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# The Future of Sony and Samsung Electronics

> Sony must become a "modernized company." A modernized company means a company that stands independent from the past glories, and the founders; a company that can be managed by ordinary people like myself. In other words, it means a company operated on a system.
>
> —*President Chubachi, Sony*[1]

> Now, other companies will no longer teach or lend us their technologies. That means Samsung must now do everything on its own, from technology development to establishing management systems. That process will be a lonely race.
>
> —*Chairman Kun-hee Lee, Samsung Group*[2]

The differences in performance between Sony and Samsung Electronics are not the results of their strategies. Rather, organizational processes and executives' leadership seem to have determined their performances. In other words, Sony's digital dream kids' strategies could have worked if they had been executed properly. The fit between Samsung's strategy in responding to commoditization with speed and its militaristic organization may have contributed to its stellar performance.

Sony and Samsung Electronics have a good deal to learn from each other. From Sony, Samsung Electronics might learn how to transition from having founders rule the firm to letting professional managers take charge and how to change from a small domestic company into a large, far-flung global enterprise. Samsung Electronics could also learn from mistakes that Sony has made, which might help it resolve some of the long-term problems that it faces. On the other hand, Sony can learn from Samsung about how it can improve the execution and implementation of its strategy.

## Superficial Crisis and Internal Crisis

### The Internal Crisis of Samsung Electronics

Although Samsung Electronics is a competitive global enterprise, it is facing a serious internal crisis. One of its problems is excessive centralization. The major decision-making power is held by Chairman Lee and his Office of Secretaries, a group-level staff organization. There are no measures to check their decisions even when they take the wrong direction. In Western companies, strong corporate governance structures guard against such absolute power. These firms have boards of directors that appoint CEOs, determine their remuneration, and approve major investments. This system has been developed to prevent firms from being run into the ground by a few managers. In some Western countries, labor unions also influence a company's major decisions. Furthermore, the media and investment analysts also serve as a check against untrammeled executive power. In Korea, however, Samsung Group is extremely influential, and the media praises everything it does.

Currently, Samsung Electronics' board has only relatives of Samsung's founder and key senior executives on its board of directors. Also, although Jong-yong Yun's nominal title is CEO of Samsung Electronics, he is really a COO; he receives instructions from and is supervised by the Office of Secretaries, and Chairman Lee decides what Samsung Electronics' major strategic investments will be. The danger of Lee's power is exemplified by Samsung Group's ill-advised foray into the automobile industry during the mid-1990s. After losing a lot of money, Samsung Group sold the business to Renault. There



was no one to oppose Lee's decision to enter this business. Although Lee's resolute decision making is considered important to Samsung Electronics' success, it may be a positive influence only when Samsung Electronics competes in businesses with clear technological trajectories, for which rapid development and production efficiency are essential. When businesses require creativity and have no clear evolutionary path, this one-man decision making may prove disastrous.

Samsung Electronics is also experiencing organizational fatigue, which has been induced by "fear-based management." Its employees and board members can be dismissed for any reason by the chairman, the Office of Secretaries, or other superior managers. The Office of Secretaries (renamed the Group Strategic Planning Office in 2007) monitors key executives' performance. Working under such stress, Samsung's employees are suffering accumulated fatigue. Indeed, despite its status as the best company in Korea, over 10% of Samsung Electronics' employees quit their jobs in their first year and over 30% do so by their third year because they are unable to bear the heavy workload. Samsung Electronics' parts suppliers, including other Samsung Group affiliates, are also under great pressure to comply with Samsung Electronics' demands to lower costs and meet delivery deadlines.

A lack of creativity is another of Samsung Electronics' weaknesses. So long as it had a clear target to pursue, such as Sony in consumer electronics, Intel in semiconductors, and Nokia in the mobile phone business, it could surmount its considerable disadvantages by benchmarking against these firms and having its employees work around the clock. The firm's corporate culture, management goals, values, and management resources have been optimized to capitalize on the benefits available to a late entrant.

As it has become a market leader, however, there is no one for it to imitate. Instead, it must lead by developing new technology and formulating innovative corporate strategies. Yet it has few creative employees who can generate genuinely new ideas. Furthermore, both engineers and managers fear failures, which make them focus on projects that may have immediate payback and low risk. Even worse, Samsung Electronics has thus far failed to accumulate technical expertise in developing new products because its R&D divisions have been focusing primarily on improving production efficiency.

Chairman Lee is aware of the "creativity gap," especially in regard to personnel, and has taken various initiatives to close it. Since 2002, he has had every subsidiary report monthly its record of securing key talent, and these records are factored in to evaluations of the respective subsidiary presidents' performance. Lee also made "creativity" the core creed for management in 2006. Currently, about 4,000 of Samsung Group's employees are considered "key members"; Samsung Electronics has about 2,800 of them. These employees are ranked as S(super), A(ace), and H(high potential), and receive special attention.

Beyond closing the creativity gap, Samsung Electronics must deepen the pool of talent that it needs to become a global enterprise. So far, it has been able to satisfy this need by hiring Koreans or Korean-Americans. Yet such people are in short supply, and are increasingly harder to find. Unless Samsung Electronics becomes more serious about hiring and promoting non-Koreans and/or purchasing firms that have promising technologies and good managers, its lack of talent in the global arena could fetter its growth.

Furthermore, Samsung Electronics shows signs of hubris. In the past, Samsung Electronics, as a late entrant, tried to maintain a willingness to learn from others. As it enjoys good performance and is acknowledged as an industry leader, however, it has become less inclined to correct its internal problems. "Samsung is having a Sony moment"—a comment by a cynic suggests that Samsung Electronics is showing signs of complacency just as Sony did 10 years ago.[3] Indeed, Samsung's performance did begin to deteriorate in 2007 due to intensified competition in memory chips and LCDs.

### Sony's Ordeals and Potentials

Chairman Stringer officially admitted that Sony's problems have resulted from strategic and organizational failures. Stringer believed that Sony's organization has become too divided and that its business units have become silos, which has made resource allocation less efficient, added to Sony's bureaucracy, and slowed decision making. He argued that Sony needed both to develop a strategic focus and to create competitive advantage by developing new products.[4] Stringer introduced an internal slogan, "Sony United," to promote teamwork, cooperation, and the marriage of key resources.



To these ends, he dissolved the Network Company structure that Idei had implemented, converted it back to the traditional business division structure, and centralized the decision-making process in order to break down internal barriers and to encourage communication across businesses. Control over product planning, purchasing, and technology development was transferred back to President Chubachi; instead of being parceled out over far-flung divisions, Sony's resources were concentrated on developing new hit products. According to Stringer and Chubachi, "this significant structural change was designed to eliminate the business 'silos' and to foster a more coordinated, efficient and rapid decision-making process."[5] They also decided to close 11 out of 65 factories to save 200 billion yen, and ordered the layoffs of 10,000 employees by March 2008. They are still considering whether to close or rationalize factories in the United States, the UK, China, and Japan.

Nonetheless, Sony still has formidable technology, know-how, and human talent. Its failure to develop new products since the mid-1990s has stemmed mainly from its organization and leadership, rather than from its lack of technological capacity. The patents and technologies Sony retains should lead to good short-term performance if Sony can overcome its recent setbacks. Moreover, Sony has a strong brand. Although one study found that Sony's brand value was declining, that study measured brand value in conjunction with the brand's financial performance (see Chapter 4). Other studies suggest that Sony remains one of the highest-ranked brands.

Also, although Sony has not been able to create synergies between its hardware and entertainment businesses, it may regain that opportunity soon if digital convergence further unites content, hardware, and communication businesses. If this occurs, Sony's portfolio is ideal, since it encompasses businesses in audio and video home electronics, computers, communications, games, film, and music, as well as a strong brand image. If Sony can exploit this potential, it will possess an extraordinary competitive edge. If it cannot, Sony has to consider seriously an option to break up the company by spinning off the entertainment and game businesses, not to mention its insurance and financial services units. A stand-alone electronics unit may enable its workers to focus on the dynamics of digital technology.

## Lessons Learned by Sony and Samsung Electronics

### The Focusing Strategy of a Latecomer

What made Samsung Electronics a global brand in the last decade was its strategic "selection and concentration." It learned the lessons of aggressive investment and fast execution in the DRAM business and applied them to flash memory and LCDs, which, like DRAM, had industry standards, involved mature technologies, and were quickly commoditized. It also used technology that it could buy from other firms. This strategy, a far cry from Sony's goal of creating unique products, compensated for Samsung's shortage of technological know-how, and allowed Samsung to reap the maximum benefit from its workforce.

Samsung Electronics was also quick to exploit the opportunities of digital technology. Because there is no difference in the quality of digital products so long as each uses the same chip set, Samsung Electronics could catch up with market leaders even though it was a late entrant and was technologically inferior in the analog world. It then allocated its marketing resources in order to improve its brand image and concentrated most of these resources in mobile phones, which was the product for which it could get the highest return on its investment. In choosing distribution channels in foreign markets, Samsung Electronics focused on selling to a small number of specialty electronics stores, adopted a high-price, high-margin strategy, and gave dealers incentives to sell its products. It also realigned its sales organizations in big cities and selected "emerging markets" around the world in which to market. What differentiated Samsung Electronics' marketing activities from those of Sony is that Samsung actively invested in marketing, and Sony did not. Sony's brand value came mainly from the company's capabilities in new product development. In contrast, Samsung Electronics erected its brand out of nothing, despite the poor quality of its products, by strategically investing in marketing and distribution.

Other late entrants can learn from Samsung Electronics' experience. Typically, late entrants try to catch up with market leaders by benchmarking them and imitating their strategies. This strategy is doomed to failure, however, because late entrants, which have fewer resources and less technological capability, can never catch up with leaders simply by imitating them. Samsung Electronics' story demonstrates that a company can create competitive advantage by using paradigm shifts such as the advent of digitalization to concentrate its resources in technologies, products, markets, and channels that play to its unique strengths.



### Core Competences and the Competence Trap

Both Sony and Samsung Electronics demonstrate that a firm's core competence can easily become its core liability.[6] Samsung Electronics makes decisions swiftly and has an execution-oriented corporate culture. These factors are common to many Korean companies, as well as to military organizations. Once the head of the organization makes a decision, the organization focuses all its effort on achieving these goals without complaints or contemplation. Samsung Electronics' other core competence is its production efficiency. It is the world's most cost-efficient producer of memory and LCDs. This advantage originates from its investments in production facilities and process technology, which reduces costs and enhances yield.

Yet these strengths are also Samsung Electronics' weaknesses. The firm's corporate culture of obedience and execution and its strong financial orientation may be rapid and efficient, but they also hinder new product development and creativity. Compared to Sony, Samsung Electronics is weak in nonmemory businesses and end products, for which creativity is required. Its end products compete on cost; they are not different from competitors' offerings. This weakness happens because the firm takes practices that are appropriate for the memory business and applies them to nonmemory ones and end products.

Unlike Samsung, Sony excels in developing original new products under its founding creed of "Freedom and Open-mindedness." Its liberal, vibrant corporate culture made Sony an engineers' heaven. Sony's engineers researched what they were interested in, and the technologies they developed gave birth to innovative new products like the Walkman, CDs, DVDs, 8mm camcorders, digital cameras, PlayStation, and Aibo. This culture requires extensive trial and error, however, until the final result is achieved. Innovation can be costly, time-consuming, and inefficient. Also, because Sony engineers were free to do what they wanted, they often concentrated on technology that was unrealistic or hard-to-commercialize. In short, Sony's organization was fit for developing new technologies and products, but was unsuitable for executing the CEO's strategies. Sony has fallen not because Idei's network strategy was ill-advised; it has fallen because the organization is incapable of executing strategies.

The case of Sony and Samsung Electronics also illustrates how difficult it is for a firm to forgo its past success and transform its culture to meet changing environments. Idei commented, "The difficulty Sony faced was that we could not forget the success of the past. Sony's success was based on the tape format, CD format, and transistor TV. People complain, 'In old days, we were clearly a leader but what are we now?' But, the world is changing. The probable difficulty of Samsung in the future will be how they can forget the success of the past, such as the success of DRAM, LCD, and mobile telecom?"

**Fit of Corporate Culture, Organization, and Leadership**

Sony got into trouble under Idei because his leadership did not complement Sony's corporate culture and organization. Sony's corporate culture of "freedom and open-mindedness" and independent business units worked well under Morita not because Sony was systematically managed but because of Morita's charisma. Morita could interfere with matters and placate complaints and uncertainty when there were conflicts among company units or business prospects were hazy.

Because Idei was Sony's first salary-man president, however, it was difficult both to expect him to have charisma and to expect his subordinates would unconditionally obey him. Idei understood his limits as a professional manager and tried to realign the organization to reflect those limits. His policies, such as the company system, a board with outside directors, and the separation of executives from board members came from his intention to operate Sony, a giant conglomerate by that time, without relying on charisma. Sony's corporate culture and management style could not be changed easily, however, so Idei's efforts were unsuccessful.

In sum, Sony's stagnation during the last decade may be the result of the mismatch of its strategy, leadership style, corporate culture, and organizational structure. By contrast, Samsung Electronics' stellar performance may derive from the close connection between its strategy of accepting commoditization while creating competitive advantages



in speed, and its execution-oriented organization under a charismatic leader. Samsung's corporate culture, emphasizing loyalty and discipline, also made it easier to effect its strategies.

**Conversion from a Family-Owned Company to a Professional Management System**

Sony's mismatch is also attributable to the difficult transition from the founders' generation to a generation of professional managers. Idei once lamented that, despite the fact that Sony had grown up to a half a hundred billion dollar company, it was still driven by the founders' vision: "I knew that running Sony was impossible because it was a company driven by the founders' vision: the founders' personal vision was the basis and the standard for every decision." This comment suggests the biggest challenge Idei faced: to satisfy employees' expectations, which had been fostered by the founders. He had to do so despite being Sony's first president who had begun as a salary-man, in addition to meeting the technological challenges that digital innovation and network technology posed. Ibuka, Sony's founder, was a great engineer, and Morita was an extraordinary manager. Ohga, although not a founder, was also considered part of the founders' generation, because he had joined Sony so close to its founding. In addition, Ohga was accomplished. He was a vocalist, and a friend of world-famous musicians, and had even once conducted the Berlin Philharmonic. He also had a pilot's license, and was a legendary manager who achieved great success with the PlayStation, despite internal opposition.

In contrast, Idei did not have as distinguished a past, and he was the lowest-ranked, youngest executive member when he was appointed. While he presented his strategic vision, he did not have enough charisma to sell it to his employees, and so he failed to meet their expectations. Ohga nominated Idei based on his personal judgment; he did not do so after thorough preparation and verification. Idei did not have sufficient time to prepare for his new position. Consequently, his leadership was challenged, and he could not realize his vision.

This confusion during the succession process provides a good lesson to other companies, including Samsung Electronics. Sony's misfortune might have started with Morita's sudden illness. He could not talk and lay in bed for six years, during which there was a vacuum of top management leadership. A top Sony executive said, "Illness is something you cannot control. Because of it, Sony had a dramatic succession. Morita was like a God. No one could possibly replace him."

Many firms throughout the world are managed by founders with strong charisma. It is critical for these firms to learn to replace the irreplaceables. Chubachi's comments that Sony must become a modernized company, operated on a system and managed by an ordinary person like himself, succinctly summarize the challenges of all firms that are undergoing the transition to a new generation of leaders. Perhaps, another challenge for Chubachi is to learn how a company run by an ordinary man can continue to be extraordinary in the future. For example, in 2006 Toshitada Doi, a famed engineer, resigned after his pet project, Aibo, a robot dog, was terminated. More than 100 Sony employees then threw a mock funeral for the Aibo. At the funeral ceremony, Doi recalled, "Aibo was a symbol of a risk-taking spirit [of Sony] that was now dead."[7] Sony has been a very extraordinary company by any measure. It can be managed by an ordinary man, to use Chubachi's phrase. It will not be possible to keep generating innovative products without the risk-taking Sony spirit. The greatest challenge for Stringer and Chubachi will be to maintain the Sony spirit.

Chairman Lee is a second-generation member of Samsung Group's founding family. It is not clear whether his family can maintain its "emperor management" control over the Samsung Group in the future. Lee and his family members own less than 4% of Samsung Group, and own even less of Samsung Group's listed companies. Moreover, with over 50% of Samsung Electronics' stocks owned by foreign investors, and as Samsung's subsidiaries become larger, it will grow more difficult to run Samsung Electronics as if it were a family-owned company. It will be interesting to see whether Samsung Electronics can maintain its core competence of orderly, responsive management when professional managers begin running Samsung Group. To prevent the confusion and errors that can occur, as they did in Sony, during this transition, Samsung must foster professional managers and establish a systematic governance structure in advance.

### Challenges in Becoming a Global Enterprise

Sony has taken many steps toward globalization. It has developed and sold its products worldwide, acquired U.S. entertainment



firms, implemented a Western-style board of directors, and even hired a foreigner as its CEO. Although these facts show how globalized Sony appears from the outside, it is questionable whether Sony's internal globalization, such as the mindset of the employees, is at the same level.

The likely causes for Sony's current problems are legion. Sony was driven by the founder's vision rather than by a systematic plan, and the organization was run based on personal relationships. It could be said that Sony's loss of control over Sony America happened because Sony promoted globalization and localization too rapidly, without considering its competence to manage the inevitable tension of its global localization strategy. Moreover, Sony's globalization may have reflected its overconfidence about its capacity for globalized management. Its adoption of COO and CEO titles from Western companies may have been unwise because most of Sony's employees perceived the president to be the CEO. This mismatch created confusion over who had ultimate power. Also, the company system turned traditionally independent departments into silos, and short-term performance indexes such as EVA hindered long-term investments such as R&D. Sony's experience shows how dangerous "visible" or "superficial globalization" can be.

Sony's problems might have stemmed from globalization that was too rapid, but Samsung Electronics' biggest problem may be its procrastination about globalizing. However grand and global its production and distribution goals are, its employees' ability to manage global operations is limited. It will also need to discard its Korean bias and hire more creative talent from other countries, because the Korean educational system does not foster creative engineers and managers. Achieving these goals will not be easy, especially because Samsung Electronics is currently enjoying its heyday. Because of its outstanding performance and the worldwide adulation it is receiving, hubris is growing within the organization and undermining the company's ability to look critically at itself and correct its mistakes. This arrogance, the pride that anything Samsung does is bound to be the best, the sense that Samsung is now a first-class global corporation that has nothing to learn from others, reminds some observers of Sony 10 years ago. Samsung Electronics must remember that in order to truly win at global competition, it must face and overcome even greater challenges in the years ahead.