Retail Internationalization: Gaining Insights from the Wal-Mart Experience in South Korea

Franco GANDOLFI
Regent University, USA
E-mail: fgandolfi@regent.edu
Phone: 1-757-352-4483
Pavel ŠTRACH
Škoda Auto University, Czech Republic
E-mail: pavel.strach@skoda-auto.cz

Abstract

Wal-Mart, the world's largest retailer, failed to capture the hearts of South Korean consumers, ultimately withdrawing in 2006 after eight years in the market. Although, it had achieved stunning successes in the U.S. and overseas, Wal-Mart was unable to apply its proven U.S. business model in South Korea. Wal-Mart is only one among several retailers that have underestimated the role of conducting cultural due diligence prior to entry into a foreign country. This paper analyzes the causes and antecedents of Wal-Mart's failure in South Korea with the discussion centering on Wal-Mart's inability to understand and respond to South Korean consumers. Wal-Mart's failure demonstrates how firms fail to alter their business practices to the idiosyncrasies of a foreign culture. The primary managerial implication is that the local culture determines the business model.

Keywords: *retail internationalization, Wal-Mart, South Korea, research case study*

Introduction

The Wal-Mart business concept has become a success story with its '*Every Day Low Prices*' slogan captivating consumers, especially in these economically challenging times. Wal-Mart is one of the largest private employers in the world and its sales revenues surpassed the $370 billion mark in 2008. Wal-Wart is North America's largest retailer and boasts a market share of an estimated 20 percent of the entire U.S. retail market. Despite Wal-Mart's unprecedented success, rising from its humble beginnings as a discount store in Arkansas to one of the world's foremost corporations, there were two market withdrawals in 2006 – from Germany, and from South Korea – that deeply impacted Wal-Mart's unrelenting quest to expand globally. While the pull-out from Germany was highly publicized, the South Korean withdrawal received little media or research attention. In this paper, we purport to uncover the potential antecedents of the withdrawal and compare them with the established retail internationalization literature.

Retail internationalization has been widely discussed in the current marketing literature. Research has provided evidence that retailers may falter when establishing international operations. Cases of Marks & Spencer in the U.S. (Burt, Mellahi, Jackson, & Sparks, 2002), K-Mart and Carrefour in the Czech Republic, Ahold in China, Lane Crawford in Singapore, Tesco and Toys 'R' Us in France, C&A in the United Kingdom, or Home Depot stores in Chile (Burt, Dawson, & Sparks, 2003) furnish prime examples of economic failure resulting in a complete shutdown or sale of operations to another, typically locally and well-established, retail chain. Over the past 50 years, 21 percent of European grocery retailers pursuing internationalization experienced divestiture, major organizational restructuring, or closure (Burt, Dawson, & Sparks, 2004). On average, it has been shown that retailers divest after seven years spent in a foreign country. Causes of failed internationalization effors in the retailing industry can be divided into four categories (Burt et al., 2003): market failure related to the risk and stability of the foreign market; competitive failure based on poorer than market average performance; operational failure meaning the inability to adapt and transfer marketing and operating approaches to the foreign market; and business failure rooted in difficulties in the home market. A further reason for failure in internationalization efforts may be insufficient adaptation to cultural and consumer-behavior related local habits (Bianchi & Arnold, 2004).

For a given retailer, internationalization may have positive effects. International efforts have been motivated by the desire to increase profitability (Evans, Bridson, Byrom, & Medway, 2008) and to diversify customer base (Vida & Fairhurst, 1998). If internationalization is pursued in order to increase profits, retailers should either approach the strategy full throttle or refrain from it completely (Leknes & Carr, 2004), rather than undertaking halfhearted efforts (Leknes & Carr, 2004). Internationalization in the retailing sector makes a positive, but small contribution to a company's sales (Etgar & Rachman-Moore, 2008). Finally, international experience from one's own retail overseas operations provides a valuable platform for learning, thus contributing to the success of subsequent international ventures (Palmer & Qinn, 2005).

Retailers, as well as other international firms, can expand internationally through various entry modes. In comparison with the increasingly popular franchising (Petersen & Welch, 2000; Doherty, 2007), setting up wholly-owned subsidiaries or joint ventures requires equity investment. Both wholly-owned subsidiaries and joint ventures are typically established to implement and utilize the core know-how of a multinational company in the subsidiary (Dunning, 1970, 1993; Kogut & Zander, 1993). In a retail setting, this means transplanting the whole retail format into another country (Helfferich, Hinfelaar, & Kasper, 1997), remaining considerate of the local market, focusing upon business performance (Rogers, Ghauri, & George, 2005), and maintaining similar market positioning (Burt & Mavromatis, 2006).

While local markets seem to converge in terms of consumer behavior (Davies & Flemmer, 1996) and customer attitudes, purchasing fast moving consumer goods (FMCG) is highly influenced by the local culture and habits (Askegaard & Matsen, 1998). Furthermore, while technology-based products, including electronic goods or cars, are similar across the globe, foodstuffs or cosmetics seem to be intimately connected to their cultural roots. Retailers, just as other multinationals, modify their product offerings (Walters & Toyne, 1989), pricing strategies (Ackerman & Tellis, 2001), and other marketing features to serve local, typically emerging markets better (Dawar & Chattopadhyay, 2002). In fact, retailers may even try to capitalize on their own or their product's countries of origin (Bilkey & Nes, 1982).

South Korea is one of the emerged East Asian markets. Consumer ethnocentrism of South Korean buyers leading to hostile attitudes to foreign products has been empirically supported (Kwak, Jaju, & Larsen, 2006), although this attitude can be managed by appropriate marketing efforts, and young affluent South Korean shoppers may show more similar characteristics to typical Western consumers (Hafstrom, Chae, & Chung, 2005). It remains to be determined whether a Western retailer such as Wal-Mart may succeed in South Korea and what local adaptation needs to be done. In this paper, we seek potential implications from Wal-Mart's South Korean experience as to what strategies, measures, and attitudes of multinational retailers may not be appropriate for the international arena.

The purpose of this paper is to determine and analyze the potential causes and antecedents of Wal-Mart's failure in South Korea resulting in a withdrawal from the South Korean market in 2006. Our case study discussion occurs in two parts – we analyze the series of events Wal-Mart was involved in South Korea between 1997 and 2006 and we then discuss potential implications of this failure, seeking to provide insights helpful to both researchers and marketing practitioners.

Methodology

Our methodological approach is based on a single in-depth case study. Case studies in organizational research are suited to illustrate and examine research frameworks, particularly in differentiated or unique instances (Eisenhardt, 1989; 1991). The case study methodology employed in this research has long been established as a valid tool of mainstream academic inquiry (Whitley, 1932), with particular support for its utilization in international business research (Ghauri, 2004). Circumstances indicating that a case research approach is appropriate – as in the present context – include the intention for in-depth contextual analysis of a specific situation that is either unique or occurs in small numbers (Yin, 2003), complexity of situations leading to the necessity to examine cases in their entirety (Flyvbjerg, 2004), and utilization of induction to expand perspectives on a problem being researched (Bonoma, 1985). Even a single case is deemed appropriate for discovery of new theoretical relationships and questioning the established ones (Dyer & Wilkins, 1991).

Wal-Mart is of particular interest since it is a global retailer still reliant mainly on the U.S. customers. The company, based in Bentonville, Arkansas, became an international firm in 1991 when a Sam's Club opened its doors near Mexico City. Just two years later, Wal-Mart International was created to oversee the company's growing international operations. Today, customers at more than 3,355 stores in fourteen countries are living proof of Wal-Mart's *Every Day Low Price* promise. In 2008, Wal-Mart International employed more than 620,000 associates in Argentina, Brazil, Canada, China, Costa Rica, El Salvador, Guatemala, Honduras, India, Japan, Mexico, Nicaragua, Puerto Rico, and the United Kingdom.

Wal-Mart's global expansion has been achieved through a combination of green-field investments, acquisitions of existing stores, and joint-ventures. These strategies have contributed to market penetration and effectively positioned the company for future growth (Jang, 2006). The retail sector has witnessed Wal-Mart's rapid expansion throughout North America, Latin America, Asia, and Europe. In 2006, the year in which the company decided to discontinue its South Korean operations, Wal-Mart International posted impressive financial results, with end sales reaching $62.7 billion and operating profits $3.3 billion, both figures representing an 11.4 percent increase over the previous year (Gerrit, 2006).

Despite many political, cultural, and business challenges around the world, Wal-Mart International has continued to experience enormous success since 2006. Wal-Mart International claims that it makes a concerted effort to embrace *and* adapt to local cultures and become deeply involved in the local community. Associates respond to local customer needs, merchandise preferences, and local suppliers. By serving each hometown in the same way, Wal-Mart International has realized considerable efficiencies and synergies. It has also achieved significant growth with potential for further development worldwide. Annually, Wal-Mart International opens as many as 250 units in its existing fourteen markets. Relocations and expansion of existing stores accounts for approximately 10 percent of these units, while the remainder represents new operating units for the company (Mark, 2006).

The Rise and Fall of Wal-Mart Operations in South Korea

Wal-Mart South Korea was established in August 1998. Wal-Mart had acquired four stores and six undeveloped sites in South Korea. At the time, the units were operated as Makro stores, a chain of Netherlands-based membership clubs. Three of the stores were located in the capital city of Seoul and one in Taejon. Each store was a single level unit with more than 100,000 sq. ft. of space. Since Makro had only been operating in South Korea for two years, the stores were fairly new. Wal-Mart's international division Senior Vice-President and Chief Operating Officer, Carlos Perez, was also part of Makro's entry into South Korea when he was executive Vice-President of Makro. The acquired units had sales of $160 million in 1997. Wal-Mart had hoped that its long-term commitment to the country would allow those sales to increase considerably. Although, along with that of all other Asian countries, the South Korean currency had declined sharply in value in the wake of the 1997 Asian financial crisis (Olsen, 2006), South Korea's economy was rebounding.

Wal-Mart had high hopes for the long-term potential for South Korea's operations, believing they would ultimately contribute to the sales of Wal-Mart's international division. While the geographical size of South Korea is comparable to that of Florida, the population is three times as large. At the time, there were 135 Wal-Mart stores and 33 Sam's Club stores in Florida. There was an underlying expectation that the (successful) business model in Florida could be replicated in South Korea (Troy, 1998). However, at the time of withdrawal from the Korean market in 2007 (9 years after initial entry), Wal-Mart was ranked in the bottom five major discount stores in the country. According to Wal-Mart's spokesperson, Wal-Mart South Korea had sales of about $787 million in 2005. Later, at a press conference in Seoul, it was revealed that the company had an operating loss of about $10 million in 2005 (Olsen, 2006).

As will be developed at length in the next section of the paper, anecdotal evidence suggests that South Koreans believe that Wal-Mart failed in South Korea primarily due to Wal-Mart's inability to understand the shopping preferences of local consumers and to adjust its business model to the prevailing domestic culture. As a result, financial gains from South Korean stores were miniscule and in spite of substantial investments, consumers chose not to make Wal-Mart a primary shopping destination.

On May 22, 2006, Wal-Mart, the world's largest retailer added its name to a list of multinationals that had failed to adjust to the taste of South Korean consumers (Choe, 2006), With this result, Wal-Mart joined other reputable firms, including Nokia, Nestlé, and Google, that had previously experienced a similar fate in South Korea. In fact, Wal-Mart was the second Western retailer to retreat from South Korea in less than a month. France's Carrefour, the world's second largest retailer behind Wal-Mart, had sold its 32 South Korean outlets to local retailer E-Land on April 28, 2006 for $1.85 billion (AFX, 2006).

Having been approached by Shinsegae retail chain (AFX, 2006), Wal-Wart sold its 16 stores to Shinsegae for $882 million, which constituted a considerable loss. Shinsegae is South Korea's largest discount store chain which operates the country's third ranked department store chain (Murdoch, 2006). Prior to the acquisition, it operated 79 stores, which accounts for 30 percent of the local market. This was followed by Homeplus, owned by British retailing company Tesco with 17 percent, and Lotte Mart, owned by Lotte Shopping of South Korea, with 12 percent (Choe, 2006). Shinsegae commented that it planned on operating the Wal-Mart stores as a separate subsidiary. The CEO of Shinsegae stated that the department store's discount chain E-Mart would absorb all 16 Wal-Mart stores in South Korea (Hyong-ki, 2006). E-Mart has 86 stores, which accounts for 30 percent of the South Korean discount market (Choe, 2006).

Shortly before the sale of its South Korean stores, Wal-Mart made major investments in other geographical areas, with mixed results. In March 2005, Wal-Mart said it had lifted its ownership in Central America's Retail Holding Co. to 51 percent and renamed it Wal-Mart Central America. The division operates 375 supermarkets in Guatemala, El Salvador, Honduras, Nicaragua and Costa Rica. It had also made two other strategic international acquisitions, boosting its holding in Seiya Ltd. to 53 percent and lifting its market position to number three in Brazil with the acquisition of Sonae Distruicao Brasil S.A. (MarketWatch, 2006). In early 1998, Wal-Mart withdrew from a three-year-old partnership to run operations in Jakarta, Indonesia, which, at the time, did not allow foreign investments (MarketWatch, 2006). On July 28, 2006, eight years after entering Germany, Wal-Mart sold its 85 German stores to rival supermarket chain Metro and booked a pre-tax loss of about $1 billion on the failed venture. Wal-Mart Germany was losing about $265 million a year on a turnover of about $2.7 billion. This was in spite of many attempts to revamp and turn around the business.

What Went Wrong?

It must be understood that Wal-Mart is a corporation that is not used to failure. In contrast, Wal-Mart was accustomed to success and not just any success, but some of the greatest successes in the history of retail. When financial failure struck at Wal-Mart, there were many stunned constituencies. Mike Duke, Head of Wal-Mart International, commented:

> *As we continue to focus our efforts where we can have the greatest impact on our growth strategy, it became increasingly clear that in South Korea's current environment it would be difficult for us to reach the scale we desired.* [Gandolfi, 2007]
>
> *We have decided to sell our business to the market leader as we believe this is the best option for our associates, customers, and shareholders*. [Gandolfi, 2007]

Wal-Mart's view on its own failure was that South Koreans simply preferred their own domestic shopping centers. While this statement is true as far as it goes, most individuals believe that Wal-Mart failed to understand South Korean's consumer preferences. Analysis of key marketing decisions made by the firm reveals missteps in distribution, product mix, and promotion strategies that could not be overcome even by an advantage in pricing. Wal-Mart had relied on its proven business model and its strategy in offering low prices for products. However, low prices alone – even *'Every Day Low Prices'* – were insufficient to make a successful business case in South Korea.

1. Distribution

As in the United States, most Wal-Mart outlets in South Korea were placed outside instead of in the cities. South Koreans, however, were used to easily accessible shopping facilities without the need to travel. Some individuals felt that Wal-Mart should have been located in the center of the cities where consumers felt more comfortable with their shopping needs. Also, South Korean consumers were used to shopping more frequently than most Americans do. They may not purchase things at once, but they will usually buy at least one item.

The South Korean culture is very tied into the markets; it is one of the largest countries that is deeply involved in local markets (Gen, 2006). South Korean consumers expect to see local products presented in a localized fashion; this is probably the main reason why South Koreans did their shopping at E-Mart, the company Wal-Mart sold its operations to, rather than Wal-Mart. E-Mart has a decidedly different, more localized approach to selling products, with a more local feel to their stores.

South Koreans are visually-oriented customers, appreciating aesthetically pleasing displays and shopping environment. As another South Korean professional commented:

> *Wal-Mart outlets in South Korea are simpler in appearance that those of E-mart and other competitors and they sell products by the box, while E-mart and Lotte mart build eye-catching displays.* [Korean newspaper]

Many South Koreans would not shop at a Wal-Mart because they did not like how the store was set up. Many housewives did not want to buy foreign foods and beverages (Choe, 2006). Some South Koreans said they were just so used to shopping at local stores and they did not really like the massive floor of a Wal-Mart's store. South Koreans have a tendency to pick out more luxurious products and surroundings, and are not very receptive to the typical Western-like box discounter (Olsen, 2006). A marketing journalist from the South Korean Times stated:

> *In fact, some South Korean ladies do not like the warehouse-like atmosphere of Wal-Mart, which the American consumers seem not to mind since the products are still cheap. They prefer the department store-like, neat, clean, and sophisticated atmosphere. If you go to E-mart which is the biggest South Korean supermarket, you never think of it as a discount market.* [Korean newspaper]

A business analyst from the South Korean Investment and Securities commented:

> *Wal-Mart and Carrefour were not aggressive enough in expanding their networks in South Korea. Once they lost the race, they could never catch up.* [Korean newspaper]

2. Product Mix

South Koreans have different consumer preferences than North Americans do; they are not necessarily interested in the same products. The pursuit of Western market strategies that mainly focus on dry goods, electronics, and clothing hurt Wal-Mart while in South Korea (Murdoch, 2006). For instance, South Koreans like fresh vegetables and fresh food rather than dry products and the type of clothing that Wal-Mart sells. A South Korean marketing professional stated:

> *Wal-Mart put off South Korean consumers by sticking to Western marketing strategies that concentrated on dry goods, from electronics to clothing, while their local rivals focuses on food and beverages, the segment that specialists say attract South Koreans to hypermarkets. South Koreans really like fresh vegetables and beverages.* [Korean newspaper]

Furthermore, it has been revealed that many South Korean housewives did not want to buy foreign foods and beverages (Choe, 2006).

3. Promotion Strategies

Wal-Mart's promotion strategies failed to resonate with South Korean consumers. South Koreans believe that Wal-Mart brought over its Western sales tactics and company culture. Wal-Mart stores are geared towards U.S. customer preferences, which include a warm, friendly greeting and standardized store layouts. Wal-Mart's approach to business is certainly successful in the U.S., but different cultures have different idiosyncrasies. Local South Korean stores adopt different selling strategies. For example, E-Mart used fancy displays and aggressive sales techniques – such as hiring clerks who entice shoppers with megaphones and hand clapping – while Wal-Mart sold products out of boxes. South Korean consumers are generally not interested in shopping in a store that has distinctly American flavor and style (Gandolfi, 2007).

4. Pricing

In the United States, Wal-Mart has been able to compensate for any arguable deficiencies in its marketing mix through overwhelming price superiority (Kiernan, 2004). This advantage never materialized in South Korea. The austere atmosphere of Wal-Mart stores, which may suggest efficiency and savings to North American consumers, failed to impress South Korean shoppers. South Koreans do not distinguish between discounts and normal prices (Gandolfi, Braun, Nanney, & Yoon, 2008). Thus, they may not see a compelling reason to shop at Wal-Mart. Moreover, when Wal-Mart first arrived in South Korea it was not in a position to capture a large market share and was unable to force competitors to sell their products at low prices. Thus, unlike in the U.S., Wal-Mart was unable to make competitors attempt to beat it at its own game.

Wal-Mart came into South Korea keeping its own culture and sales tactics, not realizing that it would have to adapt to a foreign country (Kottolli, 2006). Wal-Mart may have come to realize that any business concept is subject to relentless market, environmental, and business pressures and is continually exposed to local expectations. The retail colossus has had to learn that local customization, flexibility, and adaptation are essential ingredients in the successful pursuit of international business operations (Shin, 2006). Wal-Mart stated that it withdrew from South Korea because it did not believe that it could achieve the results it desired. A similar situation occurred in Germany where Wal-Mart withdrew its 85 stores. Following its failure in South Korea, Wal-Mart decided to focus on those foreign markets that were most profitable for the firm at the time, particularly Latin America (Gandolfi, 2007).

Discussion and Concluding Remarks

The world's largest corporation, American retailing giant Wal-Mart, failed to capture the hearts of South Korean consumers. Despite its stunning successes in the U.S. and overseas, Wal-Mart was unable to effectively apply its U.S. business model in South Korea. This paper presented the successes and failures of Wal-Mart. The discussion has pointed out Wal-Mart's inability to understand and respond to the common South Korean consumer. Wal-Mart's financial failure demonstrates that firms may still struggle to adjust their business practices to the key idiosyncrasies of a foreign culture. Wal-Mart is only one among a growing number of firms that have underestimated the role of conducting proper consumer due diligence prior to entry into a foreign country.

What lessons can be learned? The most important aspect for firms going global is an in-depth understanding of what the local customers really want, desire, and need. As firms expand internationally the virtues of flexibility and adaptability become of primary significance. However, these areas of strengths are by design, rather than by accident. They need to be incorporated into strategic thinking of firms intending to go global. Some business concepts may be recognized globally and are easily transferable, while others may be suited only to particular countries or regions.

Theory suggests that the typical market withdrawal occurs after seven years from entry. It took Wal-Mart a year longer to realize that its South Korean operations would not thrive. Based on our case, this particular failure may be classified as competitive or perhaps more as operational (Burt el al., 2003). Wal-Mart did not post solid financial results for its South Korean operations. Even more, it failed to adjust its marketing and market approaches to the consumers. Although the company tried to maintain its common internationally recognized market positioning, its adaptation to local habits was found insufficient (Bianchi & Arnold, 2004). It can be echoed for Wal-Mart that retailers need "to understand what it is that is being internationalized and the value this has to consumers in the destination market" (Burt, Davis, McAuley, & Sparks, 2005: 201). International retailers need to understand their own core competencies and values, as well as whether those values will resonate with consumers in various cultures. Transplanting a retail concept means retaining its core features while skillfully focusing on local consumers.

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