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Cannibalize the domestic market! That's the ticket!

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June 10, 1999

Even as Asia celebrates the first tentative signs of recovery from its shattering financial crisis, market-shaping trends that began earlier this decade are accelerating. Fast-moving technology is shrinking product cycles, while oversupply pushes down prices and profits worldwide. Both trends challenge Asia, which prospered by marrying imported technology with cheap labour.

But the biggest challenge is new and vigorous competition from other emerging markets. Mexico's exports have tripled in the last 10 years. Brazil is tied with China as the second-favourite investment destination for multinationals, trailing the United States.

Gone are the days when a handful of Asian nations competed mainly with each other for export orders and foreign investment. "That party is well and truly over," says Jim Walker, chief economist at CLSA Global Emerging Markets. Annual export growth of 20%-30%--routine during the Asian "miracle" years—probably won't resume. If Asian firms maintain their share of world markets, Asian exports will track global-trade growth: 5%-10% in good years, much less in bad years.

Asia needs a new source of growth. Luckily, such a source exists and it's right here at home. There is a rich seam of productivity gains waiting to be mined in Asia's domestic economies. Asia is riddled with formal and informal cartels and monopolies; credit and distribution networks are not open to all. Economies grow when firms find ways to use their assets--people, equipment, resources and capital--more efficiently. The trick is figuring out how to send firms the right signals to dig out and refine those productivity gains.

In a deregulated economy, many of those signals come from consumers exercising their freedom of choice. Asia's export-led growth model sacrificed or simply ignored domestic consumers. Producers were in the driver's seat, and in 1997 they helped steer Asia's economic juggernaut right over the cliff. Governments need to put consumers in the driver's seat to sustain the next phase of Asian growth.

South Korea is trying to do just that. A protected home market allowed the biggest conglomerates, called chaebols, to build huge manufacturing operations, in many cases without having to develop world-class design and marketing skills. "Mediocre quality at a cheaper price was our strategy," says Jong Hyun Chang, managing partner of consultancy Booz Allen & Hamilton's Seoul office and adviser to the government on corporate restructuring. The strategy "worked until China and Southeast Asia started chasing us," Chang says. "Now we need another one."

South Korea switched its export focus to emerging markets in the early 1990s, in what was considered a smart move at the time. Little noticed was that Korean exporters were losing market share in developed countries due to quality problems, rising costs and weak brands. Pulling back from developed markets deprived manufacturers of the customer feedback they needed to compete with the best, Chang says. They certainly weren't getting that feedback at home, he adds: When customers' choice is limited, they can't signal preferences.

Since the crisis, South Korea has passed plenty of legislation to encourage competition at home and give consumers more choice. It has allowed greater foreign ownership of companies, liberalized foreign-exchange transactions and removed import restrictions. South Koreans should be able to buy Japanese cars and appliances this year for the first time in more than two decades. A series of regulatory changes, including allowing foreign banks to enter the market, are designed to force Korean banks to operate for profit, instead of acting as instruments of government policy or open tills for expansion-obsessed chaebols.

If all these new measures are fully implemented "it will be a complete shift" in Korea's approach to economic management, says M.G. Sri-Ram Aiyer, the World Bank's representative in Seoul. "Now comes the difficult part," Aiyer says. "What's needed now is a behavioural change."

How difficult that is can be seen at the Samsung Group, widely viewed as the best-run chaebol. It has made substantial changes: Its strongest subsidiary, Samsung Electronics, shed 14,000 employees last year and slashed its debt-equity ratio to about 170%, from 296% before the crisis. Managing for market share is out; managing for cash flow is in.

And yet the Samsung Group is having difficulty figuring out how to focus. It has chosen three pillars: financial services, semiconductors and digital electronics. But a financial service is one of the broadest of all business categories. Nondigital electronic products and home appliances remain a huge business for Samsung, even if they aren't a declared pillar.

Such breadth makes it hard to keep up with technology developments and consumer tastes in every product line. At Anson's appliance store in central Manila, salesmen have shoved Samsung refrigerators back into a corner to highlight a newcomer--China's Haier--that has figured out what Philippine consumers want. Haier refrigerators, made in China with European technology, consume less power, an attractive feature in the Philippines where electricity is expensive.

Failure to focus also hampers brand building. In South Korea, the same brand name can decorate cars, apartment buildings, mutual funds, candy and microwave ovens. But in a competitive market, a strong brand is built around specific product characteristics. Nestle doesn't sell cars; Ford doesn't sell apartments. Lloyd D. Ward, president and chief operating officer of the U.S. appliance maker Maytag, says South Korean companies concentrated on building brand awareness. "But awareness is not enough. You need to stand for something," Ward says. "If all you have is awareness then you can always get trumped on price." Maytag became one of the best-known brands in the U.S. by hammering home the message: Maytag stands for reliability.

As Asia's former tigers grapple with all the implications of market liberalization, they can look to the Philippines for encouragement. During the 1980s, the Philippines' real GDP grew an average of just 1% a year. But after taking office in 1992, President Fidel Ramos improved banking regulation and cracked open domestic cartels. Annual GDP growth averaged 3.3% from 1990 to 1997, with almost all of the growth coming after 1992.

Consumers have been big winners. Telephone service--an essential business tool--was spectacularly bad in the old monopoly days. Some customers waited a decade for a telephone line. When it finally faced competition, Philippine Long Distance Telephone managed to work through its installation waiting list in two years.

Some Asian companies haven't waited for governments to take the lead. They've had to compete harder and innovate just to stay alive over the past two years. "This situation has taught us so many things," says Churat Pasupa, who together with his brothers runs Chueng Chai Hah, a steel-distribution business in Bangkok's Chinatown. When the REVIEW last visited Chueng Chai Hah in early 1998, Churat was sure the family business would survive Thailand's economic crisis, though he wasn't entirely sure how.

"In a way it's good that business slowed down. We had time to think," Churat says now. Chueng Chai Hah buys big coils of flat-rolled steel, which it then cuts and sells to the construction industry and makers of auto parts and electronics components. Sales to companies that make computer cases and PC parts kept the company alive as demand from the construction and auto industries plunged.

The family didn't gamble on real estate or grandiose expansion projects and is on friendly terms with its banker, Thai Farmers Bank. Still, credit is tight. Most deals with suppliers and customers are on cash terms or close to it. That means Churat has to make better use of his capital by leaving less tied up in inventory. This lowers Churat's operating costs, and at the same time frees up capital in the economy for someone else.

Clone that behaviour across the Thai economy, in businesses large and small, and the result will be a substantial gain in national productivity--and hence in economic growth. Just look to the U.S. economy, booming in part because companies such as Dell Computer decided to treat capital as a precious commodity with the aim of improving productivity.

Tight credit has forced another change on Chueng Chai Hah. The company's customers, seeking to preserve their own capital, are demanding smaller and more frequent deliveries. In the miracle years, Chueng Chai Hah sometimes turned down small orders, but it can't now. "We had problems at first because our system was designed for big orders," Churat says. "We modified our structure and now we have learned how to do it more smoothly."

Giving customers what they want, when they want it is a formula for success in services and manufacturing, at home and in export markets. By breaking up cartels and other barriers to entry, governments can force companies to be competitive--and fuel the next Asian boom.

And when the boom resumes, then what? Churat says there will be no going back to the old ways. His customers are facing new competition from foreign investors; they--and he--will have to stay nimble. "This is the trend," Churat says.