

THE AUTOMOBILE INDUSTRY

Motoring Higher and Higher

Since its start with the founding of the Saenara Motor Company in 1962, the Korean automobile industry has shown strong growth, particularly in the 1980s. The robust growth in the 1980s was largely the result of Korea's successful penetration into the North American market. Beginning in 1987, the domestic car market also began to expand considerably due to the "three lows," the active property and stock markets, and the higher wage levels. The rate of increase in the domestic car market reached an annual average of 35% from 1987 to 1990.

In 1989, motor exports began to fall, but the active domestic market supported the growth of the car industry. Since 1990, the annual growth rate of domestic market has slipped down to 10%, but exports have lately begun to grow rapidly again due to Korean makers' export market diversification strategy and the strong yen. Last year the growth rate of auto exports reached 35%.

As a result of these development, the automobile industry has grown to the point where Korea now ranks fifth in the world in automobile production, with a total production of 2,600,000 cars last year. <Figure 1>

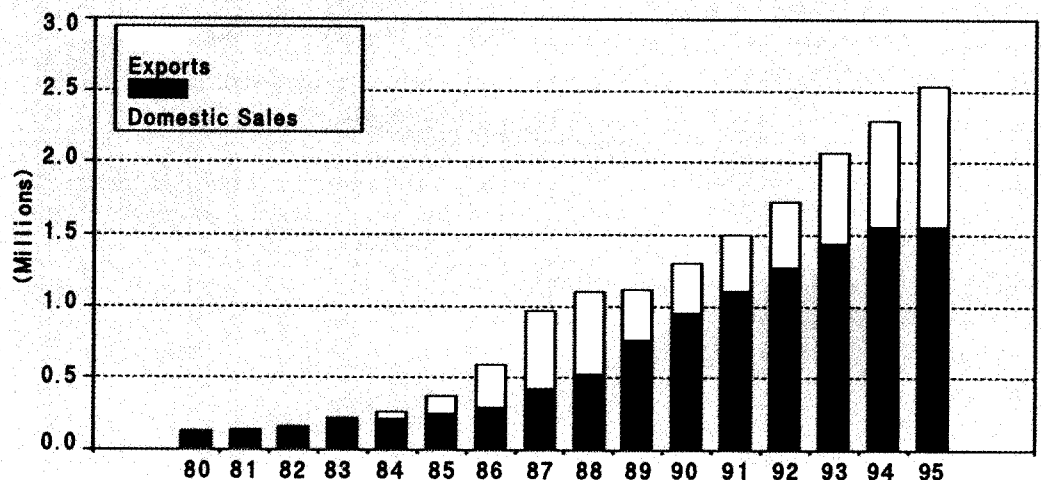
All Is Not Well

Despite this strong growth, the Korean motor industry is now facing a number of problems these days. These problems can be categorized into the following: the stagnant domestic market, the expanding imported car market, and Samsung's entry into the market.

Stagnant Domestic Market: Lately, the domestic car market has entered into a low growth period. <Figure 2> shows the trends in the growth rate of the domestic car market. One fact which stands out is that the growth rate of the domestic market last year was almost zero. Considering that the demand for small-sized cars increased

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<Figure 1> Domestic Sales and Exports



noticeably with the government's policy to promote cars with small engine sizes during the second half of the year, the growth rate for the rest of the market was actually negative.

The low growth rate in the domestic market stems from Korea's steadily worsening traffic situation caused by the high population density and inadequate social overhead capital. Thus, the solution to this can only be increasing investment and expanding social overhead capital such as roads and parking lots. The domestic car market is fully saturated. Though the domestic car market showed slight growth last year with the government's light-car-priority policy, it has actually entered into a stagnation period, which will most likely last for more than a decade until significant changes are made.

Expanding Imported Car Market: In addition to the domestic market's recent stagnancy, the expanding imported car market is also haunting domestic car manufacturers. Imported car sales only totaled some 2,000 up until 1993. However, they have increased rapidly since 1994 after negotiations between Korea and the U.S. concerning auto import liberalization and reached up to 9,000 last year.

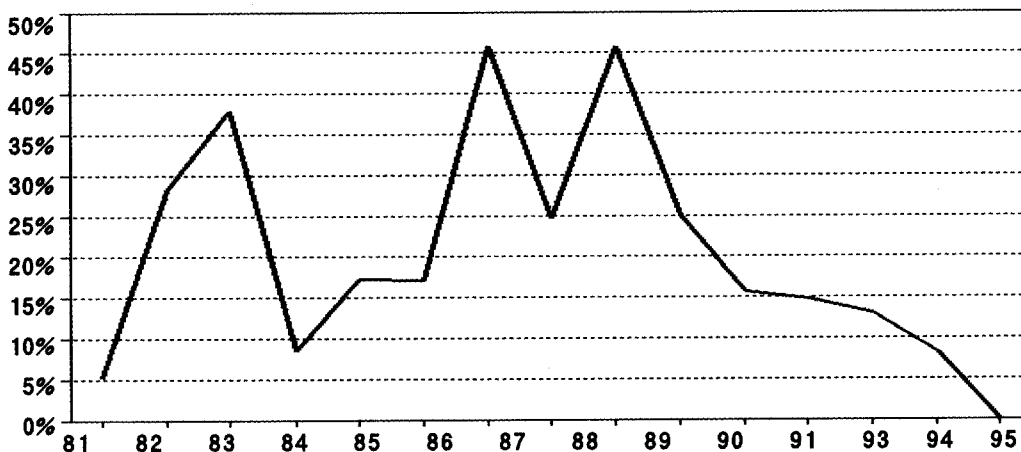
As the automobile manufacturers of the advanced nations are targeting the medium and large-size car market in Korea, this problem is especially worrisome for Korean automobile manufacturers because Korean makers try to compensate for their losses in the small-size car market with the profits from the large-size car market.

Samsung's Entry into the Car Market: Korea's existing automobile manufacturers are not only confronted by a stagnant domestic market and increasing foreign car imports but also by another difficulty, Samsung's entry into the car market scheduled for 1998. It is clear that Samsung will be able to stake out a sizeable foothold in the domestic market considering its overall size, its well-organized networks, and Korea's general cultural characteristics which emphasize brand loyalty based on blood ties and relations (i.e. Employees of Samsung, their relatives and their friends are all expected to buy Samsung cars). It is predicted that Samsung will garner a share of 15% of the car market by 2015 based on the above factors.

Samsung's entry into the car market is problematic for existing car manufacturers since the scheduled time of entry comes during this period of market stagnation. Assuming that Samsung

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<Figure 2> Growth Rate of Domestic Sales



does gain a share of 15% and foreign importers grab 10% of the estimated domestic market of 2,300,000 units in 2015, the existing manufacturers' share will only be around 1,720,000 units. In light of this year's estimated car production of 1,620,000, this means that existing makers' sales in the domestic market will only grow 100,000 by the year 2015. However, the existing car manufacturers continue to invest heavily in plants and equipment. It is expected that they will suffer from oversupply before the year 2000.

A New Strategy Is Needed

To overcome the difficulties both internal and external, the Korean motor industry must make every effort to search not for temporary expedients but instead a systematic globalization strategy and production differentiation strategy.

Globalization Strategy: Domestic car manufacturers, which produced 2,600,000 units last year, will have a combined production capability of over 4,000,000 in the year 2000. If 4,000,000 automobiles are produced, 1,800,000 of these automobiles must be expored. But considering both the localization strategies of the makers of the advanced nations and the developing nations' efforts to develop their own auto industries, this export target of 1,800,000 units seems impossible. The present export market diversification strategy is already losing its effectiveness. Now that it is difficult to expect growth based on such exports, the localization of production lines seems like a viable and attractive alternative. The Daewoo Motor Company is one maker which is pursuing such a path. Classifying the world market into a few groups according to demand patterns, economic levels and population, developing proper models suited to these groups, and manufacturing them in the local target area is needed. It is important that the locally manufactured models meet the needs of the world market as well as the

requirements of product diversification and differentiation. Furthermore, a global network controlling product transfer, R & D, and sales should be constructed.

Product Differentiation Strategy: Korean automobiles still maintain an advantage over advanced motor manufacturers in terms of price. But when it comes to quality, marketing, technology, and model development, Korean motor companies lag noticeably behind. While advanced motor manufacturers have been narrowing the price gap through endless efforts in cost reduction and the localization of their product lines, Korean manufacturers are being confronted by many difficulties due to wage increases, and now are on the verge of losing their price superiority.

It is time for Korean motor companies to change their "low-price small car" strategy. The low-priced small car market will inevitably be taken over by the developing countries. Of course it is very hard for Korean motor companies to retreat from Asian market which has such great potential, but it is time for Korea to actively challenge in the high quality-medium size motor market. It will be a little harder for the developing countries to follow into the medium-size car market, and this market is relatively less competitive, which leaves room for possible penetration. However, In order to do this, Korean car makers must first enhance their product quality.

The Korean motor industry does have some favorable prospects for the 21st century with the huge market potential of neighboring China and the possibility of the unification of the two halves of Korea. To maintain a steady growth rate under these circumstances, Korean motor companies must do their best to develop an active and systematic globalization strategy and to strengthen their non-price competitiveness and thereby successfully enter the upper market segment. VIP

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