to select a local partner and afterwards to buy out the partner. In other words, it seeks partners as a way of information-gathering; later, it tests market potentials through them and, finally, enters into the market on a full scale.

The following cases describe WAL-MART’s entry into overseas businesses. It entered Mexico in 1992 by way of a joint-venture with the largest Mexican retailer, Cifra S. A., and into Canada in 1994 by acquiring a total of 122 stores from Woolco. This strategy is also well reflected in WAL-MART Korea. The acquisition of Macro Korea served as a bridgehead into the Korean market for WAL-MART.
One of WAL-MART Korea’s defining characteristics is its emphasis on fresh foods. WAL-MART learned that Korean consumer behavior centers around the purchase of foods, which then occasions subsequent shopping activities. With only a minimal shift in emphasis from packaged foods to fresh foods, the concept of the supercenter as developed by WAL-MART matches this type of consumer behavior. That is the reason why WAL-MART changed Macro Korea into a supercenter and refunded the membership fee originally levied by the MWC.

WAL-MART’s purchasing power, considered to be its most competitive edge, is very effective in Korea, too. Competition based on price is made possible through local purchasing in Korea as well as global sourcing. After WAL-MART acquired Macro Korea, it tried to reduce the prices of products by reducing unnecessary cost, and by taking advantage of its integrated in-house supply management system in the maintenance of an optimal information and logistics system.

Nevertheless, contrary to expectations, WAL-MART is struggling in the initial stages of its operation in Korea. Sales revenue was 250 million US$ (with operating losses of 8.2 million US$) in 1999, showing only a 4.6% increase from 1998. During the same fiscal year, E-Mart and Lotte Mart recorded 1.05 billion US$ and 496 million US$ respectively; E-Mart earned 20.6 million US$ in operating income. The underlying reasons for WAL-MART’s dismal performance include late opening of its stores, the inappropriate localization strategy, and strong performance of its domestic competitors. Of these, the inappropriate localization strategy is thought by industry analysts to be the deciding factor in WAL-MART’s operational woes. WAL-MART’s inability to grasp Korean customers’ demand for customer service on par with that of department stores reveals the glaring fact that WAL-MART is clinging too tenaciously to the “global operational standards” used in America. These standards are causes of much incompatibility between the store and its customers: 1) sale in bulk and bundle, 2) uncomfortable and even intimidating height of the shelves, 3) drab store atmosphere and illumination that do not match the merchandises, 4) excessive focus on industrial products, 5) and a corresponding lack of attention to the food counter.

5. SamsungTesco

Homeplus, SamsungTesco’s store name, has grown so phenomenally for the last two years that Deutsch Bank’s Asian Distribution Industry Report described the corporation as ‘the most promising distribution player in Asia.’

SamsungTesco Corp., LTD., was set up in May 1999 as a joint venture between Samsung Corporation and Tesco, the foremost English retailer, with the largest initial paid-in capital of 258.3 million US$ among domestic retailers. Currently it operates 14 stores, including the Daegu Branch, which opened in 1997 prior to the joint venture, and the Youngdungpo Branch, which opened in 2001.

While SamsungTesco had been steadily increasing the number of domestically procured items on the basis of the localization principle, it has made a strategic turn to increase the level of imports that offer price competitiveness. Eleven items were imported in 1999, and the ratio of global sourcing from headquarters is continuously increasing thereafter. Currently, price-competitive product categories including toys, wineries, stationeries, and household necessities are supplied from overseas, and the company plans to build a global procurement system with the aid of its headquarters. For this purpose, the headquarters is holding workshops two or three times a year.

Thanks to its aggressive efforts to increase stores and merchandising, SamsungTesco took the 3rd position among discount stores in 2001, with 1.25 billion US$ in sales revenue. Geographically, it employs a so-called ‘dominant strategy,’ targeting the Seoul Metropolitan area, Youngnam Provinces, and densely populated areas in large cities in its choice of store location.

Until 2005, SamsungTesco plans to open 8 to 10 stores per year in major cities in the Youngnam Provinces, such as Ulsan, Daegu, Pohang, Kumii, and Pusan. By that time, it hopes to grow into a distribution company with 8.3 billion US$ of sales, employing 25 thousand employees at 55 branches.

SamsungTesco’s success in moving ahead of the world’s best and the second best discount stores, WAL-MART and Carrefour, can be attributed to its smooth adaptation to the peculiarities of the Korean market. For example, in order to circumvent local antipathy to foreign companies, it foregrounded the
local ‘Samsung’ brand name, making it seem more of a local company than it really is. It also provides superb customer services, and places heavy emphasis on the food corner. In addition, SamsungTesco has a distinctive competitive advantage in that, while its management practices are similar to those of local leader E-Mart, it is supported by strong financial resources and advanced management systems from headquarters.

SamsungTesco deserves a more thorough analysis as, together with E-Mart, it may soon represent one of two typical Korean discount stores and may thus provide a clue to understanding its majority shareholder’s (that is, Tesco’s) global strategies.

IV. Effects of Discount Stores on other Retail Formats in Korea

1. Effects of Discount Stores on the Korean Distribution Industry

When the Korean distribution industry was finally forced to open in 1996, and major international players advanced into Korean market, analysts expected this drastic change in the regulatory environment to pose a serious threat to existing players. The threat has not yet subsided, nor is it known whether it will subside, but for the overall distribution industry, however, the deregulation of 1996 is being considered a positive influence. The long-term effects can only be guessed at, but listed below are some discernable positive and negative consequences of the deregulation.

First, there is a natural transference of distribution management know-how, as local players feverishly study their international competition. Local players have made great strides in the areas of procurement, merchandising, stock management, logistics, and information systems. Such enhancements in productivity and management efficiency will surely contribute to the overall development of the distribution industry.

Second, traditional retailers are facing bankruptcy or are being forced to restructure. Specifically, department stores and supermarkets, now in their maturation stage, are losing ground to the relatively younger discount stores. The discount store market is full of players, local and international, and further enhancement in the status of the discount store market is expected to bring about a restructuring of the retail industry itself.

Third, the entrance of international discount stores to Korea in turn has provided international manufacturers with better inroads to the Korean market. Therefore, in coming in more direct contact with their international counterparts, Korean manufacturers have begun to recognize the need to make strategic changes in their manufacturing practice, such as quality control and R&D. In the long term, this will raise the national competitiveness of Korean manufacturers.

Fourth, retailers have improved their purchasing power. The aggressive multi-store strategy of discount stores has resulted in an increased purchasing power of retailers as a whole, elevating their relative status and negotiation power vis-à-vis manufacturers.

Fifth, customers also are enjoying the benefits. Global sourcing and intense competition among the players have resulted in availability of more and better products, better customer service, and reduction in prices.

Sixth, international players in Korea provide employment opportunities for local residents, and more and more experts on the distribution industry will be trained by those experienced in the international retail market.

In addition to these positive effects, some negative effects can be brought forward. The growth of large discount stores equipped with advanced management skills, as well as solid financial resources, is truly a burden not only to fragile retailers but also to large-scale retailers. In practice, aggressive multi-store strategies reduce existing firms’ market share considerably, and threatens even the survival of existing players. On the national level, excessive influx of foreign products and resulting trade deficits may weaken the competitiveness of distributors and manufacturers, and further jeopardize the basic foundation of distribution industry itself.

Whatever the effects, the proliferation of new retail formats and emergence of large stores will spur the modernization of the Korean distribution industry. The overall effectiveness of the distribution industry depends on existing distributors’ prompt countermeasures against changes in the competitive environment, and by improvement or elimination of ineffective procedures and habitual routines.
2. Effects of Discount Stores on Other Retail Formats

How other major retail formats, including department stores, supermarkets and convenience stores, are influenced by the growth of large discount stores is discussed in the following section.

1) Department Stores

Favorable foreign exchange rates and improved investment situation in Korea immediately following the Asian financial crisis have empowered international discount stores to aggressively open new stores in the Korean market and to implement multi-store strategies. As a result, department stores are finding themselves in an unenviable position of having to face challenges from international discount stores, as well as coping with competition from domestic discount stores. With international players aggressive entering the Korean market, many major domestic department stores have transformed themselves into other retailing formats including the discount store.

While discount stores have taken advantage of the Asian financial crisis, the department store sector suffered, for the first time in history, a decrease in revenue in 1998. Such situational factors aside, the department store sector is expected to show very minimal growth because the market is already well into the mature stage.

The trend of price cutting initiated by international players has a direct influence on the department store sector as well as the discount store business in Korea; price-competition is therefore sweeping the distribution industry overall. Although department store managers adopt more aggressive promotion strategies such as sweepstakes, profitability continues to suffer because, unlike the past, special sales do not translate to increase in sales revenue. To cope with such adversities, department stores are seeking suitable strategies of their own, such as upgrading its store image to accommodate changes in customers’ needs.

2) Supermarkets

Traditionally, foods have been available at supermarkets, traditional local marketplaces, or food sections of department stores. The growth of discount stores, however, has brought about fierce competition in the food market. Supermarket chains, whose primary interest had been on dominating market share, are consequently facing a number of structural problems, aggravated further by the Asian financial crisis.

As discount stores, typically the supercenter type, encroach into the territory of the supermarket, supermarket chains are concentrating their efforts on improving profitability rather than on increasing sales revenue.

As such, faced with increased pressure from discount stores and stiff price competition, supermarkets, particularly those located in small trading areas, are experiencing severe difficulties such as aggravated profitability. To cope with these difficulties, they are striving to differentiate themselves from their competitors by implementing local-specific strategies, improved operation management, and effective marketing activities.

3) Convenience Stores

Since 1989, when the first convenience store was made available to Koreans, the business sector has grown gradually. Due to severe competition among international convenience stores and the Asian financial crisis of 1997, however, the sector underwent considerable structural change. Among the many stores that had alliances with international players, stores that had accumulated know-how were able to reopen with a new name, and while some were merged into competitors and others declared bankruptcy.

International convenience stores moved into Korean market earlier than other retail formats and have thus secured their positions by generating revenues through the multi-store strategy. However, decline in price competitiveness and the reduced number of customers due to the growth of discount stores are the limiting factors for full-scale growth.

In the remaining untapped market there will be very little discrimination between domestic and international brands. While pursuing better services and improvement of operational efficiency, leading convenience store chains will compete fiercely for good locations.
V. Evaluation of Competitiveness of International Discount Stores in Korea

Although differentiation between domestic and international players seems no longer to be meaningful, given that markets are rapidly merging to form a giant global market, there remains a peculiar oddity that international discount stores are generally showing disappointing results in Korea compared to their local counterparts. The following section discusses the reason for their poor performance in terms of competitiveness, bottleneck, and directions for future development.

1. International Discount Stores’ Competitiveness in Korea

1) Solid Financial Resources

International firms in Korea are able to utilize solid financial resources as their bases of competitiveness. The ability to finance as many investment projects using the lowest interest rates available provides for any retailer a critical edge in implementing the multi-store strategy. This critical edge is held by international players over their domestic competition, as the former comes a step closer to providing better service at less cost to their customers.

2) Global Sourcing

International discount stores are excellent in sourcing capabilities since they source necessary products globally via a worldwide network. Based on better merchandising know-how and advantageous negotiating position, they have sufficient capabilities in developing both national brands and private brands. Global sourcing makes it possible to apply existing relationships with multinational companies to the Korean market, and contributes to maintaining price competitiveness and a dominant position in the market.

3) Use of Distribution Information Systems

Merchandising capability, the competitive power that international players enjoy, depends on how well they utilize their global sourcing capabilities and maintain more profitable positions through strategic alliances with manufacturers. In other words, it depends on how well they develop and use the distribution information system on which they have continuously been working from the outset of business. Huge amounts of information gathered globally through the international network play a central role in capturing market information effectively and enable the international players to establish a dominant position in the channel of distribution.

2. Underachievement of International Players in Korea

There are two underlying reasons for the underachievement of international players in Korea. One is the distinctiveness of local characteristics, and the other is the adverse nature of the competitive environment. Obviously, as these two aspects are like two sides of a coin, the combination of the two factors results in unsuccessful adaptation into local market.

Strong Local Characteristics

a) Antipathy towards Foreign Firms

The Korean distribution industry opened up in 1996, and since then various types of discount stores moved into this country. No sooner had the industry opened up than Korea underwent financial difficulties and had no other recourse but to receive bailout funds from IMF. At that time, antipathy against multinational companies, though vague, was nevertheless very strong, and the advantages of being an advanced company from an advanced country disappeared almost overnight.

b) Preference for Luxurious Atmosphere

Prior to the introduction of discount stores, department stores have been the dominant retailing format. While it is hard to say that Korean department stores were pursuing a more luxurious atmosphere than that of Sax Fifth Avenue, they have provided quality services to customers in general. Thus, being accustomed to this kind of service from department stores, Korean customers expected discount stores to provide similar services and atmosphere, an expectation that is still current.

c) Expectation of Floor Space

Sizable financial resources are required to run a large retail store in Korea, where real estate costs are relatively high. Since retailing formats with ample financial ability have traditionally maintained large floor spacing with luxurious interior, customers have come to associate floor space with luxury. Hence, large spaces full of ELDP products are bound to cause discomfort in the minds of Korean customers used to more luxurious surroundings.
d) Good Quality Food
For Koreans all shopping activities appear to begin with purchase of food. Food is on top of nearly all shopping lists. Korean department stores have catered very successfully to this special characteristics of Korean customers by providing very specialized food corners, and it remains for discount stores to provide quality food in an environment that can compete with department stores. The growth of a discount store is limited unless it is ready to offer fresh food as a major part of its overall operation.

e) Social Class by Income Level
In Western countries where wealth was accumulated over long periods of time, social class is relatively clearly demarcated; therefore, consumers' habits and attitudes are at a large extent influenced by class. In Korea, however, the concept of class is ambiguous, and its boundaries are so vague that consumption practice on household items is generally homogeneous, regardless of class. Thus, merchandising efforts targeting low-income levels are ineffective, and most products are of relatively good quality.

Deteriorating Competitive Environment
a) Local Players: Better Understanding of Local Customers
Even prior to market opening in 1996, Korean firms had been preparing for the new discount store format. They were given time to prepare for this changing format, during which they established a type of discount store that took into account the local characteristics of Korea. They were thus able to secure strategically advantageous store positions while international operators were undergoing trials and errors at the initial stage.

b) Competition among International Players
Around the time of market opening, most of the leading players announced their plans to enter the Korean market. They were sufficiently motivated because the Korean market was attractive in itself and as a platform for expansion towards the three other Far-eastern countries—Japan, Taiwan, and China. Consequently, fierce competition among world's best retailers was inevitable.

c) Disadvantages in Site Selection
The tendency to find security in real estate is very strong in Korea, and Korean corporations have for a long time been on a lookout for pivotal locations. Thus, finding suitable locations is difficult for the latecomers, the international retailers. The situation becomes more complicated because lease and rent are not readily offered to large retailers in Korea. The nature of the industry requires having multiple stores, and lack of quality real estate acts as a formidable entry barrier to international players.

d) Performance Criteria
Compared to their international counterparts, Korean retailers hold a different view on capital investment. While Korean firms consider 2 years as an appropriate pay-back period, the international players are happy with longer periods of time; some firms take 5 years of pay-back period at longest. One hypothesis can be set forth that Korean firms employ more aggressive strategies because of the pressure to return paid-in capital in a relatively short period of time.

Future Directions
It is not entirely clear whether the underachievement of international corporations is a predictable outcome during the period of exploration, or whether it is due to their relative competitive weakness. If the latter case is true, the domestic players are holding an enormous advantage over their international competitors, and will continue to do better.

In response, international corporations may select a Korean partner in the second tier for joint business; as a matter of fact, Samsung Tesco, a joint venture adopting this strategy, is currently the best performer among international discount retailers in Korea. If, however, the former case is true, more aggressive marketing efforts on the part of international corporations will be on the way, together with flexible transitions into other formats. Alliances among international players are a viable option, too. Actually, a merger took place among the international players, by which the parties concerned were able to acquire better market information, both in terms of quality and quantity.
VI. Expected Competitive Strategies of Foreign & Local Discount Stores

As discussed above, discount stores took a leading role in innovating not only the distribution industry overall but also other players in different formats. Yet, there are still a number of issues to be resolved.

Basically, most large discount stores do not have a systematic business strategy, and their infrastructure, including logistics and communication network, is quite weak. More seriously, they are woefully short in personnel—buyers, store managers and IT people—with the expertise to build solid business strategies and infrastructures.

International discount stores and domestic players are facing somewhat different problems. Domestic corporations lack distribution know-how, advanced logistics and information systems, financing ability, and global sourcing. International players, on the other hand, lack appropriate localization efforts, affirmative marketing activities, and location merit. The following section discusses future directions for the growth of domestic and international discount stores.

1. Domestic Players’ Business Strategies

First, local community-based marketing strategies are recommended. Rather than targeting the whole market, discount stores need to focus on the local trading area, understanding and providing for local needs. First of all, they need to implement a community-friendly program, meeting the values of the community and its needs, and providing the community with various facilities for better services and better quality of life. Additionally, they need to establish cooperative relationships with local industries, procuring necessary products from local suppliers and hiring members of the local community. Without such efforts, the discount store cannot position itself as the representative retailer in the community.

Second, training of expert personnel is of utmost importance. Systematic educational programs should be developed with specialized tasks in mind, such as merchandising, procurement, IT, logistics, etc.

Third, effective systems management strategies must be in operation. Overall effectiveness is to be achieved through SCM (Supply Chain Management). In particular, an information systems network (an ideal combination of POS, EDI, and telecommunications network) that connects sales, distribution, and supplying parties needs to be in place in order for a local corporation to compete with international players. Such a system may also help reduce logistical cost while offering precise sales forecasting. Or it may be utilized in seeking new customers and retaining existing ones. For example, while gathering and analyzing of customer information is made available by the use of membership cards, long-term loyalty from customers is to be formed by using CRM (Customer Relationship Management).

Fourth, differentiation in merchandising efforts is to be made by developing distinctive private brands. Differentiated merchandising starts with product procurement that matches store positioning, after the fundamentals of procurement policy are established. Recently, in addition to off-line businesses such as discount stores and supermarkets, on-line businesses like internet shopping malls, TV home shopping, etc., have introduced a variety of private brands. Private brands enable discount stores to maintain a higher profit ratio, to keep stable product prices, and to secure a dominant position in their relationship with suppliers. On the one hand, private brands provide retailers with such advantages as provision of differentiated products and higher profit ratio; on the other hand, manufacturers are assured of a stable revenue source. Consequently, a win-win relationship is established between retailers and manufacturers.

Fifth, a discount store needs to be redesigned into a shopping complex that provides ‘value’ for its customers. Currently, low prices, reasonable quality, and customer service are quoted as a discount store’s competitive advantage. In the future, however, ‘fulfilling customers’ value’ needs to be added to these quoted advantages. From the discount store’s point of view, the fulfilling of the customers’ value means that it should provide facilities for customer convenience. In other words, the discount store, not being a simple shopping space, has to provide a complex in which such functions as entertainment, business, and customer service are conducted.
Finally, a discount store needs to establish globalization strategies. Although the discount store business is domestic by nature, major international retailers have been expanding into overseas markets since the mid 1990's. Most of the major international discount stores have reinforced their international marketing activities to secure a source of long-term sales revenue. WAL-MART, for example, has expanded into 10 countries throughout the world as of 1999, and Carrefour advanced into 31 countries. Overseas businesses by Korean players are rare, with the exception of E-Mart, which started to expand internationally and recorded net income since its debut in Shanghai in 1996. In order to achieve long-term competitiveness, more efforts must be made to take hold of overseas opportunities, rather than to compete in a saturated domestic market.

2. International Players’ Competitive Strategies

Some of the competitive strategies recommended above to domestic players are already under operation by some international players in Korea. This does not imply that international players hold absolute advantages over their domestic competition. They need improve upon two aspects in order to be competitive in Korea.

Above all, they need better localization strategies, for their worst obstacle is the Korean antipathy toward multinational firms. It is recommended that they pay more attention to various kinds of social work, employment of local man-power, and contribution in the local economy. SamsungTesco was very successful in its localization efforts because it took on a friendly appearance by attaching the familiar name of Samsung in front of the rather unfamiliar Tesco.

Additionally, international players should be careful not to lose sight of customers’ needs and wants. Since most Koreans are accustomed to customer services provided by department stores, some stores need to upscale their quality in addition to expanding their floor space. In particular, their merchandising should take more account of the needs of Koreans. For example, they need to reinforce food merchandising and to offer various kinds of fresh food. And, it is advisable to reduce the kinds of products targeting the lower income class.
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