

A Corporate Business Leader's Unfulfilled Ambitions to Build a Major Conglomerate

—The Woongjin Group Files for Bankruptcy

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Makoto, ABE (Seoul, Research Fellow Sent Abroad, IDE-JETRO)

Foreword

The Woongjin Group, which ranked 39th in terms of assets in corporate South Korea, has effectively filed for bankruptcy. In terms of asset scale, the Woongjin Group has less than 5% of the amount of assets held by the Samsung Group. Nonetheless, the Woongjin Group's bankruptcy filing is sending ripples throughout South Korean society for two main reasons. First, it is South Korea's first major bankruptcy since the economy abruptly stalled at the start of 2012. Second, the Woongjin Group is one of only a few mid-tier to large South Korean industrial groups that have reached their current position under the leadership of the current owner in a single generation. In this report, we retrace the steps of the Woongjin Group, from its growth to collapse.

A Company Founded by a Top Salesman

Yoon Seok-keum, founder of the Woongjin Group, was born in 1945 as the child of an impoverished farming family in Gongju City, South Chungcheong Province, South Korea. After graduating from the College of Commerce and Economics of Konkuk University, Mr. Yoon joined Korea Britannica Corporation in 1971 as a salesman. Here, Mr. Yoon became No.1 in domestic sales just one month after joining the firm, and in his first year received an award given to Britannica's highest-performing salesperson out of all 54 countries where the company does business worldwide. Mr. Yoon quickly climbed the corporate ladder, becoming regional manager in 1973 and managing director in 1976. Shortly thereafter, however, he decided to set out in business for himself and establish his own company. At this time, Mr. Yoon focused his attention on the sale of English-language study materials. Mr. Yoon established the book publisher Heim International (later renamed Woongjin Publications, currently Woongjin ThinkBig). The company was set up to publish the Korean-language version of Modern English Self Learning (MESL), a series of English-language study materials that had proven popular in Japan at the time. When commencing sales, Mr. Yoon established a sales network focused on door-to-door sales comprising 186 agents under 7 branches organized by region. MESL was an expensive product that was priced four times higher than other companies' products. Nevertheless, MESL achieved solid sales with a rush of orders coming immediately after the start of sales.

To drive further business expansion, Mr. Yoon then made a direct investment in study

materials. In 1980, the South Korean government banned extracurricular education (education provided at sites other than official schools, such as cram schools and preparatory schools) in order to curb overheated competition in university entrance exams. Mr. Yoon's plan was to try making audio recordings of the classroom teaching of instructors, in order to sell packages of cassette tapes and textbooks like English-language study materials. Right away, Mr. Yoon scouted the instructors of famous cram schools and preparatory schools nationwide, and developed the *Heim High School Studies* textbooks. At the time, sales of these textbooks were sluggish because of poor market recognition. However, Mr. Yoon's strategy was to recruit former teachers as salespeople in large numbers to promote the product to parents and students. The strategy paid off. With sales increasing dramatically, Woongjin Publications successfully established a stable business foundation. Furthermore, Woongjin Publications expanded business in study materials mainly by offering textbooks to junior high school students. At the same time, the company entered the children's book publishing business. When entering this business, Mr. Yoon recruited human resources through such means as hiring graduates of Seoul National University to work in the Editorial Department—students struggling to find employment who had participated in a student uprising movement. All 36 volumes of the *Children's Village series*, Woongjin Publications' first release, became tremendous bestsellers with more than 7 million copies sold. As a result, Woongjin Publications achieved rapid growth through the 1980s with core businesses centered on door-to-door sales of study materials and children's books.

Rapid Growth through the Water Filtration Appliance Business

At the end of 1980s, Mr. Yoon created the opportunity for the Woongjin Group to achieve dramatic growth on a full scale by entering a new business based on expertise in door-to-door sales. That new business was the home-use water filtration appliance business. Prior to this, Mr. Yoon established Dong Il Industries (currently Woongjin Foods) in 1987 to manufacture and sell processed foods made from ginseng. In 1988, Mr. Yoon established Sarangs Cosmetics (renamed Coreana Cosmetics the next year, sold in 1999) in an attempt to tackle the challenge of door-to-door sales of food and cosmetics. However, in order to efficiently operate the door-to-door sales network, there was a need to diversify the range of products sold. That is when the home-use water filtration appliance business was considered. To enter this business, Mr. Yoon established Korea Coway Co. (later renamed Woongjin Coway) in 1989. At first, Mr. Yoon's plan was to import and sell water filtration appliances. However, due to quality issues, the company decided to manufacture water filtration appliances as well. Woongjin Coway manufactured water filtration appliances in line with the safety standards of the Water Quality Association of the United States. Fortunately, there was heightened recognition of the importance of safe drinking water among ordinary households following an incident in 1990 in which the chemical substance phenol spilled into the Nakdong River.

Helped by these circumstances, Woongjin Coway made a strong start.

The 1997 Asian financial crisis provided another opportunity for Woongjin Coway to achieve growth. Because of structural adjustments following the crisis, the Korean economy had weakened and water filtration appliance sales had decreased sharply. In response, Woongjin Coway launched a new rental business for water filtration appliances, rather than selling these products. What's more, rather than merely providing leases, Woongjin Coway enhanced and provided additional services such as filter replacements and water quality inspections through regular home visits. The company created a team of female sales representatives predominantly consisting of housewives, known as "Cody," and home-visiting technical staff known as "CS doctors." Through these measures, Woongjin Coway saw sales increase sharply from 277.3 billion won in 2000 to 1.008 trillion won in 2005. The rental membership reached 3.65 million people in 2005.

Entering the Manufacturing Industry - The Solar Power Generation Business

All was well up to here. Mr. Yoon, who had increased his confidence by converting the setback of the currency crisis into an opportunity, entered another new business in the latter half of the 2000s. He chose to enter two fields that were entirely unrelated to his existing businesses: solar power generation and construction.

Generally speaking, solar power generation systems are produced and sold based on a flow from polysilicon to ingot/wafers, solar cells, modules and systems. The Woongjin Group began studying the feasibility of entering the solar power generation business in around late 2005. At this time, however, the Woongjin Group was only considering launching a service to install and manage residential solar power generation equipment using Woongjin Coway's network of home-visiting technical staff. However, the Woongjin Group decided that the entry into the manufacturing sector was an appropriate course of action based on rapid growth in the manufacturing of solar power generation systems in countries such as Japan and Germany. Ultimately, the Woongjin Group established Woongjin Energy in 2006 as a joint venture with SunPower Corporation of the U.S. Woongjin Energy commenced production after licensing ingot manufacturing and module assembly technology from SunPower. Furthermore, the Woongjin Group established Woongjin Polysilicon in 2008, successfully entering the upstream polysilicon sector. In the same year, the Woongjin Group acquired Saehan Industries Inc. (currently Woongjin Chemical), a synthetic fabric and chemical materials manufacturer, and reportedly made effective use of Saehan's technicians in the polymerization process.

However, competition had intensified by this time due to the entry of numerous companies into the solar power generation business both in South Korea and overseas. Since production benefits from economies of scale, there was no choice but to expand production facilities in order to survive. Woongjin Energy and Woongjin Polysilicon also continued to expand production facilities. The result was a global oversupply of solar power generation systems. The situation was only made worse by drastic cuts in subsidies for solar power generation by European governments prompted by the European financial crisis. The worsening business performance of the two companies engaged in the solar power generation business started to weigh heavily on the Woongjin Group.

Bad Move: Acquisition of Construction Company

It was the entry into the construction industry that ultimately sealed the Woongjin Group's fate. Many companies that went bankrupt shortly before and after the currency crisis sought to rebuild their business with the support of creditor banks and foreign investment funds. The latter half of the 2000s was a time when these companies appeared on the M&A market as "chips to be sold." Mid-tier industrial groups vied with one another to acquire these companies in an effort to expand the scale of their business. The Woongjin Group acquired Kukdong Engineering & Construction Co. in 2007, followed in 2008 by the aforementioned purchase of Saehan Industries. Notably, Chairman Yoon was strongly passionate about entry into the construction sector, and constantly noted that "the construction and finance sectors are the star players of capitalism." However, amid a boom in corporate acquisitions, the Woongjin Group is said to have acquired Kukdong Engineering & Construction at a far higher price than market value.

Shortly after the acquisition, real estate market prices, which had been buoyant until then, fell into decline and stagnated. Nonetheless, Kukdong Engineering & Construction pressed ahead with the apartment development business by leveraging real estate project finance, where income from apartment unit sales was pledged as collateral for loans from financial institutions. However, a full-fledged real estate downturn took hold from 2011, causing the apartment sales business to weaken drastically. As a result, Kukdong Engineering & Construction and Woongjin Holdings, which had effectively provided a loan guarantee to the former company, started to face cash flow difficulties. The Woongjin Group tried to generate cash by selling Woongjin Coway, a blue-chip company, but was unsuccessful. Ultimately, Woongjin Holdings and Kukdong Engineering & Construction filed for a court receivership program on September 26, 2012 for corporate rehabilitation.

Many mid-tier industrial groups that acquired construction companies in the latter half of the

2000s are now facing a management crisis. These construction companies are now weighing down the corporate groups that acquired them. For example, the Kumho Group acquired Daewoo Engineering & Construction in 2007, and the LIG Group acquired Kum Young Co., Ltd. in the same year. In 2008, the Hyosung Group acquired Chin Hung International Inc. and the Taihan Electric Wire Group purchased Nam Kwang Engineering & Construction Co., Ltd. in the same year. As mentioned above, the Woongjin Group also made such an acquisition. Following the bankruptcy of the Woongjin Group, the Financial Supervisory Service is said to be closely monitoring the financial condition of some industrial groups whose construction companies are experiencing management difficulties.

Unfulfilled Ambitions to Build a Major Conglomerate

As we have seen so far, the Woongjin Group achieved rapid growth by expanding business based on door-to-door sales of English-language study materials, study magazines and children's books plus home-use water filtration appliances. However, the Woongjin Group's proactive investment in the solar power generation equipment business and construction sector in the latter half of the 2000s proved unsuccessful, forcing two Woongjin Group companies to request court receivership. Chairman Yoon is said to still be enthusiastic about turning the Group around. However, the Woongjin Group's creditor financial institutions, which have become increasingly distrustful because they were not consulted prior to filing for court receivership, are said to be determined to request the sale of the Woongjin Group's affiliated companies. Accordingly, it is still uncertain whether the Woongjin Group will survive in its present form.

In South Korea, where large conglomerates such as Samsung and Hyundai hold tremendous influence over not just the economy but society as a whole, mid-tier industrial groups aspire to expand their scale by entering new businesses. Notably, the South Korean economy in the 2000s was characterized essentially by the success of major exporting companies and a housing bubble. In such a climate, recognizing the limitations of steadfastly pursuing the door-to-door sales business, Mr. Yoon must have aspired to make significant strides in new businesses. However, these new businesses were worlds apart from his existing businesses, and the times had started to change. Companies from China and other emerging countries began proactively entering businesses where exports could be launched immediately by introducing facilities and technologies. As a result, these businesses no longer generate the level of earnings seen in the past. Making matters worse, with the collapse of South Korea's housing bubble, the construction sector is hardly the cash cow that it once promised to be. Instead, it has become a drag on the management of various industrial groups.

The South Korean economy is now facing a downturn in private-sector consumption

accompanying burgeoning household debt, in addition to slowing exports due to the sluggish global economy. Is the bankruptcy of the Woongjin Group a sign of a long-term economic slump? In South Korea in the fall of 2012, the burden of the economic downturn seems to weigh heavily on society as a whole, eclipsing signs of enthusiasm in the run-up to the presidential elections.

(Bibliography)

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