

Samsung crisis highlights S. Korea's 'chaebol' problem

SEOUL, SOUTH KOREA: Samsung's corporate car-crash over its exploding Note 7 smartphones has shone a spotlight on South Korea's "[chaebol](#)" business culture - the family-run empires whose rigid corporate structure and opaque governance style aren't always best suited to a crisis.



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Giant conglomerates like Samsung and Hyundai were widely credited with driving the stellar growth that transformed South Korea from a war-ravaged backwater to Asia's fourth-largest economy in a matter of decades.

Their business style was a top-down corporate culture where orders from the founding family and senior managers were carried out without question.

Samsung has long been seen as a model of pragmatic efficiency, with a chairman and handful of elite managers dictating an overall business plan for all divisions to follow meticulously.

Under the now-ailing chairman and family patriarch, Lee Kun-Hee, the strategy proved extremely successful over the past 15-20 years, turning the once-obscure electronics maker into a global powerhouse.

But as the firm grew in size, and its business dealings became more complex and globalised, the highly centralised decision-making process has become, some analysts suggest, a liability as well as an asset.

Unchallenged authority

Kim Sang-Jo, head of the Seoul-based corporate governance monitoring group Solidarity for Economic Reform, said a coterie of top managers in the company's "future strategy office" wield nearly unchallenged authority over the group's strategic direction.

"Whatever decision the office makes, engineers and working-level managers should follow silently, although they might think it's not humanly possible or utterly unreasonable," Kim said.

Along with a number of other analysts, Kim believes a key factor behind the Note 7 debacle was management's insistence that it be launched ahead of schedule to secure a lengthy market lead over arch-rival Apple's new iPhone.

"There was no channel for engineers to tell the management that they needed more time to test the battery and later prepare a new battery for the recall... and this lack of feedback was the biggest culprit behind this disaster," Kim said.

When the new smartphones began catching fire, Samsung announced a recall of 2.5 million units. The company blamed a battery supplier, said the problem was fixed and offered to replace all the devices.

The real damage to the company's reputation came when replacement phones also started burning up, triggering criticism that the exchange programme had been rushed in much the same way as the original early launch.

In the end, Samsung was forced to kill off the Note 7, announcing Tuesday that it was permanently halting production.

Lesson to be learned

Park Yoo-Kyung, a Hong Kong-based director specialising in corporate governance at APG Asset Management, said she hoped Samsung had learned its lesson.

"I've seen so many family-controlled firms respond to crises so slowly... or entirely miss the chance to correct their mistakes because everything has to be dictated by top management," she said.

"I really hope that Samsung will not introduce another new smartphone too quickly in its effort to put the whole crisis behind it... and that its management will do some soul-searching on whether it has a corporate culture in line with its status as a world leading tech company," Park said.

Chaebols like Samsung are not used to dealing with public scrutiny, or indeed with uppity shareholders - as Samsung showed during a bitter dispute last year with the US hedge fund Elliott Management which tried to prevent a merger of two Samsung affiliates.

This is partly due to their dominant position in the South Korean economy - Samsung alone accounts for around 17% of the country's GDP - which tends to intimidate domestic regulators.

Transfer of leadership

The disaster with the Note 7 came as Samsung navigates a complex generational leadership transfer, with Lee Kun-Hee bedridden since suffering a heart attack in 2014.

In the aftermath there will be intense scrutiny of the performance of his son and heir apparent, J.Y. Lee, 48, who is vice chairman of Samsung Electronics and was nominated to the company board just days after the initial Note 7 recall.

"Depending on how he responds, Samsung will be remembered as a model case of using a crisis as an opportunity to reinvent itself... or go down in history like Nokia," said Kim Sang-Jo.

The Lee family controls the vast \$242-billion Samsung Group through a complex web of cross shareholdings, although they only directly own about 5% of total stock.

The byzantine nature of the corporate structure was put into sharp relief during the showdown last year with Elliott Management, which is now challenging the Samsung leadership again.

Last week, the hedge fund unveiled a proposal for splitting Samsung Electronics in two in order to unlock billions of dollars in value for shareholders.

Source: AFP

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