

## **Developing Scenarios for MNCs acting on Emerging Markets**

*-The Volvo Construction Equipment Korea Case*

**Tanja Holst and Carolina Winzell**

#### Acknowledgements

This thesis marks the conclusion of our one and one-half year program in the Integrated Masters program for International Business at the School of Economics and Commercial Law, Gothenburg University.

We would like to thank Volvo Construction Equipment in Brussels and Korea, especially Hans Josefsson and Magnus Björckman, who gave us the opportunity to work with an interesting subject in a dynamic environment.

Finally, we would like to extend our warmest thanks to our supervisor, who led us through the many aspects of the thesis process, Professor Hans Jansson.

Gothenburg, January 14<sup>th</sup>, 2000

Tanja Holst

Carolina Winzell

### **Abstract**

The purpose of this thesis is to develop a scenario technique for MNCs operating on emerging markets. The focal point in the scenario development process is to create awareness of the environment in which the MNC is acting. By using the developed scenario method as a management tool, the organisation improves its preparedness for action, and thus its competitiveness. The capability for fast adaptation to the environment is crucial in emerging markets, and could be the only sustainable competitive advantage for the MNC in the long run.

The scenario technique was developed in a process involving the case company Volvo Construction Equipment in South Korea (Volvo CE Korea), thus enabling us to visualise the process.

The description and analyse of the South Korean environment defined the main driving forces of future environmental change, as well as the determinants for stability. These were the foundations for creating the different scenarios. The scenarios were primarily made to suit the needs of Volvo CE Korea, but could be used by any MNC on the Korean market. The scenarios show that each of the “futures” described constitutes a different set of opportunities and threats for the MNC. These threats and opportunities need to be considered against the MNCs strengths and weaknesses. If the decision makers within the MNC are prepared for different outcomes in the future, their chances of meeting the future opportunities and threats successfully increases.

### **Key Words**

---

South Korea, Volvo Construction Equipment Korea, Emerging market, FDI (Foreign Direct Investor), MNC (Multinational Corporation), Scenario development

## **INTRODUCTION**

The purpose of this chapter is to delineate the background of the thesis by describing the problem area, the purpose, and the delimitations of the research. Further more, definitions of central concepts in the thesis are given in order to clarify specific words or concepts for the reader. Finally, an introduction to our case company, Volvo Construction Equipment Korea, is given.

### **1.2 PROBLEM BACKGROUND**

A main trend in world business during the last decades has been the great shift of foreign direct investment (FDI), or global operations by multinational corporations (MNC's), from traditional Western markets to emerging ones.

An emerging market consists of a multitude of economic and non-economic factors and actors, including suppliers, competitors and government authorities, as well as intangibles such as culture, values and attitudes: all of these establish the external institutional set-up of a Multinational Corporation (MNC). In this complex, and for an MNC, rather unexplored market environment, it is crucial to know how to act.

One of the characteristics of emergent markets is their ever-changing market environment. The changes are to a great extent driven by the ongoing globalisation of markets and industries. In this kind of turbulent and uncertain environment, it is important for the MNC to remain flexible and thus able to respond to environmental changes that occur.

#### **1.2.1 An analytical approach to the Scenario Development Process**

In order to increase the ability to respond quickly to environmental change, techniques in scenario development have been designed. These techniques mainly consist of identification of environmental factors, which are described and judged according to their perceived level of uncertainty.

What we are missing in this approach is an attempt to explain the environmental factors. These factors are simply identified, with no further explanation given to help in developing an understanding of how and why the environment has been formed to its present shape.

### 1.3 PROBLEM STATEMENT

The main problem stems from previous studies about the particular circumstances that prevail on emerging markets and the establishment of MNCs upon these markets. We wanted to take this research further by studying what happens after the establishment phase, and through the creation of a scenario development technique make assumptions about the future situation of the investigated emerging market. This theoretical model of the scenario planning process comprises the complexity and level of uncertainty that prevails on these markets.

#### **Main Problem**

*"To create an analytical approach to scenario development for MNCs operating on Emerging Markets"*

To enable us to give an extensive picture of the situation prevailing in emerging markets, an environmental analysis will be made using the Institutions Network Approach. Following this approach, the Financial markets, Product/Service markets, Labour markets, Government and Business Mores will be explained by applying theories on culture and social values. The analysis will be made consistently from a MNC perspective, and constitutes the base for our main problem: the development of an analytical approach to scenario planning.

#### **Research Problem I.**

*"To analyse the environment of the emerging market, by explaining its institutional set-up, and by this define the drivers of future environmental change"*

How well a MNC manages its environment can be defined as its capability to handle the market environment within which it conducts business. Competitiveness, in this respect demands that the internal resources and capabilities of the MNC match the external environment. To define the internal resources, as well as the MNC's strengths and weaknesses in handling its environment, is the second step in the process of scenario planning.

**Research Problem II.**

*"To describe the MNC's strengths and weaknesses in interacting with the complex and dynamic environment in emerging markets"*

**1.4 PURPOSE**

The purpose of this study is to develop an analytical framework on how a MNC acting upon new emerging markets can create future scenarios, in order to allow it to remain flexible and prepared for action when faced with changes imposed upon it by its market environment. By explaining the emerging market's environment from a MNC perspective, we will be able to deduce the drivers of change, which will be used as variables in the created scenarios. This whole process, which will be extensively described further on in this thesis, is the solution to our main problem: *To create an analytical approach to scenario development for MNCs operating in emerging markets.*

**1.5 DEFINITIONS**

There are several concepts that are central and frequently used throughout this thesis. As a reader, certain concepts might be difficult, and thus deserve explanation.

**Chaebol:** Large Korean Business Conglomerate

**Construction Equipment Industry:** includes the actors in this industry, the level of power they can exercise, and the threat they may impose upon each other.

**Emerging Markets:** an economic sector with growth potential; a country that is deregulating its markets, and liberalising its trade and investment regimes. (Gipson, 1994)

**Institutions:** “Human life is organised in certain ways. The organisation of such basic processes is here defined as institutionalisation processes. Behaviour patterns become ingrained in society leading to a self-activated individual behaviour. Behaviour follows from certain social programmes and conventions. This behaviour complex is defined as an institution. Thus, institutions and institutionalisation concern how society is organised.” (Jansson, 1999)

**Multinational Corporation (MNC):** A Multinational Corporation is: “a firm with branches and subsidiaries in several countries from which it derives at least 25 percent of its annual sales income. Corporations become multinational to avoid barriers to entry in target markets, benefit from lower cost labour, and secure sources of cheap raw materials.” (Gipson, 1994)

#### 1.6 DELIMITATIONS

The time frame when creating the scenarios was limited to the year 2005. The connection the scenarios have with the strategy of the MNC, makes it difficult to create scenarios with a longer or a shorter future out-look. If the scenarios are supposed to have direct relevance for the MNC, a longer time frame than five years will make them unfocused.

The research was focused on South Korea due to time and monetary constraints as well as the fact that Volvo CE and South Korea have the correct characteristics for our case study, being a multinational corporation operating in an emerging market.

A further delimitation was that no active participation or interaction by managers or other employees in the process of scenario development was possible, due to time and managerial restrictions.

#### 1.7 THE CASE COMPANY – VOLVO CONSTRUCTION EQUIPMENT KOREA

We have chosen Volvo CE Korea as case company as this company fulfils the attributes essential for our study. That is, it is a multinational corporation operating in an emergent marketenvironment: South Korea. The initial incentive for us to examine this case originated from an article in Far Eastern Review, describing Volvo Construction Equipment's successful acquisition of Samsung Heavy Industries' Construction Equipment division in May 1998.

##### 1.7.1 Volvo

Volvo is an international transport equipment group with a worldwide marketing organisation and production in 20 countries. The Volvo Group has about 52.000 employees, and sales in 1998 reached approximately USD 14,4 billion. Volvo's five business areas consist of Trucks, Buses, Construction Equipment, Marine and Industrial Engines, and Aero.

##### 1.7.2 Volvo CE

The business area of Construction Equipment (Volvo CE) comprises 17% of the sales in Volvo, and has 8.800 employees. Volvo CE's product range consists of more than 130 different models; Volvo wheel loaders, Volvo articulated haulers, Volvo excavators, Champion motor graders and Volvo compact equipment are the main product groups.

Volvo is one of the world's largest producers of construction equipment, after American Caterpillar and Japanese Komatsu. The total world market of construction equipment producers is fragmented, and a majority of the players have global market shares of less than 4%, causing the industry to consolidate.



### 1.7.3 Volvo Construction Equipment Korea

In May 1998 Volvo CE acquired Samsung Construction Equipment Division (the Samsung Division) from Samsung Heavy Industries in South Korea, and registered Volvo Construction Equipment Korea Ltd (Volvo CE Korea).

Why Korea and Samsung?

The reason for the acquisition was three-sided:

- Volvo CE needed to obtain a competitive excavator line, because excavators comprise a very large share (33%) of the global construction equipment market, and Volvo CE was too small in this product line.
- Volvo CE wanted to establish an Asian industrial hub and strengthen its position in Asia.
- It was a way to enter into the large excavator market in Korea, and to introduce Volvo CE's other products in this market.

Samsung Heavy Industries were, due to their strained financial position, severely struck by the Asian Crisis of 1997. The company's business had for many years been unprofitable. This forced them to refine their diversified organisation and concentrate on their core business, thus selling off their excavator division, Samsung Construction Equipment. The weak Korean market had major consequences for the Samsung Construction Equipment division, because their broad excavator line had a strong domestic foothold, but internationally, their position was very weak. The resources that the Samsung division possessed were a broad and technologically competitive excavator range of high quality. The manufacturing facilities were rather advanced (but underinvested) and the research and development activities were of high standards.

#### **1.7.3.1 The acquisition**

Volvo CE's acquisition of Samsung's Construction Equipment division has, until now, been one of the largest foreign direct investments in Korea. For the Korean government, which is striving to make Korea an attractive country for foreigners to invest in, the Volvo- acquisition has been seen as a role model, and the support from the current government, headed by President Kim Dae Jung, has been immense.

#### **1.7.3.2 After the acquisition**

The reorganisation of the company started right after the acquisition, and a 13 percent reduction of the number of employees was carried out, mainly through early retirement agreements. The fact that the overall competitiveness of the acquired company was higher than expected made Volvo CE decide to close down its own loss making excavator production in Sweden, and turn Korea into another of its bases for the manufacturing of excavators.

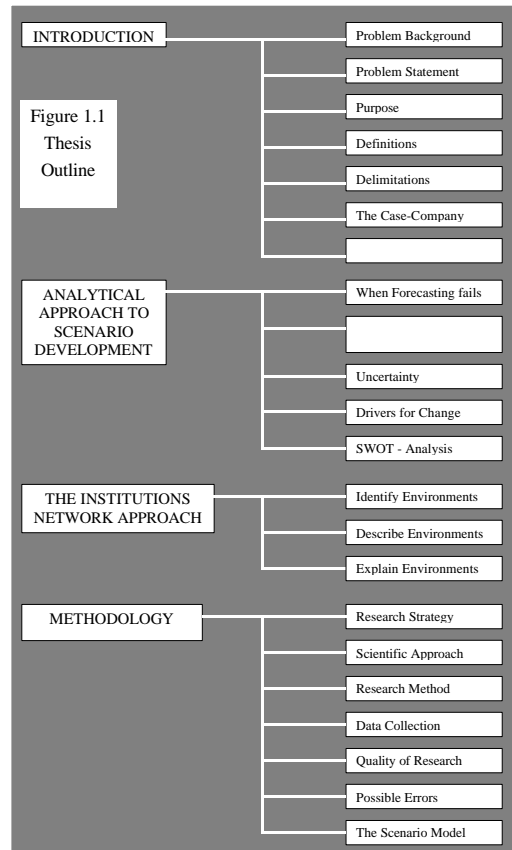
The decline of the Korean domestic excavator market was worse than expected in 1998, but improved significantly in 1999. Export volumes have grown since the incorporation of Samsung excavators into Volvo CE's global distribution network. The financial results improved and the turn-around in result came six months earlier than expected, in the second half of 1999.

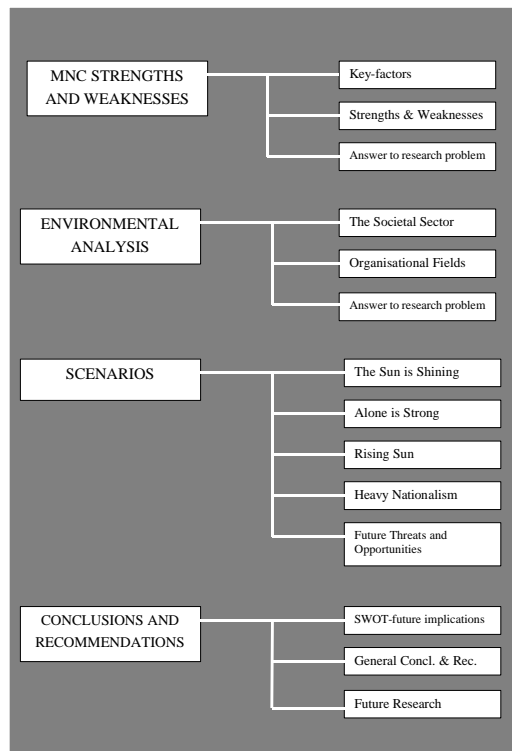
#### **1.7.3.3 The future**

In August 1999, the first shipment of Volvo brand excavators was completed and the Korean (Changwon) factory now produces Volvo brand articulated haulers as well as excavators. The extension of the product program is an initial step in making Volvo CE Korea an Asian industrial hub for Volvo. The expectation of a positive development of the Asian market is of decisive importance.

## 1.8 GENERAL THESIS-OUTLINE

This thesis is built of seven different stages that, together, will answer the stated problem and fulfil the purpose. To facilitate the reading, we have summarised these stages into a general thesis outline, shown in Figure 1.1





## 2 AN ANALYTICAL APPROACH TO SCENARIO DEVELOPMENT

There are different views on how scenarios ought to be developed. The views have two things in common: they are clearly practitioner-oriented, and no attempts for deeper analysis are shown. They are also of a rather general character, without any focus on either the specific circumstances that prevail on the different East Asian marketplaces, nor on the complexity of a multinational corporation acting upon these emerging markets. We will, in this chapter, discuss theories for general scenario development, and in the next theory chapter we will narrow the focus to a theory that will help us in analysing an emerging market.

### 2.1 WHEN FORECASTING FAILS

*“We have to forecast. We couldn’t drive the car with the lights switched off altogether. The important thing is to realise the limits of our view.”*

(Van der Heijden, 1996)

Risk is something that every company has to deal with. Sometimes changes happen in a sudden unpredictable way, and predict-and-control no longer works. When an industry is in a state of relative slow incremental change, and the time horizon is limited to one or two years, forecasting is an effective way of planning. The limitation of forecasting is its basis on the assumption that the past can be extended into the future. At the simplest level, this means a statistical extrapolation of variables. The problem with forecasting arises when the environment is less predictable, for example in emerging markets, the environment is characterised by a high degree of uncertainty. In this type of environment, forecasting could even be dangerous, as it prevents the decision maker from gaining the insight needed to come to responsible conclusions. Forecasting is sometimes done by outside experts that are not directly involved in the decision making process. This means that the decision maker does not know the amount of uncertainty that was taken into account when producing the forecast. When forecasts are based upon statistical summaries or expert opinions, the

process of scenario development is much more a conceptual description of a future, based on cause and effect. Scenario techniques force people to think about the future, and enable them to be more perceptive in realising the implication of events. The process of scenario development will create an organisation alert to its business environment and capable of reading signals of structural change early. (Van der Heijden, 1996)

## 2.2 MAIN COMPONENTS OF THE SCENARIO DEVELOPMENT PROCESS

In the literature we have examined about scenario development, there are two main components that could be distinguished. The authors van der Heijden (1998), Porter (1985), Schwartz (1996), and Schoemaker (1991) define the components that have to be identified in the initial stage of the scenario development process as:

- The environment surrounding the firm and;
- The firms current strategy

### 2.2.1 Van der Heijden's view

In order to make the right decisions, the organisation needs to understand itself, thus having a clear Business Idea, *and* it needs to understand its Environment. In the context of the organisation's purpose for survival and self-development, we develop a definition of "organisational self" which is called the Business Idea. The Business Idea expresses the company's ability to survive and develop itself in terms of organisational characteristics. In the environment there is ambiguity and uncertainty, which present multiple equally plausible futures. The Business Idea and the future environment are brought together, thus questioning the robustness of the Business Idea in the future business environment. (Van der Heijden, 1996)

The scenarios are created independently from the organisation. First when the scenarios are written they are compared to the Business Idea. (Van der Heijden, 1996)

Van der Heijden does not explain the interrelation between a firm and its environment. There are no specific analyses made that consider the influence of the environment over the firm, and the firm's own potential to affect the environment. The impact of the environment upon the "Business Idea" is only considered in the end of the scenario development process, when it is matched against the created scenarios. From our point of view, this can create scenarios that are of little relevance to the firm for which they are intended.

### **2.2.2 Porter's view**

Porter (1985) presents another view. He differentiates between macro scenarios and industry scenarios. Macro scenarios are referred to as views in which national or global economy and the political environment (including growth, inflation, protectionism, regulation, interest rates etc.) are considered.

Porter does not reflect on the firm's role in the scenario building process at all. He puts most of his emphasis on predicting industry change. In the effort to look into the future of more turbulent environments, such as the East Asian market place, that might not be enough. There is, of course, a need for analysis of the industry structural change, but there is also a need to analyse the more deeply rooted factors in the environment, such as the social institutions of a society, and the interrelation between the firm and the environment. In this version of the scenario building process there is also no further focus on the firm for which the scenario is created. The scenarios will thus be of a more general character, applicable to the industry they describe.



### 2.2.3 Schoemaker's view

Schoemaker (1995), on the other hand, discusses how political, economical, social, technological, legal and industry trends will affect the major stakeholders and the scope of the firm. He defines the scope of a firm as the markets upon which the firm acts, the products it manufactures, and the technologies it uses or develops. Stakeholders are defined by the questions: Who will have an interest in these issues? Whom they will affect? Whom could they influence?

Once again there is no consideration taken of the firm for which the scenarios are created. Even more important, there is no attention given to the specific circumstances that a multinational company experiences in emergent markets.

## 2.3 THE UNCERTAINTY OF THE ENVIRONMENT

Uncertainty is a large problem for Multinational Corporations, especially those operating in emerging markets, where market conditions frequently change. The degree of uncertainty depends on how *static*, *dynamic* or *complex* the environment is.

An environment characterised by **static** conditions is not very difficult to understand since changes in market conditions are rare and therefore easy to predict. Such an environment can easily be scanned and analysed on the basis of historical data, since historical events are likely to be repeated or continue over time. As a result, uncertainty in a static environment is often low.

A **complex** environment is characterised by diverse and interconnected factors. As a consequence, changes may be difficult to understand, and a high level of knowledge about the environment is required in order to operate in these complex conditions. The higher the number of influences, the more difficult the environment is to deal with. An example of a complex situation is a company operating in many different countries, all

representing different characteristics. Other factors increasing complexity are environmental influences that are interconnected or dependent upon each other.

Finally, a **dynamic** environment is characterised by a high rate and frequency of change. Operating in a market characterised by a high degree of dynamism forces the company to be more open to changes in organisation and management. When making an environmental analysis, (which we intend to do), it is vital to be aware of the condition of uncertainty. Uncertainty increases with an expanding degree of complexity or dynamism. If combined, complexity and dynamism may create an extremely uncertain environment. To deal with uncertainty in the environment that surrounds the company, it is suggested that scenarios be developed. (Johnson and Scholes, 1988)

The high level of uncertainty that characterises emerging markets is one reason why we have chosen to develop a specific scenario method suitable for multinational corporations acting in these dynamic environments. The scenario development process in itself possesses the power to create an openness and awareness to the possibility of environmental change, and to unfold an appreciation for the necessity of being able to adapt quickly to new environmental circumstances.

#### 2.4 DRIVERS FOR CHANGE

A driving force for change is defined as a variable within a certain cluster that has a high level of explanatory power. All the institutions we intend to describe and explain are linked in a network. The forces driving change in one institution, therefore, often amplify changes in other institutions. According to Fahey (1986, p. 31), shifts in the social segment (e.g. migration of population) may affect the political segment (e.g. distribution of regional power). Each segment, however, can evolve quasi-autonomously (i.e. the forces driving the change are located in the segment itself). Thus, social values may shift independently of technology.

These driving forces for change will have to be defined in order to create the scenarios out of the completed environmental analysis. An assumption we have made is that the opposite of drivers of change should be “Stability Determinants”, that is, factors that counteract change so that the environment remains stable. The “Drivers of Change” and the “Determinants for Stability” will be used in our analysis to summarise the environmental analysis into the level of change that will occur in South Korean society during the five-year period for which the scenarios are constructed.

## 2.5 SWOT-ANALYSIS

Developing scenarios not only requires a thorough knowledge of the environment in which the MNC is acting; the analysis also involves an understanding of the internal strategy of the investigated MNC. The SWOT framework distinguishes between two features of the company's internal environment; its strengths and weaknesses, and two features of the external environment; threats and opportunities (Grant 1998). Knowledge of these factors will help in understanding the company's strategy. A classification of the MNC's strength and weaknesses in handling its turbulent environment will be made, and, at the end of the scenario development process, be related to the opportunities and threats that the created scenarios will bring to light. However, it must be mentioned that there could be difficulties when distinguishing strength from weakness and opportunities from threats. We have tried to overcome this by carefully analysing and appraising the implications of the factors identified.

### 3 THE INSTITUTIONS NETWORK APPROACH

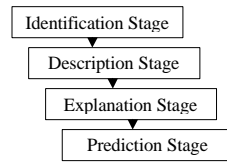
Until now we have described various approaches to scenario development, which all have one aspect in common; they all include elements of environmental analysis. In this chapter we would like to take the scenario development process one step further by introducing the Institutions Networks Approach (Jansson, 1999). This approach to environmental analysis is far more analytical than the concepts described in the previous chapter and suits our purpose very well since it is specifically designed for:

- **Multinational Corporations** (MNCs) acting upon emerging markets
- The specific turbulent environment that prevails in **Emerging Markets**

This model of environmental analysis contains some of the same elements as the earlier presented scenario development models, but, in addition it provides an explanation of how the institutions concerned influence each other, as well as the possibility the Multinational Corporation (MNC) itself has to affect its surroundings. This model, therefore gives a holistic picture of how the environment in all its complexity is interrelated to, and acts together with, the MNC. The emergent market and the MNC are here seen as institutions and networks. (Jansson, 1999)

To enhance understanding of the concept “Institutional Analysis”, we will throughout the thesis refer to the concept as an “Environmental Analysis”.

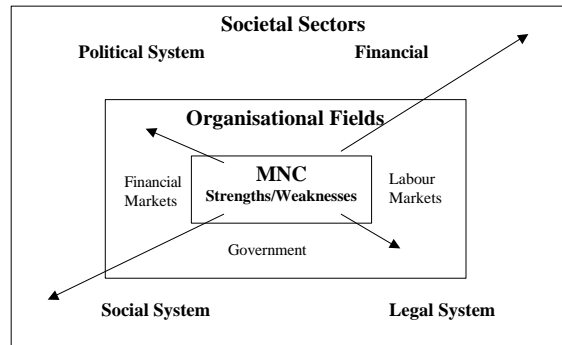
### Stages of Environmental Analysis



#### 3.1 IDENTIFYING THE RELEVANT ENVIRONMENT

It is necessary to choose the perspective from which to make the environmental analysis: Either the inside-out perspective or the outside-in perspective. Jansson (1999) suggests the inside out perspective, which starts with the MNC and then, in a stepwise manner, moves further and further away from the company.

Figure 3.1 Basic Institutions Model



Source: Derived from Jansson (1999)

The institutions we have identified as important for the case company, are those described above. We have used the inside-out perspective in the identification stage of the analysis, because we consider it important to ensure that the South Korean institutions we choose to study are selected out of the perspective of the MNC Volvo CE Korea for which the scenarios will be created.

In the inner field (the Organisational Fields) we have identified the institutions that the case-company has a direct effect on, and in the outer field (the Societal Sector) we have identified those institutions that the case company cannot affect themselves.

### 3.1.1 Models useful for identification of environmental factors

When identifying relevant environmental factors, there are models that will improve the process.

#### 3.1.1.1 The PEST model

The PEST model is often used to describe the macro environment surrounding a firm. It splits the environment into four segments:

1. The **Political** segment deals with political milieu and the regulatory environment
2. The **Economical** segment focuses on the general set of economic factors and conditions confronting all industries in society.
3. The **Social** segment is concerned with demographics, lifestyles and social values of a society.
4. The **Technological** segment focuses on the technological progress or advancements that are taking place in a society. New products, processes or materials; general level of scientific activity, and advances in fundamental science (e.g. physics) are of key concern. (Fahey, 1986)

Fahey (1986) states that all segments are related to each other, but he continues that the model does not, however, specify the types of linkages.

Each individual researcher who uses this model when analysing the macro environment must develop these linkages by him/her self.

The idea of this model is to identify and describe the macro environment and as a next step look for changes. This should be done by first describing the changes, then searching for driving forces, and lastly projecting these into developments in the future. What is useful for with this model is the definition of the change aspect and the drivers for change, which we described in section 2.3.

#### 3.1.1.2 Terpstra's model

Certain cultural models are also possible to use for identification of institutions. The strong similarity between institutional models and cultural models based on a general definition of culture is shown by Terpstra's model (1991). Society is here divided into eight parts:

1. **Law** (e.g. common law, code law, international law, antitrust policy, regulations).
2. **Politics** (e.g. nationalism, sovereignty, power, national interests, ideologies, political risk).
3. **Technology and material culture** (e.g. transportation, energy systems, tools and objects, communications, urbanisation, science, inventions).
4. **Social organisation** (e.g. kinship, social institutions, authority structures, interest groups, social mobility, social stratification, status systems).
5. **Education** (e.g. formal education, vocational training, literacy level, human resources planning).
6. **Values and attitudes**, (e.g. toward time, achievement, work, wealth, change, scientific methods, risk taking).
7. **Religion** (e.g. sacred objects, philosophical systems, beliefs and norms, prayer, taboos, holidays, rituals).

8. **Language** (e.g. spoken language, written language, official language, official language, linguistic pluralism, language hierarchy, international languages, mass media).

Because of this models' similarity to the institutions networks model, it may help in identifying and describing institutions in more detail, even giving clues for the explanation and prediction stages. This relates to the ways in which institutions found in the third rectangle (*The Societal Sector*) influence one another and institutions closer to the MNC (the second rectangle, "*Organisational Fields*"). However, because of its highly descriptive nature and strong similarity to the PEST model, it is useful for the identification stage, and gives a good base for descriptions of institutions.

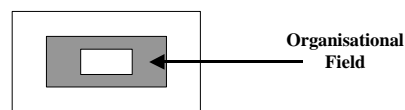
### 3.2 DESCRIBING THE ENVIRONMENT

According to Jansson (1999), the environment surrounding a firm is divided into The Organisational Field and the Societal Sector. Below, we will look into how they are best described.

#### 3.2.1 Describing the Organisational Fields - Markets and Firms

*The MNC's closest environment, in the second rectangle*

Figure 3.2 Basic Institutions Model



Source: Derived from Jansson (1999)

Now, the relevant institutions are identified. The next step is to convert the institutions into an institutional language. This is done by describing the rules, norms and values that control the behaviour of the identified institutions.



**Formal rules** include political rules, economic rules and contracts.

*Political rules* broadly define the *hierarchical structure* of the politics, its basic decision structure, and the special characteristics of agenda control.

*Economic rules* define *property rights*, that is, the bundle of rights to the use and income derived from the property.

*Contracts* contain the provision specific to a particular agreement in exchange.

**Informal rules** are broadly viewed as including codes of conduct, norms of behaviour and conventions.

We have, in this thesis, mainly looked into political and informal rules, as we found economic rules and contracts to be rather regulated in South Korea, where our case-company is situated.

Table 3.1 The Rules aspect

<b>Formal Rules</b>	<b>Political Rules</b>	<b>Economic Rules</b>	<b>Contracts</b>
<i>Describing:</i>	Hierarchical Structure	Property Rights	Following written agreements
<b>Informal Rules</b>	<b>Codes of conduct</b>	<b>Norms</b>	<b>Conventions</b>

Source: Janssons (1999)

The rules aspect is further developed by Jansson (1999) into cognitive, normative and regulative rules. According to this model, four main types of rules control behaviour:

**Frames** (thought styles) How, in this case, Koreans think, and if there are any generalisations that could be made.

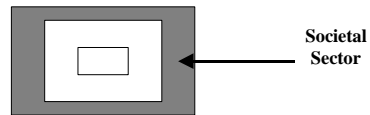
**Normative rules** (Standards, values and norms)

**Regulative rules or Enforcement Mechanisms** (sanctions and incentives)

## Describing the Societal Sector

*The outer environment in the third rectangle*

Figure 3.3 Basic Institutions Model



Source: Derived from Jansson (1999)

Two models that are well suited to describe the cultural environment of an MNC are Hofstede's cultural theory and Janssons's six cultural themes. Here follows a summary of Korean national characteristics that is built on the theories of the above researchers.

Table 3.2 Summary of Korean National Characteristics

Natural Cultural Characteristics	The emerging market SOUTH KOREA
Power Distance	HIGH <ul style="list-style-type: none"> <li>• Central decision-making</li> <li>• Hierarchical structure</li> <li>• Formal business practices</li> </ul>
Individualism/Collectivism	COLLECTIVIST <ul style="list-style-type: none"> <li>• Important to belong to a group</li> <li>• Low social mobility</li> </ul>
Work	WORK IS EVERYTHING <ul style="list-style-type: none"> <li>• Close connection between the employees personal life and the organisation</li> <li>• Energetic</li> </ul>
Morality	SHAME <ul style="list-style-type: none"> <li>• Worst thing that could happen is losing face</li> <li>• Most important is to gain face</li> </ul>

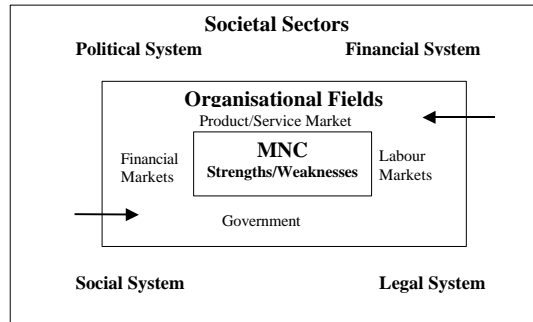
Time	TIME AS A CIRCLE <ul style="list-style-type: none"> <li>• Emphasis on the final result</li> <li>• Building up good relationships</li> </ul>
Uncertainty Avoidance	HIGH <ul style="list-style-type: none"> <li>• Reliance upon directives from above</li> <li>• Following rules is rewarded</li> </ul>
Masculinity/ Femininity	FEMININE <ul style="list-style-type: none"> <li>• Politeness and hospitality important</li> <li>• Humans are more important than profit</li> </ul> MASCULINE <ul style="list-style-type: none"> <li>• Emphasis on education, economic growth</li> <li>• No equality between gender roles</li> </ul>
Causality	HOLISTIC THINKING <ul style="list-style-type: none"> <li>• Either/or-thinking</li> <li>• Sense and sensibility is emphasized</li> </ul>

Source: Hofstede (1994) interpreted by E. Friberg and L. Persson

### 3.3 MODELS USEFUL FOR EXPLAINING THE ENVIRONMENT

In the explanatory stage, we will change perspective to an outside-in mode because the institutions within the outer third triangle (Societal Sector) are high in explanatory power. They explain why the institutions in the second rectangle (markets and firms) have the characteristics that they do. In the explanatory stage, these influences are demonstrated, as you can see in Figure 3.4.

Figure 3.4 Basic Institutions Model

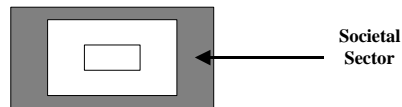


Source: Derived from Jansson (1999)

### 3.3.1 Whitley's explanation of East Asian business systems:

Explaining the Societal Sector

Figure 3.5 Basic Institutions Model



Source: Derived from Jansson (1999)

To be able to explain the various Korean institutions we will now look into The Business System Theory by Whitley (1992). This author holds a view similar Jansson's (1999) as to how the institutions within the societal sector are characterised. The Korean social institutions that have developed through history have influenced the way in which actors on the Korean market behave. The social institutions stem mainly from the pre-industrial

era, but have been influenced to some extent by changes that Japanese colonisation and civil war imposed upon the Korean nation.

#### **3.3.1.1 Pre-industrial influences on Korean institutions**

All the Korean institutions within the societal field have some of the characteristics mentioned below, but they are especially true of the Social System, as it contains factors such as country culture, the Confucian philosophy, behaviour of family/clan and business mores.

##### *High significance of hierarchical status*

The Japanese occupation as well as the military discipline throughout Korean society, has accentuated the strong Confucian emphasis on hierarchies.

The establishment of large managerial hierarchies to coordinate and control the diversified chaebols reflects three features of pre-industrial and twentieth-century Korean society:

1. the importance of Yangban (Aristocrat) status. Its elaborate grading system helped to develop widespread and *intense concern over relative status* in formal ranking systems at least among the ambitious. This has encouraged considerable competition for high ranking posts and thus a greater acceptance of formal hierarchies of managerial positions.
2. This concern for formal rank and status has been reinforced by the militarisation of the Korean society and the extensive fervor of Korean males for military discipline and activities since the '50s.
3. The strong public support and recognition for the chaebol achievements has made employment in them more attractive to college graduates from elite families.

##### *Special competence not highly valued*

In pre-industrial Korea, the educated Confucian classicists did not appreciate the value of specialised competence. Decision-making was instead based on broad diffuse interpretations of the Confucian classics.

The elite (leaders) had thus no interest in achieving technical skills, as this could not improve their moral worth. There were also no rules, norms or procedures on how to deal with administration.

*Leaders legitimise their position by moral superiority*

The rulers in pre-industrialised Korea adopted Confucian ideologies, which confirmed their superior moral worth and virtue. This high moral worth legitimised their right to rule. By controlling the interpretation of the Confucian classics and the examination systems, the elite effectively controlled the definition of high moral and virtue, and hence authority. Thus, they had full control over who could achieve leading positions in the Korean societies. Questioning the action of a leader simultaneously leads to questioning of the leaders moral...

*Conflicts are highly personal*

The Korean emphasis on moral worth rather than technical knowledge meant that conflicts were/are highly personal, and concerned more with general qualities of individuals than the merits of their particular actions. Thus, criticism of decisions and suggestion of alternatives were/are more seen as personal attacks on the integrity of the leader than as a relatively technical discussion of the advantages of different choices. As elite membership in Korea automatically included a high level of moral worthiness, debate and discussion of a leader's actions is impossible, except as an attack on his moral status.

*Scope and distance of authority relation*

Whitley suggests that Korean leaders appear remote, and are expected to deal single-handedly with all their problems. Total obedience to the patriarchal leader is expected in these companies. Our own experiences, however, coincides better with what Pye (1985, p. 67) states about the Korean leadership type: "...like the Japanese leader/father, he is expected to be sympathetic, nurturing, and sensitive to the wishes of his

followers/family". Thus, omnipotence and strength are somewhat tempered by emotional obligations, according to this view.

*Emphasis on central direction and planning*

Korea used to be dominated by central "bureaucratic" dynasties of Emperors and Kings who both reigned and ruled, today, the power is still concentrated in the central state in Seoul. The President is seen as the unquestioned leader, and each president tends to form his own constitution, reflecting his singular vision of the presidency and his distinctive ruling style. This executive authority thus becomes remarkably free from either bureaucratic or legislative constraint. This has enabled development goals to be implemented extremely quickly, but also, of course, has intensified traditional Korean dependence on the central state.

*Nurturing of state connections*

The Korean conglomerates (the chaebols) that have had the best relationship with government officials have been the most likely to grow on the market. Firms compete with each other directly through the market as much as indirectly through the central state, thus creating competitive advantages by establishing good relations with high government officials. Establishing long-term links with industry partners has been secondary to seeking political allies.

*Low degree of trust between non-kin*

The development of long-term commitments between firms depends on relative stability and assurance that such commitments will be shared in the future. Private wealth is subject to expropriation and future success is liable to the outcomes of palace intrigues; family members are the only ones who can be fully trusted. Therefore, even today Korean companies are mainly controlled by familymembers. Cooperation with other companies, such as strategic alliance, is more or less non-existent, as is vertical cooperation with suppliers or customers. If such co-operation exists, it is

mostly because relationships between the parties have been cultivated for long time, including a high degree of socializing to build a “family”.

### 3.3.1.2 The Industrialisation – a time of drastic changes

The pre-industrial institutions in Korea have lost some of their importance in the time of industrialisation. Korea essentially lacked many of the components that enabled other countries to go through the industrialisation process. They lacked the *specialist competence* due to the Confucian ideal of broad general knowledge as base for moral superiority of the leader, as well as a functioning bureaucracy that established *standard rules and procedures* to organise its activities and provide a stable predictable framework for economic development. The Japanese changed this to a certain extent when they occupied Korea in the ‘30s and ‘40s.

#### *The impact of Industrialisation on Korean Institutions*

The Japanese forced an industrialisation process mainly directed towards supporting Japanese expansion in mainland Asia, and dominated by Japanese capital and personnel. The Japanese owned about 90% of all the corporations in Korea, and modernised the Korean economy while reinforcing the patrimonial nature of Korean society (Jacobs, 1985, p. 162-70). The insecurity and instability of local enterprises during Japanese colonialism encouraged a *reliance on close family ties* among top managers as well as intense *nurturing of state connections* characteristics, which has continued into modern times.

The Korean War destroyed most of the industrial infrastructure developed by the Japanese, generated further massive movements of the population, expanded the military and established intense *factionalism and thus corruption*. It also, though, focused US political attention on Korea in a way that had not been apparent during the Japanese occupation. This led to the establishment of new training centres and an Americanisation of the army, which had major consequences. The reopened Korea Military Academy systematically set out to produce an officer class that had *high*



*cohesion, group loyalty and a strict code of conduct.* It became “a kind of island off Korea’s moral coast, governed by standards quite different from those of the society around it” (Henderson, 1968, p. 353). Gradually, the Korean military standardised recruitment and training procedures developed some career specialisation and *reduced the importance of personal favouritism in promotions* (Henderson 1968, p. 352-354). This systemic organisation of the Korean armed forces produced a powerful and cohesive social institution committed to economic development for the first time in Korea’s history. The courses of the National Defence College and other training for military elite developed skills in administration, control and decision-making, as well as emphasising development goals and the backward state of the Korean economy. The traditionally low prestige of the military in Korean society led to a much stronger commitment to economic development goals than in many military dictatorships (Steinberg, 1989, p. 129).

#### *The Hahn-Spirit*

The period of Japanese oppression led to a special force, driving the Koreans to perform to their utmost in a very competitive way. This driving force can be expressed in one word – *Hahn*, or the “can-do spirit.” Today, this makes up the psychic force motivating and energising the Koreans. The Hahn-spirit can partly be seen in the Korean drive for higher education. It has driven the South Koreans to work very hard, loyally and for long hours, as a sacrifice for their family and their country. (De Mente, 1989)

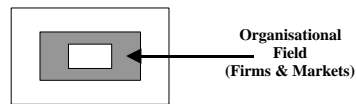
These pre-industrial and industrial influences will be used to explain the behaviour, rules, norms and values of the institutions within the Organisational Field (the second rectangle).

#### **3.3.2 Whitley’s Explanation of East Asian markets**

This field contains the markets and market actors that constitute the closest environment surrounding the MNC. There is a separation between

product/service market networks, financial market networks and labour market networks. The institutions within this field have a direct impact upon the MNC, as well as being affected by themselves.

Figure 3.6 Basic Institutions Model



Source: Derived from Jansson (1999)

Whitley (1992) gives some characteristics of the East Asian Markets and firms.

- **The extent of long-term co-operative relations between firms within and between sectors.** Markets are normally described as consisting of conflict-oriented relationships of short-term duration, and as being of an ad-hoc type, where economic agents change partners continuously with the shifting of prices. *However, in many cases, the opposite situation prevails, that is inter-firm relationships are long-term and co-operative.*
- **The degree to which relationships are personal and trustful.** In many emerging markets, relationships are more personal and dependent on individual trust than they are in more impersonal Western societies, characterised by organisational trust.
- **Types of actors,** for example the significance of intermediaries in the co-ordination of relationships
- **Important characteristics of major actors,** for example the stability, integration, and scope of business groups. Where large business groups dominate markets, as for example in South Korea, a substantial part of the domestic market network is internalised and monopolised by a few economic agents.

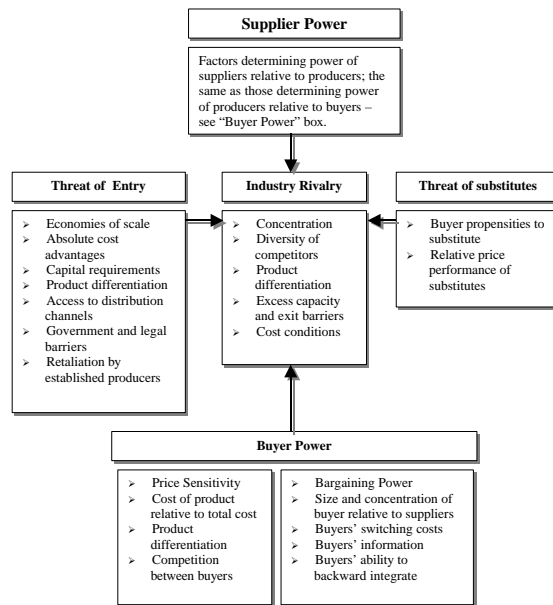
### **3.3.2.1 Product/Service market networks**

The factors just mentioned are applicable to all types of markets. Applying an economic theoretical model will further explain the product/service market. We want to achieve an overall picture of the Korean construction equipment industry, and thus we chose Porter's five forces model as a tool for analysis.

#### *Porter's five forces model*

According to Porter (1985), the construction of scenarios begins with an analysis of the current industry structure and identification of all uncertainties that may affect it, such as competitive forces. These competing forces are illustrated in figure 3.7.

Figure 3.7 Porter's Five Forces



Source: Grant (1998)

### 3.3.2.2 Financial market networks

Whitley characterises the financial market by separating it into the **capital market** - and **credit based financial systems**. The former is controlled by the market, and prices of financial assets are mainly set by market competition. Financial transactions are impersonal and rather short-term.

These types of financial market networks are mainly found in Anglo-Saxon countries.

The **credit based financial system** is characterised by the long-term relationship between banks and larger borrowers conducting financial exchange. This kind of financial system is found in South Korea.

### 3.3.2.3 Labour market networks

Whitley (1992) differentiates between two types of labour market networks: **market-based** and **organisation-based** reward systems. The purpose of this distinction is once again to separate market based and non-marketbased systems. In the first type, individual professional and craft competencies are more important, and individuals are more aware of their market value. In the organisation-based reward systems, labour market issues are mainly decided not by the market, but by individual organisations. For example, in many emerging Asian markets, it is the employer alone who makes these decisions.

### 3.3.2.4 Government Networks

MNC strategies towards government are aimed at influencing government decision-making and policies. If the MNC succeeds with this, they will achieve a competitive advantage. This competitive advantage could be over both domestic competitors and other MNCs that decide to enter the market. To achieve this, the MNC must set up effective networks with the government. The adaptation to, or influence over, government decision-making could give the MNC access to vital resources, for example, different kinds of permits to operate in the country or to locate a plant in a particular area.

In the next chapter we will describe the research design we have chosen in order to complete this thesis.

#### 4 METHODOLOGY

The purpose of this chapter is to explain and justify the way we have progressed in our studies. It will explain how we worked our way through the thesis, and explain why we chose this way of conducting our research. In the end of this chapter under section 4.7, the method of scenario development will be explained.

##### 4.1 RESEARCH STRATEGY

According to Yin there exist five relevant strategies for research: experiment, survey, archival analysis, history and case studies. Each strategy has advantages and disadvantages, but what distinguishes the strategies are: the type of research question posed, the extent of control an investigator has over actual behavioural events, and the degree of focus on contemporary (as opposed to historical) events. (Yin, 1994)

##### 4.1.1 A Case Study

Yin argues that a case study is favoured when a phenomenon is to be studied as it occurs in a real life situation. The boundaries between the phenomenon and its context are not clear, but the case study can be seen as covering both the phenomenon and the context in which it occurs. A case study is best used when a “how” and “why” question is being asked about a contemporary set of events over which the investigator has little or no control. (Yin, 1994)

The case study can be *inductive*, *deductive* or *abductive*. An *inductive* case study is used when building a theory. Since no theories yet exist on the specific topic, the researcher has to develop a new theory. This facilitates the intensive analysis and does not limit the researcher to some specific variables, which in turn increases the probability of finding critical variables and relations. (Merriam, 1998) On the other hand, when the researcher wants to find information that suits existing theories, the case study is *deductive*. When doing this, the researcher should prepare the case study by researching the literature related to the topic at hand. When a case

study is built on new or developed theories as well as old theories, it is called an *abductive* case study. Information is collected and existing theories inspire the building of a new theory. Modifying the existing theories according to one's practical knowledge, which means penetrating the problem from different perspectives. often gives interesting results. (Merriam, 1998)

There are a certain number of theories surrounding the concept of scenario development, but they are loosely coupled and do not have full relevance to our main problem. In this case study we mainly used one model, which has not been previously tested as a base for scenario development. Our main focus was to develop this model by adding a method that describes how to create scenarios. Putting the pieces together, this case study became abductive, in the sense that it is built up both from deductive and inductive studies. The interviews we conducted were combinations of qualitative and quantitative questions. In the in-depth interviews mostly “why” and “how” questions were asked. The quantitative part actually had qualitative aspects as well, because each question in the questionnaire was not only filled in, but also thoroughly discussed to make sure that we received the full spectrum of the respondent's view. The in-depth interviews provided us with explanations of important company-internal and environmental questions.

#### **4.1.1.1 Case study design**

A research design is the logic that links the data to be collected and conclusions to be drawn to the initial questions of a study, and could therefore be seen as an action plan for getting from the initial stage to the final conclusion. Each case study is a separate research strategy that has its own research design; a research design is defined as “*a plan that guides the investigator in the process of collecting, analysing and interpreting observations.*” (Yin, 1994) Yin discusses four types of design for case studies; single-case holistic design, single-case embedded design, multiple-case holistic design and multiple-case embedded design. (See figure 4.1).

Figure 4.1 Basic types of design for case studies

	Single-case design	Multiple-case design
Holistic-Single unit	<b>Type 1</b>	<b>Type 3</b>
Embedded Multiple units	<b>Type 2</b>	<b>Type 4</b>

Source: Yin (1994)

To begin with, a distinction is made between the single-case and the multiple-case design. Firstly, a single-case design is advantageous when *“the case represents the critical test of an existing, well formulated theory, when the case represents a rare or unique event or when the case fills a revelatory purpose”* (Yin, 1994, p.19). The multiple-case design is used when the same study contains more than one single case. Secondly, Yin makes a distinction between holistic and embedded design. The embedded design is preferred when the same case study involves more than one unit of analysis. These units can be selected through sampling or cluster techniques, or by other criteria. If only one unit of analysis is examined, the holistic design is used. Further more, the case study is of holistic design if no logical sub-units can be identified, and when the theory underlying the case study is holistic in nature. (Yin, 1994)

In this case study we have used an embedded single-case approach as a research design, with Volvo Construction Equipment Korea being the focal company. The study consists of several units of analysis connected to the case company, such as the nature of the Korean business environment and the internal strategy of Volvo CE Korea. The environmental units of analysis involve a description and explanation of markets and non-markets upon which Volvo CE Korea is acting, as well as analysis of the impact that the societal sector has upon these markets.



#### 4.2 SCIENTIFIC APPROACH

There are several different possible approaches in the research process. The explanatory, descriptive or causal approaches are the most relevant in our type of research design. When the researcher has very limited knowledge about the research problem, an exploratory research approach can be used. Exploratory research is common in the initial phase of the research process, and is often used when conducting pre-studies for further research. The exploratory approach is characterised by a high grade of flexibility and an ability to deal with the unexpected, and is often applied when defining the problem area and problem questions. Both secondary and primary sources are commonly used in the exploratory approach. A descriptive approach is advantageous when the purpose is to explain different phenomena, make predictions or show connections between variables. The descriptive method further outlines characteristics of a certain phenomena and tries to determine the frequency of its occurrence. Finally, the causal research approach is used when trying to explain, generalise and determine causalities between different phenomena. The cause-and-effect relation is central in the causal research approach.

In the initial phase of our research process we had difficulties in designating the precise research area and main problem. Therefore, we began with an exploratory research approach to determine whether there were any existing theories that could be used in the process of developing scenarios for MNCs in emerging markets. In the exploratory phase we obtained information, both primary and secondary, by conducting open interviews at Volvo CE's head quarter in Brussels. By using this approach, we were able to remain flexible and open to different perspectives. After research in this area we began using a descriptive approach, with which we described the process and stages of developing scenarios for our case company. Finally, we also used a causal research approach as writing scenarios mainly involves the determination and explanation of logical cause-and-effect relationships between different environmental occurrences.

### 4.3 RESEARCH METHOD

Both qualitative and quantitative research methods are aimed at giving a better understanding of a certain problem. An important note is that the case study strategy should not be confused with qualitative research. Instead, case studies can be based on any mix of qualitative and quantitative evidence.

Qualitative research is based on data that cannot be quantified. This kind of data is often called “soft” data and includes attitudes, values, beliefs and other types of data of an emotional character. The purpose of qualitative research is to understand the core of an occurrence or experience. The qualitative method is used in an attempt to understand how the different parts co-operate to create a whole. When using a qualitative research method, the researcher collects a great deal of information about just a few research units, and then examines it in-depth. (Holme, 1997) We used a qualitative study in conducting in-depth interviews in order to get information about how our case company interrelates with the Korean environment. To understand the perspective of the investigated MNC, it was important to get the viewpoint from as many functions in the company as possible. We tried to interview various people in different key-positions within Volvo CE Korea, so that we could benefit from many views and perspectives prevailing within the company.

Fundamental to the quantitative method on the other hand is that the researcher is in control and defines what relationships are of particular interest from the questions asked. In the quantitative method, the researcher collects less information about a larger amount of research units, making the study broader. (Holme, 1997) To generate a picture of what our respondents thought about the future of their company, we presented a questionnaire that included 20 statements. We wanted to see whether the respondent believed these statements or “Key Factors” as we called them, to be important for the future success of the company. The Key Factors that our respondents classified as “most important” were used as a starting-

point, and now constitute the backbone of the created scenarios. We wanted to quantify the data as much as possible without statistically validating it, to get an idea of the perspectives of the future held by people employed at strategically important positions in the company.

#### 4.4 DATA COLLECTION

Data can be collected from either primary or secondary sources. If many different sources are used in the collection of data, it is considered to possess higher validity, since the sources confirm one another.

##### 4.4.1 Primary data

Primary data collected by the researchers in order to solve a the specific problem. It is new data that has not been used before, and may consist of observations, interviews or surveys. (Merriam, 1998) We have used in-depth interviews combined with questionnaires to fulfil our stated purpose. These interviews, that included careful examination of the questionnaires, usually lasted between one and two hours.

##### 4.4.1.1 Interviews

One of the most common techniques of primary research is the interview. Interviews are especially common when the intent is to obtain in-depth information. (Merriam, 1998) Interviewing gives the opportunity to check back directly with the respondents, and to use different questioning techniques. There are many different types of questions that could be asked during an interview; among them are introduction questions, follow-up questions, probing questions and specifying questions. (Kvale, 1996) We began our interviews with introduction questions to give our respondents an idea of our knowledge of the area, and thus finding a point from which to move on. We proceeded with follow-up questions when the respondent sounded unsure and/or we wanted to penetrate the subject further. Since we already had a basic knowledge of the Korean environment and the case company, we also used probing questions, where we made statements for the respondents to elaborate on.

Interviews can be structured, non-structured and semi-structured. In structured interviews, the same questions are asked of all of respondents, and it is possible to quantify the answers. You may want the interviewees to respond to particular statements or to define certain concepts or terms. Secondly, there are the non-structured interviews. These are more flexible since the questions are unspecified, and thus can be formed and adapted during the interview. These interviews are arranged by a number of questions, which are to be analysed, but no specific formulations are pre-determined. This type of interview allows the researcher to respond to a changing situation, to an emerging world-view of the respondent, and to new ideas on the topic. Thirdly, there are unstructured, informal interviews. These are very useful when the researcher does not know enough about a phenomenon to ask relevant questions. Thus, there are no predetermined questions and the interviews are primarily conducted for exploratory purposes. The main reason to perform unstructured interviews is to learn enough about a situation to formulate questions for later interviews. Thus, this kind of interviewing technique is mainly used in the early phase of a case study. (Merriam, 1998)

We conducted a number of interviews with people in key positions who have knowledge about our area of research. In the exploratory phase, we conducted interviews at Volvo Construction Equipment's headquarters in Brussels. In this initial phase of our research process, we had difficulties designating the precise research area and main problem. Hence, the interviews were of an informal, unstructured character to help us to gain the insight necessary for formulating our main problem, and thus the understanding necessary for forming questions for the later interviews in Korea. When arriving at Volvo CE's Head Office in South Korea – Seoul, we had prepared for a combination of semi-structured and structured interviews. Out of our 13 respondents, 10 were given a questionnaire with 20 statements, which they graded according to their importance. The

questionnaire can be found in Appendix I. The statements were seen as uncertainty factors, or as we have chosen to name them, Key Factors for Volvo CE Korea's future success. The statements were simultaneously discussed to discover the world-view that each respondent possessed. At the end of each questionnaire, some empty space was left for the respondent to fill in other statements that he personally found to be of greater importance than the ones we had proposed. The interview continued in a semi-structured mode, in which we asked in-depth questions about Volvo CE Korea's internal strategy and about the company's business environment. The in-depth questions made it possible to penetrate the subject more deeply, and the respondents were able to give us more detailed information.

#### *Sampling*

To be able to conduct a single, embedded case study, certain areas and different perspectives have to be covered. The sampling was made in a non-random judgmental mode, where the respondents were chosen according to their practical knowledge of the unit we wanted to examine

Table 4.1 Respondents and purpose of the Interviews

<b>Position within MNC</b>	<b>Purpose of the interview</b>	<b>Type of interview</b>
Manager Human Resources Changwon Plant	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Executive Manager Research and Development Changwon Plant	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions

Director Manufacturing Changwon	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Executive Managing Director Overseas Operations Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Managing Director Korean sales company Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Vice President Human Resources Management Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Chief Financial Officer Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Senior Advisor Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
Vice President Customer Support Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions
President Volvo CE Korea Seoul Head Office	Confirm Key Factors	Structured interview filling in questionnaire, combined with open-end follow-up questions

Labour Union representatives Changwon Plant	Achieve information about Labour situation, both within the case company and more generally	Semi structured interview Open-end questions
Vice President Business Development Volvo CE Headquarters Brussels	Achieve knowledge about the case company's strategy	Unstructured Interview
Executive managing Director – Plant Division Samsung Heavy Ind.	Achieve a broad knowledge about environmental issues	Semi structured interview Open-end questions
Executive managing Director – Human Resources Samsung Heavy Ind.	Achieve a broad knowledge about environmental issues	Semi structured interview Open-end questions

Source: Own source - For Key-factors and in-depth questions see Appendix I.

#### 4.4.2 Secondary data

Secondary data is data that already exists; examples of this are books, articles, journals, previous studies, and statistics. We mainly collected data from the Economics library at Gothenburg University, from databases like Financial Times, ABI/Inform and Helecon. To continuously follow the development of the Korean institutions, we used business magazines and newspapers such as Far Eastern Economic Review, Asia week, and Korea Herald. The Internet provided a mass of information that we had to analyse critically.

##### 4.4.2.1 Structured search for secondary data

We collected secondary data in the initial research phase, guided by the theoretical framework “the Institutions Network Model.” This framework was used as a base from which we extracted the Key Factors that were judged by our respondents to be of importance for Volvo CE Korea's

future success. The Key Factors were then used as an instrument for conducting both structured and semi-structured interviews. The questionnaires containing Key Factors were thus used as tools for testing our own view against the respondents', and asserting whether the Key Factors would have a future impact upon Volvo CE's situation in Korea

#### 4.5 QUALITY OF RESEARCH

No matter what strategy and method is chosen, the researcher must do everything possible to ensure that the analysis is of the highest quality. The quality is often measured in terms of the research's validity and reliability. Validity and reliability, in a case study, are based on the researcher's ability to plan the study, his/her analytical skills, and the conclusions that are drawn. A qualitative investigation should provide the reader with a detailed description, which makes it possible for the reader to decide whether the conclusions drawn are logical or not. (Merriam, 1998)

##### 4.5.1 The Validity Concept

Validity is normally defined according to whether a measuring device (for example, a questionnaire) actually measures a concept of a theory. Thus, validity concerns whether a developed framework is a relevant representation of reality. Since validity is a broader and more difficult issue than reliability, there are three measures or tests that will actually facilitate the measure of the validity concept. (Merriam, 1998)

##### 4.5.1.1 Construct Validity

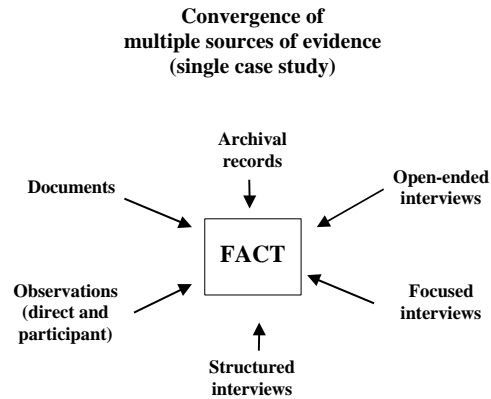
Construct validity is a measure and evaluation of the research that involves the establishment of correct constructs for the reality being studied (Yin, 1994). This may in some instances be quite difficult, and a way to strengthen this aspect is to use multiple sources of evidence. Thus describing the same fact or phenomenon through the use of different methods and paths will aid in the gathering of convincing and underlying information.



*Multiple sources of evidence – Triangulation*

Any finding or conclusion in a case study is likely to be much more convincing and accurate if it is based on several different sources of information. Triangulation provides multiple measurement of the same phenomenon (see Figure 4.2). (Yin, 1994)

Figure 4.2 Triangulation: Rationale for using multiple sources of evidence



Source: Yin (1994)

We have analysed many types of evidence, so the case study's findings are based on the convergence of information from different sources, both quantitative and qualitative. These multiple sources of evidence include structured questionnaires stating Key Factors for future success, open-ended interviews, and personal observations made about the Korean environment and the case company.

Construct validity of studies is often criticised because “subjective judgements” are used when collecting data (Yin, 1994). We have overcome this by using a theoretical model as a framework for secondary data collection. This framework was used as a guide when collecting data, as well as a base from which we extracted the Key Factors. The Key Factors were then used as an instrument for conducting both structured and semi-structured interviews. The questionnaires containing Key Factors were thus used as tools for testing our own view on whether these factors would have a future impact upon Volvo CE’s situation in Korea against the respondents’.

#### **4.5.1.2 Internal Validity**

Internal validity is a concern only for explanatory studies in which the researcher tries to determine whether event x led to event y. If the investigator incorrectly concludes that there is a causal relationship between x and y, overlooking some third factor z may actually have caused y, the research design has failed to deal with some threat to internal validity. (Yin, 1994)

We are investigating causal effects in our study, chains of events within and in-between the Korean institutions we have examined, but we are aware of the complexity both of the Korean environment and of the MNC examined. This complexity makes it impossible to achieve full internal validity, as there are too many independent variables to consider. Our purpose when creating scenarios though, is not to *prove* any causal effects, but to point out the possibility that the predicted chains of events might occur.

#### **4.5.1.3 External Validity**

External validity deals with the problem of generalising study’s findings beyond the immediate case study. Is the research applicable to other situations than the examined case? (Yin, 1994)

Since this thesis is about the process of developing scenarios for the MNC Volvo CE acting in the Korean market, we believe that the research is generalisable to any MNC acting in a similar environment, that is, an emerging market. We believe that Multinational Corporations acting in this kind of turbulent environment can use this theory to obtain extended knowledge about the complexity of their current market environment, as well as preparing themselves for possible changes, which could call for modifications of their present strategy. However, the fact that we only conducted one single-case study limits the possibility of generalisation.

#### **4.5.2 Reliability**

The reliability of research findings is a measure of the extent to which the findings could be replicated: that is, whether if the measurement process is free from random errors. The question is, can the result be repeated?

This case study has a varying degree of reliability due to two factors. First, the Korean environment that we have analysed is of a dynamic nature. It is difficult to achieve the same conditions when the market is constantly changing. Secondly, communication problems arose when we conducted interviews with some Korean respondents using an interpreter. Even if the interpreter were skilled, there might be nuances in questions and answers that have been filtered away, causing disturbances in the two-way communication process. To secure reliability in this sense, we taped all interviews and wrote each interview down, word by word, before analysing the material. Another way for us to secure reliability was the use of questionnaires in connection with the interview; this partly quantitative method contributed to an objective approach when evaluating the findings.

#### **4.6 POSSIBLE TYPES OF ERRORS**

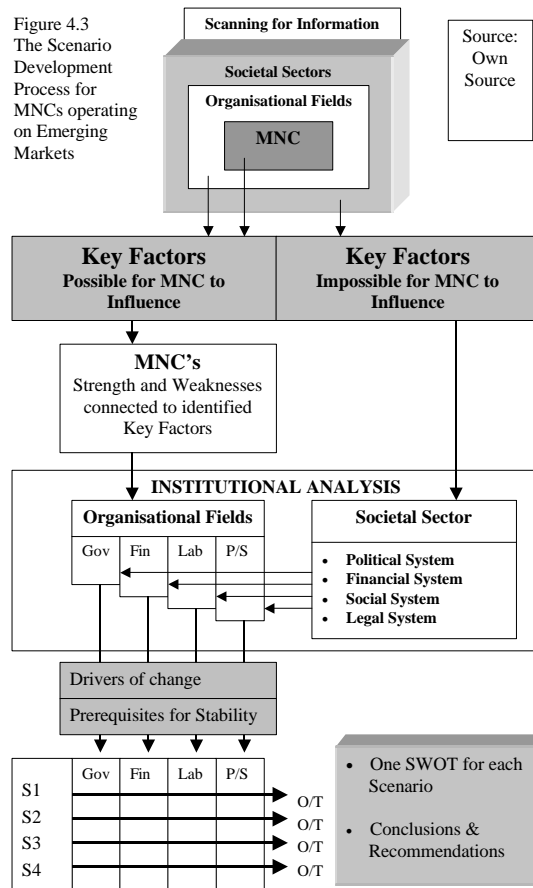
When conducting a case study, there may be various types of errors stemming from the collection of data and how it is interpreted. In the identification stage of the institutional analysis, we were confronted with the problem of selecting relevant data for the analysis. In the later

descriptive and explanatory stages, we had to deal with the complexity of explaining how these institutions affect each other. The complexity of the researched area led to the possibility of misunderstandings and misinterpretations when conducting interviews especially the interviews with non-English speaking Koreans. In an attempt to overcome these, careful explanations of the questions were made. To overcome the language barriers, we reformulated some of the questions and asked the respondents to repeat answers that seemed inaccurate. In this case study, secondary sources were used extensively, and this could lead to possible errors. We have tried to avoid this by citing all sources completely. This study could also contain errors based on human factors. One possible source of error comes from the fact that the interviewee, being an expert, might not be able to fully express himself in terms that could be understood by laypersons.

#### 4.7 THE SCENARIO DEVELOPMENT MODEL

In this section the scenario development process is described step by step. The scenario development process has been summarised in Figure 4.3. Each phase in the model is thereafter explained.

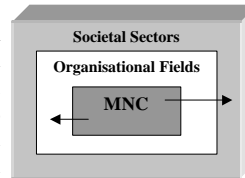
Figure 4.3  
The Scenario  
Development  
Process for  
MNCs operating  
on Emerging  
Markets



#### 4.7.1 The Scenario Development Process

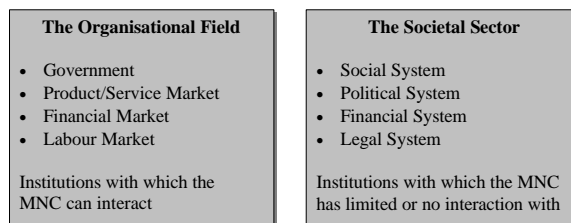
##### 4.7.1.1 Scanning the environment

To get an overview of the environment from the perspective of the Multinational Corporation (MNC), an Environmental Analysis is made. In this stage, it is vital to scan the environment for factors that are believed to have a direct impact on the MNC examined.



- Determine which surrounding institutions have the greatest impact on the firm. This is an inside-out process where the MNC is in the center, and from the viewpoint of the MNC, it is decided which institutions are of importance.
- Scan the environment for information that describes those institutions.

The institutions are divided into two main groups: firstly, those that the firm has a chance to interact with (The Organisational Field), and secondly, those institutions over which the firm has no influence (The Societal Sector). (See section 3.1 - 3.1.1.2)



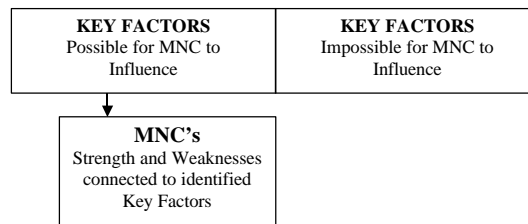
#### 4.7.1.2 Which are the Key Factors for future success?

When an overview of the external environment is achieved, the focus turns to extracting the factors from the material that are the essences of each institution. Those extracted Key Factors should be crucial for the future success of the MNC examined (See Appendix I. for Key Factors) The Key Factors that may be influenced by the MNC are also the factors that, to a great extent, are internal to the firm, and thus part of the internal strategy.

- Creating an Industrial Hub in the region
- Gaining access to the Korean domestic market

#### 4.7.1.3 Strengths and Weaknesses

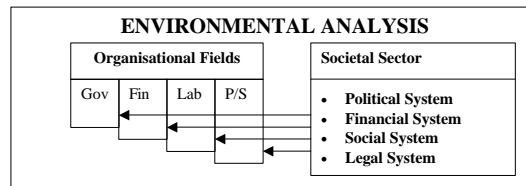
The MNC's strengths and weaknesses are connected to the internal Key Factors. The company's strengths and weaknesses in handling its environment are stated here. At the end of the scenario-development process, the strengths and weaknesses will be related to the environmental Opportunities and Threats that each of the four scenarios imposes on the MNC (See chapter 5).



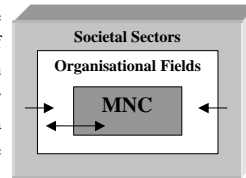
#### 4.7.1.4 Environmental Analysis

The next step, and the largest part of the scenario development process, is the Environmental Analysis. In this phase we will analyse the impact of the Societal Sector on the Organisational Field, as well as the influence that the

environment has on the MNC. This section is very important, because here we will reach an understanding of how the marketplace really functions. We will, for instance, see how the cultural and social environment affects labour and government behaviour in the country we examine. Now, the internal and external Key Factors are brought together in an institutional context, and their influence upon each other is analysed.



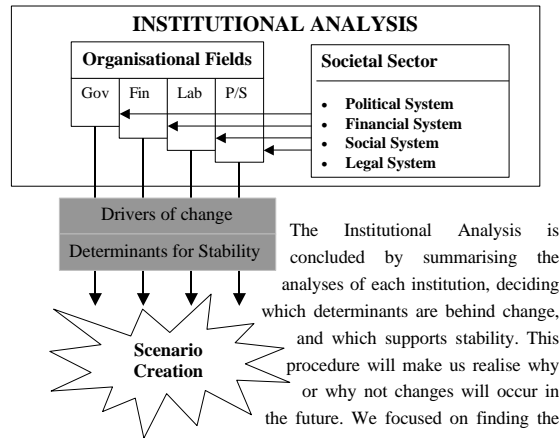
In this phase, the institutions within the Societal Sector will explain the behaviour of the markets and non-markets within Organisational Fields. An example is how the social system and country culture of a nation affect the behaviour of the government, and how the government, in turn, affects the MNC acting in the same country. It must be noted that there is always an interaction taking place between the MNC and the markets and non-markets within the Organisational Fields. That is, referring back to the previous example, the MNC can influence the way government behaves towards them (See section 3.3.1.1 – 3.3.1.2).



#### 4.7.1.5 Drivers of change

Before beginning to create the scenarios, the Institutional Analysis must be concluded.





The Institutional Analysis is concluded by summarising the analyses of each institution, deciding which determinants are behind change, and which supports stability. This procedure will make us realise why or why not changes will occur in the future. We focused on finding the Drivers of Change within the markets and non-markets inside the Organisational Field. This field, due to the explanatory process that took place in the Institutional Analysis, already contains aspects from the outer Societal Sector. The Drivers of Change “carry” the Institutional Analysis into the future by highlighting the determinants within each Institution that could bring about change. At the same time, the determinants that act as stabilising forces are pointed out. They have a neutralising effect on the Drivers of Change and must also be considered when creating the scenarios. (See section 6.3.1.1)

Examples of this could be how these determinants either drive or prevent environmental change by, for instance, going from a closed, state-controlled economy towards an open market economy. (See Table 4.2.)

Table 4.2. Exemplifying Drivers for Change and Determinants for Stability

Institutions within the Organisational Field	Drivers of Change	Stability Determinants
Financial Markets	Financial crisis	Protectionism
Labour Markets	Performance based salary systems	Country Culture Social values and norms
Product/service Market	Globalisation	Low level of innovation

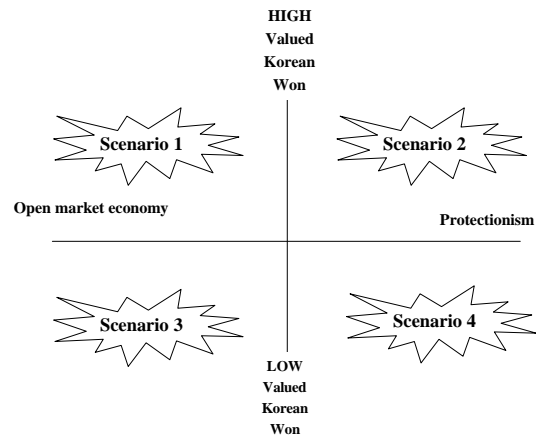
Source: Own Source

These determinants are a summary of the Institutional Analysis, and should be borne in mind when creating scenarios, as they will colour the content of each.

#### 4.7.1.6 Scenario Creation

After the Institutional Analysis is carried out, emphasis is put into the actual creation of scenarios. In our case, the 20 Key Factors were judged by our respondents, as to how important they were for Volvo CE's future success in Korea. The two factors that were experienced as ultimately important were put together in a matrix containing two axes. (See Figure 4.4.)

Figure 4.4. The Scenario Matrix



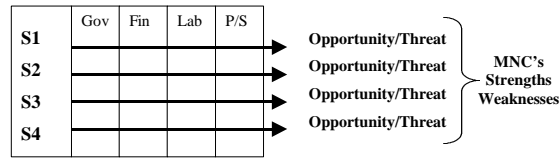
Source: Derived from Schwartz (1991)

Each of the four scenarios is then built up around the four institutions within the Organisational Field; Government, Financial Markets, Labour Markets and Product/Service Markets (See chapter 7).

Societal Sector				
Organisational Field				
	Gov	Fin	Lab	P/S
S1				→
S2				→
S3				→
S4				→

#### 4.7.1.7 Assessing future Opportunities and Threats

When the scenarios have been written, it is time to discuss each one and look more deeply into how the environment affects the MNC. Hence, each scenario is scrutinised for the threats and opportunities it will impose upon the MNC, with its strengths and weaknesses in handling its environment (See section 8.1.1 – 8.1.4)



From this, conclusions are drawn about how the MNC can react and adapt when it encounters environmental change. The focal point of the scenario development process is not to create an action plan. It is more concerned with creating an awareness that the environment in which the MNC acts is not static, and that the capability of fast adaptation could be the only sustainable competitive advantage for MNC's acting upon emerging markets.

## **5 STRENGTHS AND WEAKNESSES OF VOLVO CE KOREA**

The purpose of this chapter is to describe Volvo CE Korea's strengths and weaknesses in interacting with the complex and dynamic emerging market-environment.

Developing scenarios requires more than just a thorough knowledge of the environment in which the MNC operates. The analysis also involves an understanding of the internal strategy of the investigated MNC. The strengths and weaknesses of Volvo CE Korea will be described according to the internal Key Factors that our respondents agreed were of importance.

### **5.1 KEY FACTORS FOR FUTURE SUCCESS**

The Key Factors that we used in the questionnaire were extracted from the general Institutional Analysis we made from secondary data before going to Korea and interviewing our respondents. From our general Institutional Analysis we derived basic knowledge that, along with an evaluation of Volvo CE Korea's strategy, made it possible to determine which factors were most significant for Volvo CE Korea's success for the next five years. In the interviews, our Key Factors' relevance was confirmed, with a few exceptions and additions. The Key Factors were divided into two groups. The first group contains Internal Key Factors that lie within Volvo CE Korea's power to influence, while the second group contains External Key Factors that they cannot influence.

Internal Factors possible to influence impossible	External Factors to influence	Factors
<ul style="list-style-type: none"> <li>• Global player</li> <li>• Price competition</li> <li>• Keeping delivery agreements</li> <li>• Competitive product</li> <li>• Financing to customers</li> <li>• Increased R&amp;D</li> <li>• Domestic suppliers</li> <li>• Relationships</li> <li>• Accounting standards</li> <li>• Performance based Salary system</li> <li>• Human resources</li> </ul>	<ul style="list-style-type: none"> <li>• Functioning Financial System</li> <li>• Business Cycle</li> <li>• Globalisation of markets</li> <li>• Political reform</li> <li>• Discrimination of FDI</li> <li>• Exchange rate</li> </ul>	

The Key Factors from the first group will be further elaborated, as they are a starting point for discerning the strength and weaknesses within Volvo CE Korea. This first group of Key Factors will also be used in structuring the contents of the institutions within the Organisational Field. The Key Factors in the second group, those that are impossible to influence, will steer the orientation of the material in the institutions that lay within the Societal Field of the Institutional analysis (See 4.7.1.4).

## 5.2 STRENGTHS AND WEAKNESSES

The Key Factors were presented to our respondents for a period covering the next five years. The respondent was instructed to imagine that the year was 2005, and to look back at what factors had contributed to the present success of Volvo CE Korea. The Key Factors below will thus be presented in the past tense.

### 5.2.1 Global Player

*“Volvo CE became a very large dominant player in the globalised construction equipment industry”*

*Why is this Key Factor important?*

The construction equipment part of Volvo is the company's most profitable part. This is also an argument for why Volvo should continue to acquire construction equipment companies thus becoming a larger player. There are many small construction equipment manufacturers with market shares of 3-4%, the market is very fragmented and we can expect it to be consolidated. (Affärsvärlden, 19<sup>th</sup> of May 1999) The distance from the market leaders Caterpillar and Komatsu is still too big, and Volvo will continue its growth strategy by acquiring smaller construction equipment manufacturers. What Volvo is looking for could be measured by two variables. Volvo wants to achieve global economies of scale in production, and regional economies of scale to make distribution profitable. (Finansstidningen, 29<sup>th</sup> of Jan 1999)

#### *Strengths*

Being merely a regional player will not result in long term financial success (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999). Economies of scale are needed to stay at the number three position in the world. Volume is needed to maintain competitiveness. Volvo needs to strive to remain number three. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999) These statements are from two of our respondents, but in principal representative of all of them. Success in the business is, according to our respondents, very dependent on economies of scale. The fact that Volvo CE receives both management and financial support from Volvo Group gives them the capability to grow. This is a strength that the domestic producers in Korea are lacking at the moment, thus giving Volvo CE Korea a competitive advantage.

*Weaknesses*

At the moment, Volvo CE is positioned as number three, but they are far behind Caterpillar and Komatsu. Their position is not strong, as they are not much larger than the market follower just behind them. It could be considered a weakness to not have a distinct third position, and to be so far behind the dominating industry actors, Caterpillar and Komatsu.

**5.2.2 Price competition**

*“Price wars among the actors in the Korean construction equipment industry have not occurred”*

*Why is this Key Factor important?*

*I. Increased Profitability*

Price wars leads to profit loss, and Volvo CE Korea has pinpointed that Korean business activities must be efficient and profitable. When Volvo came to Korea, many people counted on a solution in which Volvo would pour money into the business. But that was not what Volvo had in mind. They chose to “normalise” the domestic market instead, a market where Samsung/Volvo lost money on every excavator sold. (Göteborgs-Posten, 4<sup>th</sup> of Nov 1999) Volvo increased the price while the total demand decreased, and despite this succeeded in increasing their market share as the competitors followed. Volvo managed very well to bring order to the destructive behaviour of the domestic competitors. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999) The price strategy of Volvo CE in Korea has, until now, worked out fairly well. Some are of the opinion, though, that Volvo CE Korea should “follow the rules of supply and demand”, and be more careful when setting their prices. (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999)

*II. The Korean market size*

The Korean market used to be the third largest in the world for excavators, roughly the same size as Germany's. Therefore it is important to Volvo CE



Korea's success that price behaviour on this market is not destructive. "The domestic marketing people were not aware of how good the product was and went out selling on price" (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999). The Korean sales people could not see why Volvo CE Korea not should compete in price. For them, it seemed unnatural to raise prices when the competitors kept pushing price down. From the interviews, it is evident that Volvo is very impressed by the quality and the technological level of the excavators produced in Changwon. The North American Dealer Council said in a meeting with Volvo CE Korea that the product was fantastic. However, the domestic sales people still want to keep the price low. The upper management tries to influence them in the opposite direction by providing information about the high quality level. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

#### *Strengths*

It is a strength to have a superior product. But Volvo can only turn the product quality into a resource if they succeed in communicating this to the sales people who must change their mindset.

#### *Weaknesses*

The questionnaire showed a disparity between Westerners and Koreans in perceptions of the importance of the domestic market. Generally, the Koreans focused on the domestic market, while the Westerners perceived the company as serving the global market foremost. The strategy of the company must be communicated clearly to the employees; otherwise, the difference in opinions can turn into a weakness. The respondents in the interviews also indicated that, up to now, the product has not been perceived as differentiated enough, which is a weakness.

#### **5.2.3 Keeping delivery agreements**

*"Volvo CE Korea managed to maintain competitive delivery agreements by delivering as promised".*

*Why is this Key Factor important?*

According to our respondents, this Key Factor was seen as rather unimportant on the Korean domestic market due to two reasons. First, the Korean customers are not used to speedy delivery. Normally it takes seven working days from order to delivery, and the customers have not uttered complaints of this being too slow. Volvo CE Korea is actually hoping to educate their customers in this matter, and make the offer of faster delivery times a competitive advantage in the future. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) The second reason why this is fairly unimportant on the Korean market is because it is easy for Volvo CE Korea to deliver quickly since the production facilities are situated inside Korea and fast lead-times are easy to achieve.

On the global arena, however, this Key Factor was considered to be crucial. The question of how the products manufactured by Volvo CE Korea could be efficiently distributed to other parts of the world, is at the moment, a problem.

*Strength*

Volvo CE has access to a production facility strategically placed in Changwon, a harbour town, where it should be relatively easy to ship equipment to other countries in the region.

*Weakness*

The cargo ships, which are used by Volvo CE Korea, do sometimes “forget” to load Volvo CE Korea’s equipment. This leads to severe delays and, for example Australian dealers have expressed serious aggravation about customers who have been kept waiting for their orders for months. The problem of not having globally competitive deliveries is mainly connected to the fact that Volvo CE is still a fairly small player. Hence, they cannot offer the volumes demanded for the constant flow that brings high accessibility of products, service and spare parts to customers. To

connect back to the Key Factor “importance of being a global player”, it is a weakness to be relatively small in the construction equipment market.

#### **5.2.4 Competitive Products**

*“Volvo CE Korea has been able to supply high quality products, spare parts and service to their customers”.*

*Why is this important?*

The construction equipment industry is a mature industry, and customers expect “high quality products at competitive prices”. The competition on the Korean domestic market is fierce, and to avoid having to compete solely on price, Volvo CE must supply high quality products, to differentiate themselves from their competitors.

#### *Strengths*

One of the managers explains which resources contribute to the competitiveness of Volvo CE Korea's products: “I would say I am pleasantly surprised with the manufacturing system. Not the most modern factory in the world, Samsung obviously has not put a lot of money into it the last years. But in some ways that is very good, because we have not over-capitalised the factory. And when the business is really depressed we can reach our break-even point even then. Our people have learned by the Japanese and taken the best manufacturing parts from them. I am pleasantly surprised by how advanced our manufacturing system is, and I am pleasantly surprised by the engineering capabilities.” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) Through the acquisition of Samsung's construction equipment division, Volvo CE gained access to a variety of resources. Intangible resources obtained were the access to Korean- and Asian-markets, as well as the fine reputation of Samsung's product performance. Samsung products were, objectively tested, of high quality but were not perceived to be so. The resources Volvo has added, in the form of excellent brand-reputation with regards to quality, environment and security, will make it possible in the future to position Samsung's excavators as superior

to other domestic products. In the global arena where Volvo CE Korea is competing, it is a prerequisite to have a globally strong brand name. That resource, along with Volvo's financial and product resources, creates a capability to take market shares both in the global and Korean markets. Volvo also obtained skilled human resources in the acquisition. The R&D and engineering resources are particularly valued, as they, in combination with Volvo's management's focus on profit, should result in a capability to put competitive products on the market at a steady pace. As the plant is not overcapitalised, Volvo CE Korea has a reasonably profitable production as well as the flexibility to increase their production with short notice. This creates a true capability in a global market where it is crucial to be able to react quickly to the changes in demand.

#### *Weaknesses*

The fact that Volvo CE's products are of high quality will not help if the products are perceived to be inferior to, for instance, the Japanese Komatsu. Korean customers believe Komatsu to be of superior quality, and therefore Komatsu's prices are expected to be higher. This opinion is, to some extent, shared by Volvo CE Korea's marketing people. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

#### **5.2.5 Financing to customers**

*"Volvo CE Korea's customers had the possibility to borrow money on a well functioning financial market".*

##### *Why is this Key Factor important?*

Volvo CE Korea sells most of their excavators to single customers, and therefore, product financing is an important part of the product package. Volvo CE has chosen not to include financing in its core activities, but to outsource it to Samsung Capital. Before the Volvo CE acquisition of Samsung Heavy Industries, the financing conditions were so generous that Samsung never got paid by the customers. On December 1st 1998 Volvo CE established new financing rules according to Western standards, taking

away a large part of the costs that were associated with the Samsung way of handling its product financing. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999) Volvo has since the takeover of the Samsung division, consciously worked to turn the focus to profit instead of attracting new customers. Volvo CE Korea has taken the leading position by doing so, and now many competitors have started to follow. When, for instance, Volvo CE changed the (for customers) very favourable rules of sales financing, they lost many customers. Shortly after, the competitors followed suit and changed their rules accordingly, and the customers returned to Volvo CE Korea. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999)

#### *Strengths*

Volvo CE Korea has a set of resources that allows them to be a market leader and therefore successfully change terms of credit and set product price. They are capable of initiating change in the industry and on the market. Another resource that Volvo CE Korea possesses is access to Volvo Group Finance for knowledge (consultancy and action) of how to deal with the very important matter of exchange rate. Volvo's overall strong financial situation, which means favourable hedging conditions, is also a strength.

#### *Weaknesses*

What can be seen as a weakness, though, is that Volvo CE Korea has outsourced its sales financing activities, which usually profitably handled within the company. Volvo Group Finance's hesitation to act on the Korean financial market is probably based on sound judgement, but it would be a strength to be able to manage the financial market and act on the domestic market, thus having more influence over the customers. If Volvo CE Korea could offer products, service and financing, customers would be more closely tied to them and not switch brands when exchanging their old machines for new ones. Offering financing also gives Volvo CE Korea the opportunity to arrange competitive sales offerings,

mixing the product price and the financing costs in a manner, attractive to the customer.

#### **5.2.6 Increased R&D**

*“Volvo CE Korea increased their competitiveness by putting more resources into Research and Development”.*

*Why is this Key Factor important?*

This Key-factor was not universally seen as important, but in some aspects the significance was clear: “In any industry, you need to have products in the pipeline that meet ever-increasing customer demand. The reality is that this is a relatively mature industry, with mature products; we do not see a lot of technological break-through in this industry. Where you will see advances will be in some of the supporting systems like hydraulics, maybe some manufacturing process improvements. I do not see any direct need to invest largely into improving these processes. There are others out there who are doing this and we can absorb these new technologies fast enough, and I don’t believe that it will be a competitive disadvantage to not focus on this issue.” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) “Probably it is possible for Volvo CE Korea to extract much more from R&D with the same amount of financial input as today. One of the most important strategic activities for Volvo CE Korea is R&D, but I would like a much clearer focus and clearer vision and then connect the money to this. The former R&D activities have been successful and given us good products, but today are much resources going into remodelling of existing technology: the Volvoisation of Samsung products.” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

*Strengths*

One of Volvo CE Korea’s strengths may be their strong R&D department, as well as the fact that they have been sending R&D engineers to Volvo CE in Germany and to Sweden, resulting in the sharing of knowledge and an accelerating development of new and existing products. If Volvo CE Korea

has the capability to absorb and copy new technologies quickly by using benchmarking, it is a capability. The heritage from the Samsung Division, that in its earlier days was very dependent on Japanese technology, could mean such a capability. The strong R&D department is also an indication that Volvo CE Korea should be able to absorb and adapt new technology very quickly. Volvo CE Korea also has the experience of benchmarking from the Volvoisation process of Samsung excavators, where the products were compared continually with Caterpillar and Komatsu, and then improved.

#### *Weaknesses*

One weakness in the R&D area is that many Korean suppliers are seen as unable to contribute to R&D: “We are way behind in getting the suppliers involved in product planning!” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

#### **5.2.7 Domestic Suppliers**

*“The amount of reliable Korean domestic suppliers has increased”.*

#### *Why is this Key Factor important?*

This is a question of cost. If price conditions remain equal, it is always cheaper to have good suppliers domestically. The question is whether Korean suppliers achieve the quality demanded by Volvo CE Korea. Another aspect is the unwillingness of Korean suppliers to take part in R&D.

#### *Strengths*

Volvo CE Korea has the strength of being part of a large global organisation, and is thus able to choose between many suppliers, as well as to put pressure on them to take a greater part in R&D activities in the future. Volvo has cleaned out a big share of the domestic suppliers that did not meet the Volvo requirements, and focused on larger suppliers that have an international capacity. The amount of Korean suppliers has been

reduced from 475 to 350, including 100 international suppliers. This process has been a part of Volvo CE efforts to improve the efficiency of the Korean subsidiary. (Dagens Industri, 11<sup>th</sup> of Nov 1999)

#### *Weaknesses*

One weakness that we mentioned above connected to the Key Factor “increase of resources put into R&D”, is that many Korean suppliers are seen as unable to contribute to R&D activities: “We are way behind in getting the suppliers involved in product planning!” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999). This is really a restraining factor in making Volvo CE Korea a major part in Volvo CE’s global distribution of construction equipment. The products made in Korea cannot rely on suppliers in Europe if they want to be competitive in price and delivery. Korean suppliers must be determined to compete with the Western world, thus placing more production in Korea and making Volvo CE Korea’s production more competitive. As the situation is now, it is a weakness for Volvo CE Korea to not have globally competitive suppliers to a greater extent. It is a weakness in the ongoing production, but it is first and foremost a weakness if more productlines are to be produced in Korea. The lack of globally competitive suppliers is a fact that can hinder Volvo CE Korea from extending their productlines in their Changwon factory.

#### **5.2.8 Relationships**

*“Western Management developed an understanding of how important relationships are when doing business in Korea”.*

##### *Why is this Key Factor important?*

The importance of nurturing relationships when conducting business might also seem important for Westerners. But in Korean business life, the full extent of the importance might not be completely understood. This runs through all levels of the company: relationships to customers, suppliers, and government officials the list could be endless. This was one respondent’s opinion on relationships with government officials: “The



Volvo acquisition was made under the current government (National Congress for New Politics (NCNP)), and they have a very favourable opinion about Volvo CE Korea, but if we have a new government, we will have to start from scratch. This may not be negative but may be not so advantageous as today, because now our relationship with Kim Dae Jung is very favourable.” (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999)

#### *Strengths*

Mr. Helsham (President Volvo CE, Korea) is very good at creating relationships with other people, so even though he might be weak in understanding Korean culture, he will succeed in creating the necessary relationships with the Korean government and other authorities. (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999) This is a statement from one of the respondents that is significant for the whole Volvo CE Korea organisation. Volvo does have an asset in Tony Helsham and his close relation to Kim Dae Jung.

#### *Weaknesses*

Being a Western company mainly run by Western managers is a disadvantage, because it is hard for Western people to achieve a full understanding of the capabilities needed to build up the required relationships. An example of this is the Korean supplier who is disappointed at Volvo CE Korea, because they did not participate in the golf tournaments, drinking sessions and Karaoke events which the previous Samsung Division’s management had taken part in as a matter of course. The supplier felt excluded from the “Volvo family” and for him, being relationship oriented, this was a strongly negative experience. He talked warmly about his Japanese customers who were more “understanding.” (Göteborgs-posten, 4<sup>th</sup> of Nov 1999)

#### **5.2.9 Accounting Standards**

*“The Korean accounting standards were adapted to international standards”.*

*Why is this important?*

The accounting standards, or in Korea, the lack of internationally acceptable accounting standards, are closely related to the important question of transparency. Transparency in accounting systems is important for Volvo CE Korea, as it is a prerequisite for measuring profits, and thus a necessary tool in achieving efficiency. Transparency is also a must if Volvo CE Korea is to judge the credit worthiness of their customers when offering sales financing.

*Strengths*

Volvo CE Korea is good at internal one-way communication. This is evident in the employees' opinions about the accounting standards, which they all found important, (though they did not always motivate why). Another strength that Volvo CE Korea has gained by improving the accounting standards is a greater level of transparency compared to domestic competitors. Volvo CE Korea is able to measure the outcome of its business and perform management control to a greater extent than previously.

*Weaknesses*

We cannot find any weaknesses directly connected to introducing new accounting standards. However the increased possibility to control the outcome might lead to negative responses from employees or managers who never been controlled to this extent before. This higher level of control could thus create disturbances in the harmony that the Koreans look for in their lives. Those employees might choose to go over to Volvo CE Korea's competitors for employment.

**5.2.10 Performance Based Salary System**

*"Salaries in Korea have become more directly related to performance".*

*Why is this important for Volvo CE Korea's success?*

The payment system in Samsung Construction Equipment was highly inefficient, with annual rises in pay that had no correlation to the added value the employee contributed. Since Volvo CE took over the company they have determined to change this because they believe in efficiency at all levels, including human resources. Volvo CE Korea's aim is to remove the so-called Hobong system and introduce a performance based salary system, thus increasing efficiency. The respondents in our questionnaire can be divided into two major blocks. The Western managers generally graded the question about relating salaries to performance as very important; in contrast, Korean managers had a rather different opinion. Most of them felt that productivity and labour efficiency were two factors that did not need to be correlated. A majority of the Korean managers we interviewed seemed quite aware of the fact that efficiency in connection to human resources had to be emphasised. But when we asked them the follow up question, "Do you believe that productivity and labour efficiency are two factors that need to be correlated?", many of the Korean respondents said not.

*Strengths*

Samsung had lost money on the excavators in the five years preceding Volvo CE's acquisition, and they had not made any investments in the factory (Göteborgs-posten, 4<sup>th</sup> of Nov 1999). The fact that the employees were aware of how severe the situation was for the company made it easier for Volvo CE to implement the changes needed to improve labour efficiency.

"The younger generation has a very international mindset, so they prefer to be in a Westernised company rather than in a Korean company: therefore, the future in this aspect is seen as very bright for Volvo CE Korea." (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999) When Volvo CE Korea implements a more performance based salary system, they might be able to attract the younger generation of employees that are seeking an employer

who gives them an opportunity for quicker advancement. The salaries are based on merits and overall performance, instead of time spent in the company. The resource Volvo CE Korea has in the form of Western-style management capabilities can make this transition a reality.

#### *Weaknesses*

The salary system that exists today it is a severe weakness for Volvo CE Korea, as it automatically increases wage costs independent of Volvo CE Korea's profit level. If a new salary system based on performance were to be implemented, positive outcomes of cost efficiency, flexibility and faster decision-making would result. The Korean managers were not so sure if there should be a correlation between productivity and labour efficiency. A weakness could hence be that the true meaning of this efficiency concept has not been accepted at a deep enough level among Korean management. This could lead to a silent resistance towards the changes Volvo CE wants to implement in its Korean subsidiary.

#### **5.2.11 Human Resources**

This Key Factor was not explicitly included in our questionnaire, although we covered the question of "performance based salary system", one of the main issues connected to human resources in Volvo CE Korea. As many of the respondents added this Key Factor though, it will be discussed below.

#### *Why is this Key Factor important for Volvo CE Korea's success?*

The removal of the, (according to Volvo CE), excessive number of hierarchy levels is also seen as a way of promoting the overall efficiency of Volvo CE Korea. The Koreans, on the other hand, are very fond of their company hierarchies, as they are considered a proof of status (if you have management position) and generally reflect the way Korean society is organised.

### *Strengths*

Volvo CE Korea inherited a well-educated, hard working work force from the former Samsung Division. The Korean employees could be seen, as one of Volvo CE KOREA's major resources. The hardships in the relatively recent history of Korea are today driving the Koreans to do their utmost in a very competitive way. This driving force could be expressed in one word: "Hahn", or the "can-do-spirit."

One problem, though, is the hierarchical organisation in which these employees are used to working. Volvo CE Korea, being a foreign direct investor, is able to "get away" with breaking the strict rules of hierarchy which otherwise dominate the Korean Business system. Foreigners are not expected to obey the regular codes of conduct that otherwise prevail throughout the whole of Korean society. Thus, being a foreign investor could be seen as a strength, because when introducing the necessary moves towards an efficient business organisation, they are allowed to take measures that Korean managers would not. An example is when Volvo CE's managers from Brussels began arriving in Korea. They did not move according to the strict hierarchy when they asked questions; they went directly to the person they wanted the answer from, even if he was situated at the very bottom of the organisational hierarchy. As they were foreigners, their behaviour was accepted and today, the communication over hierarchy borders has become much speedier than in the early days of acquisition.

The hierarchical structure of Samsung Construction Equipment division's organisation actually was a strength for Volvo in the acquisition phase, as they were able to quickly get a picture of the company's organisation and human resources.

### *Weaknesses*

Many Koreans see the fact that Volvo CE has cut down in management levels as a major cause for disorder. The Korean employees generally find it very important to know which positions the people surrounding them

have, in order to know how to behave towards them. Although most of the top management is from countries outside Korea, the way of thinking among the native employees has not changed dramatically (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999). Volvo CE Korea regards the hierarchical system as a weakness, as it opposes flexibility and own initiatives by the individual employees.

### 5.3 ANSWER TO RESEARCH PROBLEM II.

The current strengths and weaknesses of Volvo CE Korea will, in the conclusion of the scenario-development-process, be assessed against the threats and opportunities that each of the four created scenarios will impose on the MNC. By describing the MNC's strengths and weaknesses, the first research problem has been solved:

*“to describe the MNC's strengths and weaknesses in interacting with the complex and dynamic emerging market-environment”*

The next chapter will cover another vital part of the scenario development process: the environmental analysis. This will take both South Korean societal aspects and South Korea as a market place into consideration.

## 6 ENVIRONMENTAL ANALYSIS

The purpose of this chapter is to analyse the South Korean environment by explaining its institutional set-up, and by this define the driving forces of future environmental change.

The South Korean environment is characterised by a high degree of uncertainty, both because it is very complex for anybody except a Korean to fully understand, because of its high degree of dynamism. Korean Institutions have gone, and are going, through a great deal of change in a relatively short time period. To achieve a full picture of what this type of environment, which we call an emerging market, consist of, we will conduct an environmental analysis according to the Institution Network Approach: an Institutional Analysis.

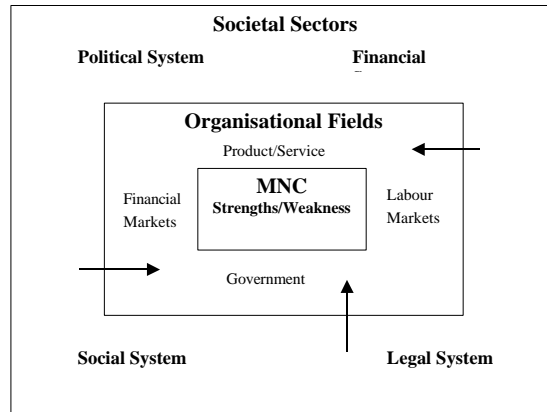
The Institutions Networks Approach explains how the institutions we have chosen to analyse influence each other, as well as the possibility the Multinational Corporation (MNC) itself has to interact with its environment. This model, therefore, gives a holistic picture of how the environment in all its complexity is interrelated to, and acts together with, the MNC.

- Volvo CE is defined as a **Multinational Corporation** (MNCs) acting in emerging markets.
- The dynamic and complex environment in South Korea is equivalent to the conditions prevailing on **Emerging Markets**

### The Institutions Networks model

The Institutional Analysis is divided into two main stages. First, the Societal Sector will be described, followed by an explanation of the institutions within the Organisational Field. The explanation of the Organisational Field will be accomplished by applying knowledge of the Societal Field to each of the institutions (markets and non-markets) within the Organisational Field.

Figure 6.1 Basic Institutions Model with arrows that show the direction the Explanatory factors takes, from Societal Field to Organisational Fields.



Source: Derived from Jansson (1999)

#### 6.1 THE SOCIETAL SECTOR

The Societal Sector describes those institutions in the South Korean external environment that the MNC has no power to influence. These external institutions are described in accordance to the Key Factors, which our respondents agreed to be important for Volvo CE's future success. Primarily the institutions within the Societal Sector will be described, since in the next phase of the Institutional Analysis, they will be used in an explanatory fashion.



**6.1.1 The Financial System**

How important are those Key Factors for Volvo CE Korea in a five-year time frame? - Is it important that...

- A favourable valuation of the Korean Won has been maintained?
- A well functioning financial system is accessible to Volvo CE Korea?
- The amount of FDI increases - Globalisation of the Korean market
- The business cycle of the Korean Construction Industry turns upward?

After the Asian crisis of 1997 the Government, led by President Kim Dae Jung, initiated a new direction for Korea's financial market in order to bring the country out of its economic crisis. There are different views as to whether the initiated changes have been profound enough. The economic trend has evidently turned upward, but the question is whether the restructuring efforts have been profound enough to sustain the economic growth. A fundamental characteristic of the Korean financial market is evident, though: it is closely interrelated with the restructuring and with the overall political system. The crucial valuation of the Korean Won can be seen as an outcome of the political and economical reforms that have taken place. The financial- and political- systems are more interlinked in Korea than in most Western countries. Korea has a credit based financial market and not a capitalistic market, implying that relationships are the basic foundation for financial transactions.

**6.1.1.1 The Valuation of the Korean Won**

One of the most important factors for the financial situation in Korea is the valuation of its currency. Korea is, today, very dependent on the export industry, in which a stronger Won means decreased competitiveness for

Korean products. In the export field, Japanese products are the major competitors, and one of our respondents expressed his view on the importance of the exchange rate like this: “The threat of Japanese competition is, first of all, related to the exchange rate. The general rule of thumb is that when the Japanese Yen stands one to ten Korean Won, Volvo CE Korea does not have to worry about Japanese competition”. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

Another aspect concerns the evaluation of the Korean Won compared to the US dollar. The focus on traditional heavy industries in Korea, such as shipbuilding, automobiles and steel industries, makes the oil import considerable, and thus makes Korea dependent on reasonable oil prices and a sound exchange rate between Korean Won and US Dollars (in which crude-oil is traded). (Seminar, 8<sup>th</sup> of Oct 1999)

#### **6.1.1.2 A well functioning financial system**

##### *The Banking System and Credit Market*

It is still far to soon to expect a sound banking system in Korea. Bank management has yet to improve. As the country's big companies start to restructure, non-performing loans are likely to rise, triggering the second wave of debt crisis possibly as soon as next year. On top of that, big commercial banks are now state-owned, which is a concern for people who remember how the government, in the past, used banks as a tool to support strategically protected companies. The reform that has just begun, is largely dependent on corporate restructuring for its success. Korean banks have yet to develop their own credit-rating system, and not rely on data provided by corporate clients to assess credit risk. (The Banker, Dec 1998) As financial products were heavily regulated and the labour laws made it difficult to close branches, the easiest way for banks to increase their profits (though not their profitability) was to increase the volume of their lending, rather than to innovate or cut costs. The absence of strong owners made it easier for chaebols and bureaucrats to dominate the banks. (The Economists, 10<sup>th</sup> of Jul 1999)

The equity market plays a vital role in the South Korean economic recovery. Minority shareholders are likely to be the best watchdogs against abuses. The government has lowered the stake required to bring a motion at a company's annual meeting, and has also brought in a rule requiring public companies to appoint a quarter of their directors from outside. As a growing number of investors are foreigners, they will not suffer in silence if they think they are being exploited. Although legislation and regulated powers now exist, creating a genuinely independent financial system will be a long, hard journey. (The Economists, 10<sup>th</sup> of Jul 1999)

*Corporate restructuring*

The new rules against cross-guarantees and cross-shareholdings will be hard to enforce. The chaebols can exploit loopholes using foreign subsidiaries and complex corporate structures.

Daewoo's declared debt (and almost all analysts suspect the real figure is higher) is almost as large as the total bail provided by the IMF to keep the entire Korean economy afloat in late 1997. Basically, chaebol owners used to run their companies with other people's money and when they got into trouble, they could count on their relationships with politicians for help. But now if they fail, they forfeit their special privileges. That is what the market wants. (Far Eastern Economic Review, 26<sup>th</sup> of Aug 1999)

Ultimately, the best master for the arrogant chaebol owners is not president Kim with his bureaucrats, but the South Korean capital market. Yet, it is the small businesses that should be the innovators and new employers in South Korea. Unless the country can straighten out its capital markets, those businesses will remain hamstrung. (The Economist, 10<sup>th</sup> of Jul 1999)

Thorough reform of the economy is the only way to restore high growth and employment. This reform must include the removal of the often-overlooked service sector policy (The Mc Kinsey Quarterly, 1998). Due to

the crisis, most Koreans are afraid to spend money, and that is hampering the recovery (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999). The lack of spending keeps the small service-businesses especially from developing, and this creates a vicious circle.

#### **6.1.1.3 Attracting Foreign Direct Investors**

No one has been more enthusiastic about rolling out the red carpet for foreign direct investors than President Kim Dae Jung. Determined to reform the economy by truly opening it to global competition, Kim has repeatedly used his office as a bully pulpit to preach the virtues of foreign investment. In fact, the real test of South Korea's newfound openness will come when the good times return. (Far Eastern Economic Review, 24<sup>th</sup> of Dec 1998) "We will do everything we can to attract foreign investment." This is the essence of a bill submitted on April 28<sup>th</sup> 1998 by the Ministry of Finance and Economy (MOFE) to accelerate foreign investment in Korea. (Business Korea, May 1998) The question is whether deeds will match the words. Foreign companies with experience in Korea know that there is often a huge gap between policy announcements, enabling legislation, and actual implementation and policy. (Mergers & Acquisitions 2, Sept-Oct 1998) "Globalisation is the buzzword," says Han Seung Soo, a parliament member and South Korea's former ambassador in the United States. "We are at the changing point in our economy. We cannot do it without help from abroad." (Tribune Business News, 14<sup>th</sup> of Aug 1998)

#### **6.1.1.4 The Business cycle of the Korean Construction Industry**

The Korean industries, which suffered severely due to the financial crisis in 1997, have shown a vivid overall recovery trend. Some industries, though, such as textile and construction, have not revealed any distinct signs of recovery. The prosperous trend that is evident in the export industry is expected to continue in almost every sector. (Seminar, 8<sup>th</sup> of Oct 1998)

The opinions of the importance of the Korean domestic market are split among the people we interviewed in Korea. One respondent says that the

Korean construction industry soon will turn upward. He means that the Korean market is of importance to the whole Korean Construction Equipment industry, and if it stays depressed for more than a year from now, Volvo CE's domestic competitors will probably die. However, an upswing in the Korean Construction Industry is considered to be vital and must happen soon, both for Volvo CE Korea and its suppliers. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

### 6.1.2 The Political System

*How important is this Key Factor for Volvo CE Korea in a five-year time frame? Is it important that:*

- Political reform that supports the economic transition, be carried out?
- The relation between South and North remains stable?
- The pace of a Korean reunification has been gradual and the South Korean society and economy has been able to handle it?

There is a strong inter-linkage between the political and financial systems, as the development in the financial area is very dependent on political reforms and legalisation to develop in the direction marked out by the Government. How, and at what pace, the Government chose to pressure the chaebols to divest their conglomerates is an example illustrating the inter-linkage. The interlinking between political- and financial-systems that exist in Korea supply the basic fundamentals for general business conditions, and consequently, for the valuation of the Korean Won.

#### 6.1.2.1 Political Reforms supporting economic transition

Economic Reforms have been carried out, but there is still a long way to go before South Korea has achieved an open and transparent market economy. The question is to what extent the recent reforms will be sustainable. The current government has pushed through many necessary, but some times

unpopular decisions regarding economic restructuring. The South Korean economy is, at the moment, depending on consistency in its politics to achieve sustainable economic development.

#### *The Constitution*

The President in Korea since February 25<sup>th</sup> 1998 is President Kim Dae Jung, and the head of government is Prime Minister Kim Chong P'il, appointed by The President. The President is chosen by general direct elections every fifth year. The last election was held on December 18<sup>th</sup> 1997, and the next is to be held by December 18<sup>th</sup> 2002. The Parliament consists of the unicameral National Assembly, called Kukhoe. It contains 299 seats and its members are elected by popular vote to serve four-year terms. The last elections were held the 11<sup>th</sup> of April, 1996 and the next is to be held in May 2000.

#### **The result of the last president election Dec. 1997**

Kim Dae Jung (NCNP) *National Congress for New Politics* 40,3%

Yi Hoe Chang (GNP) *Grand National Party* 38,7%

Yi In Che (NPP) *New People's Party* 19,2%

#### **The distribution of seats in Parliament was in February 1999:**

GNP	137 seats
NCNP	105 seats - (Kim Dae Jung's Party)
ULD	53 seats
Indep.	4 seats

Source: [www.cia.world-factbook.com](http://www.cia.world-factbook.com)

#### *Are the reforms sustainable?*

So far, what has been missing from Kim Dae Jung's program is political reform. The best way to control the power of chaebol owners would be to create a society where people can say no: a society where managers can turn down foolish investments, bankers can refuse a loan to a friend,

bureaucrats can stand on principle, and politicians feel free to ignore the orders of the party boss. The place to begin is with the presidency itself. The office holds too much power for the country's good. Although there is a cabinet, the president can rule virtually alone if he so chooses. If the president were to devolve his power to the prime minister, other ministers, and the parliament, it would establish the idea that kings of any kind are no longer omnipotent. During his election campaign, Kim Dae Jung proposed that South Korea move to a parliamentary system in which the president would no longer hold the reins of power, but instead become a moral, stabilising force, as in Germany. (The Economist, 10<sup>th</sup> of Jul 1999) A change in the parliamentary system would make a strong impression of the Government's willingness to fundamentally restructure Korea, and send a signal that the President has real convictions. "I am determined to go down in Korea's history as the president who first accomplished corporate reforms and straightened things out in the economy," the President Kim Dae Jung said; "I will remain firm". (Far Eastern Economic Review, 26<sup>th</sup> of Aug 1999)

The Government has announced a sweeping restructuring plan for the chaebol Daewoo, and will strip down to six units, from the current 25 by year's end. The problem is that the Government needs Daewoo's cooperation to avoid the messy by-products of formal bankruptcy, such as heavy layoffs and a flight out of Korean stocks and bonds. As the April 2000 national assembly elections near, Kim Dae Jung will find it harder to force painful restructuring. Sceptics say that even Kim Dae Jung is sometimes willing to put off long-term reforms for short-term political expediency. In July, he protected the Samsung Motor plant in the Pusan region and saved 50,000 jobs. Even if Kim Dae Jung manages to stay firm, it will take one or two years to clean up the mess. However, if the restructuring plan is fully implemented, South Korea's economic recovery will power ahead with minimal disruption, according to government officials. Swift and decisive action will reassure investors. And the fact that even the biggest conglomerates can be dismantled rather than bailed out

will make an indelible impression on other corporations. (Far Eastern Economic Review, 26<sup>th</sup> of August 1999) The South Korean Government is still giving the chaebols financial support. If the chaebols are treated from a pure market perspective, that is, cut off from their unpaid credit and forced into bankruptcy, the consequences would be of such magnitude that the effects would not be viable, and this cannot be allowed to happen in South Korea. The country would be ruined and put completely back on its knees. The size of the debt can only be compared to Russia's. There is no Chapter Eleven like in the USA; there are no laws that keep a bankrupt company going and protects it from its lenders. This country cannot afford massive unemployment. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) The pace of restructuring into a market economy cannot go faster; so much has happened in the last 20 years. Kim Dae Jung is believed to be firm in his reconstruction of the system; he is old and wants to be remembered as the person that carried out the political and economic transition. As the Korean system of election does not allow re-election, Kim Dae Jung has nothing to gain personally from political tactics; only his party can gain from that. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999) The general view on the restructuring from our respondents is that they are pleased with its ongoing pace, but want it to remain firm, covering every sector of society. One respondent states; "We have to be able to maintain this pace of recovery. I don't believe that the reforms that have been implemented in Korea are sufficient. We have to continue to restructure the private sector, the public sector and the banking sector as well. We have to continue to restructure the whole nation. The restructuring that has taken place until now is actually very limited." (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999)

*Politics the Korean way*

Koreans look to their politicians for favours rather than ideas. Parties are built around personal loyalties; regional and economical interests dominate the political debate. (Cederberg and Lundholm, 1997) Under these circumstances, the following statement is natural: There are few, or none, young politicians that really are driven by an inner urge to carry through



political reforms; most of the politicians in the inner circle are old men that are very conservative and resistant change (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999).

It is very difficult for Westerners to give an informed answer about what political reform is most important to economic transition. Foreigners mostly do not understand the political system of South Korea. They look on it only from the outside, without any inside knowledge. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) This observation is more justified in Korea than in other countries where the transparency is better and a capital based financial market prevails.

#### **6.1.2.2 The Korean Welfare System**

The absence of a well-developed Korean welfare system has implications for many aspects of Korean society. It influences business as well as family life for most Koreans.

The close link between government and enterprises in South Korea compels the government to support companies financially when they face difficulties in keeping employees. The government's self-interest in providing funds for the Korean chaebols is due to the absence of a functioning welfare system and the considerable social unrest that would follow major lay-offs. The funding of Korean conglomerates in distress can thus be seen as a distribution of social responsibility by the state to the chaebols. If the government decides to cut back their subsidies, it probably would have severe social effects because the chaebols will be unable to care for their employees in the traditional way. From this aspect, the behaviour of the government seems quite justified, as it avoids mass-unemployment and resultant national, economic, and social hardship.

“We see rich people get richer and poor people get poorer. The government needs to encourage public business so we can share the profit together... The Volvo system is different, they do not provide these kinds of benefits,

they include everything in the annual payment system, an annual salary. In the Scandinavian countries, the government takes all the responsibility for all the benefits. In the future, the Korean government has to encourage that kind of system that gives all the benefits to the citizens so the company can concentrate on making more and more profits.” (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999)

Korean companies do not lay off staff. Western managers emphasise the break even to an excessive extent. If employees are laid off, strikes cannot be avoided. Koreans do not have any other way to survive if they are kicked out of the company; the South Korean social system is very weak. (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999)

#### **6.1.2.3 The relation between the two Koreas remains stable**

The relationship between the two Koreas has very big impact on the Korean economy. For example, if there is a change in the relationship between North and South Korea, the Stock Market experiences a lot of ups and downs. It is impossible to say whether this is a negative or a hostile impact; anyway, it is a very big factor in Volvo CE Korea's decisions. (Interview Volvo CE Korea, 13<sup>th</sup> of Oct 1999)

North Korea seems to be gradually falling to pieces. The number of refugees is unknown; there are between 10,000 and 300,000 North Koreans in China. The refugees are said to experience China as a paradise in comparison to the circumstances that prevail in North Korea. (The Economist, 10<sup>th</sup> of Jul 1999)

#### **6.1.2.4 Gradual reunification**

Unification will be the biggest event South Korea has experienced since the Korean War in the early 1950s. It is important that a re-unification process occurs gradually, because otherwise the South Korean economy will have severe difficulties in handling the political and social aspects. Compared to North Koreans, East Germans before the German re-unification were rich,

sophisticated and well informed about life in a relatively democratic market economy. The North Korean militarism has drained civilian wealth since the 1960s. (The Economist, 10<sup>th</sup> of Jul 1999)

The North Korean regime classifies 27% of its population as “hostile”, and a further 45% as “unstable”. Ordinary North Koreans know little of the outside world, but small changes have occurred. One of the top five South Korean chaebols, Hyundai, has taken thousands of South Korean tourists to scenic places on the north side of the border. They have a six-year agreement on shipping tourists to North Korea. The chaebols are taking action in order to promote an advancement of North-South relations. An example of this is the joint manufacturing in Daewoo’s textile factory venture in North Korean. It seems like the South Korean chaebols have better connections with North Korea than does the government. (The Economist, 10<sup>th</sup> of Jul 1999)

### 6.1.3 The Legal System

The Korean legal system combines elements of continental European civil law systems, Anglo-American law, and Chinese classical thought (www.cia.worldfactbook.)

*How important is the following Key Factor for Volvo CE Korea in a five-year time frame? Is it important that:*

- **Laws for protection of foreign investors are enforced?**

#### 6.1.3.1 Legal Reform to protect FDI in general

South Korea’s appointment to the World Trade Organisation (WTO) will force the country to liberalise its legal system (International Financial Law Review, Nov 1998). President Kim Dae Jung pushed a new foreign-investment promotion law through the national assembly on the 17<sup>th</sup> of November 1998. The new law consists of more generous tax breaks and rental subsidies for foreign investors, as well as faster approval procedures for investments. (Far Eastern Economic Review, 24<sup>th</sup> of Dec 1998) In May

(1998) the government adopted a series of measures designed to stimulate investment in domestic companies by foreigners. Reforms were made to the “Acquisition of Land by Foreigners and Control”, formerly known as the “Alien Land Acquisition Act”. (International Financial Law Review, Nov 1998) This concerned Volvo CE directly, as they had problems in the acquisition stage gaining ownership of the land upon which the Changwon factory is situated.

Today, key laws have been amended to allow more foreign competition; new laws protect the rights of minority shareholders and force through more managerial transparency (Far Eastern Economic review, 26<sup>th</sup> of Aug 1999) This will render the investment possibility in a whole new light than previously; the shareholders will gain insight into company affairs, and can therefore force changes of company boards and management.

If these new laws actually are enforced, Volvo CE Korea’s situation, as a foreign investor will improve, as they will clarify both Korean business practice and general policies towards FDI. The question, though, is if it will be possible to change this to a high enough extent. The Korean company boards consist mainly of the owners of the firm, and they have traditionally controlled their businesses firmly. Gaining insight into their affairs would mean taking away the centralised control that chaebol owners have always exercised. It is hard to imagine that the owners will be willing to transfer the power in favor of the shareholders, because they see themselves as father figures for their company. Letting go of responsibility would be experienced as letting their family down. This might entail a resistance towards changes in laws and regulations concerning transparency and shareholders rights, which will be expressed in a higher degree of corruption due to attempted avoidance of the new laws.

#### **6.1.3.2 Over-regulation**

South Korea is over-regulated, and corruption follows closely behind. The many rules that exist are easy to break as long as the right connections are

there. According to Michael Breen, the author of a recent book on South Korea, “Falling foul of the law is not a problem, as long as one does not fall foul of the people who enforce it”. Simply legislating away corruption will not work; that would make criminals out of everyone. (The Economist, 10<sup>th</sup> of Jul 1999)

#### **6.1.4 The Social System**

The following social institutions are important because they are high in explanatory power, hence they will explain why the institutions in the Organisational Field behave the way they do. The social institutions could all be said to be a part of Korea’s country culture, as they have developed through history and have influenced the way actors in the Korean market behave. The social institutions stem mainly from the pre-industrial era, but have been influenced to some extent by changes that Japanese colonisation and civil war imposed upon the Korean nation. We have focused on the social institutions of Confucianism, Family-clan and Business Mores (See sections 3.3.1.1 and 3.3.1.2).

##### **6.1.4.1 Confucianism**

The Confucian Philosophy often gets blamed for being a tool for power abuse. The Korean people are kept in check by a vast amount of moral and practical rules. The social order of rank is strictly hierarchical and practically static, the aim is to achieve harmony in society. This has, to some extent, created negative dependence and authority obedience, as well as a confidence in formality, rituals and etiquette. The Confucian lifestyle could also be blamed for the subordinate position in society of Korean women. The Confucianism could also be held responsible for hindering and delaying the modernizing of Korean society, due to the quest for the “golden past” described in old Chinese Classics.

On the other hand the same philosophy is the force behind South Korea’s spectacular economic development in the passed 30 years. The most prominent contributions are: a strong work ethic, a burning longing for a

making career, thus gaining social prestige, obedience to authorities and a positive view on education and knowledge. (Cederberg and Lundholm, 1997)

#### **6.1.4.2 Family Clan**

The Family is seen as a miniature of society, and all rules within family apply to society as a whole. Obligations and responsibility toward one's own family is immense. In earlier days, this included neighbours; today this concern has moved over to work colleagues and classmates, instead. For example, it is natural to ask the son of an old work colleague for a favour. An example of this is shown in an interview with a young Korean accountant working in Brussels. The only thing he experienced as negative in Europe, except the food, was the fact that he could never rely on anyone helping him when he needed, because all the people he relied on (his family and work colleagues) were all in South Korea. If he, for instance, would get married in Korea, all of his colleagues would feel obliged to help him with the arrangements; in Brussels he has to manage on his own.

#### **6.1.4.3 Business Moeres**

The ongoing, but slow, move in Korea towards a more market-like system, is at the same time a move towards a more decentralised system, where the state does not have all the control over the business activity in the country. The fact that business moeres are undergoing a change has far-reaching impact on other areas in the Korean society. Both the family life and the Confucian philosophy of life interact with business moeres, and thus both influence and are influenced by the alterations in business moeres.

The Koreans' cultural characteristics are distinguished by high power distance, which equates to central decision-making and an overall hierarchical structure. The uncertainty avoidance is high, and thus reliance upon directives from above and the following of rules are always rewarded. This is generally in contrast with the rules and norms prevailing in a market-like system, where decision-making is delegated and dependent

upon individual initiatives from all levels. The fact that the movement towards a market-like system nevertheless takes place is definitely due to a questioning of the old system and the newly reached understanding, caused by the financial crisis, that Korea is a part of a global market. To be competitive in the global market arena, it is necessary to make adaptations, and the Koreans have slowly started this process of altering its business mores.

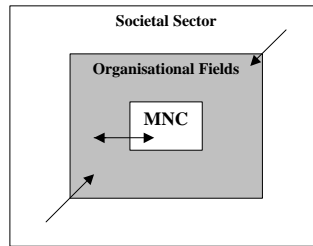
“We have realised how pragmatic westerners are when doing business. An example is, if a Korean company has visitors from overseas, the guests are taken care of, driven from the airport in a company car and usually welcomed by someone in an equivalent position. This is sometimes impractical, and in Westernised companies not practised. In Volvo CE Korea nowadays, a company car is sometimes sent, but sometimes visitors will have to travel by taxi. In a Korean company, however, this never occurs; a company car always is sent and somebody is there in person to welcome the visitor. Westerners are considered to base their decisions upon reasoning instead of other things, such as building relationships. In business, Koreans will have to be more practical and profit conscious”. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999) Koreans put much attention on relationships. They do not find this a waste of time as do many Western business people, but instead as an investment in future business activities.

“There are a lot of ways of exchanging and making personal relationships with others, like face-expression and gestures. You have to grow up with that kind of culture; it is a little bit difficult for foreigners to understand this to 100%.” (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999)

Are the reforms in Korea too ambitious? By trying to set markets free, the reforms not only threaten commercial and political interest groups, they also seek to change the way South Koreans do business with each other. Free-market ideas of relying on legal contracts, impartial regulations and transparency sit uncomfortably beside the network of personal loyalties and

obligations that still directs Korean affairs. The decentralised nature of a market system seems alien in a place that grants huge moral power to the “king” presiding over a company, a bank, or the country as a whole. (The Economist, 10<sup>th</sup> of jul 1999)

## 6.2 ORGANISATIONAL FIELDS



We will here describe and explain the market and non-market institutions which have a direct impact on Volvo CE's Korean strategy. These institutions are closely interrelated with Volvo Construction Equipment Korea, and thus the company will have an opportunity to influence them. Organisational Fields consists of the following four institutions: The Korean *Product/Service market*, the *Labour market* and the *Financial market*, as well as the non-market institution the Korean *Government*. The Key Factors which are possible for Volvo CE Korea to influence will in the Organisational Field, play a central role. These Key Factors will here be put back into context, and thus permeate and structure the following institutions.



### 6.2.1 Government

*How important is this Key Factor for Volvo CE Korea in a five-year time frame? Is it important that:*

- Volvo CE retains good relationships to the South Korean government

#### 6.2.1.1 Nurturing the right relationships

Volvo CE Korea has an excellent relationship with the present government. The management in Volvo CE Korea feels that even if the relationship between President Kim Dae Jung and Volvo CE's President in Korea, Mr. Tony Helsham, is partly personal, it also sets an example of a new way to treat foreign direct investors. A new government, if not extremely conservative, would most likely not take the risk of going backwards and worsening the relationship. This implies that Volvo CE Korea will continue to receive a treatment from the government that is adequate. This is illustrated by one of our respondents in the following: "I would like to think that the next government would continue with the reforms that have started in the country, and I think it would be a very bad signal to the community (local and global) if the next government were to have a worse relationship with us" (VCEK) (Interview Volvo CE Korea, 8th of Oct 1999). Today, the excellence of government relationships are best expressed by the award Volvo CE Korea received this spring. On the 16<sup>th</sup> of April, 1999, the Korean government thanked Volvo and three other foreign companies with awards of excellence. (Far Eastern Economic Review, 29<sup>th</sup> of April 1999)

Traditionally, the South Korean conglomerates, the Chaebols, have competed against each other by trying to achieve the best government relations. Firms actually compete with each other directly through the market, as much as indirectly through the central state, thus creating

competitive advantages by establishing good relations with government officials.

One of the key themes of the government's economic restructuring program is the end of the close relationships between government and big business, as well as the more internal relationships among the conglomerates and their various subsidiaries. One criticism, which became more forceful and relevant after the collapse of the Korean economy, was that these ties were too close. Convenience won out over proper regulation and allowed companies to accumulate, rather than solve, problems (Best's Review, Sep 1999). "In the past, the power of the chaebols was very great in Korea. In fact, some acts done by the chaebols were against the law but the Government just closed their eyes" (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999).

#### *Reliance on the State*

When Volvo CE decided to buy the Samsung Excavator division, they were told that the factory was situated on a Greenland area, and therefore the site was not for sale. Volvo CE received from the start much support from the South Korean Government, who has been explicitly welcoming towards Foreign Direct Investors. In the initial stage of the acquisition, Volvo had contact with regional officials in the Changwon area. Those officials told Volvo CE that the land upon which the excavator factory is built could not be sold, because of its Greenland status. Volvo CE told them that if they were not allowed to acquire the real estate, they were not interested in the factory either. After a while, top state government officials organised things so that Volvo CE could buy the part of land as well.

The South Korean President has decided that what South Korea needs is economic restructuring. This includes an opening up of country borders to invite foreign investors to compete directly on the South Korean market. The Korean President is seen as the unquestioned leader, and each president tends to form his own constitution reflecting his singular vision of

the presidency and distinctive ruling style. This executive authority thus becomes remarkably free from either bureaucratic or legislative constraint. This has enabled development goals to be implemented extremely quickly, but also, of course, has intensified traditional Korean dependence on the central state, and to some extent undermined the attempts of creating a democratic nation.

### 6.2.2 Financial Markets

How important are those Key Factors for Volvo CE Korea in a five-year time frame? Is it important that:

- That the Korean Accounting standard is adapted to the international standard?
- To have the right relationships when doing business?

A problem that many companies outside the sphere of the big chaebols still experience is a lack of financial resources. Recently, the Korean stock market has taken a larger part of the financing role than previously, but it cannot more than slightly compensate for the lack of a functioning banking sector. The companies most brutally hurt, are the small businesses not listed on the stock market and not able to borrow internationally and thus restricted to their own capital resources. Examples of such borrowers are Volvo CE Korea's customers who are mostly one machine owners. A form of financing that under these circumstances works well in Korea is sales financing, which is common in the construction equipment market. A step towards a better comprehensive financial market would be to enhance the accounting standards in Korea, thus improving the transparency. The lack of transparency and tools for credit assessment, are major obstacles, and a possible step forward could be pressure from foreign direct investors with an interest in the country.

**6.2.2.1 Have the right relationships when doing business**

Relationships are, at present, the base for credit assessment in Korea, and as Volvo CE Korea is a rather large and well-known company, they have the possibility to exercise some influence in this area. The banks should be interested in having a financially strong company as customer, because of the large and safe volumes that it will generate. A number of banks in Korea are state owned, and this can be an advantage for Volvo CE Korea as well. The good relationship built up between Mr. Helsham, President of Volvo CE Korea, and Korea's President Kim Dae Jung, is to Volvo's advantage. The banks should be interested in having a good relationship with Volvo CE Korea, as they should be interested in financing parts of Volvo CE Korea's business. Volvo CE Korea's transparency in accounting standards will facilitate their possibility to borrow money even more as the banks can more easily make a credit assessment of them. In a long-term view, this implies that the customers of Volvo CE Korea buying construction equipment, should have the possibility to finance the investments not only through sales financing, but also with ordinary bank loans.

**6.2.2.2 Accounting standards**

Possibly, Volvo CE Korea can use the positive outcome of the gained transparency they have experienced themselves, to convince suppliers and others of the necessity of a change in Korean accounting standards. The benefits for Volvo CE Korea are the availability of data needed to change the salary system, as well as the crucial ability to measure the result of the company. As Korean companies are also changing their focus towards a more profit centred management, instead of focusing on market shares, domestic Korean companies would benefit enormously from the transparency that accompanies the Westernised accounting systems. Korea, as a nation, would benefit from applying more international accounting standards, as this would attract more FDI (easier to evaluate for the FDIs (and also credit rating) what they exactly are buying and easier to follow up the investment) and an improved standard would also overall open up the

activity on the Stock market. If Korean companies joined the international accounting standard, international capital would more easily find its way to the Korean Stock market. Not only would the present Korean stock market be affected, but also the chances of developing a risk-capital market would increase enormously.

Accounting practices in Korea are not up to international standards (although they have been upgraded recently). A buyer of a Korean firm may not know with certainty what he has bought. There could be evaluation problems for foreign investors when they buy Korean companies, as full transparency is still lacking. (East Asian Executive Report, 15<sup>th</sup> of Aug 1998) Beginning in 1999, companies have had to comply with international accounting standards, and the supervision of the financial system has been overhauled to meet international norms (The Economist, 10<sup>th</sup> of Jul 1999).

South Korean accountants know how to keep proper books, but the business culture often demands that they do otherwise. There is a tendency to accept white lies as a normal business practice and cover-up for the well being of the company. The cross-guarantee problem has persisted despite the fact that Korean GAAP requires disclosure. The problem has been one of business practice, not of Korean law. Accounts are not consolidated even when the companies under common control constitute a single economic entity. (East Asian Executive Report, 15<sup>th</sup> of Aug 1998)

### **6.2.3 Product/Service Markets**

For the institution of Product/Service Markets, a Porter's five forces industry analysis has been made. The information obtained from this analysis has been sorted under each of the following Key Factors.

*How important are those Key Factors for Volvo CE Korea in a five-year time frame? Is it important that:*

- Volvo CE Korea improves and maintains its relationships with important stakeholders? (In this case, its customers and suppliers.)
  - The Volvo CE Korea products stay competitive regarding delivery time, service offerings and spare part availability?
- Volvo CE Korea avoids price wars on the Korean domestic market?
- Volvo CE Korea gains access to a greater amount of domestic suppliers?
  - Volvo CE Korea focuses more on R&D?

#### **6.2.3.1 Relationship to domestic customers**

The Korean customers are mostly one-machine owners, due to the Union situation during the '90s. The construction industry in Korea had massive problems with the Union. The problems were solved by reorganising the industry and influencing each worker to buy his own excavator, thus having to take responsibility and search for jobs by himself. Therefore Volvo CE Korea has a lot of small customers, and no large fleets. The government purchases construction services from large construction corporations and they, in turn, hire independent construction-workers who bring their own equipment. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999)

The Korean customers are not very sophisticated in their demands. Volvo CE is hoping to educate their customers in financial matters, the importance of spare part availability, service and delivery lead times. This can give Volvo CE a competitive advantage in the eyes of local competitors. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

#### *Customer's price sensitivity*

Volvo CE Korea's customers are very price-sensitive, because most are one-machine owners and the expense for an excavator is nearly 100% of their balance sheet. Perceived differentiation is, today, less significant for

domestic excavators. Japanese products, on the other hand, are perceived to be of ultimate quality, better than other machines sold on the market. In January 2000,

the restrictions on import of Japanese products will be abolished, thus allowing Komatsu into the Korean excavator market. This could mean that many Korean customers will buy Japanese construction equipment in the future, thus forcing some of the uncompetitive Korean manufacturers into liquidation. On the other hand, the antagonism the Koreans have towards the Japanese since the Japanese occupation, combined with a certain amount of an inferiority complex in regard to Japan, could involve some negative response to Japanese products. Before the Korean economic crisis, it was forbidden to import Japanese products in Korea. This prohibition has meant that until now, there have been no Japanese excavators on the Korean market. Komatsu, Volvo CE's main competitor on the global arena, has not been allowed to sell their excavators in Korea. Komatsu is a trendsetter and presents all the technological developments and new concepts in the industry. On January 1, 2000 the competition will be set free due to conditions set by the IMF, and it will be permitted to import construction equipment from the rest of the world into Korea. The Japanese have very favourable domestic prices on their excavator lines because of government/industry cooperation. The excavators bought in Japan are sold at very competitive prices in the surrounding Asian countries. This could mean that used Komatsu excavators could be competing with Volvo CE Korea on the Korean market in the future. Volvo CE could experience heavy competition, because Korean customers are said to believe that the Komatsu quality is outstanding (Interview Volvo CE Korea, 7<sup>th</sup> of oct 1999). The Japanese have moved, in recent years, to more disciplined marketing and are focusing on results. They would not come to Korea and deliberately cut prices in order to gain market shares. Foreign competition, Japanese or American, is not something completely negative. They will most certainly bring a higher level of sophistication into the Korean Construction Equipment Industry, educating the domestic actors not to compete irrationally on price. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999)



*Bargaining power of customers*

Because the Korean buyers of construction equipment are so small and scattered their buyer power is insignificant. On the other hand, the cost to a customer of switching to another brand is next to nothing, except when the customer is tied to the manufacturer by sales financing, in which keeping the same brand gives a better price for a new machine. There are also many sellers on the market competing heavily on price. Increased bargaining power by the buyers is also induced by the availability of information in the industry, with price being the most important information carrier.

**6.2.3.2 Relationship with domestic suppliers**

Volvo CE Korea has now cleared out a large quantity of Korean domestic suppliers that do not reach the required quality level. Volvo CE now focuses on relationships with larger suppliers that have an international capacity. 125 suppliers are now gone and in total, the amount has declined from 475 to 350 suppliers. This is said to have improved Volvo CE Korea's efficiency. (Dagens Industri, 11<sup>th</sup> of Nov 1999)

Lim Myong Sup, the owner of Dae Myong Industries (one of Volvo CE's largest supplier in Korea), is critical to Volvo CE Korea. He believes that "Volvo behaves insensitively. Volvo is only interested in good quality at the lowest possible prices. They do not want to have any other relation to us. In Samsung days, the suppliers were a part of the Samsung family even though they formally were outside actors. The suppliers got information every third month about future plans. The suppliers socialised a lot with Samsung management, playing golf, drinking and singing. The Volvo CE management has neither informed us of their strategy, nor have they shown any interest in social activities. Lim Myong Suk believes that European companies do not trust the Korean quality. Volvo demands 100% quality from the first delivery and this does not work. *The Japanese have understood that they have to send technicians to teach us, explain their systems. By doing this the ground is laid for high quality and long term cooperation.*" Lim Myong Suk is proud to have met the extremely high

quality demands by the Japanese. According to Lim Myong Suk due to Volvo CE's low capacity utilisation, Dae Myong Industries has had to let go of almost 50% of their employees. This is seen as a large problem because of the owner's feeling of obligation towards his employees, and the promise he gave to re-employ them again when the economic crisis was over. (Göteborgs-posten, 4<sup>th</sup> of Nov 1999)

The supplier in the above example emphasises the need for social relationships when interacting with his principal. In Korea, these types of relationships normally include a high level of personal trust. Volvo CE Korea is, on the other hand, characterised by typical Western values, and wants to build their relationships with their suppliers on more technical bases. They want suppliers to invest more in Research and Development activities. This would strengthen the relationship with Volvo CE Korea, because the amount the supplier has invested makes it harder for him to switch to another customer, and of course, Volvo CE Korea does not want to carry all unnecessary costs of non-core activities. The supplier, on the other hand, has little interest in investing in the relationship because of the lack of commitment Volvo CE Korea shows in refusing to socialise with the supplier in the family-like way he is used to. According to Whitley, cooperative behaviour between Korean firms is unlikely unless a family-like relationship has been establishment. The establishing of such relationships takes time, as well as an understanding of how such relationships are developed.

#### *Supplier's price sensitivity*

The level of competition between suppliers, domestically and globally, is high.

Differentiation is mainly made by the augmented product, i.e. delivery times, order systems, quality, and active participation in R&D. Korean suppliers are in this respect not globally competitive.

*Supplier's bargaining power*

The suppliers have little power because they are relatively small in comparison to the Construction Equipment manufacturers. The cost of switching depends on the level of interaction and sunk costs invested in systems and processes. Lack of transparency of Korean financial systems makes the availability of information about suppliers limited. It is hard to know if the supplier is financially stable and can fulfil his assignments. Backward integration is possible, but as the supplier industry is characterised by low margins, this is not an interesting option.

**6.2.3.3 Volvo CE Korea gains access to a greater amount of domestic suppliers?**

There is a huge supplier base in Korea that can do anything Volvo CE Korea requires, even if the suppliers now are under severe financial pressure. "A critical issue for Volvo CE Korea is to gain sufficient volume to be of interest for the suppliers, as they need to make investments in tools, etc. Nearly everything is possible to localise and get Volvo quality standards in, if Volvo CE Korea only can offer the right volume." (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

Volvo CE Korea's supplier base is adversely affected by the drop in volume, and they will face big challenges in increasing the stability of the supplier base. Volvo CE Korea could relatively easily find sources in Europe or other Asian countries, but it is always easier and usually cheaper to deal with a local supplier. They do not see any obstacles to easily switching. The barriers to switching generally are not that high for most of Volvo CE Korea's products. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

"The more Volvo CE Korea focuses on its core production, the more important it will be to have many reliable suppliers on the domestic market. In some special fields, such as hydraulics, there is an educational process going on." (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

*Focus on R&D*

Volvo has to educate its suppliers due to the complexity of the components and because of the high quality that Volvo CE demands of the devices they purchase. Volvo CE Korea's suppliers are, today, not accepting their part in R&D. They do not have the financial or organisational resources required for technical development of the parts they deliver. When Volvo CE Korea moves more production to Korea, this could be a problem. The suppliers are said to be lacking resources to contribute to the R&D process. It is said to be difficult to get them involved in the product planning process. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

**6.2.3.4 Volvo CE Korea avoids price wars**

The price war on the Korean market between the actors within the Korean Construction Equipment Industry has been murderous. Previously, this was due to the focus the Koreans have had on gaining market shares, and in the last few years even more so, due to the Asian/Korean Crisis.

Volvo CE Korea has done what they can to push the prices to a level where profit can be made. For instance, they have introduced a product financing system that has included taking away the too generous financing conditions customers were offered by the former owner, Samsung Heavy Industries. The overall product prices were also raised. The first month after the change, Volvo CE Korea's market share fell from 40% to 15%. Two months later, the competitors Daewoo and Hyundai followed by imitating the concept, and Volvo CE Korea suddenly had a 60% domestic market share. Today, Volvo CE Korea's market share has stabilised at 40%. (Interview Volvo CE Korea, 7<sup>th</sup> of Oct 1999)

Volvo CE Korea should try to educate their Korean based competitors in maintaining a price level adapted to global standards, rather than keeping their standards at the customary Korean level. Volvo CE Korea would prefer their competitors to be mature and sophisticated than to compete irrationally on price as has been done in the past. The price leadership

position Volvo CE Korea has taken will benefit them even more on a global scale than in the Korean domestic market. The margins will always be rather small in Korea and the more sophistication that is brought in, the more profit there will be for all actors concerned. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

#### 6.2.4 Labour Markets

The following institution will be explained from a social perspective, and put into relation with the following stated Key Factors:

*How important are those Key Factors for Volvo CE Korea in a five-year time frame? Is it important that:*

- Human Resources becomes Westernised in the sense that:
  - Existing hierarchies are levelled out?
  - Performance based salary systems are introduced?
  - Relationships with the Korean workforce is improved:

##### 6.2.4.1 Korean organisational hierarchies and authority types

South Korea continues to suffer from a “Confucian” labour market in which paternalistic managers bully and protect workers in equal measure (The Economist, 10<sup>th</sup> of Jul 1999). The Korean leader type is authoritarian but also sympathetic, nurturing and sensitive to the wishes of his followers (Pye 1986). Distant authority relations and hierarchies are an essential phenomenon in Korean society that is reflected to a great extent in the business life. “One matter that talks against the willingness to work for a foreign firm is the low emphasis that those companies put on titles, at least in comparison to Korean firms” (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999). Traditionally, Koreans have fought to achieve relative status and to climb up to reach high-rank posts. This has also led to a greater acceptance of formal hierarchies and managerial positions. After the Korean civil war the country became militarised and South Korean males were taught how to act in a militarily disciplined way. This high level of militaristic discipline

throughout Korean society has been an important factor in the economic development of Korea, and has reinforced traditional Confucian acceptance of hierarchical authority. In today's South Korean business life, immense status is conveyed by being able to show a business card proving a high rank position in a company. All these factors combined makes it difficult to believe that with the existing set of values, the Korean employee of today would accept a removal of existing hierarchy levels. In this study, though, there are some indications that the younger generation in Korea has other values concerning working life.

#### **6.2.4.2 Performance based salary system**

Performance is a management priority in multinational corporations. In South Korea, performance-based incentives are still largely unheard of. Pay and promotion, are determined by seniority, not merit. As a result, by the time the Asian economic crisis struck, labour productivity in South Korea was only half of that in America. LG Chemical has introduced a new system of performance-related pay, with a bonus that can be worth as much as three month's wages. (The Economist, 10<sup>th</sup> of Jul 1999)

People think that South Korea is a low cost labour country in which to manufacture. The fact is that this situation started to diminish 12-15 years ago. The chaebols have been totally fixated on growth, and have forgotten to focus on the true fundamental – profitability. Wages are particularly troublesome. With the arrival of democracy in 1987, pay started to go up. Raises were long overdue after years of repression, but workers enjoyed total job security, and had no notion that wages should bear some relation to productivity. For a whole decade, increases averaged 15% a year. This means that salaries are now almost at the same level as in Europe and the USA. If Volvo CE Korea allows this to continue, according to one respondent, they will soon price themselves out of the market place. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

In answer to the question whether the salaries in Korea should be more directly related to performance, we were told by Western managers that the important issue is that salary should reflect the “added value” contributed by the employee, and how profitable the company is. The Korean companies used to believe that they assumed social responsibility by keeping people employed, and they did not consider whether this was efficient or not. The changes that Volvo CE has made since the acquisition of Samsung have brought strong reactions, because in the Samsung days it appeared that there was always money to spend on the employees. The general opinion, though, among Western managers at Volvo CE today is that the employees must be paid according to what they contribute to the organisation. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

Volvo CE and other foreign direct investors are trying to break up the traditional salary system in Korea. The traditional salary system, the so-called Hobong system, promotes employees and assigns raises depending on age, sex, and years employed. Promotions and salaries are not at all dependent on performance and/or merits. The resistance to the implementation of a performance based salary system could also be explained by traditional Confucian values that put a focus on harmony. If a manager is supposed to evaluate an employee on the basis of the employee's skills, it could result in the employee feeling uncomfortable, because an evaluation of him as a human being is taking place. The manager would, according to this reasoning, also feel uneasy because he knows that his judgement could disturb the harmony of the relationship. To be able to measure performance accurately, the employee must be measured according to his/her specialised skills and capacity to contribute to profitability. On the other hand, the Confucian philosophy, which still prevails in Korea, puts an emphasis on the importance of general knowledge expressed in high moral worth. In this sense, a managerial decision to decrease an employee's salary on the basis that he/she is not contributing enough to profit would be experienced as an attack on the employee's personal qualities and character. Hence, when a leader has to

give opinions on how the employee is performing, it could, in a Korean context, lead to that employee losing face. A performance based salary system also aims at supporting individual achievements, and thus undermines the collectivistic, group oriented view that has traditionally prevailed in the Korean society.

*The Hobong system*

“The question is, how to preserve the best from the two worlds? It will have to be re-adjustments from both sides, and not everyone is going to feel comfortable in this transition process. This is not going to be a situation where everybody is going to feel happy in the end. We would like that to happen but it is not likely. Every company has its own culture and it is not always certain that you will fit in everywhere. The challenge is to first identify the truly competent people, the ones we feel are doing well in the new environment, making sure we have the core people moving with us.” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) To what degree are Korean employees capable of adopting to a new system built on performance, instead of the relatively secure Hobong-system? “The Hobong system is to a large extent built on the view that every employee should be treated equally. The whole situation concerning human resources in Korean companies is that there is too much collectivistic thinking; when the conditions are equal for everyone, everyone is satisfied.” (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999) This group-oriented view goes well with the Koreans’ traditionally collectivistic behavioural pattern. In this research, though, there have been signs that there is some change towards a more individualistic society. Students are looking for employment in foreign firms because of the possibility they offer for individual development, for example, in terms of language courses, and the possibility to work in other countries. “The younger generation in Korea has a very international mindset, so they prefer to be in a Westernised company rather than in a Korean company” (Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999). If the trends towards a more individualistic behaviour and an overall quest for more traditionally Western values are facts, then the foreign employers are



attractive in what they offer to employees. Their flat organisations give room for individual initiatives and salaries related to performance, as well as opportunities to advance based on skills and performance rather than old age and length of employment. All these factors will possibly outweigh the fact that foreign companies do not offer lifetime employment conditions.

#### 6.2.4.3 Relation to Human Resources

The Koreans were through the whole crisis very supportive of their country, and understood that they had to make sacrifices. Many elderly citizens for instance, gave away their jewellery as financial assistance to help their country out of the crisis. The recent recovery of the Korean economy has now started to trigger strikes and student demonstrations. The understanding between the government and labour market parties has fallen apart. Many South Koreans think they have been tormented enough and that there now exist margins for protests. (Dagens Industri, 29<sup>th</sup> of Apr 1999) The unions pulled back from a public sector strike earlier this year, but say, “the environment is set for confrontation” (The Economist, 10<sup>th</sup> of Jul 1999).

The government is showing its outward will to restructure the Korean economy, but there are many signs that this restructuring process will be rather slow. This is also true of labour issues. The Korean Minister of Labour disappointed representatives from foreign direct investors. The Minister wanted them to buy the concept that Korea was unique and that the relations between employees and the company were *not* in need of any normalisation process. That was not what the foreign companies wanted to hear, as they believe direct government interaction to be necessary in order to change the labour-regulation-system. (Interview Volvo CE Korea, 8<sup>th</sup> of Oct 1999)

“The voice of the labour union has become very loud in Korea recently. Even if a company knows how to improve efficiency, they cannot take

action because they are afraid of how the labour union will react.”  
(Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999)

The Volvo CE Korea Union believes that the general attitude amongst the employees towards Volvo CE is rather negative because of the lay-offs that have taken place. The Union believes that if Volvo CE continues to lay off people in Korea, they will not be able to avoid a strike. “In Sweden, you have a very well working social system and if you are laid off you can always find other ways to survive. In Korea, the social systems are very weak and we do not know what to do if we get kicked out of the company.” There are two things that the Volvo CE Korea Labour Union representatives want to emphasise:

- The Koreans believe the company to be an extended family. The employees today cannot find this atmosphere within the Volvo CE Korea’s organisation. The Labour Union wants to see some concrete action in the creation of a feeling of belonging in the company.
- They want to have assurance that their employment will last a lifetime. A guaranteed lifelong employment creates the security that the employees need because of the insufficient social welfare system in Korea. This security will also enhance loyalty to the company and the employees will make greater sacrifices in order to do a good job.  
(Interview Volvo CE Korea, 12<sup>th</sup> of Oct 1999)

As the Korean leader is supposed to be sympathetic, nurturing, and sensitive to the wishes of his followers and thus has emotional obligations to fulfil (Pye, 1986), the organisational climate in South Korean companies has until now been characterised by a family-like atmosphere. Due to the authority relations the employees have with the often paternalistic managers, the employees are used to doing what they are told, and therefore have never been forced to take full responsibility for their actions. This family like atmosphere is now diminishing due to Volvo CE Korea’s

emphasis on individual achievements instead of collective actions. This probably will create insecurity among those who are used to being “taken care of” by protective managers and not have had to take any initiative.

### 6.3 ANSWER TO RESEARCH PROBLEM I.

To conclude this chapter and to get into the actual writing of scenarios, we will look into how the Environmental Analysis can be summarised into factors that will either contribute to changes in society, or be part of the cause for environmental stability. This could be seen as a way to convert the environmental analysis into envisions for societal development.

#### 6.3.1 Determining the level of societal development

Both the facts that the South Korean environment will undergo changes, and that in some aspects will remain stable are vital in the process of scenario development. Examples of this could be the fact that the globalisation of markets and industries leads to changes in industry structure. The consolidation of the global Construction Equipment Industry is something that also will come to affect the Korean domestic Construction Equipment Industry. Globalisation could thus be classified as a “driver of change”. Conversely, the social system in Korea is permeated by Confucian traditional values and should be seen as a “determinant for stability”, as this philosophy contributes in conserving South Korean traditional norms and values. This could be seen, for instance, in the resistance towards tearing down hierarchies, accepting Western business practise, etc.

##### 6.3.1.1 Drivers of change vs. Determinants for stability

These “Drivers of change” and “Determinants for stability” are summarised in the Scenario Overview below. (See Table 6.1)

Table 6.1 The “Scenario overview” concluding the Environmental Analysis

<b>Institutions</b>	<b>Drivers for change in Korea</b>	<b>Determinants for Stability in Korea</b>
<b>Government</b>	<b>Kim Dae Jung</b> and his politics <b>IMF and World Bank</b> *	<b>Nationalism</b>
<b>Labour Market</b>	<b>The Korean financial crisis</b> made the workforce aware that change was needed <b>Globalisation</b> - Language skills - Foreign education <b>FDI implementation of Performance based salary system</b> *	<b>Confucianism</b> -Family clan -Hierarchies -Authority distance <b>Business Mores</b> - The Hobong System <b>Korean Country Culture</b>
<b>Construction Equipment Market/Industry</b>	<b>Globalisation</b> - Consolidation - Increased foreign competition from Jan. 2000 - More sophisticated customers demand quality and transparency <b>Open market</b> *	<b>Protectionism</b> <b>Nationalism</b> <b>Suppliers</b> unwilling to co-operate with FDIs by sharing R&D expenses

<b>Financial Markets</b>	<b>Financial crisis</b> The fall of Chaebol Law protecting minority share holders <b>Globalisation</b> <b>Open market</b> <b>Fluctuations of exchange-rate</b> *	<b>Protectionism Nationalism</b>
* Foreign Direct Investor's expectations for, and demand for change		

Source: Own Source

In concluding this analysis, we have also managed to solve our first research problem:

*“to analyse the environment of the emerging market by explaining its institutional set-up, and by this define the drivers of future environmental change”.*

After this preface of investigating the MNC and explaining its environment, the next chapter will illustrate how the actual scenarios will look.

## **7 SCENARIOS FOR VOLVO CE KOREA IN THE YEAR 2005**

In this chapter we will describe different possible scenarios for the Korean market in a five year time period. Using the scenarios, we would like to illustrate that Volvo CE Korea could be challenged by developments in Korean society, which require thorough consideration.

The Drivers of Change and the Determinants for Stability, which concluded the previous chapter, jointly represent the essence of the environmental analysis, and are used as a base when creating the scenarios.

The scenarios will be structured according to the Organisational Field in the Institutional Analysis. The four institutions from the Organisational Fields that will be treated in the scenarios are the Financial Market, the Labour Market, the Product/Service Market (Construction Equipment Industry/Market) and Government.

Overall the illustrations in the scenarios are based on a situation where Volvo CE Korea has a relation to the Korean Won in reference to a basket of currencies. No single currency or country has a single dominating influence over if the Korean Won is perceived to be high- or low-valued. The basket of currencies that are valid for Volvo CE Korea constitutes of US Dollar, Japanese Yen and EURO, as these currencies represent the countries where their competitors are doing business. This constructed basket thus determine the relative cost competitiveness that Volvo CE Korea gains relative to competitors, and enables us to discuss a high- or low-valued Korean Won in general terms.

The sensitive relationship to North Korea, is in the depicted five year period, not assumed to go through any deeper change; instead, the current situation between the two Koreas will continue to prevail. There is one exception though; in the scenario called “Alone is Strong”, the forces rushing the gradual reunification are evident.

Other basic conditions for the four scenarios depicted below are that no “force majeure” will occur in South Korea, e.g. natural disasters or attacks by hostile nations. Other general assumptions are that the global economy develops with a stable but not high growth rate, and that crude oil prices do not change significantly during the time period.

We have put the two most important Key Factors in a matrix with two axes. The Key Factors are:

- Exchange rate; a strong vs. a weak South Korean Won
- The level of openness vs. protectionism in the South Korean Economy

These two Key Factors were chosen by our respondents in Volvo CE Korea to be the most important for Volvo CE's future success. In the Environmental Analysis both factors were found to be of high importance, because the majority of what Volvo CE Korea produces is exported. (See Figure 7.1)





7.1 “THE SUN IS SHINING “

*A scenario outlined for 2005: The combination of a strong Korean Won  
and an economy characterised by openness*

**The Years 2000-2005 - A summary**

- Fundamental restructuring
- The President reduced his own power
- BOT-financing
- Entrepreneurial domestic service industry
- Global competitiveness by increase in workers efficiency
- Government increased social welfare
- Healthy competition on construction market

**7.1.1 Government**

In the Parliament election in the spring of 2000, Kim Dae Jung's party, National Congress for New Politics, was elected to run the country for the coming four years. Kim Dae Jung himself presided for the duration of appointment, until the end of 2003. After Kim Dae Jung's retirement, his predecessor, continued to govern in a consistent way, and supported by a majority of the parliament, led a fundamental restructuring of the whole society.

After the Parliamentary election, the President recommended to the Parliament that the constitution be changed so as to reduce his own power. His intent was to move towards a more democratic system in which state councils were appointed not by himself but by the Parliament. This radical step was seen as a major sign of a policy to truly change Korean society in a fundamental way, not hampered by the traditional power-centred hierarchy.

The government continued its extensive privatisation program that it had begun 1998 by selling state owned steel and electricity companies to

private interests. Due to the restrained budget of the state, the government initiated a new policy of letting foreign companies handle new infrastructure projects in water- and energy-facilities, as well as in roads via BOT- financing (Build-operate-transfer). After the agreed operating time, the companies were either given the opportunity to buy the project-enterprise, or the government listed it on the Stock Market and gradually sold the shares to Korean and foreign investors. For some projects, the shares were spread over the Korean population after the BOT-period, because they operated in areas in which Koreans have traditionally been especially sensitive to foreign ownership, e.g. industries related to the defence area.

The BOT-financed projects were initiated after the parliament election in May 2000, due to the government's promises in the election-campaign to introduce a better welfare and unemployment system. The government aimed to focus on its core-activities, and to gradually cease the direct and indirect ownership of companies by the State budget. The change in direction was supported by the voters as the turn in economical development, proved by the GDP growth of 9.5 percent 1999, made them realise that structural changes were necessary, and would bring the benefits that were no longer realistic to expect from an economy built mainly upon the reliance of chaebols on the government.

In the middle of the year 2000, Daewoo's head owner was accused of corruption, put in remand prison, and after lengthy court proceedings, ordered to serve some years in jail. The structural overhaul of the legislation, which started in 1997, became more focused on the elimination of problematic events in the beginning of 2000 and up to 2005. By enforcing existing laws in the handling of the tax evasion of Samsung in 1999 and the jailing of Daewoo's owner, the government demonstrated its firm intent to a fundamentally change society.

### **7.1.2 Financial Market**

As the payment of the USD 57-bln IMF-loan started in the year 2000, the budget of the state was burdened. Although the GDP growth figures showed that the financial crisis of 1997 had turned around, the government continued to focus on fundamental restructuring of the Korean institutions. The restructuring at the beginning of the new decade was especially aimed at shifting the focus from heavy dependence on the export-industry to a development of the domestic service-industries. Simultaneously the restructuring aimed at transforming the Korean economy from being heavily dominated by the big chaebols, to an economy that relies on smaller entrepreneurial businesses. This fundamental change meant that former government support to the chaebols, in the form of cheap or non-interest credit, diminished drastically at the beginning of the decade, and completely ended by 2005. The alteration of financial allocation meant that the financial service to smaller businesses grew. With the support of improved GAAP-standards, and following transparency, the Stock Market grew in importance as a capital supplier, even for smaller companies. To further encourage entrepreneurship in the country to flourish, legalisation facilitating the establishment of smaller companies was passed.

The government-initiated change of focus in business towards the service sector and small-scale enterprises led to an entrepreneurial era in Korea. The change in attitude was supported both by the fact that people formerly employed by the big chaebols had to seek new means to support themselves, and fact that the availability of financing for smaller companies made the transition possible. Many men and women began to run small companies in the service sector, supported by the facilitating regulations concerning establishment and availability of capital.

### **7.1.3 Labour Market**

Large groups within the Labour Union were fiercely resistant to the layoffs the chaebols enforced as an immediate result of the diminishing financial support from the government. Employees were also forced to leave their

jobs due to the overall improved focus on profitability in Korean companies. The aim of globally competitiveness and thus survival under the new conditions enforced by the government also meant an increased concentration on worker's performance and efficiency. Performance based salary systems were introduced, and replaced the Hobong system of yearly increases connected to age and years of employment. The focus on hierarchies and titles diminished and caused insecurity in the companies. Management was very much aware of the vast scope of the changes that had been initiated, and took steps to facilitate the transition. Labour Unions did not accept the fundamental change from life-long employment traditions to the supply- and demand-market of labour, and strikes paralysed parts of the industry in the beginning of the decade.

The resistance among labour Unions weakened after the initial fierce resistance, though. The reasons for reduced resistance towards the lay-offs were many; the increase in export, due to the still rather low valuation of the Won in the first couple of years after the millennium-shift, combined with the export-industry's enhanced competitiveness and ensuing growth, compensated for the majority of the layoffs. For those, hurt by the changed labour market politics, the government increased the social welfare net, thus taking over the former company-responsibility of caring for employees. The influences from the foreign direct investors in the country were more and more evident early in the first decade of the 21<sup>st</sup> century. Representatives from Labour Unions in Korea gained insight into the work and the aim of Labour Unions in the Western world.

The group oriented Korean people slowly started to change around the year 2000. As the pressure for structural change was considerable from many parties, the pace of the change accelerated considerable from the first years until the middle of the decade. The idea that globally competitive companies were a prerequisite for life-long employment was gradually accepted by the Labour Union, prompted by pressure from both the companies' management and government politics. The general politics

from the government supported the transition in different ways, as they themselves reduced hierarchy levels and the focus on titles, as a signal to the people.

#### **7.1.4 Construction Equipment Industry/Market**

The BOT- projects initiated by the government made the Korean GDP rise significantly in the years 2000-2005. The new entrepreneurial era meant a lot for the construction equipment market, and together with the BOT-projects, it boosted the market. Activity in the country was large and confidence in the future significant. Private housing- and business-construction projects took place, as well as BOT-projects within the energy- and infrastructure-sector.

Trust in Korea's new politics way gave confidence to the surrounding world and lowered the interest rate significantly from that of the end of 1999. Inflation increased due to the boost in the economy, but not to the extent that it threatened the strong Korean Won gravely. In the beginning of the decade, Korean exports prospered as the valuation of the Korean Won made the products very competitive. The Koreans managed to maintain global competitiveness, even when the currency was strengthened, by an ongoing process of quality- and efficiency-development in the industry.

Healthy competition characterised the construction equipment market in this period, since the government did not intervene in business life as before the Asian crisis. The long awaited company restructuring of Daewoo finally took place in an organised manner. The business conditions prevailing in Korea in the period allowed it to occur without too many injuries along the way.

A new direction for companies' research and development became apparent during the five years following the millennium shift. Already by the end of year 2000, foreign investors had called the government's

attention to problems with finding globally competitive suppliers within the country. The main problem, according to foreign firms, was the Korean suppliers' unwillingness to participate in research and development. Foreign investors wanted to be able to outsource a larger part of their development and production of components, but Korean suppliers were reluctant. But some domestic producers had pointed out that the Korean manufacturing industry would risk losing competitiveness if they did not catch up with Western standards in the area, so the government acted quickly. The threat from some neighbours, such as China, to take over the Korean suppliers' position as mere suppliers was also possible, if Korea did not choose to move into a more sophisticated industry structure.

The government and businesses initiated research and development programs at the Universities. The substantial management and economic undertaking foreign investors then showed had the positive outcome of strengthening reputation for long-term commitment and for having the ability to build relationships, things that generally had been questioned.

## 7.2 "ALONE IS STRONG"

*A scenario outlined for year 2005: The combination of a strong Korean Won and an economy characterised by protectionism*

### **The Years 2000-2005 - A summary**

- New conservative rulers
- Nationalism and protectionism grew together with the Hahn-spirit
- Intensified and successful focus on chaebols restructuring
- Cheaper production gained by reallocation
- Foreign aid to North Korea boosted the construction industry
- Sophisticated industry in Korea started to develop

### 7.2.1 Government

In the parliamentary election in the spring of 2000, Korea altered its political track by choosing a new Parliament consisting of conservative forces from the Grand National party. Kim Dae Jung had been appointed for presidency until 2002, but his power to act was reduced enormously when the majority of his party members from the National Congress for New Politics were replaced. Kim Dae Jung stayed at his post for the duration of his presidency, but was not able to influence politics to any significant degree.

The Grand National party won the election in large part due to the strong support they received from chaebol owners, who raised funds and placed social prestige on reducing the power of Kim Dae Jung, the man they felt had hurt them so severely by aiming to fundamentally reconstruct the Korean business life. The labour force was not pleased with Kim Dae Jung's politics either. The changes in worklife had been significant; unemployment resulted from the process of restructuring the chaebols, as well as higher demands for efficiency from the remaining workforce. The changes that Kim Dae Jung enforced in attitude, values and behaviour led to a strong nostalgia for traditional Korean values. The hunger for a high degree of self-reliance and thus nationalism grew strong among large groups of Koreans. A group of Foreign Direct Investors, who in a very self-righteous way had tried to force their business practises onto the Koreans for some years, were a major reason for the strong nationalistic feelings.

The strong feeling for the home country also supported the South Korean's desire for re-unification with North Korea. In the beginning of the decade, the Grand National party promised to work intensively towards a unified Korea. By intensively supporting the South Korean business activities in North Korea, already initiated by the large chaebols (Hyundai, Samsung, Daewoo and Lucky-Goldstar) in the end of the '90s, and at the same time, by supplying food- and other aid-deliveries, the North Korean regime was persuaded to co-operate. North Korea was then in desperate need of outside

support, especially after the severe flooding 2002. They were forced to co-operate with South Korea, as their former communist allies were not capable of supporting them financially.

North Korea's relationship with China was also extremely strained in the beginning of the millennium. North Korea had, despite several sharp instructions from China, not been able to prevent refugees from invading China; the problem was as severe as ever.

South Korea gained global competitiveness from the extraordinarily cheap workforce available in North Korea. The access to a huge potential market was in line with the government's plans to boost domestic growth by first, expanding the home market to include North Korea, and secondly, gaining access to North Korea's important natural resources, which South Korea to a great extent lacks. The two governments strictly dictated the rules of reunification, as both wanted a slow and gradual reunion. The motive for the regime in North Korea was to not expose the fundamental mistakes they had made when trying to achieve a rise in living standard after the war. They wanted catch up to some extent with the South Korean living standards before exposing North Korea's situation to the rest of the world. South Korea's motives for a slow and gradual reunification were financial; they would not be able to handle a reunification if they were not allowed to strengthen their economic situation first.

Thailand and Indonesia had been explored before the financial crisis by the big chaebols as sites for cheaper production. This development continued under the new government, but with a new intensity. The chaebols restructured their business within the country and concentrated on their core business as early as in the first year after the millennium shift. The chaebols shifted divisions between each other and started to grow very strong in the segments within which they now specialised. The chaebols grew stronger as they gained global competitiveness.



### **7.2.2 Financial Markets**

The foreign investors in Korea were shocked by the degree of forming around the new nationalistic politics in the election year 2000. After a cautious start, the new government gradually altered the regulations in the financial field back to those prevailing in the middle of the eighties, meaning there was no legal enforcement of laws (competition-laws, tax-laws etc). The nurturing of state connections was again facilitated; transparency and shareholder rights were of low concern. The organs that had been designated by the Kim Dae Jung's regime to support foreign direct investments in Korea were closed down. Foreign investors that had the slightest opportunity to withdraw from the Korean market did so because of lost confidence in the new regime, and caused a severe slump at the Korean Stock Exchange.

The banks were controlled by the big chaebols as before the crisis, but the government exercised some control to prevent unhealthy businesses from receiving new credit. The control was lame though, due to the many prevailing relationships developed by the support of the Grand National party and its leader Lee Hoi-chang during the election campaign in the spring of 2000.

### **7.2.3 Labour Markets**

The "Hahn-spirit" amongst the Korean labour force was triggered by the government slogans like; "Building a strong nation based on Korean values." The labour force was content with the fact that the Hobong system was maintained, assuring annual salary increases and the security of each employee's position in the hierarchy. Due to the expansion of business activities in large scale into North Korea, the pressure to reduce salaries was extreme. The work force was not satisfied with the worsened conditions, but as nationalism was flourishing and propaganda was extensive, the Labour Union did not take any action against the new regime. Koreans valued the fact that the economic gap between rich and poor shrank in South Korea, and that unification with North Korea was

closer than ever. The government used the process of reunification with North Korea as an excuse for measures that were taken, such as cutting salaries and severely restricting the import of foreign goods. South Korea once again globalised its business on behalf of the domestic population allowing no import of raw material or consumer goods.

#### **7.2.4 Construction Equipment Industry/Market**

The government's methods of supporting the domestic industry changed. Effort was made to increase the global competitiveness of the industry, and to find alternatives for the survival of the chaebols other than protection by any means necessary. The chaebols' restructuring was done gradually, but with a focus on real action and a conviction to succeed that was lacking in the restructuring plans in the late 90s.

Much focus was put in developing the economy in South Korea towards a more research and development intensive industry. The manufacturing of simpler goods was transferred to North Korea, Indonesia and Thailand, but under owner-control of South Korea. The basis for developing a more sophisticated industry in South Korea was excellent, with a well-educated workforce with an endless drive for moving upwards in the hierarchy. The impact of the departure of some younger and well-educated Koreans left the country in the beginning of the decade restrained the effort somewhat, but not significantly. In reality, there was no mass exodus since the majority, among other things, was tied by tight family bonds and patriotic feelings.

Now, in the end of the period of 2000-2005, the market for construction equipment is strong. The government's and industry's change towards a more sophisticated type of industry are showing quick results. The Korean engineers surpassed themselves with the pace of innovation and development of products to be introduced on the global market in 2004-2005. The new products, along with the increased competitiveness gained by using cheap North Korean, Thai and Indonesian labour means a new and

favourable position for Korea's industry. The competitiveness on the global market is strong and not even disturbed by the fact that the exchange rate is not positive for the export industry.

The potential domestic market for construction equipment is enormous, as North Korea must be developed significantly in the coming integration to meet the South Korean standard. The actual projects initiated by the South Korean Government in North Korea is thus of minor importance as the economy is a restraining factor, hampering the infrastructure and housing from developing according to the actual needs. The government has, during the whole period of 2000-2005, kept tight control of the expenditures and did not allow any domestic reforms or projects that were not politically defensible as supporting the overall aim of making Korean industry a competitive player on the global market. As a result of the surrounding world's interest in a reunified South and North Korea, though, aid from the Asian Development Bank and World Bank, among others, has supported large infrastructure projects in North Korea. These aid-projects have helped the construction industry enormously and resulted in a strong domestic market. The positive attitude from the surrounding world has also enhanced South Korea's reputation on the world trade market, needed as a compensation for the bad will provoked by continued protectionist policies. The result of these policies is that the domestic welfare system in South Korea suffers, but has future potential to develop, as the government will need to commit export incomes to projects on the domestic market to keep the population agreeable.

### 7.3 “RISING SUN”

*A scenario outlined for 2005: The combination of a weak Korean Won and openness in the economy.*

#### **The Years 2000-2005 - A summary**

- Slow but steady restructuring
- Chaebol divestment
- Transparency a tool for attracting investment
- Performance based salary system stepwise introduced
- Export industry boosted
- Construction market takes off

#### **7.3.1 Government**

The move by the government in 1998 toward a fundamental political-, industrial- and financial-restructuring in Korea, continued through the following years. The financial crisis and the resulting loan from the IMF in 1997 led to the insight that change was needed. Under pressure from IMF, the economy was opened up, although not at the pace or to the extent that some had hoped. Kim Dae Jung was firm in his direction, but due to considerations about the unemployment situation for the country and tactics regarding the election, the governments restructuring and reform was not without interruptions and delays. Kim Dae Jung and the government intended to focus to create a fundamental change towards a more open Korean society. The aim was to move towards a market economy, without causing negative outcomes such as massive layoffs or bankruptcy in some of the big chaebols, or requiring that more banks be taken over by the State. The government calculated that these things would occur if a too brusque pressure was laid on the Daewoo and Hyundai Groups. These factors made the government choose a slower but “steadier” course to a full reign of market forces in the years 2000 to 2005.

The social structure in Korea was, in the early 21<sup>st</sup> century, in need of change if it was to move towards a market economy. The government was

able to afford a very limited net of social welfare. This supported the transition, by allowing some unemployment without causing social unrest that could lead to questioning of the government's right to rule the country.

The government used the legal system in the restructuring, but it was moderately changed during the period between 1999 and 2005. The main difference was that prevailing laws began to be enforced. The pressure from the IMF as well as from outside investors slowly caused the gap between the existing laws and enforcement to be closed. The Competition law was put in use (under pressure from regulators), and increased the already heavy pressure on the five big chaebols to sell off and "exchange" industry-divisions in order to limit the misuse of competition in the country.

### **7.3.2 Financial market**

The new way of attracting investors outside the big internal groups (Chaebols, The State Banks), which was part of the aim of the openness initiated in the late '90, required a change in Korean accounting standards. As transparency from international accounting standards was gradually introduced, starting 2000, shareholders received a transparency long missed by foreign investors, and the FDI increased. The shareholders were more easily able to demand action and responsibility from the board of the company, and domestic investors were attracted to the Korean Stock Market again. The international GAAP standard was set as a standard requirement for those companies wanting to remain on, or enter into, the Korean Stock Market.

As the transparency in accounting overall opened up a greater ability for companies to be evaluated on sounder grounds, and thus be able to attract (foreign) capital with their future potential, many of the middle-sized companies, not obligated by law, followed. As many of the Korean companies suffered from under investment and lack of capital in the beginning of the 2000-century, this was a necessary step to attract capital,

and a prerequisite for the debt-burdened Korea. The reforms went slowly, though, and it was only in the middle of the decade that it was possible to begin to see the effects.

The banks, many of which were owned by the state after the crisis at the end of the '90s, became more aware of the importance of a healthy portfolio, and they increased their ability and tools for making credit analyses.

The low valuation of the Korean Won in the beginning of the 21<sup>st</sup> century was, of course, both a result of the Korean States' financial situation as well as a major asset in overcoming it. The low valuation made foreign investors interested in buying Korean shares and making direct investments in Korea. Some of the FDIs in the late '90s were fairly successful, and the number of FDIs slowly increased during the period up to 2005. The remaining hesitations to invest in Korea were mainly connected to the large cultural gap between Korea and the West. But by 2004 the major obstacles in introducing a performance based salary system were overcome, and the belief in Korea as having a great deal of potential, both for sales and production strengthened the Korean Won in 2005.

### **7.3.3 Labour Markets**

The low valuation of the Korean Won early on in the decade, along with the expanded openness of the economy, made the export industry increase. The unemployment rate rose a little, though, as the focus on efficiency in the business life made companies dismiss people. The opportunity for the export industry to establish international links when the valuation of the Korean Won was low in the beginning of the century was well managed, and the export industry's part in production rose significantly.

The expectations of life long employment, and the Hobong -salary system with automatic yearly increases were all very much questioned by the foreign companies that entered the Korean market in the end of the '90s.

As the continuous globalisation in the beginning of the 21<sup>st</sup> century put a pressure on Korean-owned companies to become more competitive, the industry slowly began to change towards a more Westernised system. In the very early 21<sup>st</sup> century, the change in the salary system was met by furious resistance from the labour market. The expected upswing in Korea's economy was temporarily delayed by strikes resisting enforcement of these changes.

Change was slow as the whole society was, and in 2005, still is, grounded in the Confucian tradition. The hierarchy and titles at work were a part of something much bigger, which has now started to change quickly, as the Hobong-system is abandoned by some of the domestic companies. The companies trying to accomplish a flat organisation and thus less of a hierarchy, are now attracting the younger well-educated generation. Women still have reduced salaries, often half that of men's, but foreign companies have already begun to pay according to performance and not gender. Today, pressure from women in domestic Korean companies has started a debate about women's rights, with some arguing that the initiated change should be supported by gender-equality legislation.

#### **7.3.4 Construction Equipment Industry/Market**

As a result of the successful sales in the export-industry, the government dared to initiate some minor infrastructure projects, despite the high interest rates prevailing in the country. The GDP growth rate of nearly 10 percent for 1999, stabilised to a more sustainable level of approximately 5 percent per year between 2000 and 2005, thus supporting the recovery of domestic construction equipment market. The cyclical characteristics of the demand for construction equipment were obvious as the development of Korea's GDP was followed by growth in the industry, with the assumption that it was slightly higher.

The high interest rate was an obstacle throughout the period of 2000-2005, though, hampering the domestic projects that should have been financed by

Korean investors. Foreign investors were also hesitant to invest money more extensively, as they thought the restructuring was going too slowly. Around 2005, the effects of the improved openness and increased transparency gave dividends and the domestic construction equipment market took off drastically. The competition in the domestic market was healthy as Daewoo and Hyundai had been forced to restructure their business and sell off some non-core business. The global competitiveness in the construction industry increased, as the construction equipment industry further consolidated in the sell out.

The high interest rate held back investments in the industry of component producers. In the beginning of the decade, the quest from the FDIs in the country was substantial, as they thought Korea lacked a competitive base of suppliers to serve the export industry. Some initiative was taken early in the decade to build collaboration between the Universities and industry, even if it is too early to accurately judge the results, and things look very promising today.

Written contracts, supplementing business that was still carried out mainly by personal relationships, were introduced into business-life between 2000 and 2005. Nowadays, these are common, and seen as valuable tools as more and more business is done internationally.



#### 7.4 “HEAVY NATIONALISM”

*A scenario outlined for 2005: The combination of a weak Korean Won and an economy characterised by protectionism*

##### **The Years 2000-2005 - A summary**

- Koreans blame the crisis on the IMF
- New conservative rulers
- A politics driven by discontent
- “Korean products and producers are all we need”.
- Younger generation disappointed
- Interest rate at an all time high
- Labour Union in line with the new government

##### **7.4.1 Government**

Shortly after the Asian crisis of 1997, Korea received help from the IMF. Many of the Koreans blamed the crisis on IMF, and did not feel that anything needed to be changed in the Korean society. The resistance towards the changes President Kim Dae Jung tried to establish was huge and caused many strikes among the labourers. The reactions from powerful chaebol owners, who saw their financial support from government disappear, were also strong. Many of the big chaebols faced law-suits regarding tax-matters and corruption, as the Kim Dae Jung government focused on restructuring and changing the traditionally Korean business life into a more Westernised one. The rift between classes increased, and the dissatisfaction in the stricken groups was huge. The ground for a politics of discontents was laid, and a success for the opposition party was not far away, in the very beginning of 2000. The Korean tradition of short-term interest in personal favours and lack of a long-term perspective in politics further increased the discontent with Kim Dae Jung, and his firm ideology-politics that made so many suffer in the transition.

The fundamental restructuring of the chaebols and the banking system began by Kim Dae Jung of the end of the '90s, finally came to an end with the new rulers, after the election in 2000. Kim Dae Jung's party, National Congress for New Politics, lost many places in the Parliament election in May 2000, and no coalition with another party was formed this time. As a result, the politics altered. Kim Dae Jung's reform work towards a market economy stopped when the Grand National party won the election. The slogan "Korean products and producers are all we need", aimed at a high level of protectionism and nationalism, illustrated a conservative politics mainly driven of discontent. Kim Dae Jung remained President until the end of his term, February 2003, but his ability to restructure the system was severely limited as a majority of the Parliament was against him. His attempts to use his constitutional right to appoint state councils that were less conservative were withdrawn, as they received no backing from the Parliament.

The Grand National party's politics were initially expressed when they undertook radical change of the laws and regulations regarding foreign direct investors in the country. All the organs to which the government, under Kim Dae Jung, had given priority, (for example, the Financial Supervisory Commission, which acted as a watchdog in charge of leading Korea's reforms in the corporate and financial sectors), were closed down. The State also reinforced laws concerning foreign direct investments, which were regulated and put under severe control.

Many people, especially the younger generation, were disappointed at the new government, they saw its politics as a backlash in Korea's development. Several well-educated and younger, more Westernised people left the country in protest of the conservative regime. They did not support the value of increased nationalism, or the related focus on traditional cultural and family/clan values, at the expense of profit, efficiency and individualism in the business life.

Students protested to some extent in the early 21<sup>st</sup> century, but only in Seoul. The attitude of the government was that “Non-nationalistic” individuals should be humbled, and the government distributed extensive political propaganda.

#### **7.4.2 Financial Markets**

The move towards protectionism meant a lot to the Korean financial market, and the results appeared quickly. The interest rate increased even before the election in the spring of 2000, due to speculations around a majority, in the coming election, with conservative opinions and protectionist values. The interest rate reached an all-time high after the election and the risk premium paid due to the greater political uncertainty made the high interest rate prevail for the next five years. Korean companies’ historically very low solvency made the situation especially serious and constrained business severely. The government had to support the big chaebols, and draining the possibilities for a functioning credit market for smaller enterprises and private persons.

As the interest rates reach such high levels, the Stock Market had little attractiveness for domestic investors. Foreign investors fled the country, due to the high perceived political risk and the overall inhospitable environment for foreigners. Smaller companies found themselves without any way to get financing, hampered commercial life a great deal.

The FDIs were partly legally restricted but even in the areas where they were not, they tried to withdraw because of a fear that their property would be confiscated, as well as an overall high uncertainty of the politics in the country.

#### **7.4.3 Labour Market**

After all the strikes around the millennium shift, employees withdrew their weapons as the new government was installed in the spring of 2000. The labour force was still not satisfied, but they agreed with new policies to a

greater extent. The government's promise to keep old traditions of lifelong employment meant severe cuts in salaries. But the government's promises that the recession would soon be over and that South Korea would flourish again kept the Union appeased. The steps toward a performance based salary system in the Korean industries that began at the end of the '90s were put aside, and the Hobong system was not questioned. In daily business life, the system meant an easier way of conducting business, as the hierarchy was clear and regulated among the management and employees. For the first five years of the decade, the labour Union was fairly satisfied with the situation, as it did not mean any fundamental changes in the system. The wage cuts were seen as a trial of the nationalistic feelings, and the Hahn spirit helped in overcoming the deterioration in standard of living.

The high level of protectionism led to a decrease in global business. Korea did not allow many imports, which were also very expensive- and therefore, some main trade countries initiated restrictions against importation of Korean products. As the Korean Won was valued low, the exportindustry survived, but it did not flourish, due to the lack of competitiveness. The earlier focus on performance related payment and the overall focus on efficiency declined as a result of the re-established focus on traditional values in the business life (i.e. the Hobong system). Export decreased steadily from the beginning of the decade until 2005. In the beginning of 2000, the exportindustry was doing well. But as time passed, the increased protectionism, along with the unfavourable costsituation stemming from the lack of efficiency, contributed to an exportdecrease, despite the favourable Won valuation. The deteriorating financial situation for Korea made it hard to start the agreed payment to IMF. The situation worsened even more as interest rates rapidly increased, due to the worsened state budget and the ensuing decrease in trust from the surrounding world.

#### **7.4.4 Construction Equipment Industry/Market**

Taken as a whole, the outcome of the politics of the years 2000-2005 was miserable for the construction equipment market, as for Korea's economy

as a whole. The growth, after reaching nearly 10 percent in 1999, declined rapidly with the new imposed protectionism. The competitiveness in the industry declined quickly as the focus on profit and efficiency changed to a focus on maintaining the old system of life-long employment and subsidies to the big chaebols.

Companies outside the largest chaebol-sphere found it difficult to finance their business early in the decade, and thus became more dependent on their cash flow. This led to extreme uncertainty avoidance and a stagnating domestic market. The large companies, like Daewoo and Hyundai, regained some of their power, as the new government was more willing to support their operations than Kim Dae Jung had been. Due to the high interest rate, however, business was plagued by overcapacity. Only those companies that had a big share of the exportmarket managed to sustain the necessary volumes. Already by the summer of 1999, Daewoo had lowered their prices due to their weak financial situation. But instead of collapsing early in 2000, as many in the business had predicted they would, they managed to survive, thanks to the financial support from the new government. Daewoo succeeded in taking shares of the shrinking construction market by starting a price war and using slogans like “A Korean with Hahn-spirit relies on *Korean* construction equipment”. The globalisation of the Korean industry deteriorated in the years 2000-2005, due to many factors. The salary system mentioned above was one, as well as the fact that the government subsidised weak companies, prolonging the process of restructuring and creating internationally competitive businesses in Korea in the long-term.

The protectionism and the propaganda of government that “Korean products and producers are all we need”, led to the opinion that FDI’s operating in the country had acquired their companies in a hostile way, and were thus deserving boycotts on the domestic market. The feeling by foreign direct investors that suppliers should take a bigger part in research

and development of components within the construction equipment industry was met with resistance.

Laws and regulations were enforced to differing extents, depending on the relationship between the persons involved. The foreigners that still stayed in the country felt insecure, as legal security was weak. Foreign companies found themselves in the situation of being discriminated against, and the law of competition was not applied if the focal company did not turn out to have a very good relationship with the authorities.

Emphasis on traditional values was reintroduced after the election of 2000. The tradition of emphasising personal relationships when conducting business was very evident in the first five years of the decade. Formal contracts were neglected, and the emphasis on relationship caused corruption to flourish. The reforms towards greater openness and the move in direction of increased transparency that had started at the end of the '90s, were abruptly cancelled from the government's agenda after the election. The transparency was thus non-existent on every level, in private business life as well as in public purchasing. This also contributed to the increased corruption.

#### 7.5 FUTURE THREATS AND OPPORTUNITIES

In this chapter, we outlined four different scenarios for the Korean market. The scenarios were primarily made to suit the needs of Volvo CE Korea, but can also be used by any MNC in the Korean market. The scenarios show that each of the "futures" described constitutes a different set of opportunities and threats for the MNC. These threats and opportunities need to be examined in the light of the MNC's individual strengths and weaknesses. If the decision makers within the MNC are prepared for different outcomes in the future, their chances of meeting future opportunities and threats in a successful way increases.

## 8 CONCLUSIONS AND RECOMMENDATIONS

In this chapter we will first present conclusions about how Volvo CE Korea will be affected by the outcome of each of the four scenarios presented in the previous chapter. Finally we will draw general conclusions about the process of scenario development.

### 8.1 FUTURE IMPLICATIONS FOR VOLVO CE KOREA

The different scenarios depicted in the previous chapter imply diverse possibilities for future environmental opportunities and threats for Volvo CE Korea. We will here draw conclusions about what this will mean for Volvo's current strategy in terms of strengths and weaknesses of the MNC today. We will only discuss those threats and opportunities that are most significant for each scenario, and that will most severely affect Volvo CE Korea

- *acting on the Korean excavator market*
- *as an Asian Industrial Hub*

#### 8.1.1 SWOT for “The Sun is shining”

*Future threats and opportunities for Volvo CE Korea as an actor on the Korean excavator market in relation to the strengths and weaknesses the company possesses today.*

Healthy competition not characterised by a price war, as depicted in this scenario, is an opportunity for Volvo CE Korea, even if the openness of the Korean market means more foreign competitors. Volvo CE has the strength of experience of more sophisticated markets, and of having developed products and services that fit these kinds of demanding customer segments. Compared to South Korean domestic producers they have a “first mover advantage” of being used to act on markets characterised by this level of sophistication. Compared to foreign competitors like CAT and Komatsu, they have a “first mover advantage”, as well, as they were the first foreign producer and distributor in South Korea.

*Future threats and opportunities for Volvo CE Korea being an Asian Industrial Hub in relation to the strengths and weaknesses the company possesses today.*

An unfavourable exchange rate, which is the result of this scenario, makes Korean products more expensive on the international market, and therefore hinders exportation. The strengths Volvo CE Korea possesses as a part of a big global organisation, with access to Volvo Group Finance, provides the possibility to alleviate some of this, but not enough. As one of Volvo CE's major objectives for the investments in Korea is that the Korean subsidiary should contribute to profitability by being a competitive production base, this is very serious. There is no internal strength that can compensate for a genuinely strong Korean Won. As we see it, the exchange rate is crucial.

Domestic suppliers, as well as the Government, are willing to change their view on participating in research and development in this scenario. A strength Volvo CE Korea possesses is its good relationship with the Government. This can be used to get in touch with suppliers that are participating in research programs at the Universities, and who want to take a bigger share than traditionally of the manufacturing and development of components. Developing relationships with, and long-term commitment to these suppliers creates an enhanced ability for Volvo CE Korea to be competitive on the global market, through the acquisition of better quality at lower cost. The chances of attracting more productlines from Volvo CE globally for establishment in Korea also increase, compared to when a big share of the components are imported from Europe.

Another opportunity is the "new" type of Korean employee that is emerging in this scenario: willing to work hard in order to achieve individual success and less concerned about rank and the status this conveys. Volvo CE Korea was one of the first companies to introduce a flat organisation built on efficiency and profitability, as well as individual performance based salary systems. This fact can be seen as a strength in the



context of this scenario, where employees appreciate the values that Volvo CE Korea has promoted since the acquisition.

The expected salary increase and connected inflation in the context of this scenario can be a threat to global competitiveness. A strength of Volvo CE Korea in this context, is their far-sightedness in leaving the Hobong system for a performance based system, because salaries are then connected to achieved profit.

#### **8.1.2 SWOT for “Alone is strong”**

*Future threats and opportunities for Volvo CE Korea as an actor on the Korean excavator market in relation to the strengths and weaknesses the company possesses today.*

The opportunities and threats challenging Volvo CE Korea in this scenario are many and varied. First of all, the domestic market will be very large and booming, due to the advances towards North Korea, and the surrounding world's ensuing of financial aid. The need for construction equipment, in work on infrastructure and housing projects in North Korea is boundless; its only limitation is financing. A strength of Volvo CE Korea is their access to an entire product range of construction equipment within Volvo CE, as well as trucks and buses within the Volvo organisation. Volvo CE Korea is thus able to act and fully take part in the aid programmes carried out by the World Bank and others. Another strength is that North Korea may be reluctant to use American products, such as Caterpillar, and thus will prefer Swedish/Korean products. Sweden as a nation will most likely support the reunification, and thus address some financial aid to North Korea. This will increase the good will towards Sweden and the chances of selling Volvo-brand products.

The intensified and successful focus of the Government on chaebol restructuring would imply a domestic market that is less plagued by price competition from state-subsidised companies than before. These factors,

along with the fact that foreign competitors will be barred from Korea, imply a positive development for Volvo CE Korea. As market leader, they have the ability to set price and take an even larger proportion of the market than before. As Volvo CE, by tradition, is used to compete in markets that are sophisticated in the same way as the Korean market in this scenario, Volvo's organisation and products are a strength.

On the other hand, the market will be plagued by heavy nationalism and protectionism that will affect Volvo CE Korea severely if they are still perceived as a foreign company. A weakness, in this case, would be that Volvo CE Korea is fairly well known, and thus a possible target for nationalistic hostility.

As relationships will play a more significant role in this scenario, a threat for Volvo CE Korea could be that they have a limited understanding of Korean business culture. The relationships have consequences in areas in which the business mores of the Western world usually do not attach major importance. One example is the enforcement of laws, which will be depending on what kind of relationship each of the opponents have with the authorities.

These threats can be met if Volvo CE succeeds in being perceived as a Korean company by selling a larger part of the company back to Samsung, who now owns only a minority share of 13%. This act would require conversion of the Westernised work methods partly applied in Volvo CE Korea. Volvo CE Korea's relation with the Kim Dae Jung Government can probably be seen as a threat if the new Grand National Party Government wants to demonstrate its alteration in politics, and therefore make an example out of Volvo CE Korea in the opposite direction of the former Government.

*Future threats and opportunities for Volvo CE Korea being an Asian Industrial Hub in relation to the strengths and weaknesses the company possesses today.*

One important opportunity for Volvo CE Korea in its role as an actor on the domestic Korean market, is the cheaper labour force which should result from an allocation of production to North Korea and other surrounding low cost production countries. Even if Volvo CE Korea does not choose to locate its production outside South Korea, a downward pressure on the overall wage level would result from increased unemployment in South Korea. Volvo CE Korea here has a strength in that the factory is not over-invested and thus rather dependent on physical labour force.

Conversely the boost in the domestic business cycle may prevent unemployment and also drive up inflation, which is unfavourable. An overheated market along with a strong currency could prevail. This would have a major negative impact on Volvo CE Korea as an Asian hub, as their exports become less competitive on the global market. Nationalism and protectionism will be a threat, as they hinder working methods and salary systems, both crucial for Volvo CE Korea to be globally competitive. Overall, this scenario is a threat when it comes to export.

### **8.1.3 SWOT for "Rising Sun"**

*Future threats and opportunities for Volvo CE Korea as an actor on the Korean excavator market in relation to the strengths and weaknesses the company possesses today.*

High interest rates prevail in Korea in this scenario. High interest rates are a threat to Volvo CE Korea, since they act in a very cyclical industry. The Construction Industry relies on infrastructure projects. The likelihood of such projects diminishes with higher interest levels, as investors choose other countries with higher potential or wait until the interest rate drops.

Volvo CE Korea is strong though, because having strong financial backing, they are able to withstand a prolonged recession. The fact that Volvo CE Korea, unlike domestic producers, exports a large share of its products, is also a strength in this scenario, because it makes them less dependent on the domestic market.

Slow reforms are an additional threat for Volvo CE Korea. The fact that the Government does not force the big, unprofitable chaebols to restructure at a faster pace (out of fear for unemployment and ensuing social unrest) puts Volvo CE Korea in a situation of unfair competition with Daewoo and Hyundai. The Korean companies receive subsidies, which distort competition by keeping the financially weak Korean conglomerates alive. The strength of Volvo CE Korea in these circumstances is their position as market leaders in Korea, which enables them, at least to some extent, to set the market conditions.

An opportunity arising in this scenario is that the financial market starts to open up. Volvo CE Korea is strong because Volvo companies traditionally offer sales financing. This gives Volvo CE Korea a possibility, jointly with Volvo Group Finance, to act very quickly and establish a financing function internally in Volvo CE Korea. Volvo CE is thus able to take advantage of this very profitable part of their core business also in South Korea.

*Future threats and opportunities for Volvo CE Korea being an Asian Industrial Hub in relation to the strengths and weaknesses the company possesses today.*

A favourable exchange rate is an opportunity facing Volvo CE Korea in this scenario. A strength for Volvo CE Korea is that they sell the majority of their products on the global market, and this scenario makes the exported products more globally competitive. The capacity of the factory is not fully reached and thus can relatively easily be used for producing more product

lines. Because of the favourable exchange rate, it is now more favourable to export Volvo CE's products from South Korea than from, for instance, Germany, which has, especially in this scenario, a much stronger currency.

#### 8.1.4 SWOT for “Heavy Nationalism”

*Future threats and opportunities for Volvo CE Korea as an actor on the Korean excavator market in relation to the strengths and weaknesses the company possesses today.*

Nationalism and propaganda for Korean products constitute a threat for all foreign investors in the country in this scenario as well as in the scenario “Alone is strong”. The threats are evident, at least for those that intend to sell their products in the Korean marketplace. A weakness for Volvo CE Korea, according to this scenario, is that a majority of the managers are Westerners. The changes that have been enforced, for example the removal of hierarchies, are all directed towards a Volvo-isation of the company. All these changes that have taken place imply that Volvo CE Korea wants to leave traditional Korean values behind and remove the established Korean way of doing business. According to our findings, Volvo CE Korea is perceived as a foreign company, and thus will probably be one of the victims of nationalistic propaganda, perhaps culminating in strikes and boycotts of Volvo-brand products. In this situation Volvo CE Korea should use the former relationship with Samsung Heavy Industries and try to settle an agreement of joint ownership, making the company more “Korean”.

*Future threats and opportunities for Volvo CE Korea being an Asian Industrial Hub in relation to the strengths and weaknesses the company possesses today.*

A difference between the “Alone is strong” scenario and this one is that the products for export should still be competitive, due to the weak Won. A substantial part of Volvo CE Korea's business is export, which must be maintained without delays from boycotts and the like.

The main threat in this scenario is that the surrounding world may refuse to buy Korean products, as Korea itself now has severe import restrictions. This threat is, probably partly avoidable for Volvo CE Korea, as they have the strength of being part of a large global organisation. Sweden will most likely not enforce any import restrictions against Korea, and thus export from Korea can be handled anyway, even if it must go through a second country. On the other hand this is complicated and, cost- and delivery-competitiveness will diminish substantially, thus severely questioning Korea's position as an Asian Industrial hub. The competitiveness can only be retained if the low valuation of the Korean Won compensates for the increased costs.

Emphasis on traditional values and norms increases under this scenario, and is a threat for Volvo CE Korea both in its characteristic of serving the domestic market and as a company exporting to the global market. The increased protectionism and nationalistic feelings are in opposition to many of the measures Volvo CE Korea has taken and wants to take: a collision with traditional values and norms. Volvo wants to achieve profitability and efficiency in their Korean business activities, expressed in terms of a flatter organisation and a performance based salary system. In the context of a protectionist scenario, this strategy could constitute a weakness for Volvo CE Korea.

## 8.2 GENERAL CONCLUSIONS AND RECOMMENDATIONS

Altogether, the examples of opportunities and threats challenging Volvo CE Korea's strengths and weaknesses in the above scenarios are illustrations of various contexts within which an organisation in Korea must be prepared to manage. Many MNCs in the world operate under similar circumstances. They operate in emerging markets that, to some extent differ from one other, but still have many common characteristics. The main thing the emerging markets have in common is a high level of uncertainty, which makes traditional strategy tools less dependable. One

such conventional tool is forecasting. A better tool for handling uncertainty in these environments is the creation of scenarios. The process of scenario development is a superior management tool in handling the insecurity prevailing on emerging markets.

#### **8.2.1 Scenarios make people think!**

If a MNC active in an emerging market engages successfully in the development of scenarios, several positive outcomes will result. The scenarios, describing different futures, serve as a management tool in preparing the decision makers for different opportunities and threats that societal change presents. The benefit of using scenarios, and especially the method presented in this thesis, is that they prepare the organisation, and the individuals within it, to take action more thoughtfully and rapidly than MNCs not using scenarios as a management tool. If decision makers are engaged in the process, the MNC gains the capability of reading the signals of environmental change faster than its competitors, and achieves a competitive advantage by being able to more rapidly adapt to new circumstances.

This method also provides a deeper understanding of the market place as a whole, which supports more accurate decision making. If the people that are in charge of making forecasts become engaged in the scenario development process, their ability to make trustworthy forecasts will be enhanced. The scenario method will help, by the deep knowledge of environmental issues it provides.

If the local management succeed in transferring the implication of the developed scenarios throughout the company, it should create a better awareness of what needs to be done internally, to meet different opportunities and threats. It would also raise awareness in the employees that measures taken in the company should be viewed from a longer perspective than is generally done in domestic companies today. Modifications and changes in the way of doing business may be met with

less resistance if the view of the future and the need for increased flexibility, are grasped by a majority of the employees. The scenario development process is especially useful because it depicts complex situations and relationships in “a colourful and vivid” way, that is logical and useful when communicating with employees.

When a forecast is proven inaccurate, it will be much easier to alter the mind-set and redirect action if the decision-makers have gone through the process of developing scenarios. The process in itself also creates a genuine and deep understanding of the environment within which the MNC is operating.

### 8.3 SUGGESTIONS FOR FUTURE RESEARCH

The positive outcome of creating scenarios could be further enhanced if the process involves active participation by the decision-makers within the organisation. By engaging the organisation’s employees in the process, an institutional knowledge emerges that further enables the organisation to adapt more quickly and effectively to the changing environment.

When creating scenarios, it could be an advantage to prolong the time period used to a period of ten years, instead of five. In a longer time period, it is more likely that societal sectors such as Country Culture and Business Mores will change, thus enabling the authors to be more creative when developing the scenarios.

The next logical step to take, after having created this method for scenario development, would be an actual implementation of this strategic tool by Multinational Corporations acting in emerging markets. This area has not been covered in this thesis. Therefore, we look forward to future research on the ways in which this could be successfully done.



## LIST OF REFERENCE

**Literature**

Cederberg, C., and Lundholm, J., "*Koreaboken*", (1997), Koreanska Sällskapet, Norra Skåne Offset, Hässleholm, Sweden

De Mente, B., "*Korean Etiquette and Ethics in Business*", 1989, NTC Business Books, Lincolnwood

Fahey, L., "*Macro-environmental Analysis for Strategic Management*", 1986, West Publishing Company, St. Paul, USA

Gipson, C. R., J.D., Ph.D., "*Dictionary of International Trade and Fiance*" 1994, McGraw-Hill Inc., New York, USA

Grant, R. M., "*Contemporary Strategy Analysis*", 1998, Blackwell Publisher Inc., Oxford, UK

Henderson, G., "*Korea: The Politics of the Vortex*", 1968, Harvard University Press, Cambridge, MA, USA

Hofstede, G., "*Cultures and Organisations- Software of the Mind*", 1994, HarperCollinsPublishers, London, UK

Holme, I.M., "*Forskningsmetodik: om kvalitativa och kvantitativa metoder*", 1997, Studentlitteratur Lund

Jacobs, N., "*The Korean Road to Modernization and Development*", 1985, University of Illinois Press, Urbana, IL, USA

Jansson, H., "*International Strategic Management in Emerging markets: Global Institutions and Networks*", 1999, Book Manuscript, Center for

## LIST OF REFERENCE

International Business Studies, School of Economics and Commercial Law,  
Gothenburg University, Sweden

Johnson, G. and Scholes, K., *"Exploring Corporate Strategy"*, 1988,  
Prentice Hall, New York

Kvale, S., *"Interviews – an introduction to qualitative research  
interviewing"*, 1996, Sage Publications Inc.

Merriam, S. B., *"Qualitative Research and Case Study Applications in  
Education"*, 1998, Jossey-Bass Inc., San Francisco, USA

Porter, M. E., *"Competitive Advantage"*, 1985, The Free Press, New York,  
USA

Pye, L.W., *"Asian Power and Politics: The Cultural Dimension of  
Authority"*, Harvard University Press, Cambridge, MA, USA

Schoemaker, P., *"Scenario Planning: A Tool for Strategic Thinking"*,  
Winter 1995, Sloan Management Review

Schwartz, P., *"The Art of the Long View- Planning for the Future in an  
Uncertain World"*, 1991, Bantham DoubledayDell Publishing Group Inc.,  
New York, NY, USA

Steinberg, D.I., *"The Republic of Korea"*, 1989, Westview Inc., Boulder,  
CO, USA

Terpstra, V., David, K., *"The Cultural Environment of International  
Business"*, 1991, South Western Corp., Cincinnati, USA

Van der Heijden, K., *"Scenarios: The art of strategic conversation"*, 1996,  
John Wiley and Sons Ltd, Chichester, UK

Yin, R.K., “*Case Study Research: Design and Methods*”, 1994, SAGE Publications, Inc. Thousand Oaks, CA, USA

**Journals/ Articles**

Affärsvärlden, “*ANALYS: Volvos dyra val*”, 19th of May 1999

Business Korea, “*Speeding up reform*”, Kyong-Hwan, L., May 1998

Dagens Industri, “*Volvos Koreakranar lyfter lönsamheten*”, Larsson, G., 11th of Nov 1999

Dagens Industri, “*Industrin har redan repat sig*”, Larsson, G., 29th of Apr 1999

East Asia Executive Report, “*Taking Account in South Korea: What Potential Buyers Need to Know About M&A in the Hermit Kingdom*”, Erlich, Craig & Mann, 15<sup>th</sup> of Aug 1998

Far Eastern Economic Review, “*Battle of Wills*”, Lee, C., S., 26<sup>th</sup> of Aug 1999

Far Eastern Economic Review, “*Open Sesame-South Korea warms towards foreign investors*”, Lee, C. & Vatikiotis, M., 24<sup>th</sup> of Dec 1998

Finanstidningen, “*Nya Volvo ska bli störst i Världen*”, 29th of Jan 1999

Göteborgs-Posten, “*Bättre å bättre dag för dag...*”, Lökvist, C., 4th of Nov 1999

Göteborgsposten, “*Volvo uppträder okänsligt*”, Lökvist, C., 4th of Nov 1999

## LIST OF REFERENCE

International Financial Law Review, “WTO will force Korea to open up legal services”, Mulrenan, S., Nov 1998, Volume 17, Issue 11

Knight-Ridder/Tribune Business News, “Seeking recovery, South Korea Courts Foreign Investment”, Ginsberg, T., 14<sup>th</sup> Aug 1998

Mergers & Acquisitions, 2 ” Why inbound buyers are wary of deals in Korea”, Moskowitz, K., Sep-Oct 1998, No2

The Banker, “The wrong medicine”, Lee, C., Dec 1998

The Economist, “Renouncing heaven’s mandate”, 10<sup>th</sup> of Jul 1999

The Economist, “Yesterday’s war, tomorrow’s peace”, 10<sup>th</sup> of Jul 1999.

The McKinsey Quarterly, The roots of Korea’s crisis”, Baily, M. et al, 1998, No 2

### Internet Sources

[www.odci.gov/cia/publications/factbook/ks.html](http://www.odci.gov/cia/publications/factbook/ks.html)

[www.volvo.com](http://www.volvo.com)

### Other Sources

Notes from a Seminar held by Dr.Kim Kyung-Won at The Samsung Economic Research Institute, Seoul, Korea, 8<sup>th</sup> of Oct 1999

Material from Volvo Construction Equipment Group, 99/ Investor Relations

### Interviews

Interview – Volvo CE Korea, Seoul Head Office, 7<sup>th</sup> of Oct 1999, Mr.Bengt-Åke Bjernerup, Vice President Customer Support

## LIST OF REFERENCE

Interview- Volvo CE Headquarter, Brussels, 26<sup>th</sup> of Aug 1999, Mr. Gilles Boutte, Vice President Business Development

Interview- Volvo CE Korea, Seoul Head Office, 7<sup>th</sup> of Oct 1999, Mr. K.J. Cho, Executive Manager Research & Development

Interview- Volvo CE Korea, Seoul Head Office, 7<sup>th</sup> of Oct 1999, Mr. K.J. Cho, Executive Managing Director Overseas Operation

Interview – Volvo CE Korea, Seoul Head Office, 8<sup>th</sup> of Oct 1999, Mr.Tony Helsham, President Volvo CE Korea

Interview- Volvo CE Korea, Changwon Plant, 12<sup>th</sup> of Oct 1999, Mr. J.H.Heung-Sik, Executive Managing Director- Human Resources, Samsung Heavy Industries

Interview – Volvo CE Korea, Seoul Head Office, 8<sup>th</sup> of Oct 1999, Mr.Kurt Jonsson, Vice President Human Resource Management

Interview- Volvo CE Korea, Changwon Plant, 13<sup>th</sup> of Oct 1999, Mr.Kim, Manager Human Resources

Interview- Volvo CE Korea, Changwon Plant, 12<sup>th</sup> of Oct 1999, Mr. H.D. Koo, Executive Managing Director- Plant Division, Samsung Heavy Industries

Interview- Volvo CE Korea, Changwon Plant, 12<sup>th</sup> of Oct 1999, Labour Union Representative

Interview- Volvo CE Korea, Seoul Head Office, 8<sup>th</sup> of Oct 1999, Mr JH Lee, Managing Director Korea Sales Company

## LIST OF REFERENCE

Interview- Volvo CE Korea, Seoul Head Office, 7<sup>th</sup> of Oct 1999, Mr.Peter Lindbäck, Senior Adviser.

Interview – Volvo CE Korea, Seoul Head Office, 8<sup>th</sup> of Oct 1999, Mr.Eric Nielsen, Chief Financial Officer

Interview- Volvo CE Korea, Changwon Plant, 12<sup>th</sup> of Oct 1999, Mr. W.S. Suk, Director Manufacturing



<b>1</b>	<b>INTRODUCTION .....</b>	<b>1</b>
1.1	PROBLEM BACKGROUND .....	4
1.1.1	<i>An analytical approach to the Scenario Development Process</i> .....	4
1.2	PROBLEM STATEMENT .....	5
1.3	PURPOSE .....	6
1.4	DEFINITIONS .....	6
1.5	DELIMITATIONS .....	7
1.6	THE CASE COMPANY – VOLVO CONSTRUCTION EQUIPMENT KOREA .....	8
1.6.1	<i>Volvo</i> .....	8
1.6.2	<i>Volvo CE</i> .....	8
1.6.3	<i>Volvo Construction Equipment Korea</i> .....	9
1.6.3.1	The acquisition .....	10
1.6.3.2	After the acquisition .....	10
1.6.3.3	The future .....	10
1.7	GENERAL THESIS-OUTLINE .....	11
<b>2</b>	<b>AN ANALYTICAL APPROACH TO SCENARIO DEVELOPMENT .....</b>	<b>14</b>
2.1	WHEN FORECASTING FAILS .....	14
2.2	MAIN COMPONENTS OF THE SCENARIO DEVELOPMENT PROCESS ..	15
2.2.1	<i>Van der Heijden's view</i> .....	15
2.2.2	<i>Porter's view</i> .....	16
2.2.3	<i>Schoemaker's view</i> .....	17
2.3	THE UNCERTAINTY OF THE ENVIRONMENT .....	17
2.4	DRIVERS FOR CHANGE .....	18
2.5	SWOT-ANALYSIS .....	19
<b>3</b>	<b>THE INSTITUTIONS NETWORK APPROACH .....</b>	<b>20</b>
3.1	IDENTIFYING THE RELEVANT ENVIRONMENT .....	21
3.1.1	<i>Models useful for identification of environmental factors</i> .....	22
3.1.1.1	The PEST model .....	22
3.1.1.2	Terpstra's model .....	23



3.2	DESCRIBING THE ENVIRONMENT .....	24
3.2.1	<i>Describing the Organisational Fields - Markets and Firms..</i>	24
3.3	MODELS USEFUL FOR EXPLAINING THE ENVIRONMENT .....	27
3.3.1	<i>Whitley's explanation of East Asian business systems:</i> .....	28
3.3.1.1	Pre-industrial influences on Korean institutions .....	29
3.3.1.2	The Industrialisation – a time of drastic changes .....	32
3.3.2	<i>Whitley's Explanation of East Asian markets</i> .....	33
3.3.2.1	Product/Service market networks .....	35
3.3.2.2	Financial market networks .....	36
3.3.2.3	Labour market networks.....	37
3.3.2.4	Government Networks .....	37
<b>4</b>	<b>METHODOLOGY .....</b>	<b>38</b>
4.1	RESEARCH STRATEGY .....	38
4.1.1	<i>A Case Study</i> .....	38
4.1.1.1	Case study design .....	39
4.2	SCIENTIFIC APPROACH .....	41
4.3	RESEARCH METHOD .....	42
4.4	DATA COLLECTION .....	43
4.4.1	<i>Primary data</i> .....	43
4.4.1.1	Interviews .....	43
4.4.2	<i>Secondary data</i> .....	47
4.4.2.1	Structured search for secondary data .....	47
4.5	QUALITY OF RESEARCH.....	48
4.5.1	<i>The Validity Concept</i> .....	48
4.5.1.1	Construct Validity .....	48
4.5.1.2	Internal Validity .....	50
4.5.1.3	External Validity .....	50
4.5.2	<i>Reliability</i> .....	51
4.6	POSSIBLE TYPES OF ERRORS .....	51
4.7	THE SCENARIO DEVELOPMENT MODEL .....	52
4.7.1	<i>The Scenario Development Process</i> .....	54
4.7.1.1	Scanning the environment .....	54

4.7.1.2	Which are the Key Factors for future success? .....	55
4.7.1.3	Strengths and Weaknesses .....	55
4.7.1.4	Environmental Analysis .....	55
4.7.1.5	Drivers of change .....	56
4.7.1.6	Scenario Creation .....	58
4.7.1.7	Assessing future Opportunities and Threats .....	60
<b>5</b>	<b>STRENGTHS AND WEAKNESSES OF VOLVO CE KOREA</b> .....	<b>61</b>
5.1	KEY FACTORS FOR FUTURE SUCCESS .....	61
5.2	STRENGTHS AND WEAKNESSES .....	62
5.2.1	<i>Global Player</i> .....	63
5.2.2	<i>Price competition</i> .....	64
5.2.3	<i>Keeping delivery agreements</i> .....	65
5.2.4	<i>Competitive Products</i> .....	67
5.2.5	<i>Financing to customers</i> .....	68
5.2.6	<i>Increased R&amp;D</i> .....	70
5.2.7	<i>Domestic Suppliers</i> .....	71
5.2.8	<i>Relationships</i> .....	72
5.2.9	<i>Accounting Standards</i> .....	73
5.2.10	<i>Performance Based Salary System</i> .....	74
5.2.11	<i>Human Resources</i> .....	76
5.3	ANSWER TO RESEARCH PROBLEM II .....	78
<b>6</b>	<b>ENVIRONMENTAL ANALYSIS</b> .....	<b>79</b>
6.1	THE SOCIETAL SECTOR .....	80
6.1.1	<i>The Financial System</i> .....	81
6.1.1.1	The Valuation of the Korean Won .....	81
6.1.1.2	A well functioning financial system .....	82
6.1.1.3	Attracting Foreign Direct Investors .....	84
6.1.1.4	The Business cycle of the Korean Construction Industry .....	84
6.1.2	<i>The Political System</i> .....	85
6.1.2.1	Political Reforms supporting economic transition .....	85
6.1.2.2	The Korean Welfare System .....	89

6.1.2.3	The relation between the two Koreas remains stable .....	90
6.1.2.4	Gradual reunification .....	90
6.1.3	<i>The Legal System</i> .....	91
6.1.3.1	Legal Reform to protect FDI in general.....	91
6.1.3.2	Over-regulation .....	92
6.1.4	<i>The Social System</i> .....	93
6.1.4.1	Confucianism .....	93
6.1.4.2	Family Clan .....	94
6.1.4.3	Business Mores .....	94
6.2	ORGANISATIONAL FIELDS .....	96
6.2.1	<i>Government</i> .....	97
6.2.1.1	Nurturing the right relationships.....	97
6.2.2	<i>Financial Markets</i> .....	99
6.2.2.1	Have the right relationships when doing business .....	100
6.2.2.2	Accounting standards .....	100
6.2.3	<i>Product/Service Markets</i> .....	101
6.2.3.1	Relationship to domestic customers .....	102
6.2.3.2	Relationship with domestic suppliers .....	105
6.2.3.3	Volvo CE Korea gains access to a greater amount of domestic suppliers? .....	107
6.2.3.4	Volvo CE Korea avoids price wars .....	108
6.2.4	<i>Labour Markets</i> .....	109
6.2.4.1	Korean organisational hierarchies and authority types .....	109
6.2.4.2	Performance based salary system .....	110
6.2.4.3	Relation to Human Resources .....	113
6.3	ANSWER TO RESEARCH PROBLEM I. ....	115
6.3.1	<i>Determining the level of societal development</i> .....	115
6.3.1.1	Drivers of change vs. Determinants for stability.....	115
<b>7</b>	<b>SCENARIOS FOR VOLVO CE KOREA IN THE YEAR 2005</b>	<b>118</b>
7.1	“THE SUN IS SHINING “ .....	121
7.1.1	<i>Government</i> .....	121
7.1.2	<i>Financial Market</i> .....	123

## Table of Contents

7.1.3	Labour Market.....	123
7.1.4	Construction Equipment Industry/Market.....	125
7.2	"ALONE IS STRONG" .....	126
7.2.1	Government .....	127
7.2.2	Financial Markets.....	129
7.2.3	Labour Markets .....	129
7.2.4	Construction Equipment Industry/Market.....	130
7.3	"RISING SUN" .....	132
7.3.1	Government .....	132
7.3.2	Financial market.....	133
7.3.3	Labour Markets .....	134
7.3.4	Construction Equipment Industry/Market.....	135
7.4	"HEAVY NATIONALISM" .....	137
7.4.1	Government .....	137
7.4.2	Financial Markets.....	139
7.4.3	Labour Market.....	139
7.4.4	Construction Equipment Industry/Market.....	140
7.5	FUTURE THREATS AND OPPORTUNITIES.....	142
<b>8</b>	<b>CONCLUSIONS AND RECOMMENDATIONS.....</b>	<b>143</b>
8.1	FUTURE IMPLICATIONS FOR VOLVO CE KOREA .....	143
8.1.1	SWOT for "The Sun is shining" .....	143
8.1.2	SWOT for "Alone is strong" .....	145
8.1.3	SWOT for "Rising Sun" .....	147
8.1.4	SWOT for " Heavy Nationalism" .....	149
8.2	GENERAL CONCLUSIONS AND RECOMMENDATIONS .....	150
8.2.1	Scenarios make people think!.....	151
8.3	SUGGESTIONS FOR FUTURE RESEARCH .....	152
	<b>LIST OF REFERENCE.....</b>	<b>153</b>