

Case study for samsung electronics



Case Analysis for Samsung Electronics 1. What is SMIC's strategy? Should Samsung be concerned about SMIC? SMIC seems to execute the same kind of strategy Samsung used before to succeed. The strategy is selling their products at low prices and growing their market share at the expense of profitability. SMIC may threaten Samsung's business in the future, but not too much. Although SMIC can get many resources, such as cheap funds and lands from Chinese government and foreign investors, SMIC only focuses on producing chips, not designing chips.

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The cost of the application of a new tap today is 3 billion and it is difficult for SMIC with sales revenue of 365.8 million in 2003. Samsung's success depends on its constant technology innovation, leading to high quality products and efficient manufacturing process which will benefit Samsung with high retail prices and low cost. SMIC seems hard to get core technology from their partners unless forming a joint venture. However, cooperating with chip manufacturers in Taiwan seems more attractive for the leading technology owners.

Except the technology, Samsung still enjoy unit cost advantage in raw materials, R&D and depreciation. SMIC may threaten Samsung's old generation products. However, memory chip industry is a tech-oriented industry, Samsung can still maintain its leading position because its advantage in innovation. What Samsung should concern is that the fast growing Chinese market (estimated to be the second-largest semi-conductor buyer in 2010), their global competitors may get market-entry advantages through cooperating with SMIC. 2. The low cost position.

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Samsung operating profit advantage over the industry composite is \$2.11 per unit, 34% from selling price and 66% from cost advantage. To SMIC, it is 1.78 per unit, 70% from selling price and 30% from cost advantage (Exhibit 1). For the comparative cost analysis, Samsung have unit advantage over the industry composite in all the five elements. They are raw materials 36%, labor 27%, depreciation 18%, R&D 3%, SG&A 25.29%. Compared to SMIC, Samsung has advantages in raw material 36%, depreciation 17% and R&D 25%, but has disadvantages among labor 57% and SG&A 48% (Exhibit 2).

1 Analysis Samsung VS Industry Composite

a. Samsung's unit selling price advantage comes from two aspects. First, PC OEM manufacturers would pay 1% price premium to reliable suppliers. Second, Samsung can customize its products for some special use because its diverse products line to get premium. Third, Samsung has the most advanced products which can enjoy high selling price during the first several-month launching time.

b. Samsung's unit raw material cost advantage come from three aspects. First, the material suppliers will give maximum 5% discount to large volume buying.

Second, the usage of 12-inch wafer (reduce 10% cost per chip) and 0.11 μ m processing technology(80%, the highest yield rate) makes Samsung get more chips with same amount of materials. Assuming the weighted average raw material cost per chip of Samsung is 100%, the Micron will be 134%, Indineon 116% and the Hynix 161% (Exhibit 3).

c. Samsung's unit labor's cost may be explained by the salary differences between Samsung (\$44000 per year) and the industry (\$49312 per year, weighted average by production volume). Also, there are some invisible issues.

Samsung provides equal and competitive corporation value, unique evaluation and promotion system and humanity warfare for their employees. These elements make Samsung more productive, so the labor cost per unit is lower. d. The reason for Samsung's unit depreciation cost advantage per unit is similar to that of raw materials. With high processing technology (0.117 m) to control yield rate (Samsung 80% vs Industry weighted average 59%), Samsung can produce more efficiently. So the depreciation per unit is lower. The production efficiency advantage (25%) is higher than the cost depreciation advantages (17%).

That may be because Samsung uses more advanced and expensive machine. e. Samsung's advantage in unit R&D cost may come from three ways. First, the competitive corporation culture drive employees to devote themselves in innovation. And the technical person works together with the manufacturing one, making the innovation process more efficient. Second, the innovation method is effective. They can use same core technology to develop different products types, such as the DDR and Rambus. Third, centralization of the R&D facilities saves an average 12% fab construction costs. Samsung's unit SG&A cost advantage comes from the efficient management structure of the country reducing the general administration cost and good reputation of products reducing the sales expenses. 3. 2 Analysis Samsung VS SMIC a. Compared to the industry composite, Samsung's profit advantage over SMIC mainly from the price realization (70%), and the cost advantage only stands for 30%. The huge price gap results from several aspects. First, the quality and reputation for SMIC is lower. Second, the technology SMIC used was one or two generation older than Samsung.

Third, use the low price strategy to get the market share. Finally, SMIC using purchasing rights exchanging for technology partners, the price of product selling to their partner may be lower than the marketing price. b. The reason for Samsung's unit material cost advantage seems similar to the one over industry composite. c. The disadvantage of labor cost is because the average salary of SMIC is only a quarter of Samsung. d. The reason for Samsung's unit depreciation cost seems similar to the one over industry composite. The gap should be larger.

However, the SMIC gets cheap loans and government support, and buy old product line from Motorola. These issues may help SMIC reduce the gap. e. Samsung's unit R&D cost advantages may be explained with SMIC's start-up status. It usually spends a lot at the early age of innovation. To build a new fab for SMIC is more expensive than Samsung. f. The disadvantage of Samsung in unit SG&A may be explained by SMIC's strategy. Now, SMIC has to manufacture the products for their technology partners. SMIC seem to focus less on marketing their brands and become an OEM factory. 3. Can Samsung retain its cost advantage?

If lose, what would happen at Samsung and SMIC? In my opinion, the main drive for Samsung's profit is its innovation, which can lead to high selling price and low manufacturing cost. The raw materials advantages may be decreased with increasing SMIC production volume and advanced manufacturing technology. The labor disadvantage is hard to say because Chinese labor cost is also rising. The depreciation advantage may be decreased by the efficiency improvement of SMIC. The R&D gap may also be

decreased by the development of SMIC. SA&G depend on to what degree SMIC want to promote their own brand.

So the Samsung's cost advantages over SMIC will be decreased in the future and even lose. However, assuming that someday Samsung loses its cost advantages, it is still very likely that Samsung is ahead of SMIC by one or two generation. Samsung still can make more profit by with higher selling prices. Even though SMIC can get government support and cheap funds, it cannot acquire the same kind of corporate culture and the centralized R&D facility. By the way, SMIC cannot tolerant long time profit loses as a public company and the national security concerns may put more resource on logic chip. 4. Options and recommendations. a.

Joint venture: Corporate with SMIC or other chip manufacturers in China to produce low end DRAM. Even the low end technology is attractive to China and get government support. Open the potential Chinese market and reduce cost. But it is hard to maintain the relationship with the constant requirement of technology transfer. b. OEM: License SMIC and make it as an OEM manufacture for Samsung. Transfer our low end technology to SMIC. The longer SMIC keeping the contract, the less threat. However, SMIC seems unwilling to accept this contract unless it faces profit pressure. SMIC's ability may not reach the Samsung products requirement. . Focusing on our own business: Samsung's core competency is constant and efficient innovation. Memory chip industry is technology-oriented and the advantage cannot be achieved in few years (Unless competitor gets breakthrough such as total substitute, which is little probability). The corporate value cannot be copied in a short time. Samsung may reallocate its resources of DRAM (profit,

manufacturing capacity of old chips and R&D) towards more promising flash memory business. By doing that it can still keep its leading position in memory chip industry. I recommend this option.