



Corporate Tycoon

CASE STUDY 3 - SAMSUNG MOBILE
TECHNOLOGICAL GIANT LOSING IN
COMPETITION



Corporate Tycoon





Samsung is the largest South Korean multinational conglomerate company headquartered in Samsung Town, Seoul. Samsung Electronics, particularly the mobile phone business, has been its most important source of income. In 2012, Samsung has outperformed Nokia in the global mobile phone market and became the market leader. However, in the high-end smartphone market in recent years, despite its enormous marketing expenditure, Samsung could hardly keep up with Apple's iPhone's massive profit margins. It has lost its market share to Apple's premium smartphones and low-budget, high-volume brands such as China's Huawei and Xiaomi. Besides declining profit and market share, Samsung Electronics faces other issues such as negative publicity related to intellectual property infringement, labour abuse, and product safety violation, much to the detriment of Samsung's brand image.

Background

In 1938, Samsung was a trading company founded by Lee Byung-chul. Today, it has numerous subsidiaries and affiliated businesses. Following Lee's death in 1987, Samsung was separated into four business groups — Samsung Group, Shinsegae Group, CJ Group, and Hansol Group. In 2015, Samsung had about 80 companies, diversified into construction, consumer electronics, financial services, shipbuilding, and medical services, among others.

In the late 1960s, Samsung entered the electronics industry which became one of its strongest drivers to subsequent growth. To date, Samsung Electronics has become one of the most notable Samsung industrial subsidiaries.

Other notable Samsung subsidiaries include:

- Samsung Heavy Industries, the world's third-largest shipbuilder measured by revenue (Arnold, 2015)
- Samsung Engineering and Samsung C&T, both among the world's largest 50 construction companies (ENR the Top 250 International Contractors 2015, 2016))
- Samsung Life Insurance, the world's 12th-largest life insurance company (Statista, 2016)
- Samsung Everland, operator of Everland Resort, the oldest theme park in South Korea
- Cheil Worldwide, the world's 15th-largest advertising agency measured by 2013 revenues

Samsung has a major influence on South Korea's economic development, politics, media, and culture. Its affiliate companies produce about a fifth of South Korea's total exports. Samsung's revenue was equal to 17 per cent of South Korea's USD 1,082 billion GDP (Rosenbaum, 2014).

Samsung Electronics

In the late 1960s, Samsung Group entered the electronics industry. It formed several electronics-related divisions in Suwon. Its first product was a black-and-white television set. Since the 1990s, Samsung has increasingly globalised its electronics business with three major segments, namely, consumer electronics, IT & mobile communications, and device solutions. Mobile phones and semiconductors have provided its most important source of income. See Table 1 for Samsung Electronics' net revenues and operating profits by operating segment.





Table 1: Samsung Electronics's net revenue and operating profit by operating segment between years 2013–2014 (All monetary values are in billions of USD)

Year	2013		2014	
Operating segments	Net revenue	Operating profit	Net revenue	Operating profit
Consumer electronics				
Visual Display				
Digital Appliances	42,228.14	1,403.935	42,103.65	993.65
Printing Solutions				
Health & Medical Equipment				
IT & mobile communications				
Mobile Communications	116,467.60	20,939.54	93,770.45	12,218.26
Network Business				
Device solutions	56,851.40	8,390.558	55,197.65	7,912.54
Semi-conductor	31,409.29	5,779.014	33,333.39	7,363.44
Display Panel	25,033.34	2,500.69	21,585.09	553.89

Source: 2014 Samsung Electronics Annual Report

Today, being one of the most important Samsung industrial subsidiaries, Samsung Electronics is the world's second largest information technology company measured by 2014 revenues, only after Apple Inc. See Table 2 for Samsung Electronics's financial summary between year 2012–2014 and Table 3 for the world's top 10 largest technology companies by revenue.

Table 2: Samsung Electronics's financial summary 2012–2014 (All monetary values are in billions of USD)

Year	Sales	Operating Profit	Cash Flows from Operating Activities	Cash Flows from Investing Activities
2012	168.53	24.34	31.82	(26.25)
2013	191.64	30.83	39.14	(37.50)
2014	172.80	20.97	30.99	(27.49)

Source: 2014 Samsung Electronics Annual Report





Table 3: World's largest technology companies by revenue (All monetary values are in billions of USD)

Rank	Company	Industries	Revenue	FY	Employees	Market Cap	Headquarters
1	Apple Inc.	mobile devices, personal computing, software	233.72	2015	115,000	668.90	Cupertino, CA, USA (Silicon Valley)
2	Samsung Electronics	mobile devices, semiconductor, personal computing	189.50	2014	326,000	177.51	Suwon, South Korea
3	Foxconn	OEM component manufacturing	132.07	2013	1,290,000	32.15	New Taipei City, Taiwan
4	HP	personal computing and servers, consulting	111.45	2014	317,500	65.30	Palo Alto, CA, USA (Silicon Valley)
5	Microsoft	business computing	93.58	2015	118,584	452.19	Redmond, WA, USA
6	IBM	computing services, mainframes	92.79	2014	379,592	158.85	Armonk, NY, USA
7	Amazon.com	internet retailer, cloud computing, app hosting	88.99	2014	154,100	175.22	Seattle, WA, USA
8	Sony	electronic devices, personal computing	72.34	2014	140,900	31.70	Tokyo, Japan
9	Google	internet advertising, search engine, miscellaneous	66.00	2014	53,546	373.34	Mountain View, CA, USA (Silicon Valley)
10	Panasonic	electronics devices and components	\$64.00	2014	271,789	\$32.50	Osaka, Japan

Source: Financial statements of various companies

Samsung's mobile phone business

The mobile phone industry is highly competitive and largely driven by revolutionary technological innovation. Companies in this sector have mostly used aggressive promotional strategies of pricing in order to pursue growth and gain crucial market share; Samsung is no exception. In the first quarter of 2012, Samsung Electronics beat Nokia, the market leader since 1998, to become the world's largest mobile phone maker by unit sales. Since 2012, Samsung has remained the leader in the worldwide smartphone market for the number of units sold.





Business problems

Declining profit of Samsung Mobile

In 2013, Samsung Mobile was the most profitable segment within Samsung Electronics, contributing

65.9 per cent of its total profits (Dilger, 2015). The Mobile group in 2015 accounts for only 32.4 per cent of the profits at Samsung Electronics, a dramatic reversal directly attributed to increasingly intense competition from Apple's premium smartphones and low-budget, high-volume brands such as China's Huawei and Xiaomi.

In the high-end smartphone market, the performance of Samsung Mobile's Galaxy products has been disappointing. Despite being the market leader in total units sold, Samsung still cannot keep up with iPhone's massive profit margins, even by rolling out the Galaxy Note 5 and S6 Edge, two of its flagship smartphones. Samsung's 2013 margin was 18.7 per cent (Shih, 2014). Between 2014 to early 2015, Samsung smartphones maintained overall margins of around 15 per cent (Tilley, 2015). On the other hand, in the first quarter of 2015, Apple earned 92 per cent of the total profit of the world's leading eight original equipment manufacturers (OEMs), with an impressive 65 per cent increase over the same period in 2014. This profit is remarkable, considering that it accounts for less than 20 per cent of all smartphone sales. Samsung, on the other hand, received only 15 per cent of the total profit. Owing to the fact that many companies hardly broke even and actually lost money in the smartphone business, the total share of profitable players was greater than 100 per cent (Ovide & Wakabayashi, 2015).

For years, the company had profited by targeting consumer demand for big-screened "phablet" devices. However, that ended abruptly in 2014 after the launch of iPhone 6 and iPhone 6 Plus.

In 2012, Apple and Samsung essentially split industry profits 50-50. Now, Apple stands far above the others. That high-end tier has really shifted away from Samsung to Apple. In the first quarter of 2015, Apple sold 43 per cent more iPhones than a year earlier, and at a higher price. The average iPhone price in the quarter rose by more than USD 60 to USD 659, given the strength of the larger-screen iPhone 6 and 6 Plus models (Ovide & Wakabayashi, 2015). On the other hand, Samsung failed to protect its leadership from iPhone's competition in the high-end market.

Samsung and many of its new rivals mostly use Google Inc.'s Android operating system, making it harder for them to distinguish their offerings, and prompting many to compete by cutting prices. In 2014, Apple's iPhone sold for a global average of USD 624, compared with the measly USD 185 for smartphones running Android. The overall image of Android phones was adversely affected by the mass introduction of low-budget Android devices.

With market saturation and intensified competition, smartphones are more than likely to commoditise – similar to Personal Computers (PCs) – while margins are likely to contract further in the long run. In 2015, Samsung's smartphone revenue increased, but profits shrank compared to the previous quarter. To remain competitive, Samsung lowered the prices of two of its flagship smartphones – the Galaxy S6 and S6 Edge – as the global smartphone market became more saturated. However, the price cut was followed by disappointing sales of Galaxy S6 during the second-quarter, along with a lower handset average selling price due to increased sales of mid- to low-end products.

Another possible cause is the supply problem related to the innovative screened Galaxy S6 Edge. Samsung misread the market demand for its unique curved screen Galaxy S6 Edge model. It did not focus on producing normal versions that went head-to-head against the iPhone. Instead, it focused on regular S6 sales in the hope that it would outpace S6 Edge four-to-one (Campbell, 2015).





However, during the launch, the S6 Edge model quickly ran out of stock. Much to Samsung's surprise, customers did not buy the regular flat-screen Galaxy S6, but they either waited, or bought another manufacturer's handset.

Despite the market leader status by units sold, Samsung had been losing its market share year-on-year, from 32.2 per cent in second quarter of 2012 to 21.4 per cent in the second quarter of 2015 (See Table 4).

Table 4: Worldwide smartphone vendor market share in number of units sold

Period	Samsung	Apple	Huawei	Xiaomi	Lenovo*	Others
2012Q2	32.20%	16.60%	4.10%	1.00%	5.90%	40.20%
2013Q2	31.90%	12.90%	4.30%	1.70%	5.70%	43.60%
2014Q2	24.80%	11.60%	6.70%	4.60%	8.00%	44.30%
2015Q2	21.40%	13.90%	8.70%	5.60%	4.70%	45.70%

Note: *Motorola figures are captured under Lenovo.

Source: *International Data Corporation (IDC) Worldwide Quarterly Mobile Phone Tracker (2015)*

Samsung expects its smartphone sales to grow at best modestly vis-à-vis Apple's premium smartphones and low-budget, high-volume brands such as China's Huawei and Xiaomi. To save the situation, Samsung plans to cut its mobile sector spending, modify the Galaxy product pricing, and introduce more mid- and low-end models to its smartphone line-up; a strategy meant to capitalise on gaps between competing product ranges.

Marketing expenditure – may not always yield expected benefits

Besides the disappointing performance of Galaxy S6 and the supply problem of S6 Edge, Samsung's enormous marketing expenditure to launch flagship products also greatly undermined profit.

Samsung became the world's biggest advertiser in 2012, spending USD 4.3 billion on marketing, compared to Apple's USD 1 billion (Kim, 2013). Yet, in 2015, Samsung's global brand value of USD

37.9 billion was less than half of Apple's (USD 145.3 billion). See Table 5 for the world's 10 most valuable technology brands.





Table 5: The world's most valuable technology brands — 2015 ranking (All monetary values are in USD)

Ranking	Brand	Brand Value (in Billions USD)	1-Year Value Change	Brand Revenue (in Billions USD)	Company Advertising (in Billions USD)	Advertising Spending as Percentage of Annual Revenue
1	Apple	145.3	17%	182.3	1.2	0.66%
2	Microsoft	69.3	10%	93.3	2.3	2.47%
3	Google	65.6	16%	61.8	3.0	4.85%
4	IBM	49.8	4%	92.8	1.3	1.40%
5	Samsung	37.9	8%	187.8	3.8	2.02%
6	Facebook	36.5	54%	12.1	0.135	1.12%
7	Amazon.com	28.1	32%	87.5	3.3	3.77%
8	Cisco	27.6	-2%	48.1	0.196	0.41%
9	Oracle	26.8	4%	38.8	0.079	0.20%
10	Intel	25.8	-8%	55.9	1.8	3.22%

Source: The world's most valuable brands (Forbes, 2015)

Samsung Electronics spent an estimated USD 3.8 billion on advertising and marketing in 2015. Samsung spent more on advertising than both Microsoft and Apple put together. At 2.02 per cent of annual revenue, Samsung spent about three times of its annual revenue on advertising and promotion, compared to Apple (0.66 per cent). According to Kim (2013), "The outlay buys publicity in TV and cinema advertisements, on billboards, and at sports and arts events from the Sydney Opera House to New York's Radio City Music Hall. Google Inc. spent less on buying Motorola's handset business".

To compete with Apple, Samsung would spare no effort to push its flagship products through aggressive marketing and promotional campaigns. But the money spent may not bring the desired result. Although Samsung's advertising presence surpasses its rivals, its marketing has failed to address its need for a unique, positive, and consistent brand identity.

Earlier in 2013, Samsung's New York launch of its latest top-of-the-range Galaxy smartphone drew flak for its sexist portrayal of, in Kim's words, "giggling women chatting about jewellery and nail polish while the men discussed the new phone".

In 2013, a Samsung-sponsored short-film contest finale at the Sydney Opera House received poor reviews for blatant product placement in a series of "behind the scenes" videos. In the United Kingdom, viewers responded negatively to a product placement deal with ITV's popular X-Factor talent show. According to Kim, a viewer posted on Twitter, "Is this a singing competition or an extended Samsung advert?"

Samsung had started collecting brand equity data among both end users and dealers since 1994. In the 1990s, Samsung reported that its brand image was strong on dimensions of "value for money", "affordability", "ease of use", and "simplicity". But it was not as strong on the "quality" dimension, particularly in the United States and Western Europe. Some consumers also associated Samsung with the terms "cheap" and "copycat".





For a company long seen as a follower and not an innovator with differentiated or premium product, Samsung is still not able to outperform Apple's branding. With strong and highly differentiated products, Apple can afford to spend less because of its reputation for being a leading brand in innovation and creativity.

Samsung's next branding agenda is to direct marketing campaigns to present a cutting-edge image of its products, and even laud its technology 'world firsts' before they are ready for prime time, such as curved smartphones. In a statement to *Reuters*, Samsung said it will "continue to leverage [their] brand power to maintain growth momentum, while focusing on optimizing the efficiency of [their] marketing activities". This statement reiterates co-CEO J.K. Shin's words, "Our product innovation and marketing strategy have made Samsung the world's most preferred smartphone brand. Now we'll move from the most preferred brand to become one of the world's leading aspirational brands" (Kim, 2103).

However, Samsung's marketing projects aimed at projecting an innovative image had failed to win over customers. The team needs to evaluate its practice of maintaining such a high level of marketing expenditure in the long run.

Controversies and criticism over Samsung

Besides declining profit and ineffective marketing expenditure, Samsung Electronics is also facing a number of other issues, such as negative publicity on intellectual property infringement, labour abuse and product safety violation.

Apple lawsuit

Apple sued Samsung on 15 April 2011 in the United States District Court because several of Samsung's Android phones and tablets, including the Nexus S, Epic 4G, Galaxy S 4G, and the Samsung Galaxy Tab, infringed on Apple's intellectual property including its patents, trademarks, user interface, and style (Kane & Sherr, 2011). Apple's accusation included specific claims for patent infringement, false designation of origin, unfair competition, and trademark infringement, as well as state-level claims for unfair competition, common law trademark infringement, and unjust enrichment. By August 2011, Apple and Samsung were litigating 19 ongoing cases in nine countries. By July 2012, the legal disputes expanded to more than 50 lawsuits around the globe, with billions of dollars in damages claimed between them (Jagadish, 2013).

On 24 August 2012, the jury returned a verdict that was largely favourable to Apple. It found that Samsung had diluted Apple's trade dresses related to the iPhone and wilfully infringed Apple's utility patents on iPhone's "bounce-back effect", "on-screen navigation", and "tap to zoom"; and design patents that covers iPhone's features such as the "home button, rounded corners and tapered edges" and "on-screen icons". The jury awarded Apple USD 1.049 billion in damages and Samsung zero damages in its counter suit (Lowensohn, 2012).

While Apple won a ruling in its favour in the United States, Samsung won rulings in South Korea and Japan. In South Korea, the court ruled that Samsung violated one of Apple's utility patents, over the "bounce-back" effect in iOS, and that Apple was in violation of two of Samsung's wireless patents. In Japan, the District Court ruled that Samsung's Galaxy smartphones and tablets did not violate an Apple patent on technology that synchronises music and videos between devices and servers.





Labour abuse allegations

One of the biggest controversies Samsung had, besides the lawsuit on intellectual property infringement, was labour abuse. Since 2012, Samsung Electronics has been accused of breaching labour law at six China-based factories by China Labor Watch (CLW), a US-based non-profit organisation. The investigative report published by the group alleges a series of “illegal and inhumane violations”. The report was clearly a fresh blow to Samsung’s reputation following the recent high-profile US legal defeat to Apple.

More than a dozen CLW investigations of labour conditions at China-based Samsung factories and Samsung supplier factories have uncovered wilful labour violations. These include unpaid overtime wages of more than 200 monthly hours, abuse of labour dispatch and student workers, inadequate social insurance, and more occupational health and safety hazards. Undercover investigators from CLW reported that workers at all the eight Chinese factories, of which six are controlled by the company, routinely worked more than the legally permitted amount of overtime. They worked more than the legal maximum of 34 hours’ overtime a month. At seven factories, the average was more than 100 hours, with workers at one factory reaching 186 hours. Most of these factories did not uphold workers’ legal rights to a labour contract. These workers also had inadequate means of expressing grievances to their managers (China Labor Watch, 2015).

One of the most serious violations was the employment of child labour in Samsung’s supplier factories. Samsung Electronics was the subject of several accusations about child labour in its supply chain from 2012 to 2015. In August 2012, CLW first exposed the use of child workers by HEG, a Samsung supplier in Huizhou, a city in Guangdong province. Despite Samsung’s public statement that it had found no child labour after subsequent inspection, near the end of 2012, the CLW uncovered more child workers in HTNS, another Huizhou- based Samsung supplier. That report alleged that the use of workers under the age of 16 was “common practice” in the factory. In June 2014, CLW uncovered many child workers (under age 16) in the Shinyang Electronics factory. Owing to its “zero tolerance” policy for child-labour violations, Samsung terminated its contract with the company after investigation provided evidence of Shinyang using underage workers.

Around the same time as CLW’s investigations, Samsung published its 2014 sustainability report *Global Harmony*. In the report, Samsung claimed that it inspected working conditions at 200 suppliers in 2013 and found “no instances of child labour” (Osborne, 2014).

In South Korea, Samsung faced accusations that it failed to protect workers from carcinogenic substances at its semiconductor plants. A court in 2011 ruled that Samsung had caused the death of two workers. Despite Samsung’s announcement that its plants are now safe, there is reason to worry that more cases may follow (Simpson, 2014).

In 2012, Samsung’s main competitor Apple Inc. was also accused of labour law breaches at Foxconn factories in China, where millions of Apple products are assembled each year. However, Apple Inc. and its main manufacturing contract electronics supplier Foxconn quickly reacted to the criticism and agreed to tackle violations of working conditions of more than a million assembly-line workers. They promised better pay and working conditions as well as compensation for the workers in question. The media labelled it as a “landmark decision that could set the bar for the rest of the sector” which “changed the way Western companies do business in China”(Gupta & Chan, 2012).





Product safety issues

Despite growing popularity of Samsung's Galaxy smartphones, several incidents of explosions of the handsets have been reported. In July 2013, a Swiss teenager suffered second and third-degree burns in the thigh when her Galaxy S3 smartphone exploded in her pocket. A similar incident had occurred earlier in May 2013 when a Reddit user was "awoken by a loud noise" and the phone was "on the verge of setting alight and his bedroom had filled with smoke" (Woollaston, 2013).

Samsung's Galaxy S4 caused several other accidents. A house in Hong Kong was allegedly set on fire by an S4 in July 2013 (Zolfagharifard, 2013), followed by minor S4 burn incidents in Pakistan and Russia. A minor fire was also reported in the United Kingdom in October 2013. There were a few more reported Galaxy S4 explosions in India and the UAE.

Another Galaxy model also had this flaw. In South Korea in 2011, the battery from a Samsung Galaxy Note allegedly exploded in a man's pocket while he was walking along the street, causing second-degree burns and a one-inch wound to his thigh (Woollaston, 2013). It was the second time that year a battery from the Galaxy Note was said to have exploded in South Korea.

According to a Samsung spokesperson,
Once we have gotten hold of the product in question, we will conduct a thorough examination to determine the exact cause of this incident. We would like to assure our customers that we have always employed strict quality control and safety standards to ensure a safe and pleasant user experience (Woollaston, 2013).

Some users of the phone have also reported swelling batteries and overheating. Samsung had offered new batteries free of charge to customers that were affected by such incidences.

What was reported next surprised the public. In December 2013, a Canadian YouTube user uploaded a video showing the damage caused while charging the battery of his Samsung Galaxy S4 handset. Although the battery did not explode, his handset caught fire. He contacted Samsung for a replacement for the damaged handset. To his surprise, he was instructed to sign a legal document that would compel him to remove the video from YouTube, remain silent about the agreement, and surrender all future claims against the company. Samsung's letter also demanded that he remain silent about the settlement details.

According to the letter from Samsung,
As a condition of exchanging the phone with a similar model, *** agrees to remove his YouTube video or any other link or statement relating to these matters, and refrain from making other videos or statements about or relating to the matters set out herein.

No further response from Samsung was received after this letter. The letter was posted online by the uploader subsequently. Samsung's approach backfired quickly. Within a week, Samsung's letter gathered over 270,000 views while the video racked up over 700,000 views (Zolfagharifard 2013).

Lithium-ion batteries are widely used even though they are known to be hazardous when overheated. Several similar incidents occurred over the years. Overheated batteries led Nokia, Dell, Apple, Lenovo, Panasonic, Sharp, Toshiba, Hitachi, and Fujitsu to recall products.





But the response of Samsung Electronics to the incidents left millions of Samsung users disappointed.

Besides intellectual property law suits, labour abuse, and product safety violation, Samsung also went through many other controversial malpractice cases, including accusations of bribing in many financial scandals, price fixing, and hiring students to attack competitors in online forums.

Concluding remarks

Samsung has increasingly globalised its activities since its creation in the 1930s. Samsung Electronics, particularly the mobile phone business, has become its most important source of income. Samsung Electronics went through many problems, controversies, and illegal cases, some of which are still affecting its operations today. How can Samsung Electronics improve its profitability and brand value despite the negative publicity? How can Samsung respond to criticism and controversies? These are issues that warrant much thinking.





End-of-Case Questions

Question 1

Apply product life cycle (PLC) model to the smartphone market. What are the key characteristics of each stage? Identify the current stage that smartphone business is in. Recommend actions that Samsung Electronics should take to succeed at this stage of PLC.

Question 2

Based on the case, evaluate Samsung's marketing communication strategy in terms of its brand equity. Recommend appropriate marketing/branding strategies to help Samsung Electronics improve its brand equity.

Question 3

Identify the most appropriate branding architecture that corresponds with the case of Samsung and Samsung Electronics. Evaluate the branding architecture.

Question 4

Evaluate Samsung's crisis management strategies. Recommend areas of improvement.

