

Profitability of Foreign Companies in Korea: Another Reason to Invest

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This report is based on research funded by Invest Korea. It is intended that a longer and more academic version of the paper is to appear as an Occasional Paper of the East Asia Institute of Cambridge University.

Foreword

This report represents research conducted during November and December 2004 using public information. The report reflects a consideration of statistical data taken from public sources filed with the financial authorities in multiple jurisdictions. It is naïve to suppose that such a study can fully comprehend the accounting complexity of 110 of the largest multinational corporations in the world, and there is every indication that if the complexity could be fully analysed, then the results would be more favourable to Korea.

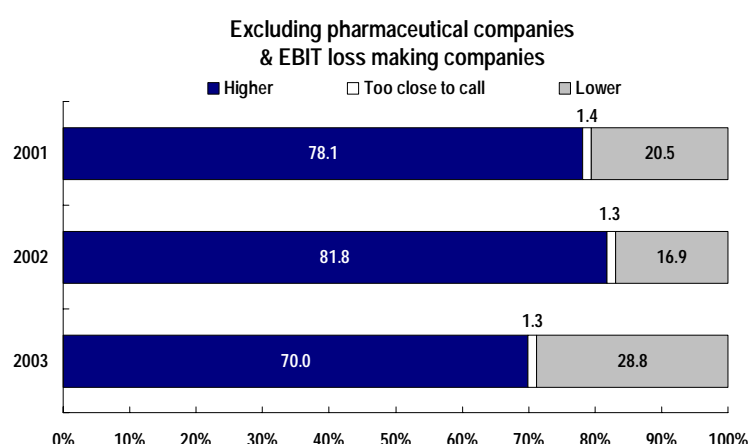
Executive Summary

The study on profitability of foreign direct investment 2001-3 has concluded that, in terms of shareholder value, foreign direct investment in Korea has yielded 70.0% of investors a markedly higher rate of return on assets employed than the global average of the same firm.

The purpose of the study was to test empirically whether the perception by foreigners that high wages, labour militancy or market restrictions was affecting profit could be substantiated. The overall conclusion was that none of these factors prevented the majority of foreign direct investors from making profits, which exceeded the global average. However, further liberalization would allow more rapid restructuring in a slower growth economy.

The rate of profit is closely related to the state of the Korean economy, and the number of firms making above average profits declined from 82% of companies in 2002 to 70% of companies in 2003.

Diagram E.1. Net profit / Assets (2001 – 2003)



Foreign investment in Korea was markedly absent before the IMF crisis due to closed markets and market restrictions, and existing investment was not very successful. The liberalization of the market has increased foreign investment and the success rate of foreign investment. As a result between 2001 and 2003 the global ratio of revenue derived from Korea by foreign invested companies increased from 1% to 1.5% but still has not reached Korea's proportion of world GDP of 1.7%. Further investment can be expected to achieve this.

Korea was also increasing its regional share of sales and profit as well as its global share. In 2001, Korea sales made up 11.4% of regional sales, and this rose 9.6% in two years to 12.5% in 2003. To measure Korea's position in the region more accurately, this study made some preliminary assessment about the relative profitability of investment between Korea and China. In 2002, 54% of companies in Korea reported margins higher than world wide average, compared with 42% in China. In 2003, investment in China came closer to the level of Korea, as 44% of companies in Korea and 42% of companies in China reported margins higher than the average. Notably, profit failures in China were fewer than in Korea with only 27%, while 47% of the companies in Korea failed to report

a profit. In terms of overall profitability as measured by the rate of return on assets, Korea still leads China by a marked degree, indicating that shareholder's assets are used more productively. The profit from Korea is approximately 28% of that of China for 2003, against 10% or less of assets suggesting that overall return on assets is higher in Korea.

According to JETRO, 84.2% of Japanese-affiliated manufacturers in Korea achieved an operating profit in 2003 while 74.4% of the respondents in China did so. On average, 79.6% of Japanese-affiliated manufacturers in Northeast Asian countries posted operating profit.

The ultimate reason to invest in Korea becomes clear after looking at the comparison with China and observing Japanese investors' actions - production in Korea is considerably lower in cost than Japan, and is also of higher quality than in China at present.

Both the productivity of capital in the case of the majority of foreign investments, and of labour in almost all foreign direct investments was well above that of the global average of the parent company.

A series of case studies emphasized that foreign companies had been able to merge operations and restructure to achieve some of the most profitable units in the world despite unionisation.

A list of the "keys to success," collected from interviewing various successful companies, boils down to collective wisdom of forming aggressive and effective strategies to plough through the extreme fast time economy of Korea by always staying at the edge of innovation and speed, efficient management and attention to details. At certain times like the Asian financial crisis of 1997-8, the ultimate secret to survival and success was for the companies to carry out total overhaul in every aspect of their operations.

Table E.2. Companies by year of establishment

Established	Number of companies	Net Profit / Asset	Net Profit / Sales	EBIT / Sales	Sales / Employee(US\$)
1950 – 1959	2	7.5%	7.9%	7.5%	672,268
1960 – 1969	5	7.6%	5.7%	9.9%	1,028,554
1970 – 1979	10	18.7%	10.7%	14.7%	553,521
1980 – 1989	33	9.4%	5.6%	8.8%	667,177
1990 – 1997	35	2.4%	1.9%	4.0%	1,175,015
1998 – 1999	15	6.1%	3.1%	5.4%	1,492,554
2000 – 2003	10	-0.7%	-3.7%	-2.8%	1,290,452
Total (Average)	110	6.5%	3.8%	6.3%	1,004,161

The study also offered some observations on companies, which make a loss at the level of EBIT. For the companies making a loss, the study has identified six factors. They are as follows:

- Length of time in Korea
- Size
- Sector
- Absence of local manufacturing capability
- Inefficient restructuring
- Random factor

A strong theme of the study was how profitable manufacturing in Korea remains. The majority of investors with factories in Korea were achieving operation rates, which outshone most other equivalent operations in the world. High wages were outshone by even higher productivity in both production and sales.

Foreign investors interviewed complained about restrictions especially in the labour market, which prevented a rapid adjustment in times of difficulty. The consultants noted that while sales per employee and return on assets were outstanding, profit at both EBIT and Net Profit was lower than these indicators would suggest should be the case. Consequently it was assumed that inefficiencies in the average operation caused by labour inflexibility and other operating conditions existed.

The study considered the reasons for profit failure as well as success and concluded that only 5.4% of all investment failed for reasons which could not be explained by product life cycle or start up or restructuring.

110 foreign invested enterprises were considered as the sample including all major subsidiaries of Fortune 500 companies. Financial analysis was from public source documents in Korea and the country of origin and supplemented by interviews.

The study was directed by Dr Tony Michell who is a fellow of the East Asia Institute of Cambridge University, and a future working paper from the Institute would supplement some of these findings

1. The Debate on the Cost of Production in Korea

1.1. Introduction: Are foreign companies in Korea profitable?

There is a perception that direct investment in Korea is unlikely to be very profitable, except in special cases. This perception is derived from several sources. We may list five:

- Experiences in the 1980s and early 1990s when Korea still had considerable protectionist barriers
- Continued special pleading by interest groups such as US car companies whose sales are in some way restricted in Korea
- A widespread belief that Korean labour is expensive and also truculent with militant trade unions
- A commonly stated belief that the Korean labour law restricts the flexibility of operation of companies and thus reducing their profitability
- Korean concerns about the cost of production in Korea. If Koreans are moving production out of Korea, why would foreigners invest in Korea?

This study sets out to test this perception empirically by looking at the profitability of foreign companies in Korea in the period 2001-2003. If a large number of foreign companies can be demonstrated to be making above average profits in Korea, and if we can find consistent internal reasons why the majority of lower than average profitability companies make less money, then we can conclude that well managed companies with healthy structures can be highly profitable in Korea. Reasons for making lower profit may relate to company life cycle, the structure of the industry or other objective factors. If such reasons prevail loss-making companies, then the perception is demonstrably false.

If on the other-hand the majority of companies are making below average profits with no particular explanation other than market conditions, regulation, inflexible labour laws and other parts of the litany of complaints against Korea, then the perception might be considered as founded on fact.

1.2. The part and not the whole

Multinationals are exactly that – multinational. There is no obligation on a company to consolidate its business in Korea into a single Korean registered entity. Indeed the multidivisional structure of multinationals means that different divisions often deal with Korea in different ways. Some products may be handled through trading operations, some manufactured in Korea and some products sourced from other companies in Korea. For service companies the structure may be different again. Even the investor which derives its greatest share of global income from Korea, Philips, has a major entity in Hong Kong holding Korean assets and sells about US\$400 million per year to Korea from overseas subsidiaries which leave no trace in the records of Philips Korea Ltd., LG.Philips LCD Ltd., or LG.Philips Displays.

For BAT (British American Tobacco), Korea is the fastest growing market, but most of the profit flows through a branch, Rothman's Brands Far East, which pays taxes in Korea, but is not consolidated in the financial returns of BAT Korea or BAT Manufacturing Korea. BAT is understood to make rates of profit equal to or above its global parent, but this is not evident from the public source records used as the statistical basis for this study.

Multinationals in the same general business area handle the same business process in different ways. IBM procures over US\$4 billion in product from Korea, but all these purchases are handled by global off-shore divisions, and no record of these sales or the profits are left in any of the IBM entities in Korea. Hewlett Packard, by contrast, purchases products through its Korean entity and exports in the name of the Korean company, so Hewlett-Packard's Korean records cover a business-dimension that is not recorded for IBM Korea.

Consequently, the methodology used cannot capture the full contribution of foreign companies in Korea to their parent company. There is every indication that if it were possible to include the full contribution, it would raise the overall record of profitability of doing business with Korea.

1.3. Preliminary Findings

Our findings are clear. The majority of foreign invested companies in Korea exceed their global parents in the best measure of profitability, from the point of view of shareholder value return on assets employed. Most measurements of profit are governed by management skill and strategy, the efficiency of the company and the level of economic activity. So when the Korean GDP growth rate plunged from 7.0% in 2002 to 3.1% in 2003, profitability was negatively affected. Table 1.1 shows how the return of assets was increasing in 2001-2 and deteriorated in the more difficult year of 2003.

Table 1.1. Return on assets employed
More profitable than global average (adjusted sample)

2001	78.1%
2002	81.8%
2003	70.0%

As Table 1.1 shows in 2003 on an adjusted sample basis 70% of foreign companies achieved a higher return on assets than their global parents. On an unadjusted basis, which includes start-ups and the problem sector of pharmaceuticals 56.4% of the 110 companies studied were more profitable. Profitability could have been higher if the foreign companies could have operated more efficiently since 89.7% of the unadjusted sample and 92.5% of the adjusted sample had a higher sales to asset ratio than their global operations in 2003.

There is another important measure which emerges, highly relevant to the five issues which are seen as forming a negative impression on the prospects for investment in Korea, and this is the level of labour productivity as measured by sales per employee.

Productivity in Korea is rising twice as fast as global productivity in the same firm. Table 1.2 summarises this achievement.

Table 1.2. Productivity measured by sales per employee

Unit: US\$

	Korean	Global
2001	759,954	343,722
2002	935,968	338,072
2003	1,004,161	396,257

Table 1.2 shows that labour productivity had risen 32% above 2001 levels in two years in Korea, compared with 15% globally. (It has also risen well above wage increases)

Therefore in terms of productivity of both capital and labour, foreign companies are achieving a remarkable performance, but on the performance of productivity of capital, there could be some grounds for improving efficiency.

In terms of operating profit to sales, the results are slightly less clear. About 60% of companies exceed or equal their global parents in operating profit and net profit and 40% do not. For many of the companies falling below the level of the global parent, specific reasons can be found.

This report examines these preliminary conclusions in the following sequence. Chapter 2 explains the methodology used, and Chapter 3 describes the characteristics of the sample of companies and their importance in Korea and to their parent companies. Chapter 4 examines the results of the study in terms of profitability in more detail, including some basic regional comparisons.

Chapter 5 looks at the causes of profitability, and those companies which make less than average profitability to discover some basic reasons, and whether less profitable companies will achieve a higher level of profitability in the future. As noted, if all companies are included in the results then the number of less profitable increases. In further research, the majority of companies excluded with the exception of pharmaceutical companies can be found to have unusual characteristics, which do not reflect profitability related Korean circumstances, but rather corporate issues such as start up modes and transfer pricing issues. However a limited number of companies, which might be expected to do well in Korea but do not, and there are famous names amongst them. Does this reflect the Korean market system or some other factor such as inappropriate strategies and inappropriate management? These issues are considered more at length in section 6 and in specific detail in the Occasional Paper.

Chapter 6 looks at six very different companies in terms of how they are achieving their present profitable status.

Chapter 7 takes a preliminary view of the key question as to whether investment in Korea is likely to continue to be a wise choice in terms of profitability compared with Japan and China as the Northeast Asian economy evolves. A higher percentage of foreign companies in Korea are currently more profitable than those in China. Foreign investors believe that the Korean government needs to make further liberalizations to ensure that this continues to be true. This is an area where further research would be valuable. The final chapter

sums up the key findings of the report and indicates further areas of research. This report is to be complemented by an occasional research paper which it is intended to issue through the East Asia Institute of Cambridge University, which will add further detail chiefly of academic interest.

The basic conclusion is that the majority companies of all sizes can and do make significantly higher profits in Korea than their global average. However, as in all businesses, not all companies succeed, and those who do not adapt creatively to the challenges of a fast moving and highly competitive market may make lower profits or even lose money. The percentage of unexplained failure is 5.4%.

2. Methodology

2.1. Sample

The study used basic public information as its starting point, the financial reports made to the Financial Supervisory Service (FSS) and the Annual Reports of major foreign invested companies, starting with the *Fortune 500*. As of August 2004, 263 companies out of *Fortune 500* have invested in Korea but some of these foreign companies are not required to make returns to the FSS because of smaller assets or corporate form.

The study used the *Fortune 500* industrial classification for comparative purposes. This divides the leading international companies into 26 industrial categories.

This process yielded 110 companies earning between US\$5 million in sales and US\$5 billion. Table 2.1 lists the characteristics of the companies.

Table 2.1. Companies by size of sales and sales per employee (2003)

	Number	Sales / Employee (US\$)
US\$1 billion and above	12	1,570,784
US\$500-999 million	16 (2)	1,419,946
US\$250-499 million	11 (4)	902,581
US\$100-249 million	25 (2)	1,086,306
US\$50 – 99 million	24 (1)	665,613
US\$5 – 49 million	22 (4)	694,420

(Numbers in parenthesis: Companies not in *Fortune 500* in sample)

The sample is weighted towards well established companies. The reason is that most major multinationals established some sort of base in Korea prior to 1997. In particular in the years after Korea permitted imports of consumer goods and domestic distribution and sales was liberalized a large number of companies set up sales and marketing companies without associated manufacturing.

More discussion on FSS returns and *Fortune 500* is available in Appendix 1

2.2. Definitions and qualifications of profit

In any exploration of the profitability of foreign invested companies in Korea, the question of methodology must be faced first. While profitability is the quest of all companies, the way in which profit is recorded in large multinationals may vary according to the strategic goals and life cycle of the company.

From the point of view of shareholders, the efficiency with which the company's capital or assets is used is of paramount importance. When a project is analyzed, the company's ability to clear a return on capital threshold is a key criterion. Indicators such as net profit or operating profit as a percentage of total sales or more sophisticated methodologies such as EBITDA do not measure the efficiency of the use of assets, but the efficiency of the operation itself, and the profit margins that can be achieved in the market. An increase in

capitalization might achieve a higher net profit to sales ratio, but a lower rate of return on assets.

Net Profit to Assets:

We have accepted that the best measure of profit is the one of most interest to shareholders, return on assets employed, measured by the ratio of net profit to assets. All other measures of profitability are subsidiary to this. As noted, 65.7% of companies in Korea exceeded their parents by this measure in 2002.

EBIT:

Measures such as EBIT (Earnings before interest and tax) and net profit to sales basically measure the efficiency of the operation. EBIT should be positive. A company with negative EBIT is in general either starting its business, restructuring or going out of business.

In studying the profitability of multinationals with multiple subsidiaries, negative EBIT can however represent the “part is not whole” syndrome, in that the profit is being taken by the multinational head office or overseas, for a variety of reasons related to research costs, dual taxation agreements and other aspects of business. For this reason pharmaceutical subsidiaries generally make less profit than their parent companies, and for some famous names in Korea this may also be true. Further consideration of this issue is given in section 2.6.

Net Profit:

Net profit may reflect many other activities of the company including windfall profits or losses, restructuring charges and other unique circumstances. It may also reflect the leverage choice of the firm or short-term financial costs related to investment or renewal of equipment. In general foreign companies in Korea during the years studied had a higher net profit to sales ratio than EBIT ratio. This reflects such issues as profit from exchange rate differences and currency hedges moving in favour of the company.

Global sales as contained in the Annual Reports are consolidated accounts. The accounts of the Korean subsidiaries are non-consolidated, even for the several subsidiaries of companies such as GE or Philips in Korea. This makes no detectable difference to profit figures but makes the local sales ratio to global sales only a general indication of the importance of the company in Korea to the global organisation.

2.3. Regional Comparisons

All regulatory authorities for listed companies require that annual reports give a regional break down of sales. However there is no consensus amongst companies or regulators on what is sufficient data, and what constitutes an appropriate regional breakdown.

Table 2.2 gives a summary of the companies with regional data. Of the 110 companies, 76 have regional sales data, and 62 include in their international data the Asia Pacific region as a district entity. Other companies have data merely distinguishing

“international” from “domestic sales”, or class the Asia-Pacific region as the “rest of the world”. Only 24 companies give regional EBIT.

Table 2.2 Companies with regional data (2003)

	Number
Companies with regional data	76
Companies with Asia Pacific data (Sales)	62
Companies with Asia Pacific data (Sales and EBIT)	24

Table 2.2 shows that only about half the sample can be directly compared with official figures for the region, and only a quarter on the basis of one measure of profitability.

Further information specifically on China was added, principally from the China Economic Quarterly.

2.4. Exclusions

In order to measure the profitability of foreign companies in Korea, it is necessary to consider the particular circumstances of each company and those of each industry grouping. Data was classified according to the whole group and to the retained sample excluding certain companies.

More comments are in appendix 1.

2.5. Indicators: Measurements of Success – Individual or Industry Grouping

The following full set of indicators of success were considered:

- Sales to assets
- EBIT
- Net Profit
- Return (Net Profit) on Assets
- Sales per employee
- Interest rate coverage

For more details, please refer to appendix 1.

2.6. Other issues

Qualitative factors and currency of analysis are also explained in appendix.

A longer research period would have allowed the writers of this report to apply more tests to the data collected see if the data series could have been extended, and then apply more sophisticated measures of correlation between GDP growth and profitability both in Korea and at a global level.

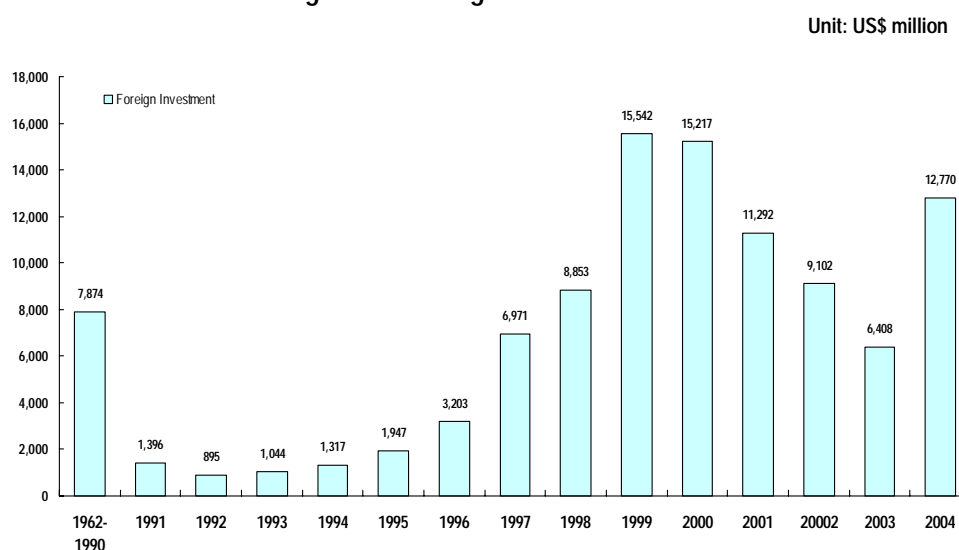
Further analysis will be given in the occasional research paper to be published later.

3. Major Foreign Investors in Korea

3.1. Foreign Companies in Korea

Foreign investment in Korea was markedly absent before the IMF crisis of 1997-8, due to the number of closed markets and market restrictions. Although there was rapid liberalisation from 1997 onwards, the perception remained that Korea was a difficult market, and companies stood a limited chance of success there. The continuing liberalization of the Korean market has increased investment and the success rate.

Diagram 3.1 Foreign Direct Investment



Source: Ministry of Commerce, Industry and Energy, Investment Commitment Basis

Diagram 3.1 shows the volume of foreign direct investment by year from 1962 to 2004. The total volume of investment from 1962 – 1990 was only US\$7.9 billion (unadjusted for inflation) or an average of US\$272 million per annum. During 1991 – 1995 the average investment per annum was US\$1.3 billion. 1996 showed that Korea's liberalization was being recognized and investment reached US\$3.2 billion. Foreign direct investment then soared, reaching US\$15.5 billion in 1999 and US\$15.2 billion in 2000. After extraordinary opportunities in terms of acquiring bankrupt companies had been completed, foreign direct investment settled back to about US\$10 billion per annum.

In terms of the number of investors, 5,337 companies had invested in Korea by 1990, and during the next five years additional 2,932 companies made investment. Between 1996 and 2004 a further 21,045 investments were made (some being reinvestments).

The size of some of the Korean subsidiaries of foreign companies will come as a surprise to those not familiar with the changing business scene in Korea. 12 foreign invested companies in the sample had sales of US\$1 billion and above in 2003, rising significantly from 9 in 2002 and 4 in 2001, and 16 companies had sales of US\$500-999 million, showing a growth from 12 in 2001.

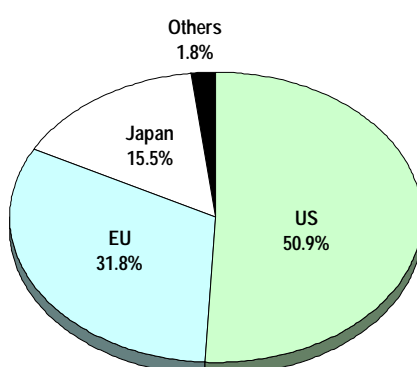
Table 3.2. Companies by Size of Sales

	2001	2002	2003
US\$1 billion and above:	4	9	12
US\$500-999 million	12	16	16
US\$250-499 million	17	11	8
US\$100-249 million	15	22	28
US\$50 – 99 million	23	23	24
US\$5 – 49 million	29	27	22
No data or not existing	10	2	0
Total	110	110	110

Table 3.2 shows dramatic growth of foreign companies in Korea by size. Little of this growth stemmed from new acquisitions in this period. More than 90% of the companies that grew were already in existence in 2001 and seized the Korean opportunity. Most notably, smaller foreign companies were growing. 29 companies in the sample had sales of less than US\$50 million in 2001, but by 2003 only 22 were in this category. This dramatic upward shift in sales is remarkable, considering that Korea was an economy that was only performing well in the export sector, which had not primarily been the focus of foreign investors.

By nationality, the companies in the sample are as shown in diagram 3.3. It can be seen that the majority of companies are American or European, and 17 are Japanese. New Chinese investments will only appear in this analysis for 2004 or 2005.

Diagram 3.3. Companies by Nationality



Region	Country	Number
US		56
EU	UK	9
	Germany	9
	Netherlands	5
	Switzerland	5
	France	4
	Sweden	2
	Finland	1
	Sub-total	35
Japan		17
Others		2

Companies achieved considerable efficiency in sales per employee, a crude measure of labour productivity. In general, subsidiaries should have a slightly higher sales per employee than the home office, which is where the administration is, but the scale of difference is dramatic in the case of Korea.

Table 3.4. Companies by Sales Per Employee (2003)

Unit: US\$

	Number	Sales / Employee	
		Korean	Global
US\$1 billion and above	12	1,570,784	564,730
US\$500-999 million	16 (2)	1,419,946	286,258
US\$250-499 million	11 (4)	902,581	349,361
US\$100-249 million	25 (2)	1,086,306	331,436
US\$50 – 99 million	24 (1)	665,613	578,339
US\$5 – 49 million	22 (4)	694,420	280,701

It can be seen from table 3.4 that the difference between Korean and global sales per employee is considerable, except in companies in the US\$50-99 million category.

The exception to this process is the mid-sized companies with sales between US\$50 million and US\$99 million. Not are their sales per employee significantly lower than larger companies, but slightly higher than the parent companies.

Companies have generally responded to the relatively high cost and inflexibility of labour by increasing productivity. The growth in sales per employee measured an average of 32% in two years in Korea, compared with 15% for the global operations.

3.2. The importance of Korea

The increase of investment inevitably raised the share of investors' global income coming from Korea. In 2001, Korea sales made up 1.0% of global sales, and this rose 50% in two years to 1.5% 2003. 1.0% may not seem very large, but it must be remembered that most of the companies in the sample had only 12-13% of their sales in the Asia-Pacific.

Table 3.5. Korean Share of Global Sales

	Korea / Global
2001	1.0
2002	1.2
2003	1.5

By increasing Korea's share of global sales from 1% to 1.5%, companies' sales were beginning to approach Korea's scale in the world economy. Korea in 2003 was the world's 11th largest economy measured in terms of GDP. Its share of global GDP in that year was 1.7%. Korea's share in the global market of those companies in the sample rose 50% in two years, although in absolute terms this only took Korea from 1% of global sales in 2001 to 1.5% in 2003.

By company the share of Korean sales ranges from 0.25% in the case of nearly half of the investors to 35% in the case of Fairchild Semiconductor. On the whole, the big companies globally achieve big local sales, and small companies on a global basis achieve small sales. The less favourable market conditions of 2003 led to a slippage of global share for some companies.

Table 3.6. Ratio of Korean Sales to Global Sales

	2001		2002		2003	
20% and above	2	2.2%	3	3.1%	3	3.1%
10% -19.9%	1	1.1%	2	2.1%	2	2.1%
5% - 9.9%	5	5.6%	3	3.1%	5	5.2%
1% - 4.9%	24	26.7%	29	30.2%	26	27.1%
0.5% -0.99%	14	15.6%	16	16.7%	16	16.7%
0.03% -0.49%	44	48.9%	43	44.8%	44	45.8%
Total	90	100.0%	96	100.0%	96	100.0%

There is a pipeline effect built into these market shares. Those companies which entered the market since 1999 are still building their businesses. The data suggests that companies build their sales fast and their profitability more slowly.

Table 3.7 shows the companies by year of establishment in the sample. 85 were established before the IMF and 25 after the IMF. Although the new companies are large as measured by sales per employee, the 10 companies founded most recently are on average unprofitable at both EBIT and Net Profit level, in spite of their above average sales per employee.

Table 3.7. Sample by year of establishment

Established	Number of companies	Net Profit / Asset	Net Profit / Sales	EBIT / Sales	Sales / Employee (US\$)
1950 – 1959	2	7.5%	7.9%	7.5%	672,268
1960 – 1969	5	7.6%	5.7%	9.9%	1,028,554
1970 – 1979	10	18.7%	10.7%	14.7%	553,521
1980 – 1989	33	9.4%	5.6%	8.8%	667,177
1990 – 1997	35	2.4%	1.9%	4.0%	1,175,015
1998 – 1999	15	6.1%	3.1%	5.4%	1,492,554
2000 – 2003	10	-0.7%	-3.7%	-2.8%	1,290,452
Total (Average)	110	6.5%	3.8%	6.3%	1,004,161

The pipeline effect is that the new companies should be able to increase their sales considerably in the future. It is argued elsewhere that the profit pipeline is likely to be even more full. Creating a profit in Korea takes time. According to AMCHAM's survey of profitability, in China it takes at least 6 years for the majority of companies to become profitable. In Korea, table 3.7 suggests that it takes at least four years. The 10 companies founded between 2000-2003 should begin to be profitable in 2004.

3.3. The part and not the whole

As noted in section 1, multinationals are exactly that – multinational. The total number of subsidiaries of most major multinationals runs into hundreds and sometimes thousands. The annual reports represent a consolidated overview, but of the actual subsidiaries some are accounting entities and some are operational companies, each of which may have some dealings with Korea. There is no obligation on the company to consolidate its business in Korea into a single Korean registered entity. Indeed the multidivisional structure of multinationals means that different divisions deal with Korea in different ways. Some products may be handled through trading operations, some manufactured in Korea and some sourced from other companies in Korea. For service companies, the structure may be different again. Even the investor which derives its greatest share of global income from Korea, Philips, has a major entity in Hong Kong holding Korean assets and sells about US\$400 million per year to Korea from overseas subsidiaries which leave no trace in the records of Philips Korea.

For BAT, Korea is its fastest growing market, but most of the profit flows through a branch, Rothman's Brands Far East, which pays taxes in Korea, but is not consolidated in the financial returns of BAT Korea or BAT Manufacturing Korea. BAT is understood to make rates of profit equal or exceeding its global parent, but this is not evident from the public source records used as the statistical basis for this study.

Multinationals in the same general business area handle the same business process in different ways. IBM procures over US\$4 billion in product from Korea but all these purchases are handled by global off-shore divisions and no record of these sales or the profits are left in any of the IBM entities in Korea. Hewlett Packard, by contrast, purchases products through its Korean entity and exports in the name of the Korean company, so Hewlett-Packard's Korean records cover a business-dimension, which is not recorded for IBM Korea.

Multinationals are rational organizations and view their profit based on the complete value chain. Profit margins may be created at each step of the process, especially in transnational business, and recorded in the various countries involved in the transaction or transfer the profit from one subsidiary to another through transfer pricing. The definitions of transfer pricing for tax and customs purposes and for accounting purposes may be very different. For companies involved in sales and distribution and after services in Korea, the choice of where to book the profit lies in balancing corporate preferences and tax or custom requirements. These in turn may vary from nationality to nationality based on national tax rates and the respective tax treaties. As a general rule however it is simpler to add a front end margin (higher profit on the product in country of origin) than repatriate profits (back end margin). The higher the customs tariff, the less this is valid. From this perspective the era of WTO with falling customs tariffs may lessen apparent profit of the enterprise in the country in which the ultimate customer is located.

In the 1980s and early 1990s, many companies acted as commission agents for their parent company. Few foreign companies still sell totally on commission, but many companies may sell a part of their product on commission. By agreement between National Tax Service (NTS) and foreign trading companies in the course of permanent establishment negotiations and tax suits, it was agreed that under Korean tax rules, a commission agent may not receive more than 8% of the price of the goods sold. From 8% must cover all expenses except advertising and promotion expenses which may – or may not – be apportioned. Although this guideline is technically abolished, the general advice to companies is that NTS cannot be trusted in a future investigation if the rate of commission is exceeded. In this instance, Korean tax laws impose an artificial barrier which will limit profit for the Korean subsidiary.

Consequently the methodology used cannot capture the full contribution of foreign companies in Korea to their parent company. There is every indication that if it were possible to include the full contribution, it would raise the overall profitability of doing business with Korea.

3.4. Conclusions

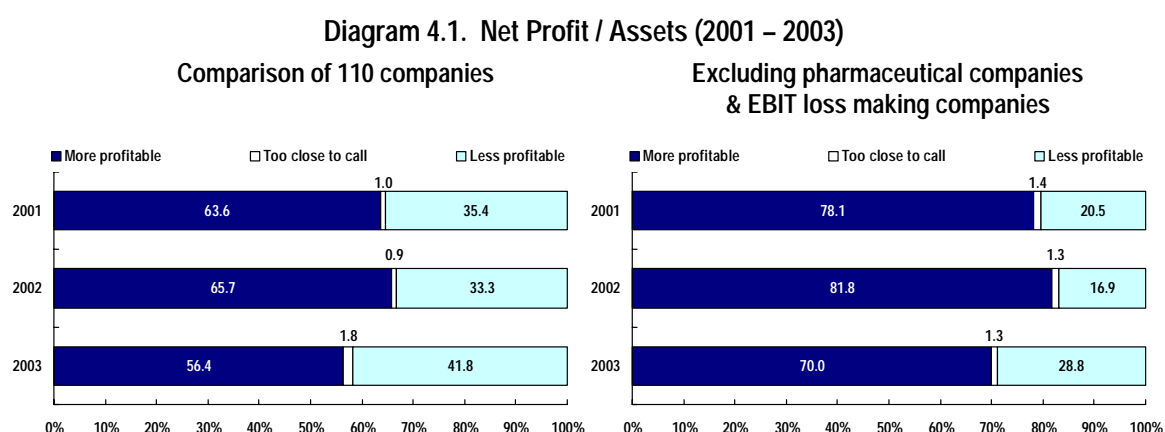
Foreign companies have increased their sales in Korea rapidly in recent years, most particularly in the category of very large companies with local sales of more than US\$1 billion. American companies outweigh other investors in our sample. This is expected to change as more regional investment occurs from Japan, China and other Asian countries. To that effect, Japanese investment increased 300%.

Korea is the fifth largest producer of many kinds of manufactured goods. However, most foreign companies are still under represented in Korea. Nevertheless, the share of Korean sales to global sales at 1.5% in 2003 is rising towards Korea's share of global GDP, which was 1.7% in 2003.

4. Profitability of Foreign Investments

4.1. Return on Assets – Shareholder Value

Diagram 4.1 shows the basic conclusions from the study, which shows that, in 2003, 70% of foreign direct invested companies in our adjusted sample are more profitable than their global parents, and a further 1.3% had a rate of profitability approximately equal to the global parent. This 70.0% of companies that matched or exceeded the parents in profitability has to be set against the 28.8%, which were less profitable.



In the more favourable economic circumstances of 2002, 81.8% of the adjusted sample and 65.7% of all companies were more profitable. Only 16.9% of the adjusted sample failed to equal the global profit rate.

If we reinsert the excluded companies (which have suspect data or belong to the unprofitable pharmaceutical sector) then the majority of companies are still more profitable than their parents as shown in diagram 4.1, but the percentage of companies that are less profitable rises to 41.8%.

Essentially diagram 4.1 shows that the majority of foreign invested companies have good control over their investments and have judged them well. There are no wasted assets in these investments in Korea. In terms of shareholder value, the majority of shareholders have done extremely well out of their direct investments in Korea, and if their parent companies could perform at the Korean rate then all of these multinationals would increase their value significantly.

4.2. EBIT and Net Profit – Measures of Efficiency

In terms of net profit to sales and EBIT as shown in diagrams 4.2 and 4.3, net profit and EBIT fell in 2003 compared with results in 2001 and 2002, reflecting the imbalance between domestic sales and exports in the Korean economy. In the adjusted sample, the percentage of profitable companies fell from 64.9% to 48.8% in the same period in terms of net profit to sales. The percentage of less profitable companies rose from 29.9% to 40%. In the unadjusted sample, companies outperforming their global operations both in terms

of by net profit and EBIT fell from 55.7% in 2002 to 41.4%. In China, only 42% of companies reported profits which were higher than average in both 2002 and 2003, according to the annual AMCHAM survey.

Diagram 4.2. Net Profit / Sales (2001-2003)

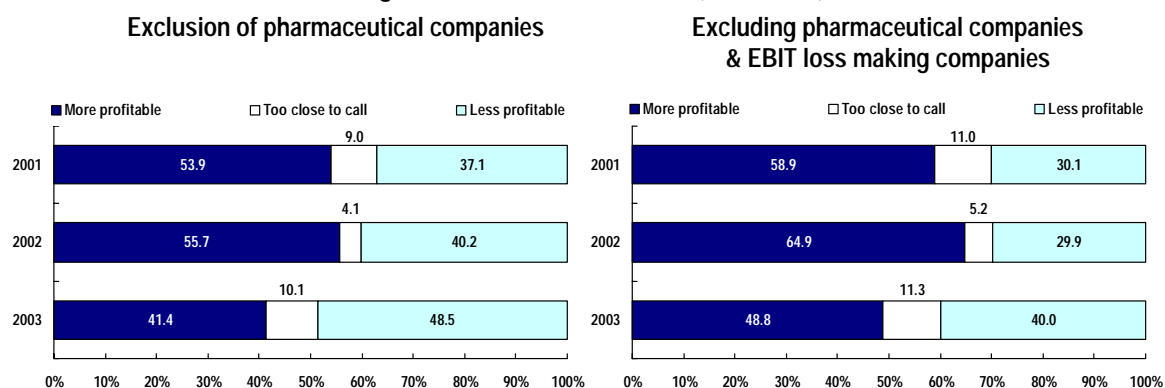
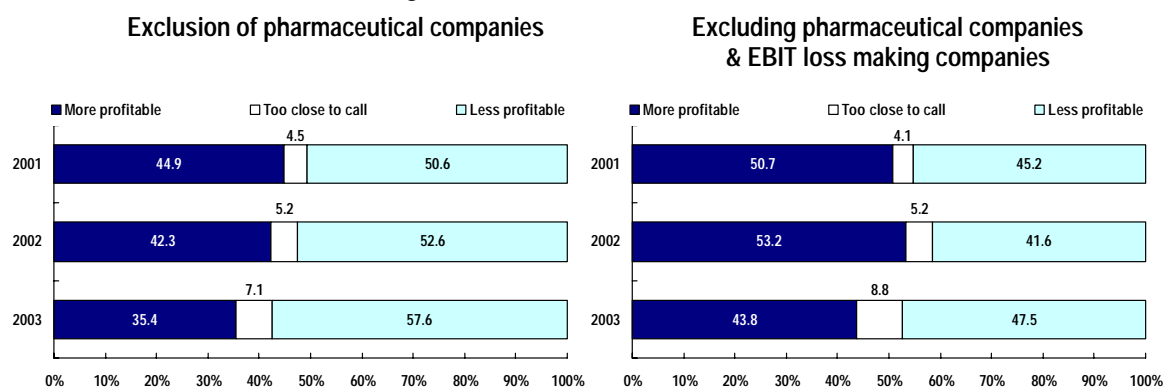


Diagram 4.3. EBIT / Sales (2001-2003)



With all companies included, the poor economic conditions of 2003 created a situation where less profitable companies exceeded more profitable companies for the first time.

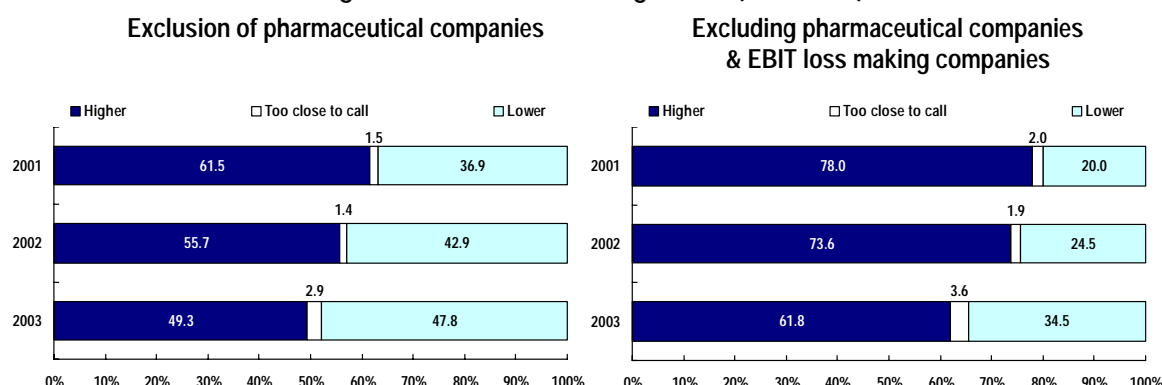
Net profit to assets measures the efficiency with which an investment is used, as well as being the key indicator of shareholder value. EBIT and net profit to sales ratios measure the efficiency of the operation, not the efficiency of the use of capital. The higher the rate of profit on a given volume of sales, the more efficient the operation or the higher the margin that a company is able to charge in the Korean market.

In general, the Korean market is seen as highly competitive on prices, and therefore in order to achieve an above global profit, the operation must be highly efficient in terms of cost control. Diagrams 4.2-4.3 show that, in 2002, 55.7% of companies had higher net profit to sales ratio and 42.3% had higher global EBIT to sales ratio than their global parents. But in the more difficult economic circumstances of 2003, only 41.4% of companies were more profitable although the number of companies too close to call increased so that the total of above and on par companies in 2003 was 51.5%, compared with 59.8% in 2002.

The fact that sales per employee increased but net profit fell indicates some inflexibility in adjusting to an economic downturn.

4.3. Interest Coverage Ratio

Diagram 4.4. Interest Coverage Ratio (2001-2003)



Interest coverage ratios were at their highest in 2001 and fell in 2002 and 2003. The fall from 61.5% to 49.3% in the unadjusted sample is mirrored by the fall from 78% to 61.8% in the adjusted sample. In short, the average foreign company increased its borrowing in 2002 and 2003.

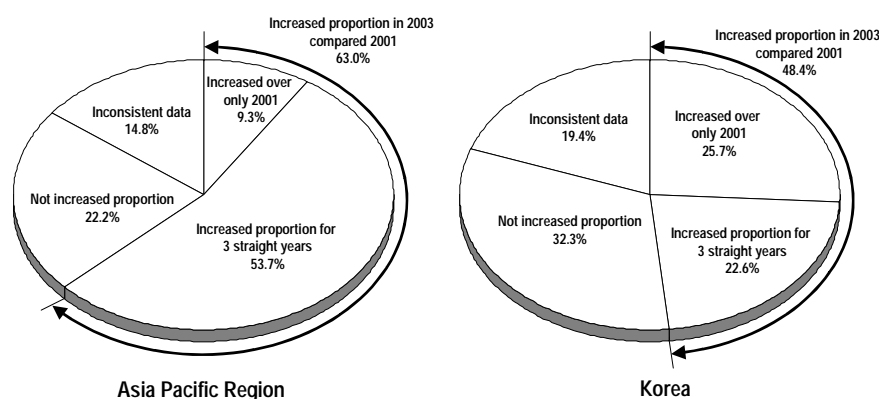
It remains true that Korean subsidiaries' interest coverage ratios are usually higher than those of its global parent companies. Although the number of higher local ratios declined in 2003 in comparison to the 2001 and 2002, the adjusted sample excluding pharmaceutical companies and EBIT-loss making companies shows that the local ratios were still generally higher than the global ratios. This means that companies are secure and use a low level of leverage.

The interest coverage rate is a comparative measure. Nearly all multinationals use debt a lot less than Korean companies.

4.4. Regional Comparisons

All regulatory authorities require that annual reports give a regional break down of sales for listed companies. However, there is no consensus amongst companies as to what is sufficient data and what constitutes an appropriate regional breakdown.

Diagram 4.5. Regional Comparison (Sales)



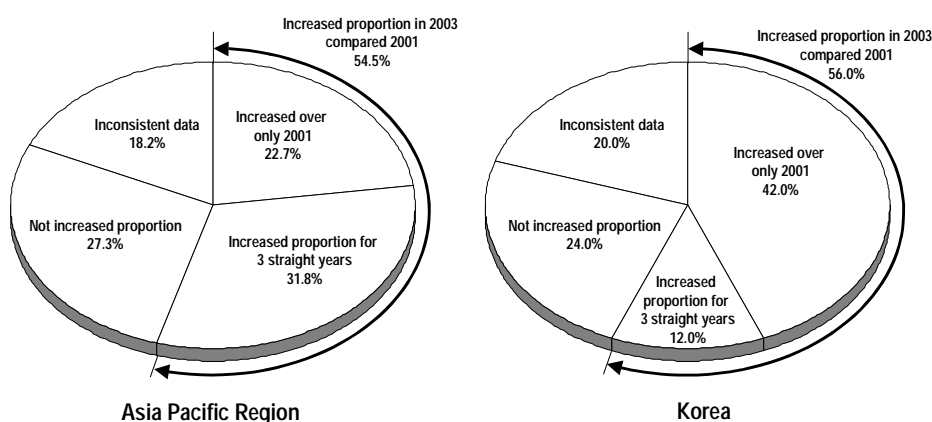
	Sales in AP region to Total sales	Sales in Korea to AP region
No. of companies which increased their proportion in 2003 comparing to 2001	34	30
No. of companies which increased their proportion for 3 straight years	29	14
No. of companies which did not increase their proportion	12	20
Companies with inconsistent data	8	12
Total	54	62

Diagram 4.5 shows that of the 62 companies for which a regional comparison is possible, 30 out of 62 companies that provided the regional data increased their sales in Korea as a proportion of regional sales.

Because of fluctuating exchange rates and economic growth rates, a straight three-year increase of sales is not as common as an increase in sales between 2001 and 2003.

Diagram 4.5 shows that the performance of Korean subsidiaries in the Asia Pacific region was not superior to that of the overall Asia Pacific. 63% of global companies increased their sales in the Asia Pacific as a percentage of global sales between 2001 and 2003. Only 48.4% of the companies increased their Korean sales between 2001 and 2003. However, the growth of the successful companies was so dramatic that in total it outweighed the failure of some companies to grow. Poor performance in 2003 mainly explained this discrepancy.

Table 4.6. Regional Comparison (EBIT)



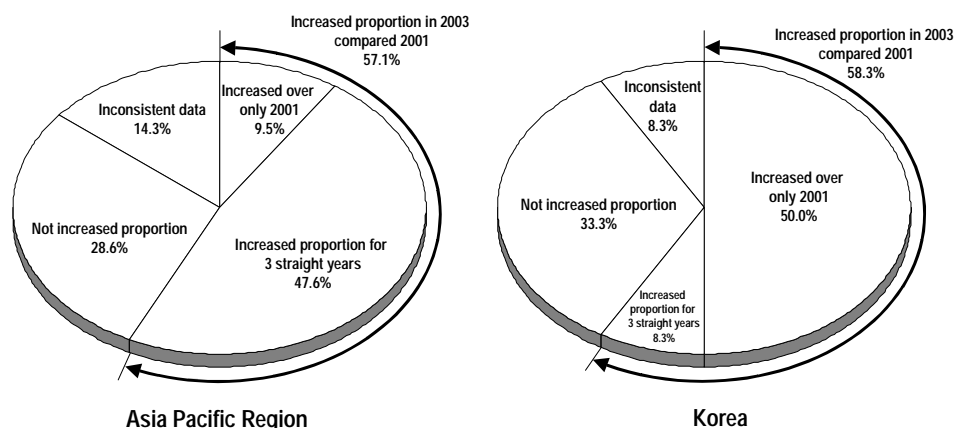
	EBIT in AP region to Total sales	EBIT in Korea to AP region
No. of companies which increased their proportion in 2003 comparing to 2001	12	14
No. of companies which increased their proportion for 3 straight years	7	3
No. of companies which did not increase their proportion	6	6
Companies with inconsistent data	4	5
Total	22	26

The 26 companies with regional profit data in their annual reports showed 12 companies increased their rate of profit in the AP region to total ratio. The 14 companies increased their share of local profit relative to the region.

Again, exchange rate fluctuations may distort these conclusions, but in general most local companies increased their profit compared with the AP total.

Operating income to sales data provides a measurement of profitability of the Korean companies compared to their regional peers. Diagram 4.7 shows that 14 out of 24 companies increased their profit at EBIT in comparison to results of 2001.

Table 4.7. Regional Comparison (EBIT/ sales)



	AP	Korea
No. of companies which increase the ratio in 2003 comparing to 2001	12	14
No. of companies which increased the ratio for the 3 straight years	10	2
No. of companies which did not increase the ratio	6	8
Companies with inconsistent data	3	2
Total	21	24

4.5. Labour Productivity

The majority of companies in Korea have a much higher sales to employee ratio and a higher EBIT per employee than the global parent. During the three years under study, the productivity measured by sales to employee increased considerably, as shown in diagram 4.8. EBIT per employee increased sharply in 2002 and fell in 2003, while globally companies increased their efficiency largely due to the recovery of the US and Japan economy.

Table 4.8. Productivity of sales to employee

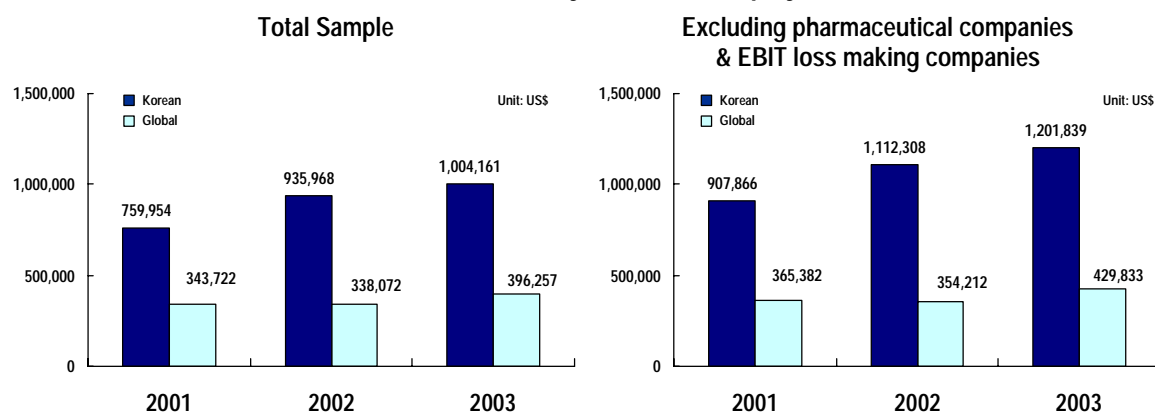
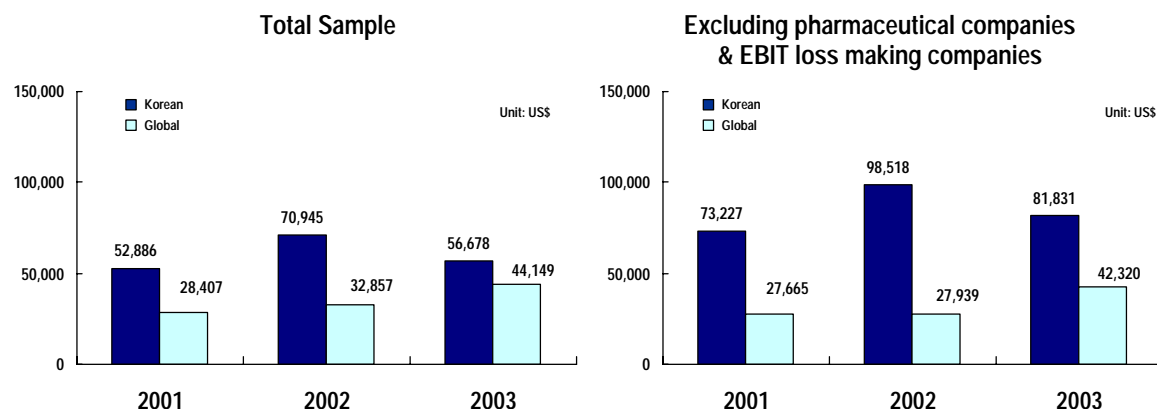


Table 4.9. Productivity of EBIT to employee



Excluding the loss making companies at EBIT level, companies in Korea greatly increased their profitability per employee in 2002, reaching close to 400% more profit per employee than the global average, but this fell back in 2003 to 200%.

4.6. Profitability by Industrial Sector

As previously noted, the pharmaceutical sector faces special problems which are analysed in Chapter 5. Are there any other sectors with similar problems? Table 4.10 gives the comparison by industrial sector.

Table 4.10. Industrial Sector Profitability 2003

Net profit / Assets by industry			Net Profit / Sales by industry		
	Global	Korean		Global	Korean
Computer Services	-0.2%	2.4%	Trading	0.4%	-8.8%
Insurance	0.4%	1.7%	Retailers	1.8%	2.2%
Trading	0.5%	-21.7%	Automotives	1.9%	2.6%
Metals	1.7%	-8.4%	Chemical	2.7%	-1.7%
Automotives	1.8%	6.2%	Metals	2.8%	-15.5%
Electronics, Elec. Equip	2.2%	7.4%	Food and Drug Stores	2.9%	0.9%
Diversified Financial	2.3%	-2.5%	Electronics, Elec. Equip	3.4%	3.0%
Entertainment	2.4%	12.6%	Mail, Package, Freight delivery	3.4%	3.3%
Chemical	2.4%	-1.6%	General Merchandise	3.5%	0.1%
Semiconductors, other components	4.0%	16.7%	Insurance	4.2%	3.4%
Mail, Package, Freight delivery	4.4%	5.7%	Entertainment	5.7%	6.0%
Aerospace and defense	4.5%	22.9%	Aerospace and defense	5.7%	15.3%
Food and Drug Stores	4.5%	0.9%	Computer Equip	5.9%	3.8%
Tobacco	5.2%	6.2%	Semiconductors, other components	6.3%	5.1%
Computer Equip	5.9%	6.2%	Network, Other Comm.	7.1%	-0.5%
Building materials, glass	6.6%	36.4%	Computer Services	7.1%	2.3%
Network, Other Comm.	6.6%	-1.5%	Food Services	7.6%	-4.6%
Retailers	6.7%	3.2%	Food Consumer	7.8%	2.6%
Food Services	7.8%	-1.3%	Tobacco	9.0%	4.8%
Miscellaneous	7.9%	14.8%	Building materials, glass	10.7%	40.6%
General Merchandise	8.6%	0.1%	Miscellaneous	10.8%	12.1%
Food Consumer	9.9%	4.9%	Petroleum Refining	11.1%	14.4%
Household Products	10.1%	14.6%	Diversified Financial	11.2%	-11.3%
Beverages	10.8%	22.6%	Household Products	11.8%	12.9%
Pharmaceuticals	11.2%	5.2%	Beverages	13.8%	13.9%
Petroleum Refining	14.4%	22.9%	Pharmaceuticals	16.9%	3.9%

The first evident fact is that each industrial sector has very different rate of return on assets. This reflects the different structure of industries and their capital intensity, as well as the

cyclical pricing phenomenon that very frequently occurs in sectors like the chemical industry. The difference in performance by industrial sector reflects a number of factors.

In terms of net profit to assets, Korean subsidiaries of 15 industrial classifications performed significantly better than their global industrial sector, and 12 performed worse, 5 of these sectors making a loss. However, for some of these sectors, foreign companies were only represented by 2 or 3 companies per industrial category. A comparison of the Korean sample compared with the Global sample is given in table 4.11.

In terms of net profit to sales, 9 industrial sectors were more profitable on average than the global average, and 17 less profitable. As appendix 2 shows, in the 21 sectors where there is more than one company in the sample and more than one company in the Fortune 500 category, there are 46 companies making a higher than average profit and 64 companies making a lower than average profit. Further consideration of industrial sectors is given in chapter 5.

Table 4.11. Samples by Industry

Industry		Number of company
A.	Aerospace and defense	1
B.	Automotives	13
C.	Beverages	4
D.	Building materials, glass	3
E.	Chemical	6
F.	Computer Services	2
G.	Computer Equip	10
H.	Diversified Financial	1
I.	Electronics, Elec. Equip	16
J.	Entertainment	2
K.	Food Consumer	5
L.	Food Services	2
M.	Food and Drug Stores	2
N.	General Merchandise	1
O.	Household Products	1
P.	Mail, Package, Freight delivery	2
Q.	Metals	2
R.	Network, Other Comm.	4
S.	Petroleum Refining	4
T.	Pharmaceuticals	11
U.	Semiconductors, other components	4
V.	Retailers	1
W.	Tobacco	3
X.	Trading	3
Y.	Miscellaneous	4
Z.	Insurance	3
Total		110

The overall conclusion of this section is that the rate of profit is unique to the sector. When the foreign investment is well established, Korea can be significantly more profitable.

4.7. Overall Assessment

It would be surprising if all foreign invested enterprises in Korea were more profitable than their parent organizations when we are measuring only part of a multinational's activity in Korea as explained in the previous chapter.

In 2002 the majority of companies made a higher than average profit as measured by return on assets, net profit and EBIT/sales. On an adjusted sample basis this pattern

remained true, but the number of companies making a higher than average return on assets was 81.8%, falling to 70.0% in 2003.

The majority of foreign direct invested companies therefore were better than their global parents at using both capital and labour.

That a majority are making more profit than the global average is an important conclusion. More significantly, if companies are losing money in Korea, for the most part it is not due to the low productivity per worker.

5. Why are companies profitable?

5.1. Profitability in Korea

The report opened with a consideration of the perception that direct investment in Korea is unlikely to be very profitable, except in special cases. This perception was noted as derived from several sources. We listed five main sources:

- Experiences in the 1980s and early 1990s when Korea still had considerable protectionist barriers
- Continued special pleading by interest groups such as US car companies
- A widespread belief that Korean labour is expensive and truculent
- The concern that the Korean labour law restricts flexibility of operation
- Korean concerns about the cost of production in Korea

This study set out to test this perception empirically by looking at the profitability of a large sample of foreign companies in Korea. The report has shown that the majority of foreign invested companies were highly profitable in 2001 and 2002, although this profitability weakened in 2003. The profit decline in 2003 came primarily from weaker economic growth and not *prima facie* from any of the five reasons given above.

In this chapter we look at three issues

- The secrets of success – the reasons companies attribute their profitability to
- Whether companies could be more profitable if certain restrictions or inflexibilities were removed
- Why a minority of companies make a loss

5.2. Secrets of Success

Making a profit is not guaranteed. 52 of the *Fortune 500* made a loss in 2003 which was a relatively good year for the global economy. In the 1990s, blue chip companies such as IBM made losses. The global median return on sales was only 3.5%, and the return on assets was only 1.9%, less than the bank interest rate. These rates are for companies generally making half of their sales in their home markets. Making money in a foreign market is generally more difficult than making money in the home market.

The secrets of success according to successful companies in specific industries in Korea include:

- “keeping unproductive labour practices imposed by labour unions to a minimum” - building company
- “pushing senior managers to adopt stretch targets” - electronics company
- “using the speed factor to bring new products to market faster than in other countries” - hi-tech company

- “working with the partner to utilize the best of the Korean and western systems” - retail company
- “harnessing the amazing Korean abilities in R&D to beat the rest of the world” - several companies in chemicals and machinery manufacturing
- “letting the Koreans lay out the production facility” - automotive company
- “select employees with care and train them well” - adhesives
- “let Koreans plan their own processes and use their attention to detail” - automobile company

Companies interviewed believed that of profitability lay in successful strategies in three main fields:

- The extreme competitiveness of Korean manufacturing processes and production engineering
- Management strategy which puts the company into a competitive posture in Korea either through product technology, continuous innovation or efficiency of the staff
- Painsstaking attention to detail, combined with high quality staff and/or good JV partners.

Even companies with negative EBIT such as Samsung Rockwell, GM Daewoo and Nestle acknowledged that their manufacturing operations were some of the lowest cost in the world, and that the quality of Korean production engineering offered world leadership. The best example of this was GM Daewoo, a company formed by GM’s take-over of Daewoo, which had appointed a Korean manager who joined the new company as the regional production manager handling not only Korea but plants in Australia, China and South East Asia. Successful companies like ABB and LG-Philips also turned this expertise into high rates of profit.

For other companies at the leading edge of their global operations, the ability to innovate fast in terms of product was felt to be the key competitive advantage which could lead to profitability. Most companies felt that since the financial crisis of 1997-8, Korean competitors for the most part had begun to compete on product, quality and service rather than price, and that this gave foreign companies more opportunity to succeed and be profitable in the 2000s compared with the 1990s.

Companies which had entirely renewed their operational management systems since 1998-9 and paid full attention to every aspect of their operation felt that this had made a significant improvement in their business. In contrast, those foreign companies which had not made the overhaul were those which made a sub-standard profit.

The case studies in the next chapter will illustrate the success of companies in which restructuring was possible without facing insuperable difficulties from unions or other regulatory restrictions. What is true of most of the case studies is that outstanding managerial leadership was also required.

5.3. Could companies be more profitable?

Most companies interviewed believed that if increased flexibility were granted by the Labour Law would significantly increase profitability. This was felt more strongly by companies that had made acquisitions than those that had built up their own operations.

A change in the Labour Laws they believe would result in a much more cooperative attitude amongst labour leaders inside the firm. In return for productivity bonuses, the proven skill of Korean in production processes could be applied to productivity in the rest of the firm.

There is good reason to believe that in the economic slowdown of 2003, the inflexibility of the labour system forced companies to retain costs which could have been shed in many other countries. At the same time, productivity per employee measured by sales per employee grew rapidly in 2003 and this was not translated into either returns on assets or EBIT. Again the conclusion indicated is that the inflexibilities of Korea exist in times of downturn and prevent companies from exploiting their productivity gains in full.

Companies which felt they were underperforming believed that they did not have the correct management team, and that better harmony amongst managers, breaking down Korean style "silo" mentality, was an essential process.

Amongst loss making companies there is clearly a room for improved management practice. Reforms or changes that some companies claimed would be impossible to achieve in Korea were in fact being achieved by other companies.

5.4. What makes companies less profitable than their global parents?

In this section and the following section, we offer some observations on those companies with lower than global profitability and then on those 21 companies which make a loss at the level of EBIT. Six factors are identified which account for under performance. Four are not related to Korean circumstances and two are.

The first and most important factor is Time

There is a very marked difference between the operating profit and net profit of the 85 companies established before 1998 and the 25 companies established between 1998 and 2003. Table 5.1 shows this very clearly.

Table 5.1. Profitability of companies established before and after IMF

Established	Number of companies	Net Profit / Asset	Net Profit / Sales	EBIT / Sales	Sales / Employee (US\$)
Before IMF	85	7.5%	4.8%	7.6%	884,293
After IMF	25	3.4%	0.4%	2.2%	1,411,713

Companies established before 1998 are slightly smaller, slightly less efficient in terms of labour productivity, with sales per employee just below 60% of sales per employee of those established post 1998. (This ratio remains the same whether we take the complete or adjusted sample.) However, old and established companies are much more profitable.

Table 5.1 shows that they have 3.45 times the EBIT and 12 times the net profit of those companies established earlier. Table 5.2 gives a further breakdown of measures of profitability by year of establishment.

Table 5.2. Sample by year of establishment

Established	Number of companies	Net Profit / Asset	Net Profit / Sales	EBIT / Sales	Sales / Employee (US\$)
1950 – 1959	2	7.5%	7.9%	7.5%	672,268
1960 – 1969	5	7.6%	5.7%	9.9%	1,028,554
1970 – 1979	10	18.7%	10.7%	14.7%	553,521
1980 – 1989	33	9.4%	5.6%	8.8%	667,177
1990 – 1997	35	2.4%	1.9%	4.0%	1,175,015
1998 – 1999	15	6.1%	3.1%	5.4%	1,492,554
2000 – 2003	10	-0.7%	-3.7%	-2.8%	1,290,452
Total (Average)	110	6.5%	3.8%	6.3%	1,004,161

The second factor is Size

Nineteen of the 35 companies founded in 1990-1997 had a 2003 sales volume of under 100 billion won. 5 of the 21 loss making companies were some of the smallest companies in Korea included in the sample. The tendency is that a small foreign company usually has too many specialist staff for its sales volume. This means that a high wage bill lowers operating profits.

The third factor is Sectoral

Table A.2. in the Appendix contains an analysis of companies by sector. The one sector which is clearly unprofitable is the pharmaceutical sector. In the sample of 11 pharmaceutical companies only one, Pfizer, was more profitable than its global company. Pharmaceutical companies represent 10% of the sample.

Because of the above reason of prevailing unprofitability across the entire sector, pharmaceutical industry was the mainly excluded category. This pattern of unprofitability is rooted in the nature of the industry. Pharmaceutical companies carry all their profit in the home country where the main costs of R&D in developing new drugs are accounted. Although the companies in Korea may have a mix of locally manufactured and imported products in their sales portfolio, the development cost is carried either in licensing fees or full import cost. This is not to say that this lower profitability pattern is not also attributable to Korean circumstances such as reimbursement issues, but the basic structure of pharmaceutical company subsidiaries is different from other sectors, and should be treated separately. The Korean Ministry of Health's attitude towards reimbursement fails to give adequate recognition to proprietary brands compared with generic drugs with lower efficacy. In general, Korea's level of reimbursement through the insurance system is lower than in other OECD countries, lowering profits below the global average.

Table 5.3. Summary of Pharmaceutical Companies

Global	Net profit / sales	Local	Net profit / sales
Pfizer	8.7%	Pfizer Pharmaceutical Korea Ltd.	15.0%
Johnson & Johnson	17.2%	Johnson & Johnson Korea Ltd.	8.5%
Johnson & Johnson	17.2%	Johnson & Johnson Medical Korea Ltd.	-2.4%
GlaxoSmithKline	21.0%	GlaxoSmithKline Korea	-1.1%
Novartis	20.2%	Novartis Korea Ltd.	2.1%
Roche Group	10.6%	Roche Korea Co., Ltd.	4.4%
Merck	30.4%	Merck Ltd.	8.0%
Aventis	10.7%	Aventis Pharma Co., Ltd.	0.8%
Astra Zeneca	16.1%	Astra Zeneca Korea Ltd.	-5.2%
Eli Lilly	20.4%	Lilly Korea Limited	9.1%
Abbott Laboratories	14.0%	Abbott Korea Ltd.	3.6%

No other sector had such a clear unprofitability. In every other sector where there were more than one company in the Fortune 500 classification, local companies were pretty evenly and randomly distributed to both higher and lower sides of their global companies' performance, indicating that there was no sector where a well structured company could not succeed. However, in most categories there were companies which performed well and companies which did not do so well. The Fortune 500 separates the four major foreign retailers that should belong to the same sector into three different classifications. Table 5.4 shows how three of the four performed well, and one, Wal-Mart, was one of the 21 loss makers.

The best way to show that a company has a structural problem is comparing it with its industry peers. But Carrefour, Tesco and Costco all make a profit. What is significant, as table 5.4 shows, is that sales per employee are significantly lower for Wal-Mart than the other three chain stores.

Table 5.4. Sales per Employee

Korean subsidiaries	Sales (US\$ mil.)	EBIT (US\$ mil)	Employee	Sales / Employee (US\$)	Global 500	Sales (US\$ mil.)	Employee	Sales / Employee (US\$)
Wal-Mart Korea Co Ltd	659.5	-11.3	3,800	173,565	Wal-Mart	258,681	1,500,000	172,454
Samsung Tesco Co., Ltd.	2,159.5	81.1	8,317	259,644	Tesco	51,372	230,680	222,698
Carrefour Korea, Ltd.	1,224.5	33.0	6,183	198,038	Carrefour	79,664	419,040	190,110
Wholesale Korea Costco	368.8	3.8	1,037	355,654	Costco Wholesale	48,107	103,000	467,058

However, on a global basis, Wal-Mart's sales per employee ratio is closely in line with the global average. But this global ratio is lower than that of its major competitors. It appears as though Wal-Mart is sticking to global guidelines which are not adequate to Korean conditions. Certainly, Wal-Mart Korea is not achieving the same level of productivity per employee as its foreign peers are achieving.

The fourth factor is Reliance on Sales and Distribution

Companies which are purely in sales, marketing and distribution and without manufacturing appear to be in a less profitable situation than those companies where local manufacturing is an important part of their sales portfolio. Of the 35 companies founded in 1990-1997, the cohort in which the profitability is lowest, 27 have no manufacturing or only limited manufacturing. The remaining 8 are service companies for which manufacturing is inappropriate. Of previous 27, five were losing money at EBIT level and are discussed below.

Pure sales and distribution companies are likely to have an element of allowable transfer pricing in that sales and distribution may be placed low in the product value chain. Once the effect of sales and distribution of imports is fully integrated into the entire value chain, the operation as a whole is profitable but the Korean segment is not.

The fifth factor is Insufficient Restructuring

The Korean market changes quickly and wages rise relatively fast. This means that a company must continually increase its productivity to match changing costs. Companies which cannot achieve this on a continuous basis must restructure at intervals. Several features of the nature of foreign invested companies may retard this process, particularly in companies which the full value chain is not exposed in Korea. These features may include changes in management, either too often or too infrequent, head or regional office inattention or inappropriate global strategies.

The sixth factor is a set of Random Factors

Each company may encounter special circumstances which are unique to the company but nonetheless affect its profitability.

Microsoft Korea

Unit: US\$ million, %

	Sales	Net Profit	Asset	EBIT	Technology fee / sales (%)
1999	130.2	35.7	81.6	43.3	28.1
2000	186.6	37.8	103.2	37.2	46.5
2001	180.3	9.5	77.3	2.5	61.1
2002	179.8	29.5	154.6	-20.5	64.3
2003	195.4	7.3	172.7	-9.1	57.0

Microsoft believes that the cost of making Korean language manuals and software cannot be recovered in the price of software sold. Another significant reason to explain Microsoft Korea's EBIT loss is its global parent's policy for taking away a part of Microsoft Korea's sales revenue in the name of "technology fee", thus effectively rendering Microsoft's subsidiaries to "rent" from its parent the technology and products on what seems much like a commission-based agency system. Where Microsoft Korea began to experience dramatic decline in EBIT in 2001, the ratio between this "technology fee" over sales was more than 60%. From there the company saw this ratio remain at such high percentage at 64.3% and 57.0% in 2002 and 2003 respectively, showing a big increase from the years prior to 2000.

Unilever Korea

Unit: US\$ million

	Sales	Net Profit	Asset	EBIT
2001	91.9	4.9	40.3	6.6
2002	130.2	4.8	61.0	5.9
2003	123.6	-5.8	53.6	-5.8

Unilever Korea's loss in terms of EBIT and net profit was largely due to the low domestic consumption rate in Korea in 2003. While the company's sales had increased by 42% in 2002, it slid down by 5.1% in 2003 due to Korea's economic downturn. In addition, Unilever Korea spent 10.7% more on advertising expenses in 2003, which amounted to

19.8 billion won or US\$ 16.6 million. Sales revenue dropped due to decline in unit sales prices of its products. More selling and administrative expenses were incurred by aggressive marketing strategies such as product bundling.

McDonald Korea

Unit: US\$ million				
	Sales	Net Profit	Asset	EBIT
2001	115.7	-4.7	142.7	6.0
2002	133.8	-12.1	163.4	1.6
2003	117.1	-17.7	153.6	-6.4

Depressed consumer spending as a result of general slowdown of the economy in 2003 coupled with the much fanaticized “well-being” movement for healthier life style to dramatically curb sales growth in the fast-food industry. Also, fast-food brands fiercely competed against each other in order to expand their markets, sometimes swallowing devastating losses. To make the matters worse, 2003 was plagued with the mad-cow diseases and the bird-flue along with many unfavorable trends like the “well-being” trend and the struggling economy as mentioned above, creating an industry-wide loss for the fast-food sector. McDonalds Korea increased its advertising expenses in 2003 by 25% from the previous year, but resulting sales revenue actually decreased by 12%.

Nestle Korea

Unit: US\$ million				
	Sales	Net Profit	Asset	EBIT
2001	173.6	12.0	85.5	17.7
2002	194.6	16.4	97.8	16.5
2003	176.9	-3.6	104.1	-1.1

Nestle Korea suffered through a long-stretched strike of 145 days. The company’s Chungju plant’s rate of operation was only 30% at the end of November 2003. The amount of coffee produced by the company drastically fell from 950 tons before the strike to 280 tons. Production of creamer, Nesquick and other products came to a halt, and the company had to resort to 100% import for these products to sell in the domestic market.

According to AC Neilson’s data, Nestle’s share in the coffee market fell to 30.7% by the end of September 2003, recording a 2.1% fall from a year ago.

5.5. Why do companies make a loss?

Twenty-two companies (including 3 pharmaceutical companies) or 21% made a loss in Korea in 2003 at EBIT. Actually making a loss at EBIT level is unusual, and indicates a life cycle or structural or managerial problem in the company. This can include such reasons as:

- Being in start up mode
- Running down the business
- Loading costs onto import prices
- Transfer pricing issues
- Product cycle issues

- Bad management strategy
- Inability to restructure due to the labour law
- Failure to adjust to Korean competition

Only if the cause of loss is attributable to the last two reasons is the loss germane to the unprofitability of investment in Korea debate.

The analysis of loss makers includes issues of size. Of the 21 companies making a loss, five were some of the smallest foreign companies in Korea included in the sample. Five more had issues relating to pricing in Korea relative to pricing globally and were importing rather than manufacturing. Three more were start up companies or restart up companies like GM-Daewoo, (though one of these might be regarded as a failure) and two had product life-cycle issues. The remaining six are problematic, the more so because they include the world famous names such as Unilever, Nestle, McDonald's licensee, GE, Sharp, and Wal-Mart, the world's largest company. On a separate note, the world's biggest software giant Microsoft was making a loss at EBIT but a profit at net income in this case, the loss at EBIT can be attributed to the cost of supporting the Korean language in windows and other products.

The causes for other major companies will be examined in more detail in the working paper, but these companies represent just 5.4% of the sample and may be failing for reasons closer to the common perception of Korea.

5.6. Conclusion

Profits are ultimately derived from the efficiency of the operation and its ability to adjust to changing circumstances. Companies which were able to export did well in 2003, and those that relied on the domestic market faced greater challenges. Some companies misjudged their opportunities for 2003. Others matched their structures to the market. There is the suspicion that the Korean environment delayed adjustment, but only 5.4% of the sample could be said to be suffering from the Korean disease as diagnosed in the first chapter.

The relationship between both the length of the operation and the six factors which are identified as impacting profitability and the performance of the company is important. The quality of management and the way management addresses these factors is also a significant part of the profitability equation.

As will be shown in the following chapters, manufacturing operations in Korea can be turned into very profitable parts of a global business. White-collar productivity tends to lag behind manufacturing, and while in the retail sector, operations which rely on high labour productivity, profits can be made, management needs to be highly responsive to achieve profitability.

Chapter 6 presents case studies where vigilant management has created profitable enterprises in Korea despite being faced by fairly unfavourable global or local circumstances or by head office resistance to increasing the size of Korean operations.

6. Case Studies in Profitability

Our case studies concern six companies that have achieved a high level of results in Korea. These include the second largest investor in Korea in terms of sales, a company currently excluded from our primary sequence but destined to enter the primary sequence when its start up phase is complete, an example of a restructured company which illustrates the flexibility which is possible in Korea, the Delphi company illustrating the potential for profitable partnership in Korea, 3M, and Fuji-Xerox.

In most of these case studies, alert managers took advantage of the financial crisis to restructure their operations for greater profitability. In all cases manufacturing in Korea increased.

6.1. Philips in Korea: Seizing Big Opportunities

Philips Korea represents a case where a vigilant and aggressive local manager was able to persuade global management that manufacturing in Korea was still a highly viable option. Through his action Korea accounts for about 15.1% of Philips global sales. The key issue is that manufacturing in Korea can become a global source for a multinational, as well as Korea becoming a major market.

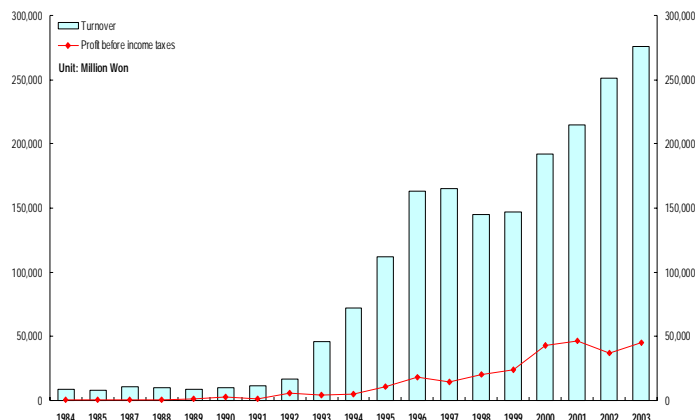
Philips illustrates the complexity of the study and at the same time how good management brings effective results for the company. Philips had a manufacturing venture in Korea in the 1980s which was an old style operation designed to exploit cheap labour. Profitability disappeared in the rapid rise of wages in the late 1980s and the operation was closed down in the early 1990s. Head Office management formed the opinion that there would never again be profitable manufacturing in Korea.

Sales in Korea takes four forms, direct by overseas divisions and not recorded as sales by Philips Korea or only included as commissions, import and sales by Philips Korea, manufacturing and sales by LG-Philips LCD and LG Philips-Display Devices. A further LG-Philips JV is based in Hong Kong but holds Korean assets.

This case study concerns the determination of the manager of Philips Korea to ensure that the group was fully represented in Korea. Consequently, a bigger share of Philip's sales emanates from Korea than that of any other company.

Mr. BJ Shin of Philips (1993 - to present) who is an outstandingly strong leader, BJ Shin transformed Philips Korea division by division. Stretch targets succeed in a sales company, and the CEO of the Korea operation must challenge each division's tendency to set easy targets. With this no nonsense "can-do" spirit from the top, Mr. Shin passed the 1997 sales goal set by the previous (expatriate) general manager in 1994, 18 months after assuming office. In 1994, 1995 and 1996 sales grew by nearly 50% per annum.

Diagram 6.1. Philips Korea (1984-2003)



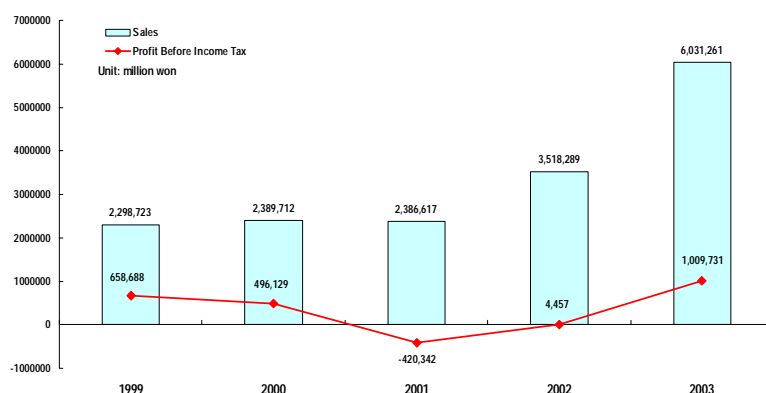
BJ Shin came with 17 years of experience in Philips Korea and had made it his business to understand all aspects of the company. This was often only achieved by changing the division manager, bringing in a “can-do” manager. Mr. BJ Shin’s essential view was that from the day he took over the rules should be No nonsense, the business comes first and a full days work for a full days pay. BJ Shin’s analysis was that Philips was full of under-performers who had set themselves easy targets under expatriate management and that those days were over. When meeting a “Can’t Do” mentality from his managers, Mr. Shin’s attitude was to first encourage and then if this failed - eject. Leadership counts, but creating a human resource system that survives successors is a more lasting creation.

When the IMF crisis began in Korea he immediately began lobbying for acquisitions and was rewarded by securing corporate attention for 2 massive strategic mergers with LG divisions.

LG. Philips LCD and LG.Philips Displays are successful joint ventures between Royal Philips and LG that almost instantly became leading global producers of Thin film LG. Transistor Liquid Crystal Displays (TFT-LCDs) and Cathode Ray Tubes (CRTs) respectively.

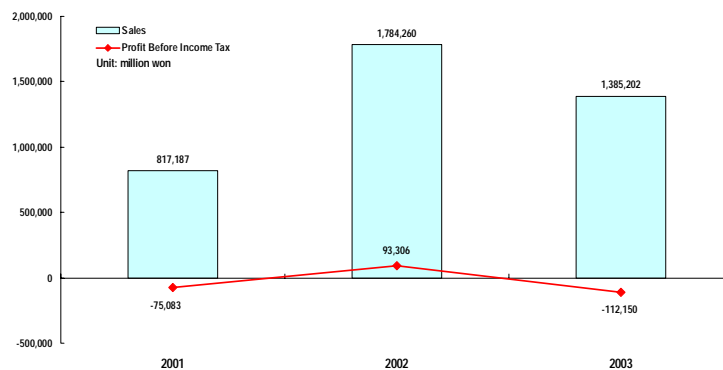
Philips LCD’s TFT-LCD technology is used in various flat screen applications such as wall-hanging TVs and computer and notebook monitors.

Diagram 6.2. LG Philips LCD



LG.Philips Display’s CRTs are used to produce Colour Picture Tubes (CPTs) for TV sets and Colour Display Terminals (CDTs) for computer monitors.

Diagram 6.3. LG Philips Display



These two companies success was brought about by adopting the strengths of Royal Philips and LG groups, coupled with efforts propelling themselves to be the leaders in their product categories.

LG. Philips LCD was created in 1999 has consistently broken many of industry's records. The company was the first to ship more than 1 million 15.1-inch TFT-LCD monitors in October 2000. It produced its 4-millionth 15.1-inch TFT-LCD monitor since the first shipment in 1997 in October 2001. In that same month, the company introduced 29-inch high definition television units, the largest of its kind. Also in 2001, the company produced 3.2 million LCD for monitors, setting an annual record for this segment as well. The company exports 95 percent of production to overseas to countries like Taiwan, China, and Japan.

LG.Philips Displays was created later in 2001. This was a merger of Philips and LG's TV divisions, partly in recognition that the product itself had a limited future life cycle, and therefore global consolidation made sense. The company has 34 factories around the world and records annual sales figures over \$5 billion. It is the world's largest supplier of television and monitor tubes, with two new factories in Mexico and Czech Republic. Today, one out of four televisions sets or computer monitors has a LG.Philips Displays tube inside. The company seeks to increase the rate to one out of three by 2005. While the company moves to adjust its existing industrial infrastructure to be more cost-efficient by shifting production to manufacturing facilities in low-cost countries, LG.Philips Displays remains very much committed to Korean market in the long-term.

As a result, Philips derives a larger proportion of its global sales from Korea than any other investor, except Fairchild Semiconductor.

6.2. ABB: Restructuring to Become a Global Hub

ABB Korea is an exemplary case that shows how a company can survive difficult times and capitalize on new opportunities to reinvent itself by efficiently pulling together its inner resources and quickly adapting itself to changes in the market.

The important issue here is whether subsidiaries can be merged in a way that makes the new company an efficient and highly profitable venture. Even in a traditional business like the manufacture of transformers, ABB Korea could become a centre of regional excellence exporting to China and other Asian markets with much lower wage costs while attaining one of the highest contributions to global profitability. ABB Korea today ranks close to the top as a profit generator within the ABB group.

ABB, a leader in power and automation technologies, entered the Korean market in 1987. Ten years later, ABB Korea became a major contributor to Korea's nuclear and thermal power program.

By 1997, just before the Asian financial crisis, ABB Korea in the South had led two projects to design and build the Ulchin and Youngkwang nuclear reactors and had also built the Poryuon thermal power plant. At the same time, it was operating three joint ventures – at Chonan, Suwon and Busan – and owned a subsidiary at Chungju, producing a variety of power generation and automation equipment.

Upon facing the financial crisis of late 1997, ABB Korea merged its four separate manufacturing operations into one, moving all of its activities to the Chonan factory completed in 1998. It bought out its three joint venture partners to create the much-needed synergy and solidarity within the company to survive the difficult times. Although this consolidation required trimming of a portion of its workforce, the management kept its most seasoned workers for a successful start at the new plant.

Such move indeed led to bring about another major change; ABB globally divested itself totally of its nuclear and thermal power generating businesses, thus focusing its structure on its Power Technology division and Automation Technology division. The logic behind this re-structuring was the strategic observation that when they were focused on power generation solutions, most of their business was commission-based (because they did not produce any products), therefore providing them with very little corporate stability to survive the difficult times. The result of that change is a dramatic increase in its client base, going from Korea Electric Power Co. as its sole client in the past, to a diverse group of clients, including POSCO, cement, paper and automakers.

The development of Chonan plant also enhanced the company's commitment to Korea by giving the company a direct responsibility of 350 employees. In addition, implementation of localized management in appointing Mr. Yunsok Han as the CEO raised enthusiasm and career ambition of the staff, giving them hopes for top jobs and open opportunities.

People and teamwork are the key words to describe ABB Korea's growth achievement. In order to achieve a strong sense of community, the company took two-pronged approach: one from the systematic point of view and other from the humanistic point of view.

First, the company sets its annual financial goal at the start of each year, and shares its up-to-date financial and management status with the workers twice a year. In addition, the company has in place merit-based compensation system that encourages employee contribution for the company's growth. The compensation amounts to 23% of the company's total salary expense, and is never forfeited even if the company as a whole makes a loss for the year because the reward is measured and handed out according to each division's performance.

Secondly, it has a great employee welfare system that easily allows various clubs to be formed. Employees actively participate in those clubs, playing sports or doing other various activities together, building close relationships and boosting their morale. The company subsidizes almost 50% of the budget for those clubs. The management devotes itself in maintaining excellent labour relations. Mr. Han visits the Chonan plant four days out of a week, and almost everyday that he is there, he plays tennis with the tennis club and goes out to eat and drink with the workers afterwards. The management is much more sensitive to the concerns of the union compared to other companies, and helps the two parties to cooperate better on projects. So the generous investment and socializing efforts earn invaluable returns in procuring higher labour-efficiency that leads to greater output.

In recent years, ABB Korea captured about 21% of the domestic transformer market worth 60 billion won. Its rapid growth was accomplished effectively in just three years after its major restructuring. It employs one of the largest technical sales forces fielded by a foreign company in Korea.

Diagram 6.4. ABB Korea

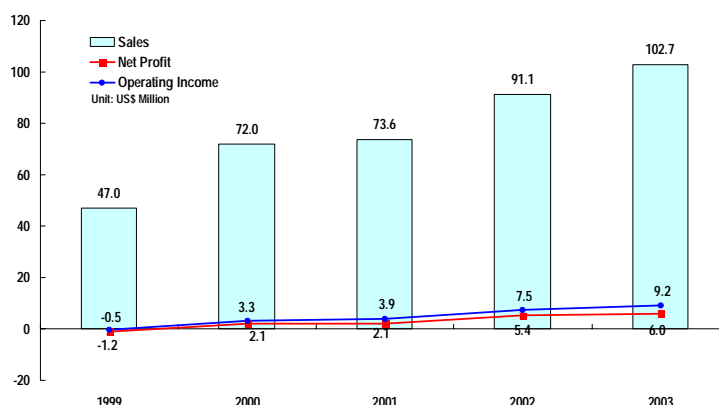


ABB Korea accomplished 5 consecutive-year growth at the average rate of 25% per annum in both sales and net profit. Export record for 2004 is expected to cap around \$20 million by the end of the year. The company plays a critical role in providing electrical power facility and automation equipment for ABB branches in ten countries in Asia Pacific region, on top of effectively functioning as the global production headquarter for small and medium sized transistors.

Collectively, the keys to success that delivered above results were its quick and appropriate reaction to the economic conditions and changes, strategic corporate decision to redirect its focus, local commitment to Korea, and lastly the management's dedication to foster healthy labour relations.

6.3. Delphi: Surviving the Asian Crisis and Becoming a Regional Hub

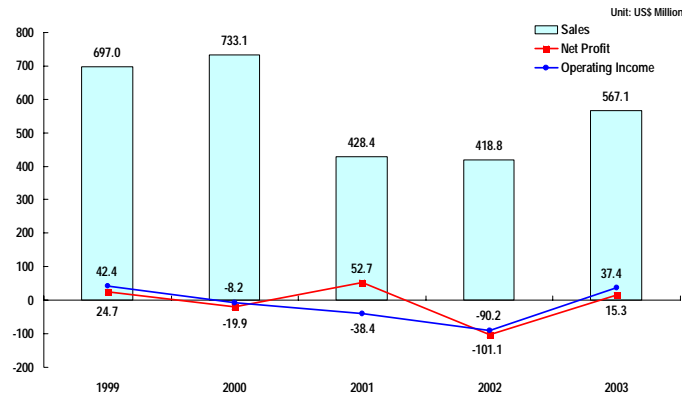
Delphi represents the successful case of increasing profitability on a reduced income. Delphi in 2004 grew by 15%, and expects to grow by the same factor in 2005. It represents 40.7% of Delphi's sales in the region, and Delphi has recently created two research centres.

Delphi Korea was established in 1984 as a joint venture between General Motors Corporation, Daewoo Motors, and some other divisions of the Daewoo Group. Delphi Automotive System, Inc. was spun off from the GM group in 1999 and thus became the part owner of Delphi Korea. With a rapidly developing Korean auto market, six joint venture subsidiaries of Delphi Korea – Korea Delphi Automotive Systems Co. Ltd (KDAC), Delkor Corp., Shin Sung Packard Co. Ltd., KDS Co. Ltd., Daesung Electric Co. Ltd., Delphi Diesel Systems Korea Ltd. – were inaugurated. In addition, a wholly owned subsidiary, Delphi Sungwoo Corp., was launched in 2000.

KDAC is the Delphi group's largest presence in the Asia/Pacific region. In 1999, KDAC peaked as the Korea automotive industry's biggest-earning company, selling almost 50 percent more than the second-ranking company.

In 2002, Delphi Korea saw a sound return on its investments (\$850 million in total revenue out of accumulated investment of \$250 million), a success to which KDAC was one of the biggest contributors.

Diagram 6.5. Delphi Korea



Delphi was caught by the collapse of Daewoo Motors to which it was a major supplier. But the company was able to restructure to produce a higher profit on lower sales as shown in 2003.

Korea Delphi's strategy for success is to carefully observe the market trend to "catch the wave" in a timely fashion while focusing on securing diverse client base and staying close to the clients' needs. The company supplies to OEMs across the board in Korea's automotive industry – including GM-Daewoo, Hyundai/Kia, Ssangyong, Renault Samsung, Fiat, and Mitsubishi, as a "cheabol-neutral" supplier." Korea today as the world's fifth largest carmaker must stay ahead.

From the beginning, Delphi's Asia/Pacific division focused on hiring and training Korean engineers to foster significant engineering and technology transfers as part of the Delphi group's global investment strategy. But Delphi Korea is no longer at a mere receiving end but develops its own technology and in some cases exports them to other Delphi locations around the world.

Delphi Korea's latest focus rests on helping automakers reduce lead times in getting new models to market, especially in meeting the increasing demand and popularity of Sports Utility Vehicles (SUVs). The company provides its clients with common rail fuel injection (CRFI) system, which allow the OEMs to produce diesel-engines that meets the increasingly tougher emission standards worldwide. This CRFI system enables Delphi Korea to put itself in an excellent position for both upcoming domestic SUV market and a wider export market in Europe and other part of the world. The domestic market is scheduled to open up once allowed by the government in 2005.

Delphi Corp. has opened its second Korean technical center in Yongin, Kyonggi province in July 2004. This new center was created by \$20 million in investment and became the home of 240 engineers and 40 support personnel. The center will focus on developing gasoline and diesel engine management systems for its customers. Its first technical center is located in Munmak, Kangwon Province. Together the centers will be funded by 4% of sales annually, as is the company's policy to stay competitive and at the frontier of new technology.

Delphi Corp.'s CEO, J.T. Battenberg III, visited Korea for the inauguration of the center. He showed optimism and enthusiasm for the Korean auto parts market by saying that it will achieve 15-20% growth by the end of the year, with similar growth prospect for the following year. It is unusual to establish two technical centres in the same country, as one per country is the norm for the rest of the Asia-Pacific region. Battenberg explained that it was due to Korea's significant contribution to the region's total sales last year – amounting to \$1.1 billion out of \$2.7 billion, – as well as the presence of highly talented Korean engineers. With the growing trend of Korean companies entering the Chinese market, he said it was a very appropriate decision increase Korea's research and development capacity. Delphi will continue to maintain its high product quality while aptly responding to the growing market pressure to lower cost through adapting the "lean-production method," a cost-efficient method used by Toyota. Delphi Korea recorded around 840 billion won (\$800 million) in sales in 2004 with expected record to exceed 1 trillion won (\$953 million) the next year.

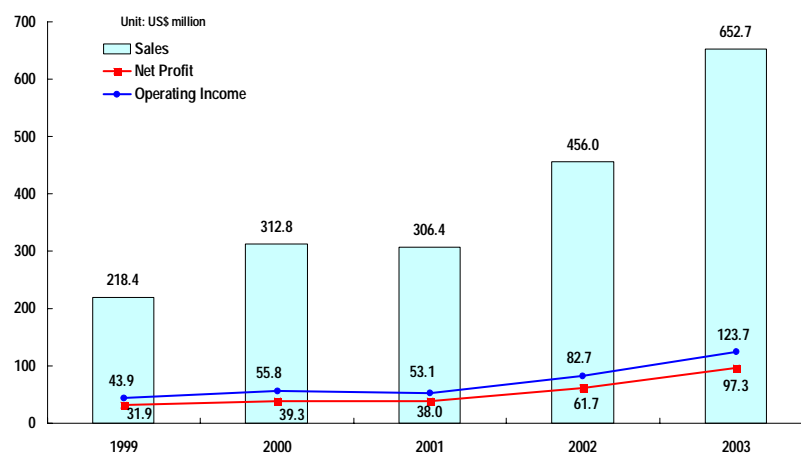
Delphi Korea's deep and strong relationship with its diverse client base and its relentless efforts to respond to new market trends in providing value-solutions allowed Delphi Korea to grow into a formidable presence in the Korean automotive industry. Delphi was one of the few companies in Korea to move from loss in 2002 to profit in 2003, a profit that reached above global average.

6.4. 3M : Dedication to Excellence and Using Korean Manufacturing Expertise

3M is an example of a company handling a large number of complex lines and attaining the seventh largest turnover amongst 3M's 37 manufacturing ventures. 3M Korea currently ranks high as a money-maker within its parent company, placing in seventh out of 3M's 37 manufacturing ventures worldwide in the operation's turnover in 2001.

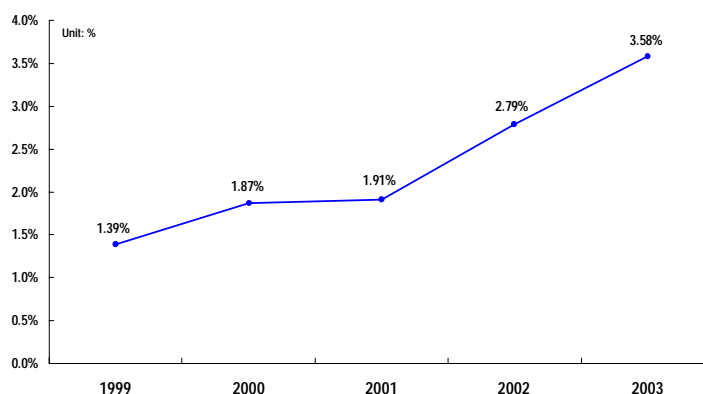
3M Korea was founded in 1977, at a time in which it was still rare to find a foreign subsidiary company in Korea. 3M partnered with the Doosan group in a 60/40 venture.

Diagram 6.6. 3M Korea Sales



In recent years, the company has seen a great growth in sales since Korea's strong recovery from the financial crises and burgeoning Brightness Enhancement Film (BEF) demand from Korea's world-class TFT-LCD manufacturers.

Diagram 6.7. Sales Ratio (Local to Global)



3M Korea's 2004 initial yearly sales target was 948 billion won (\$903.8 million), but the current prospects indicate that it will comfortably surpass that target, reaching 1 trillion won in sales revenue, according to internal opinion. 2003 sales was 780 billion won (\$743.1 million), so the 2004 growth is expected to be roughly in between 25% and 28% of the previous year. Also, within that 2003 result, 7.5% came from products developed in Suwon research center. The company draws nearly 50% of its sales revenue from Brightness Enhancement Film (BEF) – used for LCDs, Plasma Display Panels (PDP) – used for PDP TVs, and Thin Film Transistor Liquid Crystal Display (TFT-LCD) – used for cell-phone and TV monitors.

3M Korea's major clients are Samsung Electronics and many other big-name display manufacturers. The company is well aware of the fact that its growth is contingent upon the growth of these client companies. Therefore, it strives to ensure its clients' success not only by catering for their exact current needs but by "thinking-ahead," meaning it analyses the future industry prospects for its clients, providing anticipatory solutions.

3M Korea's profitability is a product of its localization policy. It manufactures locally, operating under the in-house cost centre system rather than importing its products from abroad. The company also promotes localizing its management, recognizing the fact that the people who know the Korean market should be the ones to who manage the company. The management implements a balanced mix of western and local styles of management, supporting both the performance-based remuneration system and the Korean style of revered title system. 3M Korea furthered its local commitment when it converted its Suwon plant into a technology centre to redesign and modify their existing products to suit the local market, as well as giving technical support to its customers.

The company tops its effectiveness at having a very systematic and meticulous internal organization. Sales, marketing and profit management for the company's 20,000 products is handled by six major business departments, each one responsible for three to five product categories. There are thousands of products in each category, all grouped according to similarities in characteristics. A total of 35 divisions, each with its own business manager, marketing manager and sales team, handle a range of several hundred similarly grouped products.

After 25 years of operation, the company still has no union, showing off a high degree of harmony the company has managed to achieve. In place of a union the company holds regular quarterly meetings with its employees to gather opinions and receive requests. However, pay is said to be not discussed at these meetings because the company's human resource department in anticipatory manner surveys salaries at peer companies and decides what remuneration to offer. The company pays within the top-third range of salaries, keeping its employees generally very content.

3M promotes profit-driven innovation policy that directs all of its branches and subsidiaries that sales of new, higher margin products released within the past four years must make up 30 percent of total sales. 3M Korea far surpasses this requirement since 68 percent of its total sales are made up of the products released within the past four years. This profit-driven innovation policy allowed 3M Korea to always be alert at the presence of a good new opportunity, which was the rise of demand for BEF to be used for backlight panels. 3M Korea took opportune actions by expanding its Naju plant to increase production and by introducing the Asian Display Center within the Suwon Technology Centre to provide technical support and aid product innovation for customers throughout Japan, Korea and China.

Earlier in the year 2004, 3M had projected total of 50 billion won (\$47.7 million) in direct investment to Korea. 40% of this budget is planned to be vested in the expansion of research and development facilities. This physical facility expansion is coupled with staff expansion plan to 200 employees from current 100 employees in a 3-year span. The company also announced plans for hiring about 140 new employees across the entire company for this year alone. CEO Joaquin Delgado is confident that 3M Korea will be able to grow 3-4 times in the Korean market in the near future.

6.5. Fuji Xerox: Overcoming Union Opposition and Using Korean Strengths to Exploit the Regional Opportunity

Fuji Xerox is an example of a company in which relations with labour unions played a major role, but which, through good management was turned from a loss making subsidiary into one of the most profitable within Fuji-Xerox's operations.

Fuji Xerox Korea was launched in 1991 (then named Korea Xerox) as joint venture between Korean company Donwha Sanup and Fuji Xerox. Following the financial crisis of the late 1997, Fuji Xerox Korea has been led by Nobuya Takasugi, who handled the labour-union issue and engendered a strong relationship between the management and the union.

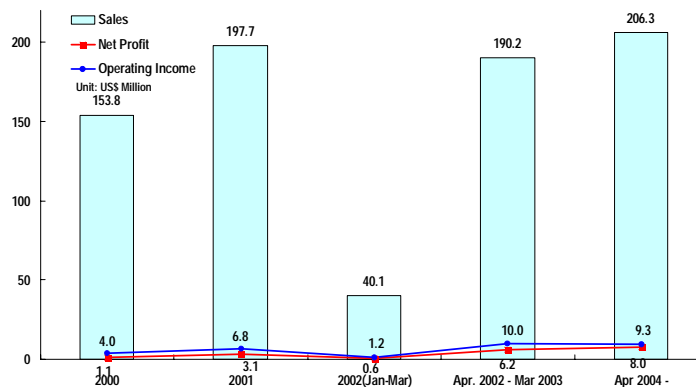
Nobuya Takasugi improved the company's return on assets from minus 3.0 percent in 1998 to 7.0 percent in 2002 and to 7.7 percent in 2003.

As soon as Takasugi took over the company in 1998, he was immediately faced with the problem of having to handle the losses. When he told the union that the company could not pay their annual bonus, union workers threatened to strike. Takasugi tried to borrow money from the bank but the company had no credit. He then asked the union to wait for one or two months, and eventually paid out all bonuses. From that point on, Takasugi began to build credibility with the union.

He then moved quickly to cement his credibility by laying out a number of initiatives that greatly improved the transparency and two-way communication with the union. They include a quarterly video presentation that he makes in which he discusses company performance and events; a quarterly workshop between directors and departmental heads; "Talk Plaza," a meeting twice a year with the company's line workers; plus visits to line workers where he and the workers sit down and eat and drink together. He earned a nickname of the "Sam-gyop-sal"(a traditional Korean meat) chairman because that is something no top Korean manager would normally do.

His enormous success with the union was apparent when the union settled without negotiation in 2001, stating that they felt that they and the management had already talked enough on the subject anyway through informal channels and meetings.

Diagram 6.8. Fuji Xerox Sales



(In 2002, Fuji Xerox adjusted its accounting period to begin in April. The column in the middle represents the 3-month gap in shifting the accounting period.)

Along with such effective leadership and much dedication to ensure customer satisfaction and top product quality, Fuji Xerox became a true leader in improving office environment efficiency. It was the first company to implement an office equipment lease system in Korea, and is fully committed in providing premium quality customer service and close monitoring of products.

The company has been given numerous awards for its excellence, a testament of the company's premium brand status and achievement. The company received the "Excellence in Fostering Healthy Labour-Relations Culture" award in 2001, becoming the first foreign company to be given this award. In that same year, the company was chosen as the "Fair and Ethical Foreign Company of the Year" by the Association for the Commercial Fairness and Ethical Practice. Then in 2004, the company was acknowledged for implementing and practicing environment-friendly management system, and thus qualified for ISO 14001 certification given by the International Organization for Standardization and also received an award of excellence by the Minister of Department of Commercial Resources. Lastly, Fuji Xerox was chosen as the number one company by the Association for Product Efficiency for 3 consecutive years in the customer satisfaction category.

6.6. GM Daewoo: Using Acquisition to Create a Regional Presence

GM-Daewoo is one of the companies which is excluded from the primary series because in 2003 it made a loss at EBIT level. This case study shows how GM-Daewoo expects to become profitable in 2004, and to exceed GM's global profitability thereafter as the core production units become a major strategic manufacturing base.

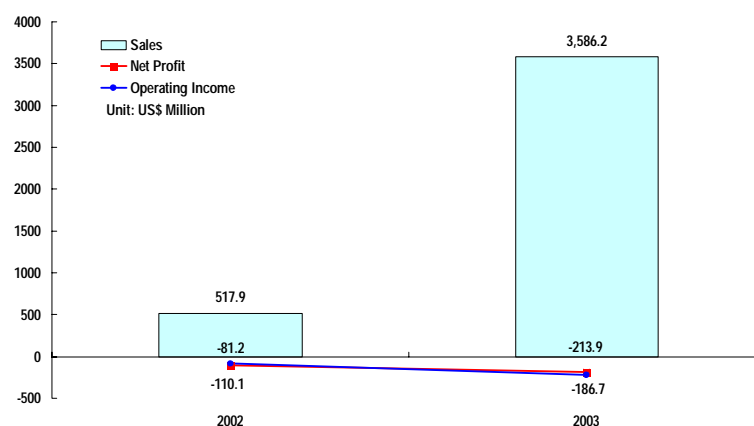
After two years of struggle, Daewoo announced its bankruptcy, General Motor's successful take over of the troubled company in 2000 allowed Daewoo to reinvent itself as GM-Daewoo and to pull off a strong comeback.

In November 2001, GM and Daewoo finalized their negotiations. The terms stated that GM and its allied companies together with the creditors will invest \$400 million and \$197 million, respectively, and that Daewoo's Changwon and Kunsan plant will remain in the company but Bupyeong facility will not. Also, the agreement announced that the most of existing Daewoo management team will remain. GM brought in Nick Reilly as the new CEO to lead the newly formed company to embark on its new business adventure.

GM acquired Daewoo despite its substantial operating losses and debts at the time because it wanted to increase its presence in Asia/Pacific region in general and saw in Daewoo a strategic potential to carry out their vision.

GM's risk-taking paid off in just 2 years. By 2003, GM-Daewoo showed a remarkable growth in sales, displaying sales figure that is 7 times higher than that of 2002.

Diagram 6.9. GM Daewoo Sales



GM-Daewoo is now becoming a strategic manufacturing base for GM's Asia/Pacific market. In some cases where countries like China or Thailand puts high tariffs on imported cars, the company tackles the situation by licensing the local GM businesses to produce the product and supplying them with parts instead.

GM Daewoo rose to the top in export ranking among the GM group companies, showing fast growth and emerging as a strong player in the group. GM Daewoo exported 561,946 units by the end of third quarter of 2004, which is 108% rise from the same period in the previous year and 183% rise from the year before that. In terms of export distribution channels, its client countries increased to 140 countries in North America, Europe and other areas of the world, boosting the company's status as the strategic technology base in Asia for the GM group within just 2 years. The projected export quantity for 2005 is 900,000 units. The company's aggressive marketing bore fruitful results in pushing its market share up almost 3% from 20.9% upon launch in 2002 to 23.8% by September 2004.

The company is currently concentrating on research and development of new models, totalling in 5 models introduced to the market thus far. GM Daewoo is putting in efforts to strengthen its presence in small and compact car market as well. It built a factory in Changwon to produce engines of wider size range. In addition, GM-Daewoo showed a big increase in its scale of employment by 50% by hiring 2800 new employees.

GM Daewoo announced a large investment plan of about 1,740 billion won (\$1,654 million) last March for future product development for the next 2-3 years. This is the biggest investment announcement in the entire GM group history. The specifics of the budget includes: SUV development, full-size car development, capitalization expenditure for Bupyeong plant's manufacturing equipment, new compact-car model development, and technology development for acquisition of Daewoo Power Train. This investment plan effectively declared GM-Daewoo's intention to be the top car-maker in the Korean market.

6.7. Conclusion

What these six case studies have in common is that they each achieve high profitability based on a manufacturing base and tough management determined to make a success of restructuring. Union problems did not prove an insoluble problem to achieve a high return on assets even in the case of Fuji-Xerox although unions are reputed to take a tougher line against Japanese investors than western investors.

No structural inflexibility prevented ABB from merging its four ventures in Korea with very different backgrounds and salary systems into a single venture which became a centre of regional excellence and global profitability.

GM-Daewoo and Delphi have been able to restructure their operations to create a new level of profitability, both using Korean competences to drive their activity in the region. 3M Korea has also driven up its global share of sales by 275% in the period between 1999 and 2003, also capitalising on Korean competences.

A similar story of good management and relentless restructuring could be told for all the successful companies in the sample.

7. Profitability of investment in Korea versus China and Japan

7.1. Regional Importance

In terms of regional importance, Korean investments have only increased their market share from 11.4% to 12.5% in the period studies – 9.6% over two years. The region's growth as a total share of Asia Pacific's sales to global sales rose 6.6% in the same period. This means that for the multinationals in the sample, Asian business is growing only slightly faster than their overall business. Korea is growing 50% faster than Asia as a whole.

Given the rise of multinationals' China business, Korea's rate of growth is still significant, and means that Korea and China are taking market share from other markets in Asia as they increase their share of global sales.

Table 7.1. Ratio of Korean Sales to Regional Sales

	Korea / Region	Region / Global
2001	11.4	12.0
2002	11.7	12.2
2003	12.5	12.8

While Korea is growing faster than the region, the region is growing faster than the rest of the world.

7.2. Why invest in Korea rather than China?

Foreign investment in the past has been a case of investing in each national market, with the growth of Free Trade Areas (FTA) and reduction of trade barriers since the creation of the WTO (World Trade Organisation), the rationale for the replication of ventures in each country is fading. Still investment in Korea is required to access the Korean market, and companies continue to invest in Korea to manufacture for export, especially to China which consumes nearly half of the production put out by a number of major foreign companies based in Korea, including Samsung-BP and Samsung-Total. As noted in the case studies, companies investing in manufacturing capacity in Korea continue to derive above average profits from these operations.

Foreign invested companies are growing their business in Korea faster than elsewhere in Asia. Asia has risen as a global share of sales multinationals sales by 6.6% over the last two years from a low base.

Although the return on assets in Korea is high, how does Korea compare directly with China when it comes to profitability? The American Chamber of Commerce in Beijing and Shanghai makes an annual survey on the same basis as our main line of analysis, based around margins above or below the global average. Table 7.2 shows the results.

Table 7.2. 2004 American Chamber of Commerce profitability survey responses

From Darkness to light	1999	2002	2003
Proportion of companies reporting margins higher than world wide average	13	42	42
Proportion of companies reporting margins on par with world wide average	29	29	31
Proportion of companies reporting margins lower than world wide average	58	29	27
That dream took a long time getting here...			
Proportion of companies in China five or fewer years that are profitable			57
Proportion of companies in China six or more years that are profitable			81
In profits, services suck			
Proportion of manufacturing businesses that are profitable			80
Proportion of service businesses that are profitable			62

* Includes responses from both the Beijing-based American Chamber of Commerce – China and the American Chamber of Commerce – Shanghai

Source: China Economic Quarterly Q4 2004

These are compared in table 7.3 with the equivalent results in Korea (although the Korean sample is for all investors and not merely American companies).

Table 7.3. Comparison of Korea and China

	2002		2003	
	Korea	China	Korea	China
Proportion of companies reporting margins higher than world wide average	54%	42%	44%	42%
Proportion of companies reporting margins on par with world wide average	5%	29%	9%	31%
Proportion of companies reporting margins lower than world wide average	42%	29%	47%	27%

Source: CEQ, KABC

Although Korea has a higher percentage of companies with above average operating margins than China, it also has a higher percentage of lower than average operating margins than China. Foreign companies in China have a suspiciously high number of companies with an average margin.

It is not easy to make direct comparisons of overall profitability, although some interesting inferences can be made. China is currently attracting 10 to 11 times the amount of capital that Korea attracts per annum according to UNCTAD, and has 38,581 foreign invested manufacturing businesses according to the Chinese National Bureau of Statistics. The Bureau does not record non-manufacturing businesses, but China is estimated to have approximately five times the number of foreign invested enterprises that are present in Korea.

The Bureau of Economic Analysis records the profits of American corporations from each country which the *China Economic Quarterly* interprets as follows:

Table 7.4. Total profit by country
Asian Top Ten: US equity claims on earnings from affiliates in Asia, 2003

	Country	US\$ million
1	Japan	9,167
2	Singapore	6,974
3	China (adjusted)	4,399
4	Australia	3,707
5	Hong Kong (adjusted)	3,043
6	Malaysia	1,947
7	Indonesia	1,283
8	Taiwan	1,274
9	South Korea	1,252
10	Thailand	1,142
Regional Total		35,546

Sources: Bureau of Economic Analysis, CEQ estimates

The profit from Korea is approximately 28% of that of the Chinese figures for 2003, against 10% or less of the assets suggesting that overall return on assets is higher in Korea.

On the basis of this data, Korea has been clearly more profitable than China up to the present time, but the potential for those companies with margins on par with worldwide average in China to move into higher than the average profits persists. If Korea currently has more success stories than China, it also has more under performance stories.

Commentators on China such as the *China Economic Quarterly* remain skeptical of China's inherent profitability. It is noted that five US corporations are responsible for one third of all profit in China, and the addition of three more would probably bring the total to half of all the profit. If return on assets were taken as a measure, the *China Economic Quarterly* suspects that "players which cannot afford to waste cash, earn more consistent returns than big companies that squander money."

Most recent foreign investments in Korea have had half an eye on China. As noted in chapters 5 and 6 Korea's manufacturing efficiency is outstanding. This makes the use of manufacturing assets in Korea extremely attractive both to supply the local market, and the Chinese market. The example of the largest investment of 2003 illustrates this point.

Total (Atofina) buys Samsung Petrochemical

The largest foreign investment of 2002 was in manufacturing, and was the acquisition of 50% of Samsung Petrochemical, one of the most modern petrochemical complexes in Korea. Total's reason for buying was strongly linked to the need for petrochemicals in China (and 50% of the acquisitions sales are exported to China.)

Atofina has recently renamed itself as Arkema (www.arkemagroup.com). Arkema announced plans to double sales in Asia to EUR 500m by 2010, indicating that most of its sales should come from new production facilities. Korea is one of the key sites from which Arkema aims feed supplies to generate their increase in sales, banking on the joint venture with Samsung. Samsung-Atofina has also renamed itself to Samsung Total, and it aims to develop its plant in Daesan, South Chungcheong Province, into a global name in three years by devoting itself to putting more focus on research and development. For Arkema group, investing in Korea serves as a strategic move to secure a manufacturing base as well as establishing a firm market position in the region, which is demonstrating a rapid growth in demand for petrochemicals in recent years.

The best example to support the argument that producing in Korea makes sense to serve the Chinese market is that of Chinese firms themselves. Sinochem bought Inchon Oil in 2004, and Shanghai Auto Works has almost completed the purchase of Ssangyong Motors. If the future of manufacturing really lies in China, why would Chinese companies buy existing capacity in Korea?

Some Koreans suspect that the Chinese are really seeking to purchase technology. But in the case of Inchon Oil, there is no special technology. It is a very run of the mill oil refinery. The answer is simply that manufacturing in Korea is managed extremely efficiently, and any asset operated by Koreans will bring a good return. Secondly there is a continuing shortage of manufacturing capacity in China, and this is likely to continue into the foreseeable future.

Sinochem buys Incheon Oil

Sinochem, China's largest importer of petroleum, invested US\$500 million in Incheon Oil in 2004. The purpose was simple – to export petroleum products to China, as it hopes to get a slice of the lucrative domestic market from giants PetroChina and China Petroleum & Chemical Corp (Sinopec). According to a source from one of Sinochem's subsidiaries, Sinochem's initial plan is to sell refined oil products to South Korea's domestic market, but there are also plans to sell to China, Asia and other international markets.

With no domestic refineries of its own and the mainland government's reluctance to approve any more new greenfield projects, the state trader plans to turn Incheon into its refining base for the China market in the future, with the possibility of importing oil to booming eastern cities such as Shanghai, Shenzhen and Guangzhou.

There remains a fear amongst investors that Chinese companies will in the end swamp some product markets, notably the commodity markets. But the rising interest of Chinese companies in investing in Korea indicates that it is more likely that Korean based companies, whether foreign or domestically owned, will be drawn into the greater Chinese economy, rather merely being outclassed by Chinese companies.

The Japanese also believe that investing in manufacturing in Korea makes sense. Japanese investment into Korea increased 300% in 2004 by the end of October. The investment was in a wide range of manufacturing and represented both a recognition of the value of Korean plant and prepositioning for the expected Free Trade Agreement (FTA) which is to be signed between Korea and Japan in 2005. This agreement is likely to further boost the movement of manufacturing from Japan to Korea. Renault-Nissan has already planned to substantially increase investment in their Busan plant, reducing capacity in Japan.

Renault-Nissan moves production out of Japan

On November 29th 2004, the CEO and Chairman of the Renault Group announced that over the next three years, Renault would invest US\$570 million to set up an engine plant, extend production lines and other infrastructure, in order to make South Korea a base for exports to the European market and other parts of the world, especially to the emerging Asian markets. Production capacity is to be raised from 300,000 to 500,000 vehicles, half of which will be exported by 2010.

The latest vehicle is again based on a Nissan design, the high end Tiania and a Renault engine. The expansion will both move production of engines from both Japan and France, and this make Samsung-Renault the leading exporter of Nissan-Renault's high end cars, taking a model which would need production capacity expansion in Japan if world markets were to be served from Japan.

Asked at a press conference to compare production in Japan and S.Korea, the chairman declined to answer the question stating, "I don't want to be unkind to my friends in Japan."

Likewise, in terms of actual production, Fuji Xerox Korea, mostly producing peripheral equipment, has to battle on two sides of production performance - competing with China for lower production costs in China and competing with Japan for better research and development (R&D) skills. However, it can turn the table around to its advantage, since Korea has better R&D skills than China and lower production costs than Japan. So the

company is gearing up to equip itself for the dual capacity of both quality R&D and low cost production to consolidate its place in the Fuji Xerox group as a quality production base. Fuji Xerox Korea's estimated export record for 2004 is 130.8 billion won (\$125 million), showing 125% increase from the last year's record.

Table 7.5. Operating profit in 2003 and outlook for operating income in 2004

	Operating profit in 2003			Outlook for 2004		
	Profit	Balance	Loss	Will improve	No change	Will be worse
Average	79.6	4.4	16.0	49.8	30.8	19.4
Korea	84.2	-	15.8	55.3	18.4	26.3
Taiwan	90.4	4.1	5.5	29.6	46.5	23.9
Hong Kong	89.7	2.9	7.4	43.1	40.0	16.9
China	74.4	5.4	20.3	55.2	26.8	18.0
ASEAN	70.9	10.3	18.7	49.0	34.4	16.7

Source: Japan External Trade Organization

According to an annual survey of Japanese-affiliated manufacturers in Northeast Asia conducted by Japan External Trade Organization (JETRO)'s in 2004, 84.2% of respondents in Korea achieved an operating profit in 2003, while 74.4% of respondents in China and 79.6% of total respondents posted operating profit.

Regarding the outlook for 2004, the percentage of replies of "will improve" was higher in Korea than in China or the average.

The profitability of service operations is not so clear. In manufacturing, Korean techniques are hyper-effective. In white-collar jobs and some service areas, foreign managers feel that practices have not been fully modernised and wages are relatively high considering the actual productivity of the employees. Sales and distribution operations which have little or no manufacturing associated with them appear to be less profitable than their global parent. The five-day week is suspected to add to this problem.

In conclusion foreign investment in manufacturing in Korea is likely to continue for the foreseeable future.

7.3. Conclusion: Manufacturing in Korea makes sense

The conclusion that Fuji-Xerox came to is essentially one which many multinationals with direct experience in Korea have reached. Production in Korea is considerably lower in cost than Japan, and is also of higher quality than in China at present. At least one foreign company, Diageo, the world's largest producer of alcoholic drinks, is even restarting simple operations like bottling bulk products in Korea because of the high productivity of the operation and the fact that only in Korea can it achieve the quality which the Japanese market demands at a reasonable price.

R&D is much more sophisticated in Korea than China and surprisingly often lower in cost, since the required skill levels in Korea are in abundant supply but in short supply in China.

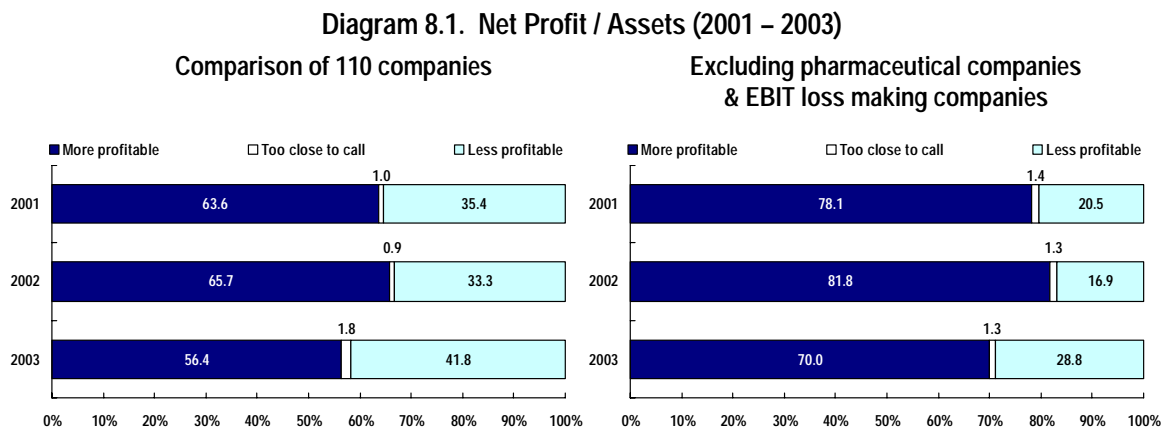
In this respect, while some consultants predicted that Korea would be caught between Japan and China in a nutcracker effect, in practice, multinationals identify Korea as the

place to put research centres and production process that require sophistication or exceptional quality.

8. Conclusion

At the outset of the report it was stated that if a large number of foreign companies can be demonstrated to be making above average profits in Korea, and if we can find consistent internal reasons why the majority of lower than average profitability companies make less money, then the perception is demonstrably false, and we can conclude that well managed companies with healthy structures can be highly profitable in Korea.

It would be surprising if all foreign invested enterprises in Korea were more profitable than their parent organizations when we are measuring only part of a multinational's activity in Korea as explained in chapter 3.



That a majority of companies are making more or equal profit is an important conclusion. It is a matter of concern that about 33.3% of companies were making a lower profit or an actual loss even in a favourable year like 2002. But as the examination of the companies making a loss at EBIT level showed, there are generally structural and company life cycle reasons why this is so.

Most importantly, if companies are losing money in Korea, for the majority it is not the result of low productivity per worker. Rather, productivity per worker is high, and if multinational companies could reach the sales per worker of their Korean subsidiaries they would be very profitable indeed.

The basic conclusion is that majority of companies of all sizes can and do make significantly higher profit in Korea than their global average. However as in all businesses, not all companies succeed, and those that do not adapt creatively to the challenges of a fast moving and highly competitive market may make lower profits or even lose money.

The most striking feature of foreign investment in Korea is the growth in size of foreign companies. The figures are worth repeating as a conclusion.

Table 8.2. Companies by Size of Sales

	2001	2002	2003
US\$1 billion and above:	4	9	12
US\$500-999 million	12	16	16
US\$250-499 million	17	11	8
US\$100-249 million	15	22	28
US\$50 – 99 million	23	23	24
US\$5 – 49 million	29	27	22
No data or not existing	10	2	0
Total	110	110	110

The growth of these companies should in turn lead to greater profitability as the companies turn their management attention on deriving economies of scale. Most foreign companies are already deriving high productivity in terms of both sales and EBIT per employee, and this essentially destroys the argument that Korean labour is destroying profitability. The premise that Korean circumstances destroy profitability is therefore disproved.

There is evidence that responding to a downturn takes time and that continued liberalisation and deregulation would reduce this time, but foreign investors in Korea can look forward to their subsidiaries mastering these problems and producing increasing profits in 2004, 2005 and 2006.

Appendix

Appendix 1. Methodology

A.1. FSS Returns

All *chusik hweisa* with assets of more than 7 billion won must file their financial reports with the FSS, whether they are foreign or Korean owned. These financial reports must be audited by the local affiliates of international accounting firms. A small number of foreign companies in the sample chose the less usual form of *yuhan hweisa*.

A.2. Fortune 500

The *Fortune Global 500* groups together the world's largest corporations, ranked by sales. *Fortune* has compiled the Fortune Global 500 since 1994. It has been compiling the US 500 since 1955. Corporations are ranked on the basis of sales, and data on profit, number of employees and other related data. Data on EBIT is not collected. Data on EBIT was collected from Bloomberg data or annual reports directly. In general it has been necessary to revert to the annual reports of all companies to pick up additional information and insights, particularly in gathering regional data.

The study uses the *Fortune 500* industrial classification for comparative purposes. This divides the 500 leading international companies into 26 industrial categories. While this study followed *Fortune's* categories, the consultants are unhappy about this element of the Fortune structure, since it separates companies which are basically in the same business into three different categories. The picture is more complicated with true conglomerates such as GE or United Technologies, in terms category should they be placed.

A.3. Exclusions

The first exclusion comes in data for 2001. 10 of the 110 companies did not exist in 2001 and therefore are not included in analysis for that year. By industrial sector, it became clear that of the eleven pharmaceutical companies, only one exceeded its parent in profitability. The reasons for this are explained below.

After due consideration it was decided to exclude from the primary sequence those companies that made a loss at EBIT level. Making a loss at net profit level may have reasons unique to particular years. Making a loss at EBIT is an indication of a serious state of affairs. Excluded companies included General Motors Daewoo where the restructuring and rebuilding of the company was not complete, MAN Truck and Bus Korea Ltd and other companies in start up mode.

Excluded companies include a group of six long established companies such as Unilever, Nestle, McDonald's and Wal-Mart. These are troubling names, and due consideration of their situation is given in chapter 5, and further detailed analysis in the Occasional Paper.

It was decided that for basic analysis 22 companies which were making a loss at EBIT should be excluded from the primary results. This excluded three pharmaceutical companies. As noted in section 2.4, a loss at operating profit level is an indication of one of several factors:

- Start up
- Restructuring
- Part not whole perspective
- Going out of business

Chapter 5 analyses the excluded companies from this perspective.

In total, 30 companies were excluded from the primary sequence, 8 as pharmaceutical companies, 3 as pharmaceutical companies making a loss at EBIT, and 19 as making a loss at EBIT.

No banks or financial companies were included in the study, except insurance companies and GE Capital.

A.4. Indicators: Measurements of Success – Individual or Industry Grouping

- Sales to assets
- EBIT
- Net Profit
- Return (Net Profit) on Assets
- Sales per employee
- Interest rate coverage

The last item is an indication of leverage put into measure the peculiarly Korean phenomenon of over-leveraging.

The best measure of a company's profitability in a particular country is to compare it with the company's global profit. Each company has its own characteristics and life cycle. Comparison might also be made to industry average but this is a more complex measure.

In the tables with analysed results, we have inserted a category "too close to call". This is where the rate concerned is within plus or minus 0.3% points of the global parent's performance. Given the multitude of factors which can affect profitability in a particular year, companies with a rate approximating to the global average are put into this category.

In terms of net profit to assets, Korean subsidiaries of 14 industrial classifications performed significantly better than their global industrial sector, and 12 performed worse. However, for some of these sectors, foreign companies were only represented by 2 or 3

companies per industrial category. The largest category, where every *Fortune 500* company was represented, as already noted, was pharmaceuticals.

A.5. Qualitative Factors

In order to assess qualitative factors, interviews were conducted with 25 of the companies in the sample.

These interviews yielded important conclusions, and companies interviewed also indicated where profit could be higher if Korean regulations were eased. Almost all respondents showed some reluctance to comment on the profitability of their operation for a number of reasons. One was a fear of either tax office or journalistic response, and the other was that it might weaken arguments with the labour unions where companies were struggling to improve productivity.

It is important to record that the data given in this report is dealing with averages and not specific information. Any reference to a specific company should not be used uncritically but should be confirmed with the company in question.

A.6. Currency of analysis

For convenience, all local Korean data was converted into dollars of the year in question, 2003 accounts into 2003 dollars (exchange rate 1US\$=1192.6 won), 2002 accounts into 2002 dollars (exchange rate 1US\$=1186.2 won), and 2001 accounts into 2001 dollars (exchange rate 1 US\$=1313.5 won). This is to permit comparison with international data, which is generally in US dollars. In general this creates no distortion. The one measure which creates a distortion is comparison of sales from year to year which will either exaggerate or under-represent growth rates.

Appendix 2.

Table A.1. Sample by industry

	Investor	Company Name	Established	Major Shareholders
A.	Aerospace and defense			
1	Honeywell	Honeywell Co., Ltd.	1989	Honeywell International Finance Co. 100%
B.	Automotives			
2	GM	GM Daewoo Auto & Technology Company	2002	GM Holden Investment Pty Ltd. 44.6%, Suzuki Motor Corporation 14.9%, Shanghai Automotive Industry Corporation 10.6%
3	DaimlerChrysler	Daimler Chrysler Korea Ltd.	1996	DaimlerChrysler AG 100%
4	BMW	BMW Korea Co., Ltd.	1995	BMW Holding B.V. 100%
5	Ford	Volvo Car Korea Co., Ltd.	1997	Ford Motor Company 100%
6	Volvo	Volvo Construction Equipment Korea Ltd.	1998	Volvo Korea Holding AB 100%
7	Volvo	Volvo Truck Korea Ltd.	1990	Volvo Truck Corporation 100%
8	Delphi	Korea Delphi Automotive Systems Corporation	1984	Delphi 50%, Daewoo Motor 24.99% Others 25.01%
9	Denso	Denso PS Electronics Corp.	1976	DENSO 51 %, PS Tec 49 %
10	Goodyear Tire	Goodyear Korea	1991	The Goodyear Tire & Rubber Company 100%
11	Michelin	Michelin Korea	1991	Compagnie Financiere Michelin 100%
12	Renault	Renault Samsung Motors Co., Ltd.	2000	Renault Group BV 70.1%, Samsung 19.9%, Others 10.0%
13	Toyota	Toyota Motor Korea Co., Ltd	2000	Toyota Motor 100%
14	MAN Group	MAN Truck & Bus Korea Ltd.	2001	MAN Nutzfahrzeuge Aktiengesellschaft 100%
C.	Beverages			
15	Coca-Cola Amatil	Coca-Cola Korea Bottling Co., Ltd.	1996	Coca-Cola Amatil
16	Coca-Cola	Coca-Cola Korea Co., Ltd.	1974	The Coca-Cola Export Corporation 100%
17	Pepsi Cola	Pepsi Cola Korea Co., Ltd	1993	7-UP Nederland B.V. 100%
18	Diageo	Diageo Korea	1989	The Seagram Company Ltd. 100%
D.	Building materials, glass			
19	Lafarge	Lafarge Byucksan Gypsum Korea Co., Ltd.	1998	South Korea Plasterboard Corporation (subsidiary of Lafarge Gypsum International) 50% Siamsum Corporation 50%
20	Lafarge	Lafarge Gypsum Korea Co., Ltd.	1998	South Korea Plasterboard Corporation (subsidiary of Lafarge Gypsum International) 50% Siamsum Corporation 51%
21	Lafarge	Lafarge Halla Cement Corporation	1998	Financiere Lafarge 39.9% State of Wisconsin Investment Board 30.1%
E.	Chemical			
22	BASF	BASF Company Limited	1988	BASF Beteiligungsgesellschaft GmbH 100%
23	Dow Chemical	Dow Chemical Korea Ltd.	1992	The Dow Chemical Company 100%
24	Bayer	Bayer Korea Ltd.	1989	Bayer A.G 100%
25	Dupont	Dupont Photomasks Korea Ltd.	1995	DuPont Photomask Inc. 100%
26	Akzo Nobel	Akzo Nobel Amides Co, Ltd.	1998	Akzo Nobel Chemicals International B.V. 100%
27	Mitsui Chemical	Kumho Mitsui Chemicals, Ins.	1989	Mitsui Takeda Chemicals, Inc. 50 %, Kumho Petrochemical 50%
F.	Computer Services			
28	Microsoft	Microsoft Korea	1988	Microsoft Corporation 100%
29	Electronic Data Systems	EDS Korea Ltd.	1996	E.D.S World Corporation (Far East) 100%
G.	Computer Equip			
30	IBM	IBM Korea Inc.	1967	IBM World Trade Americas/Far East Corporation 100%
31	HP	HP Korea	1984	Hewlett-Packard Company 44.11%, HP Europe B.V. 55.89%
32	Fujitsu	Fujitsu Micro Electronics Korea Ltd.	1999	Fujitsu Ltd. 100%
33	Fujitsu	Fujitsu Korea Limited.	1974	Fujitsu 100%
34	Dell	Dell Computer Corporation	1995	Dell International Inc. 100%
35	Canon	Lotte Canon Co., Ltd.	1985	Canon 50%
36	Xerox	Fuji Xerox Korea Co., Ltd.	1974	Fuji Xerox Co., Ltd. 64% Fuji Xerox Asia Pacific Pte., Ltd. 36%
37	Sun Microsystems	Sun Micro Systems Korea Ltd.	1990	Sun Microsystems California Inc. 100%
38	Ricoh	Sindoricoh Co., Ltd	1960	Ricoh 20.01%
39	Oracle	Oracle Systems Korea	1989	Oracle Corporation 100%
H.	Diversified Financial			
40	General Electric	GE Capital Korea Ltd.	1995	General Electric Capital Asia Investments, Inc. 100%
I.	Electronics, Elec. Equip			
41	Siemens	Siemens Co., Ltd	1989	Siemens Aktiengesellschaft ("Siemens A.G.") 100%
42	Siemens	Siemens Automotive Systems Co.	1987	Siemens Aktiengesellschaft (Siemens A.G., 65%) Seoul City Gas (35%)
43	Hitachi	Hitachi-LG Data Storage Korea, Inc	2000	Hitachi 51% LG Electronics 49%
44	Sony	Sony Korea Corporation	1990	Sony Holding Company (Asia) B.V. 100.0%
45	Sony	Sony Electronics of Korea Corporation	1992	Sony Holding (Asia) B.V. 100%
46	Toshiba	Toshiba Digital Media Network Korea Corp.	2001	Toshiba Corporation 100%

	Investor	Company Name	Established	Major Shareholders
47	Toshiba	Toshiba Electronics Korea Corp.	1999	Toshiba Electronics Asia(Singapore) Pte, Ltd.
48	Philips	Philips Electronics Korea Ltd.	1976	Philips Electronics N.V. 100%
49	Philips	LG.Philips LCD Co., Ltd.	1985	Philips 50% LG Electronics 50%
50	Philips	LG.Philips Displays Korea Co., Ltd	2001	LG.Philips Displays Investment B.V. 100%
51	Emerson Electric	Emerson Process Management Korea Limited.	1988	Rosemount Inc.(70%) Emerson Electronic Company (30%)
52	ABB	ABB Ltd.	1987	ABB (Asea Brown Boveri) Ltd. 100%
53	Sharp	Sharp Korea Co.	1972	Sharp 50.0%
54	Rockwell	Rockwell automation Korea Ltd.	1991	Rockwell Automation International Holdings LLC 100%
55	General Electric	GE Samsung Lighting	1996	GE Pacific Private Ltd. 55%
56	General Electric	GE Medical System	1984	GE Holding France S.A.R.L.100 %
J. Entertainment				
57	Time Warner	Warner Bros Korea	1989	Time Warner Entertainment Company, L. P.100%
58	Walt Disney	The Walt Disney Company (Korea) Ltd.	1992	The Walt Disney Asia, Inc.100%
K. Food Consumer				
59	Nestle	Nestle Korea Ltd.	1987	Nestle S.A. 100%
60	Nestle	Ralston Purina Korea Inc.	1999	Nestle S.A. 100%
61	Unilever	Unilever Korea Ltd.	1992	Mavibel B.V 100%
62	Kellogg	Nongshim Kellogg Company	1980	Kellogg 90%
63	Heinz	Heinz Korea Ltd	1986	H.J.Heinz Co. 100%
L. Food Services				
64	McDonald's	Shin MC Co., Ltd.	1986	
65	Starbucks	Starbucks Coffee Korea Co. Ltd.	1997	Starbucks Coffee International, Inc. 50%
M. Food and Drug Stores				
66	Carrefour	Carrefour Korea, Ltd.	1994	Carrefour Group 100%
67	Tesco	Samsung Tesco Co., Ltd.	1999	Tesco Holdings B.V. 89%
N. General Merchandise				
68	Wal-Mart	Wal-Mart Korea Co Ltd	1993	Wal-Mart Stores, Inc. 100%
O. Household Products				
69	Kimberly-Clark	Yuhan-Kimberly	1970	KCC 23.6%, Kimberly-Clark Inc 46.4%. Yuhan Corporation 30%
P. Mail, Package, Freight delivery				
70	FedEx	Federal Express Korea Co., Ltd.	1999	Federal Express International Inc. 100%
71	DHL	DHL Korea	2000	DHL Worldwide Express B.V. 30%
Q. Metals				
72	Alcoa	Alcoa Korea Ltd.	2001	Alcoa International Holdings Company 100%
73	Alcan	Alcan Taihan Aluminum Limited	1999	Alcan Inc. 58.1%, Taihan Electric Wire 20.1%
R. Network, Other Comm.				
74	Nokia	Nokia TMC Ltd.	1984	Nokia 100%
75	Motorola	Motorola Korea Inc.	1992	Motorola Inc.100%
76	Cisco System	Cisco Systems Korea Ltd.	1994	Cisco Systems Inc.100%
77	Corning	Samsung Corning Co., Ltd.	1973	Corning Incorporated 50%
S. Petroleum Refining				
78	BP	AsPac Oil Korea limited (BP Korea)	1997	Castrol Limited 100%
79	Exxon Mobile	Mobil Korea Lube Oil, Inc.	1973	ExxonMobil Yugen Kaisha 50%
80	Chevron Texaco	LG-Caltex Oil Corporation	1967	Caltex(Overseas) Limited 40%, Chevron Texaco Global Energy Inc. 10%,
81	Royal Dutch/Shell	Hankook Shell Oil Co., Ltd.	1960	Shell Petroleum N.V. 53.85%,
T. Pharmaceuticals				
82	Pfizer	Pfizer Pharmaceutical Korea Ltd.	1959	Pfizer Corporation (50.5%) Pfizer Investment Capital Limited (49.4%)
83	Johnson & Johnson	Johnson&Johnson Korea Ltd.	1983	Johnson & Johnson 100%
84	Johnson & Johnson	Johnson&Johnson Medical Korea Ltd.	1988	Johnson & Johnson Korea Holding Inc. 60.37%, DePuy Inc. 39.63%
85	GlaxoSmithKline	GlaxoSmithKline Korea	1969	Glaxo Group Limited100%
86	Novartis	Novartis Korea Ltd.	1984	Novartis AG 17.6%, Novartis Pharma AG, 80.7%, Dong Wha Pharmaceutical 1.7%
87	Roche Group	Roche Korea Co., Ltd.	1983	Roche Pharmholding B.V. 100%
88	Merck	Merck Ltd.	1989	Merck AG 100%
89	Aventis	Aventis Pharma Co., Ltd.	1991	Aventis Pharma S.A. 60.0%, Handok Pharmaceutical 35.0%
90	Astra Zeneca	Astra Zeneca Korea Ltd.	1992	Astra Zeneca Continent B.V. 100%
91	Eli Lilly	Lilly Korea Limited	1982	Eli Lilly Netherlands B.V. 100%
92	Abbott Laboratories	Abbott Korea Ltd.	1988	Abbott Laboratories100%
U. Semiconductors, other components				
93	Intel	Intel Korea	1989	Intel Microprocessor Corp.100%
94	Texas Instruments	Texas Instruments Korea	1988	Texas Instruments (T.I.) Incorporated 100%
95	Fairchild	Fairchild Korea Semiconductor Ltd.	1998	Fairchild Semiconductor International, Inc. 100%
96	Amkor	Amkor Technology Korea, Inc.	1999	A.T.L. Limited 100%
V. Retailers				
97	Costco Wholesale	Wholesale Korea Costco	1998	Costco Wholesale International Inc. (96.7%) Shinsegae (3.3%)
W. Tobacco				
98	Altria Group	Philip Morris Korea Inc.	1990	FTR Holding S.A. (Philip Morris International Inc.) 100%
99	British American Tobacco	British American Tobacco Korea Limited	1990	Brown & Williamson Overseas Ltd. 100%

	Investor	Company Name	Established	Major Shareholders
100	British American Tobacco	British American Tobacco Korea Manufacturing Limited	2001	British American Tobacco (Investments) Korea Ltd. 100%
X. Trading				
101	Marubeni	Marubeni Korea Corporation	1995	Marubeni 100%
102	Itochu	Itochu Korea Ltd.	1994	Itochu 55.35%, Itochu Singapore Pte., Ltd. 44.65%
103	Sumitomo	Sumitomo Corporation Korea Ltd.	1994	Sumitomo 100%
Y. Miscellaneous				
104	3M	3M Korea Ltd.	1977	3M Company 100%
105	Dentsu	Dentsu Inovak Inc.	1999	
106	Nike	NIKE Sports Korea Co., Ltd	1986	Nike Inc. 99.94%
107	Yahoo	Yahoo Korea Corp.	1997	Yahoo! Inc. 67%, Softbank Korea 20.6%, Softbank Corp. 8.3%, Yahoo! Japan 4.1%
Z. Insurance				
108	Allianz	Allianz Life Insurance Co., Ltd.	1954	Atropos Vermoegensverwaltungsgesellschaft mbH (Allianz AG) 100%
109	ING Group	ING Life Insurance Korea Ltd.	1991	ING Insurance International B.V. 80%, Kookmin Bank 20%
110	Metlife	Metlife Korea	1989	Metlife International Holdings, Inc. 100%

Table A.2. Net profit / Assets by industry (2003)

	Average		More profitable companies	Less profitable companies
	Global	Korean		
Computer Services	-0.2%	2.4%	EDS Korea Ltd.	Microsoft Korea
Insurance	0.4%	1.7%	Allianz Life Insurance Co., Ltd. ING Life Insurance Korea Ltd. Metlife Korea	
Trading	0.5%	-21.7%	Sumitomo Corporation Korea Ltd.	Marubeni Korea Corporation Itochu Korea Ltd.
Metals	1.7%	-8.4%	Alcan Taihan Aluminum Limited	Alcoa Korea Ltd.
Automotives	1.8%	6.2%	Daimler Chrysler Korea Ltd. BMW Korea Co., Ltd. Volvo Car Korea Co., Ltd. Volvo Construction Equipment Korea Ltd. Volvo Truck Korea Ltd. Korea Delphi Automotive Systems Corporation Goodyear Korea Michelin Korea Renault Samsung Motors Co., Ltd. Toyota Motor Korea Co., Ltd.	GM Daewoo Auto & Technology Company Denso PS Electronics Corp. MAN Truck & Bus Korea Ltd.
Electronics, Elec. Equip	2.2%	7.4%	Siemens Co., Ltd. Siemens Automotive Systems Co. Hitachi-LG Data Storage Korea, Inc. Sony Korea Corporation Sony Electronics of Korea Corporation Toshiba Digital Media Network Korea Corp. Toshiba Electronics Korea Corp. Philips Electronics Korea Ltd. LG.Philips LCD Co., Ltd. ABB Ltd. GE Samsung Lighting	LG.Philips Displays Korea Co., Ltd. Emerson Process Management Korea Limited. Sharp Korea Co. Rockwell automation Korea Ltd. GE Medical System
Diversified Financial	2.3%	-2.5%		GE Capital Korea Ltd.
Entertainment	2.4%	12.6%	Warner Bros Korea The Walt Disney Company (Korea) Ltd.	
Chemical	2.4%	-1.6%	Dow Chemical Korea Ltd. Bayer Korea Ltd. Dupont Photomasks Korea Ltd. Akzo Nobel Amides Co, Ltd.	BASF Company Limited Kumho Mitsui Chemicals, Ins.
Semiconductors, other components	4.0%	16.7%	Intel Korea Texas Instruments Korea Fairchild Korea Semiconductor Ltd.	Amkor Technology Korea, Inc.
Mail, Package, Freight delivery	4.4%	5.7%	Federal Express Korea Co., Ltd. DHL Korea	
Aerospace and defense	4.5%	22.9%	Honeywell Co., Ltd.	
Food and Drug Stores	4.5%	0.9%		Carrefour Korea, Ltd. Samsung Tesco Co., Ltd.
Tobacco	5.2%	6.2%	British American Tobacco Korea Limited British American Tobacco Korea Manufacturing Limited	Philip Morris Korea Inc.
Computer Equip	5.9%	6.2%	IBM Korea Inc. Fujitsu Micro Electronics Korea Ltd. Fuji Xerox Korea Co., Ltd. Sun Micro Systems Korea Ltd. Sindoricoh Co., Ltd.	HP Korea Fujitsu Korea Limited. Dell Computer Corporation Lotte Canon Co., Ltd. Oracle Systems Korea
Building materials, glass	6.6%	36.4%	Lafarge Byucksan Gypsum Korea Co., Ltd. Lafarge Halla Cement Corporation	Lafarge Gypsum Korea Co., Ltd.
Network, Other Comm.	6.6%	-1.5%	Samsung Corning Co., Ltd.	Nokia tmc Ltd. Motorola Korea Inc. Cisco Systems Korea Ltd.
Retailers	6.7%	3.2%		Wholesale Korea Costco
Food Services	7.8%	-1.3%		Shin MC Co., Ltd. Starbucks Coffee Korea Co. Ltd.
Miscellaneous	7.9%	14.8%	3M Korea Ltd. NIKE Sports Korea Co., Ltd Yahoo Korea	Dentsu Innovak Inc.
General Merchandise	8.6%	0.1%		Wal-Mart Korea Co Ltd
Food Consumer	9.9%	4.9%	Ralston Purina Korea Inc. Nongshim Kellogg Company	Nestle Korea Ltd. Unilever Korea Ltd. Heinz Korea Ltd
Household Products	10.1%	14.6%	Yuhan-Kimberly	
Beverages	10.8%	22.6%	Coca-Cola Korea Co., Ltd. Diageo Korea	Coca-Cola Korea Bottling Co., Ltd. Pepsi Cola Korea Co., Ltd

	Average		More profitable companies	Less profitable companies
	Global	Korean		
Pharmaceuticals	11.2%	5.2%	Pfizer Pharmaceutical Korea Ltd. Johnson & Johnson Korea Ltd. Roche Korea Co., Ltd.	Johnson & Johnson Medical Korea Ltd. GlaxoSmithKline Korea Novartis Korea Ltd. Merck Ltd. Aventis Pharma Co., Ltd. Astra Zeneca Korea Ltd. Lilly Korea Limited Abbott Korea Ltd.
Petroleum Refining	14.4%	22.9%	AsPac Oil Korea limited (BP Korea) Mobil Korea Lube Oil, Inc. Hankook Shell Oil Co., Ltd.	LG-Caltex Oil Corporation

Table A.3. Net Profit / Sales by industry (2003)

	Average		More profitable companies	Less profitable companies
	Global	Korean		
Trading	0.4%	-8.8%	Sumitomo Corporation Korea Ltd.	Marubeni Korea Corporation Itochu Korea Ltd.
Retailers	1.8%	2.2%	Wholesale Korea Costco	
Automotives	1.9%	2.6%	Daimler Chrysler Korea Ltd. Volvo Car Korea Co., Ltd. Volvo Construction Equipment Korea Ltd. Volvo Truck Korea Ltd. Korea Delphi Automotive Systems Corporation Goodyear Korea Michelin Korea	GM Daewoo Auto & Technology Company BMW Korea Co., Ltd. Denso PS Electronics Corp. Renault Samsung Motors Co., Ltd. Toyota Motor Korea Co., Ltd. MAN Truck & Bus Korea Ltd.
Chemical	2.7%	-1.7%	Bayer Korea Ltd. Dupont Photomasks Korea Ltd. Akzo Nobel Amides Co, Ltd.	BASF Company Limited Dow Chemical Korea Ltd. Kumho Mitsui Chemicals, Ins.
Metals	2.8%	-15.5%		Alcoa Korea Ltd. Alcan Taihan Aluminum Limited
Food and Drug Stores	2.9%	0.9%		Carrefour Korea, Ltd. Samsung Tesco Co., Ltd.
Electronics, Elec. Equip	3.4%	3.0%	Siemens Co.,Ltd Siemens Automotive Systems Co. Hitachi-LG Data Storage Korea,Inc Sony Korea Corporation Sony Electronics of Korea Corporation Toshiba Digital Media Network Korea Corp. Philips Electronics Korea Ltd. LG.Philips LCD Co., Ltd. ABB Ltd.	Toshiba Electronics Korea Corp. LG.Philips Displays Korea Co., Ltd Emerson Process Management Korea Limited. Sharp Korea Co. Rockwell automation korea ltd. GE Samsung Lighting GE Medical System
Mail, Package, Freight delivery	3.4%	3.3%		DHL Korea Federal Express Korea Co., Ltd.
General Merchandise	3.5%	0.1%		Wal-Mart Korea Co Ltd
Insurance	4.2%	3.4%	ING Life Insurance Korea Ltd.	Allianz Life Insurance Co., Ltd. Metlife Korea
Entertainment	5.7%	6.0%	The Walt Disney Company (Korea) Ltd.	Warner Bros Korea
Aerospace and defense	5.7%	15.3%	Honeywell Co., Ltd.	
Computer Equip	5.9%	3.8%	Fujitsu Micro Electronics Korea Ltd. Fuji Xerox Korea Co., Ltd. Sun Micro Systems Korea Ltd. Sindoricoh Co.,Ltd.	IBM Korea Inc. HP Korea Fujitsu Korea Limited. Dell Computer Corporation Lotte Canon Co., Ltd. Oracle Systems Korea
Semiconductors, other components	6.3%	5.1%	Intel Korea Fairchild Korea Semiconductor Ltd.	Texas Instruments Korea Amkor Technology Korea, Inc.
Network, Other Comm.	7.1%	-0.5%	Samsung Corning Co., Ltd.	Nokia tmc Ltd. Motorola Korea Inc. Cisco Systems Korea Ltd.
Computer Services	7.1%	2.3%	EDS Korea Ltd.	Microsoft
Food Services	7.6%	-4.6%		Shin MC Co., Ltd. Starbucks Coffee Korea Co. Ltd.
Food Consumer	7.8%	2.6%	Ralston Purina Korea Inc. Nongshim Kellogg Company	Nestle Korea Ltd. Unilever Korea Ltd. Heinz Korea Ltd
Tobacco	9.0%	4.8%	British American Tobacco Korea Manufacturing Limited	Philip Morris Korea Inc. British American Tobacco Korea Limited
Building materials, glass	10.7%	40.6%	Lafarge Byucksan Gypsum Korea Co., Ltd. Lafarge Halla Cement Corporation	Lafarge Gypsum Korea Co., Ltd.
Miscellaneous	10.8%	12.1%	3M Korea Ltd. NIKE Sports Korea Co., Ltd Yahoo Korea	Dentsu Innovak Inc.
Petroleum Refining	11.1%	14.4%	AsPac Oil Korea limited (BP Korea) Mobil Korea Lube Oil, Inc. Hankook Shell Oil Co., Ltd.	LG-Caltex Oil Corporation
Diversified Financial	11.2%	-11.3%		GE Capital Korea Ltd.
Household Products	11.8%	12.9%	Yuhan-Kimberly	
Beverages	13.8%	13.9%	Coca-Cola Korea Co.,Ltd.	Coca-Cola Korea Bottling Co., Ltd. Pepsi Cola Korea Co.,Ltd Diageo Korea

	Average		More profitable companies	Less profitable companies
	Global	Korean		
Pharmaceuticals	16.9%	3.9%	Pfizer Pharmaceutical Korea Ltd.	Johnson&Johnson Korea Ltd. Johnson&Johnson Medical Korea Ltd. GlaxoSmithKline Korea Novartis Korea Ltd. Roche Korea Co., Ltd. Merck Ltd. Aventis Pharma Co., Ltd. Astra Zeneca Korea Ltd. Lilly Korea Limited Abbott Korea Ltd.

Glossary

Chusik Hweisa

company limited by shares – company in which the members' personal liabilities are limited to the par value of their shares and are not legally responsible for the liabilities of the company. In order to establish a chusik hweisa, 7 or more promoters must be involved to draft up the articles of association and issue company shares. In the case of incorporation by promotion, by which the promoters claim all of company shares without bringing in outside shareholders, a chusik hweisa is formally established after it has collected all of the contributed capital on the issued shares. A chusik hweisa can also choose the method of incorporation through Initial public Offering (IPO), which is the first or primary offering of stock to the public. In this case, the company must conduct an organizational meeting to gather all or most of its shareholders and properly register the entity to be official. All chusik hweisas conduct general meetings of shareholders, board of trustees meetings, and internal audits, and all of these functions at the end of each accounting period.

Company life cycle

Various stages of a company over its lifetime

7 stages of a business

1. Seed Stage:
A business is just a thought or an idea.
2. Start-Up Stage:
The business is established and now exists legally. Products or services are in production, and the company has its first customers.
3. Growth Stage:
Revenues and customers are increasing with many new opportunities and issues. Profits are strong, but competition is surfacing.
4. Established Stage:
The business has now matured into a thriving company with a place in the market and loyal customers. Sales growth is not explosive but manageable. Business life has become more based on routines.
5. Expansion Stage:
A new period of growth into new markets and distribution channels. Opportunities rise to gain a larger market share and find new revenue and profit channels.
6. Decline Stage:
Changes in the economy, society, or market conditions can decrease sales and profits.
7. Exit Stage:
May be an opportunity for the business to cash out on all the effort and years of hard work. Or it can mean shutting down of the business.

Sales Per Employee

Sales /total number of employees – roughly measures **labour productivity**

EBIT

Earnings Before Interest and Taxes - but after all product / service and sales costs are accounted for.

GDP

Gross Domestic Product - is the value of all the goods and services produced by workers and capital located within a country (or region), such as the United States, regardless of nationality of workers or ownership. Domestic measures relate to the physical location of the factors of production; they refer to production attributable to all labour and property located in a country. The national measures differ from the domestic measures by the net inflow – that is, inflow less outflow – of labour and property incomes from abroad. Gross Domestic Product includes production within national borders regardless of whether the labour and property inputs are domestically or foreign owned.

Interest Coverage Ratio

EBIT/Interest Expense –a measurement of the number of times a company could make its interest payments with its earnings before interest and taxes; the lower the ratio, the higher the company's debt burden.

Net Profit

Company's total earnings, reflecting revenues adjusted for costs of doing business, depreciation, interest, taxes and other expenses. Same as Net Income.

Over-leveraging

a balance sheet condition where the entity is incapable of servicing its debt load (interest payments) with available capital sources. Simply put, the entity is carrying too much debt.

Product Life Cycle

a marketing theory in which products or brands follow a sequence of stages in their sales, including : introduction, growth, maturity, and decline.

Return on Assets

net income/total assets (ROA) - shows the after tax earnings of assets. Return on assets is an indicator of how profitable a company is. Use this ratio annually to compare a business' performance to the industry norms: The higher the ratio the greater the return on assets. However this has to be balanced against such factors as risk, sustainability and reinvestment in the business through development costs.

Sales to Assets

sales revenue/total assets – measures the amount of sales revenue generated per asset owned by a company.

Yuhan Hweisa

private company – a company whose shares are not traded in the open market. Yuhan hweisa is established by issuing equal amount of shares to each contributor. In this case, the contributors of capital are the employees of the company, and their personal liabilities are limited to the par value of their shares and are not legally responsible for the liabilities of the company. A yuhan hweisa generally carries fewer liabilities than a chusik hweisa.