

MARKETING PROBLEMS OF THE SMALL BUSINESS IN KOREA

—with particular reference to marketing of the
silk fabrics produced in the Kyongpook area—

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I. Introduction

The common goal of all less developed and developing countries is to reach the stage of "take-off" in the shortest period of time. To achieve this goal, they want to establish favorable trade relations with other foreign countries. For this purpose acceleration of industrialization and rapid increase in the productive power are considered to be the most effective target. In Asia along, more than 20 countries have established three-to-ten year economic development plans and are pouring efforts to carry them out effectively. But actually they are not "economic development plans" but really are "production acceleration plans".⁽¹⁾ The first and second economic development plans of Korea are no exceptions.

Of course production is one of the most fundamental element for economic

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(1) This problem was clearly pointed out by Prof. Kindleberger. See, Charles P. Kindleber; *Economic Development*, New York, McGraw-Hill, 1958, p. 107.

development. But without simultaneous development in the field of modern marketing, it cannot be assured that the produced goods will make the fullest contribution to increasing national income and the level of further production. Thus, it is quite true to say that "production may be the door to economic growth of the underdeveloped countries, but marketing is the key that turns the lock".⁽²⁾ Without effective marketing system operating, uninterrupted flow of goods which are already scarce enough can not be expected. Therefore the problems of marketing certainly deserves more attention, especially in the underdeveloped and developing countries which are longing for rapid economic development.⁽³⁾

But blind application of theories developed in, and for, the advanced industrial economies to solve the marketing problem of an underdeveloped economy should be avoided. It is vitally important in the social science which pivots around the historical, social, and cultural background that, for a theory developed in a specific environment to be applied to another country which has different conditions in time and space, the conditions of the country must have basic similarity to the society from which the theory has originally emerged. This point of view is also applicable in marketing problems.⁽⁴⁾

In this respect, it is important to understand how a wholesaler plays his role in the operation of marketing system in developing countries. An important fact is that in underdeveloped and developing countries the goods produced by small scale enterprises which are many in number and which have vulnerable financial status occupy greater portion of market supply. And the wholesaler whose role is to distribute the goods is relatively small in number but stronger than most of the small scale producers in the financial status. Therefore the balance of power in competition is always in favor of the middlemen, and

(2) Woodruff J. Emlen; "Let's Export Marketing Know-How", *Harvard Business Review*, Nov.-Dec., 1958, p. 70.

(3) For the relation between marketing and economic development, see Peter F. Drucker; "Marketing and Economic Development," *Journal of Marketing*, Jan. 1958, pp. 252-259.

(4) For a detailed discussion, see J. N. Chaturvedi; *The Theory of Marketing in Underdeveloped Countries*, Allahabad, India, Kiatb Mahal, 1959, and also see Chong Yeong Lee; "Problems of Agricultural Marketing in Underdeveloped Countries-with particular reference to rice marketing in Korea (in English)", *Collection of Thesis*, Vol. VIII, Chung-gu College, Taegu, Korea, 1964, pp. 275-296.

consequently the marketing system also depends upon the role placed by them.⁽⁵⁾

The purpose of this paper is to show the role played by the middlemen in marketing goods produced by the small business in Korea, with particular reference to marketing of silk fabrics produced by a number of small scale weaving companies, in the Kyongpook area.

II. Background Information

It is customary in Korea to divide fabrics into three large groups; cotton, silk, and woolen. Rayon and nylon fabrics are customarily included in the silk fabric. Therefore the silk fabric is defined, for the purpose of this study, as any fabrics woven with silk, rayon, or other chemical yarn.

As shown in Table-1, the Province of Kyongsang Pukdo (Kyongpook) has 38% of total silk fabric weaving firms in Korea.

(Table-1) Number of Silk Fabric Weaving in Korea (1966)

Province	Number of Firms	Percentage
Seoul	38	8.4%
Pusan	55	11.9
Kyonggido	35	7.5
Chungchong Pukdo	8	1.9
Chungchong Namdo	76	16.4
Cholla Pukdo	19	4.1
Cholla Namdo	11	2.6
Kyongsang Pukdo	177	38.3
Kyongsang Namdo	41	8.9
Total	460	100.0

Note: The source; Textile Year Book, 1967. Korean Textile Association.

Almost all the silk fabric weaving firms in the Kyongpook area are located in the city of Taegu which is the capital city of the province, and therefore Taegu is called the textile city of Korea. Approximately 41% of the products are consumed within the province and 46% of the products are consumed in Seoul, the capital city of Korea.

This study was conducted during the period from August 1 to October 30, 1962. Of the firms in the Kyongpook area, 131 firms are members of the

(5) Hee Bum Park: "Theory and Practice of Price" in *Collection of thesis*, Vol. IV. Taegu College, Taegu, Korea, 1966.

Kyongpook Fabric Cooperatives. Of these 131 firms, 10 firms were selected (by judgement) for intensive personal interview. Besides, wholesalers and retailers and officials of the Fabric Cooperatives were interviewed, as shown by Table-2.

(Table-2) Number of Persons Interviewed

Classification	Number of Persons
Raw yarn merchants	4
Weaving Companies	10
Wholesalers	12
Retailers	11
Fabric Cooperative	2
Total	39

In order to supplement the result of interviews, mail questionnaire was used for the remaining 121 weaving companies and the results were analyzed.

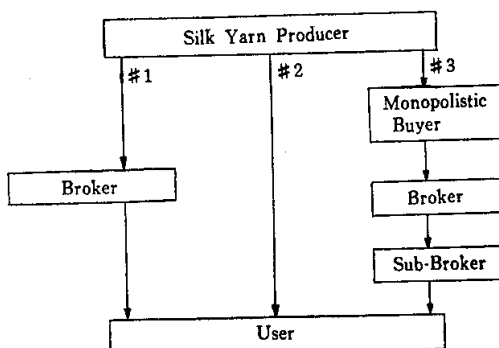
III. Raw Yarn Purchasing

The raw yarns for weaving silk fabrics which are defined for this study are silk, rayon, nylon, and chemical fiber. Although some differences were found in the channel and practice employed by fabric weaving companies for purchasing raw yarn, there were many elements in common.

1) Silk Yarn

Three channels of procurement which are employed by weavers for purchasing silk yarn are shown in Figure-1.

(Figure-1) Distribution Channel for Silk Yarn



The broker in Channel #1 has his office stationed in one place and his function is to find buyers of silk yarn for the seller. He receives ₩ 1,000 per

bale of sales commission from the seller when the sale is made. This means that the broker is functioning properly for the creation of possession utility and may not be considered as "non-productive". Since there are 177 silk fabric weaving companies and many more small scale users in the Kyongpook area, it would not be practical for a silk yarn producer to make direct contact with each of them.

For the production of the silk fabrics for export, Channel #2 is employed. When a weaver receives export L.C. from a foreign buyer, the raw yarn for the production of the export fabric may be purchased directly from silk yarn producers at export price by issuing local L.C.⁽⁶⁾ For the silk yarn producer, the amount of yarn sold to export weavers is recognized by the Korean government as silk yarn export and various privileges are granted. About 31% of the total volume of silk yarn consumed by weavers are purchased through Channel #2.

In many instances merchants with large amount of capital buy up almost all the yarn produced by a certain producer and resell it through brokers, as shown in Channel #3. The broker is usually connected with yarn users through a number of sub-brokers whose function is to find yarn sellers for buyers, whereas the function of the former broker is to find buyers for sellers. The sub-broker does not have a stationed office and he just shuttles around seller's brokers and users.

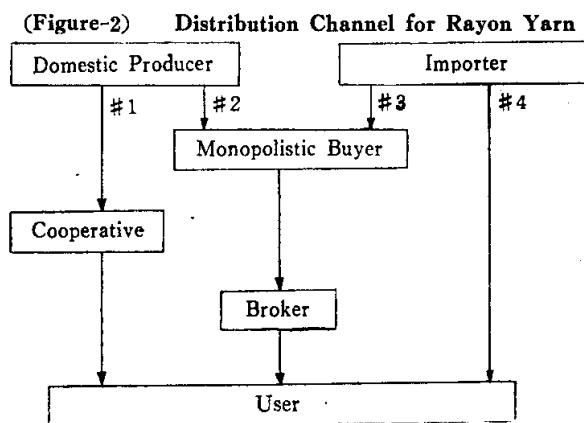
As it may be understood, Channel #3 is very round-about and the monopolistic buyer plays very influential role in the flow of silk yarn. Without performing any productive function, he just takes monopolistic title to the substantial volume (it is estimated to be about 50% of total production) of raw yarn, by taking advantage of the tight operating fund situation of the yarn producer. Frequent fluctuation in the price of raw yarn is said to be often caused by such monopolistic merchants.

2) Rayon

Rayon yarn is also distributed in a similar way to silk yarn, but the difference is that rayon yarn is supplied not only by domestic manufacturers but also

(6) The price of raw silk yarn distributed directly from a yarn producer is ₩ 185,000 per 10-kwan bale, whereas ordinary market price is ₩ 200,000. Ten kwans weigh approximately 82.67 lbs.

by importers, while silk yarn is supplied solely by domestic producers. Channels of its distribution are shown in Figure-2.

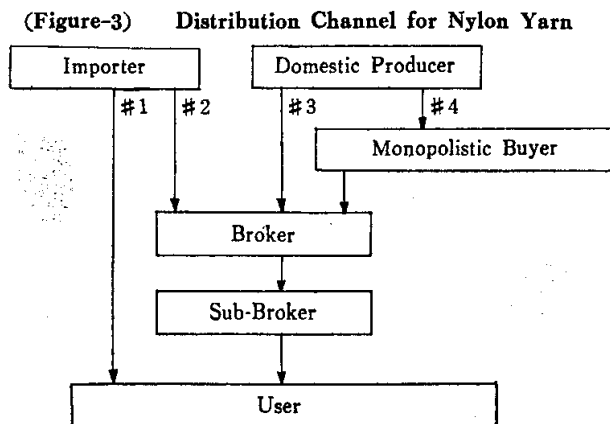


For the production of export fabrics, rayon is directly distributed, or rationed, to its users through the Textile Cooperative, as shown by Channel #1, or imported by the users directly or indirectly, as shown by Channel #4. And for the fabrics of domestic consumption, Channel #2 and Channel #3 are utilized generally.

In Channels #2 and #3, monopolistic merchants very often intervene as in the case of the channel for silk yarn, and they have substantial effect on the flow of rayon yarn.

3) Nylon

Besides numerous kinds of fabrics for domestic consumption, nylon yarn is used to produce export fabrics, such nylon taffeta, lace, raschel, tricot, etc, which consume considerable amount of nylon yarn. The typical distribution



channel is shown in Figure-3

For the production of export nylon fabrics, raw filament nylon yarn is permitted for import free of duty through Channel #1. Two of the interviewed weaving companies have foreign trade departments of their own, through which they trade with foreign countries directly. All the other firms import foreign-made yarn indirectly through trade companies. Sometimes, Korean trading companies receive export L.C. from foreign importers and sublet the weaving process to weaving companies. In such cases, weaving companies operate only as wage weavers. This was shown in Channel #1.

Channels #2, #3, and #4 are for the fabric for domestic use. Brokers in these channels operate for sellers to find buyers of yarn, and they have stationed offices. They are strictly commission merchants whose sales commission is ₩ 3 per pound of nylon transacted. As is the case of other yarns, these brokers are connected with weaving companies usually through a number of sub-brokers whose function, without having stationed offices, is to find sellers of yarn for weaving companies, the yarn users. Their sales commission is ₩ 1.50 per pound of nylon yarn and they receive it from main broker. This means that the sales commission of a main broker is halved when a sale is made through a sub-broker.

The monopolistic buyer again intervenes in the channel. Being a speculative merchant with large amount of capital, he often utilizes main brokers as his sales agent. He just takes title to the yarn and manipulates market by controlling the supply. Here again we can find a possible harmful element which may hamper smooth and effective flow of raw yarn.

By foregoing analysis, it becomes clear that a characteristic element which is common in all channels of raw yarn purchasing is the existence of the speculative monopolistic merchants. without having sales shops, neither warehouses, he simply takes advantage of the hard-pressed operating fund shortage of yarn producers and monopolistically takes title to practically all the yarn produced. He resells it when the market condition is in his favor, or he actively manipulates the market.

In order to eliminate the harmful element and to make the round-about marketing channel shorter, it is considered that more efforts on the part of the raw yarn producer are necessary to intensify their marketing activities, so that

they may be connected with the users of their products only through main brokers who are commission merchants.

IV. Product Planning

The characteristic feature of modern marketing is not in the selling efforts for produced goods, but in the efforts of planning saleable products. Therefore product planning, the essential part of which is to determine what kind of goods to produce, is the starting point and important foundation work for the smooth flow of produced goods.

The most important part of the product planning of silk fabrics is the determination of the structure and design of fabrics. About 90% of the weaving firms have full-time designers, but the basic idea of product planning is derived usually not from within company but from some outside sources. This means that the fabric weaving company, usually small in scale, lack in the effort to squeeze out creative ideas of their own.

The main source of idea for the design of the fabric for domestic consumption is the fabric wholesalers. In many cases, a fabric wholesaler shows sample piece of fabric to a weaving company and order its production. In such cases, the weaving company has nothing to do with design of the fabric, but just produces the designated fabric as ordered by the wholesaler.

The second source of the idea for the product design is the weaving company. However their ideas are usually not creative ones but are based on the informations of oversea travellers and samples of foreign-made fabrics. The designer of the company makes some modification to the foreign design, taking into consideration the specific tastes of domestic market, and confer with executives of his company.

Of these two sources of idea, opinions of fabric wholesalers play far more influential role. A weaving company has to rely of the wholesaler's information for the product planning, without making active efforts to lead the initial stage of marketing its product. When such practices continue for sometime, the whole process of marketing activities will be dominated not by the producer but by the wholesaler.

This fact may be one of the important reasons why merchants rather than producers play more influential role on the process of marketing fabrics in

Korea. In order for a producer to lead and direct the flow of his goods to consumers, he needs to put greater emphasis on his marketing activities from the beginning of planning and designing his products. That the whole process of marketing activities of goods be carried out according to the plan and under the direction of the producer of the product is considered as a vital factor for modernizing marketing system.

For designing the fabrics for export, the idea mostly comes from oversea importers. In other words, an oversea importer sends a weaver in Korea those sample pieces of fabrics which seem to have better chance of success. In rare cases, Korean weavers offer foreign importers sample pieces of fabrics which they designed, based on various foreign fabric designs they collected through Korean trading companies and other sources. Then the foreign importer makes whatever changes he thinks necessary and the modified design is sent to the Korean weaver for production. Since most of the fabrics are exported through trading companies, however, such direct contact with a foreign importer is not common. Rather than that, the Korean weaver usually sits and waits for a trading company to come with sample designs and he just produces the designated fabrics.

Such practices are caused by the fact that the silk fabric weaving firms, mostly small in scale, in Korea have very scarce knowledge of foreign custom and foreigner's favorite designs, and they do not have enough fund to collect informations directly through overseas marketing research organizations.

Here again we can find dominating force of merchants on the marketing process of silk fabrics, starting from its initial stage. For more active cultivation of overseas markets, the producer should not entirely rely on a trading company for the overseas market information but take more active measures to collect necessary informations directly. Since such practice seems impossible for small-size weaving companies, however, they may take collective action through their cooperative association to collect the overseas market information.

V. Marketing Channel

In 1963, a similar study was made on the marketing problem of the silk fabrics produced in the Kyongpook area. Between the studies conducted in 1963 and a significant difference in marketing channels employed by the weaving

company is that wholesalers occupy less proportion than sales agents or company owned retail stores in 1967.

(Table-3) Percentage of Marketing Channels Utilized by Fabric Weavers

Channel	1963	1967
Branch Office	3.2%	2.0%
Sales Agent	4.2	12.7
Wholesaler	83.2	71.3
Retailer	7.6	4.8
Own Retail Store	1.8	9.2
Total	100.0	100.0

Note: Source for the figure of 1963 is Dept. of Commerce, Chung-gu College; Present and Future of Textile Industry in the Kyongpook Area, 1963, p. 20.

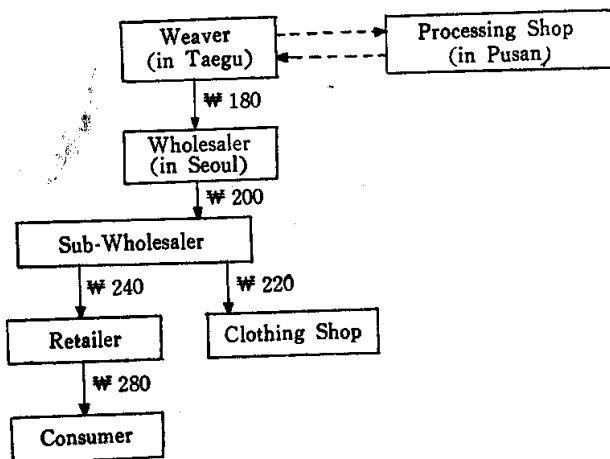
The goal of marketing channel policy is to increase sales by eliminating as much middlemen's margin as possible to the extent that the efficiency of marketing function would not be lessened. From the point of view of this argument, it seems that the tendency shown by Table-3 is desirable, because the table shows that producers tend to rely less on wholesalers for the sale of their products.

But according to what was revealed by personal interview, the word "sales agent" used by the fabric industry meant "the patronizing wholesaler who maintains steady relationship with a particular producer in dealing with his products". In other words, a wholesaler may or may not become a customer of a producer, depending upon the marketability of the products, but a sales agent accepts goods from a producer without any formal contract, disregarding the marketability of the product, because of long-established relation with the producer. However in either cases, once the product is transferred to a wholesaler or a sales agent, the producer has no influence thereafter on the marketing of his products. Therefore a wholesaler and a sales agent have virtually the same meaning.

Typical marketing channel of silk fabrics and each channel member's marketing margin are shown in Figure-4.

The chart shows that a weaving company sends its raw texture to a processing shop in Pusan for sizing and resin processing. When the processing is finished,

(Figure-4) Distribution Channel of Silk Fabrics(I)



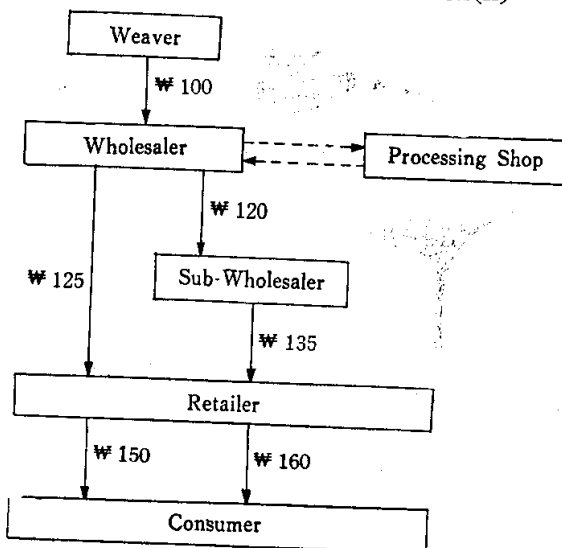
- Note: 1. This is a typical marketing channel for nylon tricot produced by A Company in Taegu, Kyongpook.
2. Numbers show the price of nylon tricot per yard.
3. Necessary processing is sizing and resin finishing and it is done by a processing shop located in Pusan, approximately 200 miles south of Taegu where the weaving plant is located. The processing charge is ₩15 per yard.
4. The wholesaler buys up all the fabrics produced by the weaver and ship it to Seoul, the largest market located 500 miles north of Taegu and where his main store is located.
5. Real lines show the movement of ownership.

the processed fabric is sent back to the weaving company in Taegu, and from here the fabric is transferred to a monopolistic wholesaler who has his main store in Seoul, the largest consuming market in Korea. This is the channel for a new design fabric. When a fabric is newly designed and seems to have good marketability, a monopolistic wholesaler buys up all the quantity from its producer before the production is completed. Therefore, if any wholesaler or retailer who wishes to buy that particular fabric, he has to rely upon the monopolistic wholesaler for its supply, not on the producer. This means that once the product is monopolized, the monopolistic wholesaler is capable of enjoying monopolistic profit by manipulating market. The additional profit thus gained obviously goes to the wholesaler, not to the producer nor consumers.

However, when a particular design begins to enjoy good market demand, imitated products follow very soon and the happy days of monopoly is over. Then the monopolistic wholesaler becomes just a regular wholesaler (sub-wholesaler in Figure-4) and the distribution channel becomes shorter.

Sometimes, raw texture is sold by a producer to a monopolistic wholesaler and the processing is done under the responsibility of the monopolistic wholesaler, as shown by Figure-5.

(Figure-5) Distribution Channel of Silk Fabrics(II)



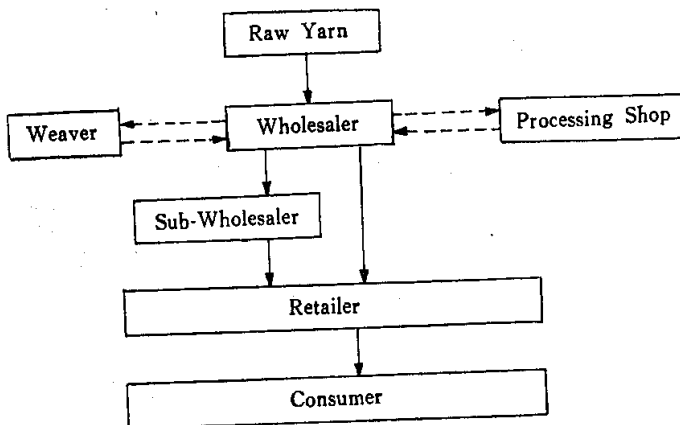
- Note: 1. This is a typical marketing channel for Nylon taffeta produced by B Co. in Taegu.
 2. Channel #1 is for local consumption, and Channel #2 is for distant consumption.
 3. Numbers shown are the price of nylon taffeta per yard.

Therefore in this case, the wholesaler has complete control of the leadership in marketing fabrics. This is due not only to the fact that the wholesalers in general have more capital than most of the weavers but also to the fact that the producers have no organized sales net work and they tend to place emphasis on production only.

When a further development is made along such line, more complete domination of marketing by a wholesaler is found frequently, as in the case of the marketing channel employed by S wholesaler, shown in Figure-6.

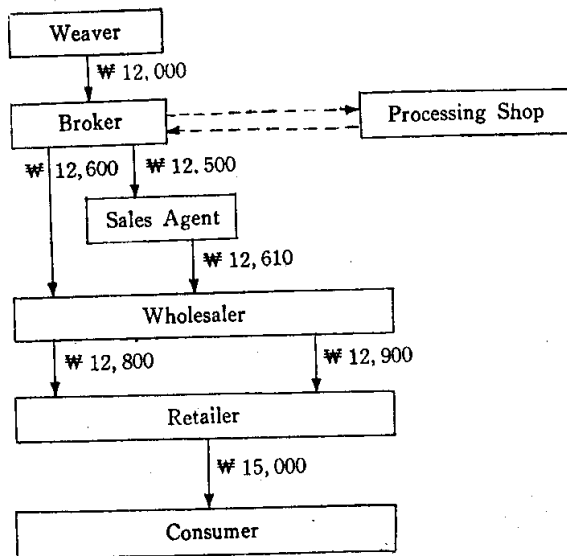
As shown in Figure-6, a wholesaler often purchases raw yarn and let a weaving company produce designated fabrics for him. When the weaving is completed, the wholesaler let a processing shop to do final finishing of the raw texture. Then the wholesaler markets his finished materials according to his marketing plan. Therefore, the wholesaler alone is responsible for the whole process, from production to marketing, and the producer falls into the position of just a hired weaver.

(Figure-6) Distribution Channel of Silk Fabrics(III)



A significant recent tendency is that producers often utilize brokers to find buyers for their production. The function of the broker is to find buyers for producers and receive sales commission in return (usually 1% of sales). The reasons for utilizing brokers, as stated by the interviewed producers are as

(Figure-7) Distribution Channel of Silk Fabrics(IV)



- Note: 1. This is a typical marketing channel of rayon double-figured satin produced by C Co. in Taegu.
 2. Brokerage is ₩ 100 per 40 yds.
 3. Numbers shown are prices of rayon double-figured satin per 40 yds.
 4. Processing charge is ₩ 410 per 40 yds.

following;

1. The broker takes responsibilities of collecting sales credit for the producer.
2. Since producers usually do not accurately know about the credit status of wholesalers and retailers, they would want to rely on the informations offered by the broker.
3. By utilizing brokers, producers, mostly small in scale, do not have to hire full-time salesmen.

Some companies make heavier utilization of brokers. They let a broker in charge of the processing of raw texture, and selling and collection of credit. In spite of the growing responsibility of brokers, they are not wholesalers because they receive a fixed rate of sales commission. Figure-7 is a typical distribution channel when brokers are utilized.

Brokers are utilized mainly for local market, but the tendency is that the role of well-informed brokers are becoming more and more important. This means that producers tend to rely on brokers for local market, and sometimes even for distant markets. Therefore producer's information on the market of their products become thinner. This is perhaps another important reason for a producer's not being able to take leadership in marketing their products.

VI. Marketing Costs and Profit Margin

Marketing costs include shipping cost, packing cost, various sales expenses and dealer's profit. Therefore, costs for dying, resin finishing, ironing, sizing and other processing are not included in the marketing costs.

To be accurate, every component element of marketing costs should be measured individually and the result should be added together to calculate total marketing costs. Because of limited fund and lack of available data, only dealers' gross margins are calculated to show a rough range of marketing cost of silk fabrics in Korea. The gross margin also varies widely, depending upon fluctuation of price and condition of monopoly. For the purpose of this study, therefore, only typical gross margin in the silk fabric industry is considered.

Let us consider the marketing cost of silk fabrics for domestic consumption. The middleman's gross profit in dealing raw yarn for domestic fabrics is typically shown in Table-4.

(Table-4) Marketing Margin of Raw Yarn

Yarn	Unit	Producer's	Monopolistic Buyer's		User's
		Price	Price	Profit Rate	Price
Silk	21 d. 10 kwan	₩195,000	₩200,000	2.5%	₩200,000
Cotton	23 s. 1 bale	50,000	51,000	2.4	51,000
Rayon	150 d. 1 bale	40,000	44,000	10.0	44,000
Nylon	70 d. 1 pound	540	550	2.3	550

Note: In the monopolistic buyer's profit, brokerage is included.

Here again, it is clear that the monopolistic buyer enjoys approximately 2.5% of sale profit without much contributing to the creation of any kind of utilities. The profit margin is 10% for rayon yarn which is caused by frequent change in price. These figures are average margins which mean that the monopolistic buyer's profit may become more than the figures in the Table-4 when he exercises his power to manipulate market. Therefore how to eliminate the monopolistic buyers in the distribution channel of raw yarn is one of the biggest problems to be solved for the betterment of the present marketing structure.

But the activities of the raw yarn broker seem to be necessary and their brokerage is considered to be reasonable, as shown by Table-5

(Table-5) Brokerage of the Raw Yarn Broker

Yarn	Unit	Brokerage	
		Amount	Rate
Silk	Bale	₩1,000	0.5%
Cotton	Bale	200	0.4
Rayon	Bale	100	0.25
Nylon	Pound	3	0.5

It is the practice of the yarn market that brokerage is not paid percentage-wise but in a fixed amount disregarding price fluctuation. But the fixed amount may be converted to percentage rate as shown in Table-5, by dividing the brokerage by the price of the yarn per unit.

The marketing gross margin for the fabric dealer is very difficult to be measured accurately, but typical margins as were revealed through the interview are shown in Table-6.

(Table-6) Marketing Margin of Fabric Dealers

Fabric	Prod- ucer's	Wholesaler's		Sub-Wholesaler's		Retailer's		Consumer's	Marketing
	Price	Price	Profit	Price	Profit	Price	Profit	Price	Cost
Tricot	₹190	₹200	5%	₹220	9%	₹250	12%	₹250	28%
Taffeta	110	120	9	135	11	160	16	160	31
Net Weave	46	49	9	53	8	60	12	60	23
Rayon Satin	310	325	5	350	7	400	13	400	18

Note: 1. Figures are prices per yard of fabric.

2. Rate of Marketing cost is meant to be the percentage of the total marketing costs to consumer's price, and is calculated by the following formula;

$$\left(\frac{\text{Consumer's price} - \text{Producer's price}}{\text{Consumer's Price}} \right) \times 100 = \text{Rate of Marketing Cost}$$

3. Profit rate for each stage of dealer is the rate to his selling price.

We can observe from Table-6 that, a wholesaler's profit is relatively higher than a retailer's profit which is usually 30 to 40% in industrialized countries. The retailer's low profit margin is partially compensated by the surplus in the volume of the product. It is an ordinary practice that when a weaver packs his fabric, he adds one yard more to the customary 40-yard packing. This surplus is a source of additional profit for the retailer.

The wholesaler's profit may be increased higher if we consider the possibility of manipulation of price through his strong position in the channel of fabric marketing. Often, fabric wholesalers are considered as a kind of speculative merchants.

(Table-7) Relative Prices of Selected Consumer Goods

Item	Producer's	Wholesaler's	Retailer's
	Price	Price	Price
Soy sauce	62	77	100
Socks	82	90	100
Rayon fabrics	70	90	100
Dress shirts	82	94	100
T shirts	69	92	100
Shoes	71	88	100
Laundry soap	82	87	100
Silverware	80	87	100
Sewing machine	73	94	100
Florescent lamp	75	91	100
Dry battery	63	74	100
Pencil	56	76	100

Note: The source; The Medium Industry Bank, Monthly Statistical Review, May 1967, p. 13.

As a reference to the reader, a similar study conducted by the Medium Industry Bank is shown in Table-7.

The sales commission for the broker whose role is to serve as salesman for a producer of fabrics is not so high, and is shown in Table-7

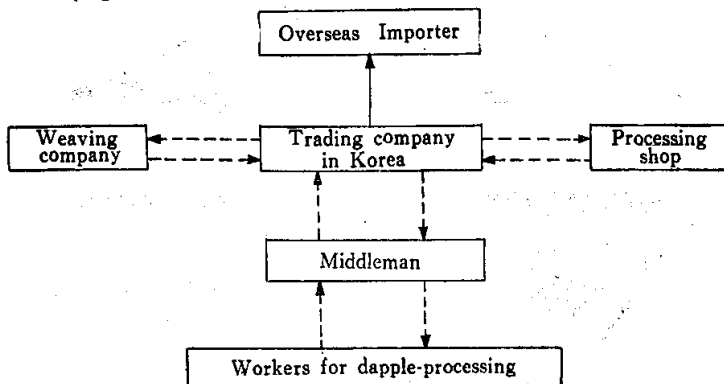
(Table-7) Brokerage of Fabric Brokers

Fabric	Brokerage
Tricot	1.0%
Nylon taffeta	0.5
Net weave	1.0
Rayon satin	0.8

For the production of fabrics for export, necessary raw yarn is permitted to be imported free of duty when export L.C. for the fabric is received. Then the raw yarn is woven into the designated fabric and necessary finishing is made for export. Therefore, marketing margin of export fabrics is different in its nature. In this study, dappled silk and nylon-tricot, which are very popular export items, are taken up for consideration.

The belt for Japanese women's kimono is made of silk fabric which requires a particular processing for dyeing, called dappling. The raw texture for dappling has been imported from Japan for bond-processing and the finished product re-exported to Japan. But a recent tendency is that the raw texture is woven and dappled in Korea and is exported to Japan to be used for Japanese women. When a trading company receives export L.C. for dapple processing, the work is carried out through the channel as shown by Figure-8.

(Figure-8) Export Channel of Dapple-Processed Fabrics



The exporter hires a weaving company for the fabrication of raw texture

and then send the raw texture to a processing shop for steaming. The steamed raw texture is then distributed, through a number of middlemen under the company, to individual workers for dapple-processing. Usually women labor in rural area is utilized for this purpose. Profit for the exporter is fairly stable. A typical cost and profit for the dapple-processing is shown in Table-8.

(Table-8) Export Profit of Dapple-Processed Fabric

Cost of raw silk yarn	₩2,564 per piece
Weaving cost	600
Steaming cost	100
Processing for dappling	1,000
Middleman's commission	10
Export cost(total of above costs)	4,274
Export price, FOB Pusan	5,304
Exporter's gross profit	₩1,030

- Note: 1. One piece is 10 m².
 2. Export price in US dollar is \$19.50.
 3. All figures are for one piece of the fabric.

Another popular export item is nylon tricot for which nylon yarn is allowed to be imported free of duty. Usually nylon yarn of 300 denier in size is imported and the yarn is divided into 20 denier yarn for weaving. Unlike the dapple-processed fabric, however, export of nylon tricot and many other nylon fabrics for export are made at a loss, as shown in Table-9.

(Table-9) Export Profit of Nylon Tricot

Cost of raw yarn	₩36.40 per yd.
Cost of dividing yarn	17.50
Weaving cost	40.00
Processing cost	11.00
Packing and other expenses	25.00
Export cost(sum of above costs)	129.90
Export price, FOB Pusan	114.24
Exporter's profit	₩15.66(loss)

- Note: 1. All figures are for a yard of the fabric.
 2. Free-of-duty import price of raw yarn is 71 ¢ per pound, and the export price of nylon tricot is 42 ¢ per yard. These prices are converted into Korean won at the rate of 272 won to one dollar.

Table-9 shows that for every yard of nylon tricot exported, the exporter, or the weaving company when it exports through its own foreign trade depart-

tment, has to bear a considerable amount of export loss, The excutive manager of a weaving company whom the writer interviewed said;

“As to the nylon fabrics for export, I would say it satisfactory if the export price barely meets the cost of production.”

A greater part of the export deficit is usually covered by the extra amount of nylon yarn which may be imported free-of-duty. In principle, raw nylon yarn may be imported only on the condition that the importer use all the yarn to weave nylon fabrics for export. But during the process of weaving, some loss of yarn is unavoidable. Usually the Korean government is quite generous in allowing the rate of weaving loss. Presently the Government recognizes 18% of weaving loss of nylon yarn for ordinary nylon fabrics, but actual loss-rate is considered to be far lower probably about 5%-and the extra yarn which was imported free-of-duty will add ₩ 356 per pound of nylon yarn to the exporter's profit, if the extra yarn can be traded at market price or can be used for the production of domestic nylon fabrics. The calculation is shown in Table-10.

(Table-10) Profit gained by Nylon Yarn Import

Free-of-duty import price	₩184 per pound
Domestic market price	₩550
Profit by trading	₩356

This illegal profit might be considered as a kind of unofficial compensation for the export deficit, but such an illegal practice contributes in no way to the improvement of operational efficiency of weaving firms.⁽⁷⁾

VII. Market Research and Sales Promotion

No systematic market research or sales promotional activities are conducted by any of the silk fabric weaving firms in the Kyongpook area. Since none of

(7) Their deficit is also partially covered by the legal support from the Korean government, which includes 10% deduction in commodity tax, 50% deduction in income tax, 100% deduction in corporate tax, and privileges in shipping and electricity charge. According the report made by the Korean Productivity Center in November 1967, the average export cost of 48 main export items was ₩ 286, 62 to earn \$1.00, or ₩ 272. And the average deficit which amounts to ₩ 14. 62 is covered by various compensation measures taken by the Government; such as financial support, raw material import, tax deduction, deduction in railroad charge and others, and the final profit is about 6% of the export price.

them employ full-time salesmen, information concerning the market of their products is provided by wholesalers. The wholesaler is the biggest source of information on the type of fabric design which seems to have good marketability, and on the trend of consumer's taste concerning fabric design. In addition to the information provided by wholesalers, information concerning foreign markets is collected through books, travellers and trade companies, and all these informations are considered for designing so called "hit design".⁽⁸⁾

When a design is determined, the weaving company determined the minimum volume of demand based on its wholesaler's advice. Since retailers usually wish to stock at least some of any kind of newly-designed fabric, the wholesaler may be able to roughly estimate, by taking into consideration the number of his customer-retailers, the minimum volume of demand for the specific design of fabric. Based on this estimate, the weaver determines the quantity of production.

When a new design is determined, it is kept in tight secret. The weaving company would not release the design for export trade shows or any kind of domestic trade shows. Only after all the planned production is completed, the fabric is released to the market, all the volume at once. If the product becomes a hit design and quickly becomes a popular fabric in the market, imitated designs usually appear in the market within two months. Therefore the time period in which a weaver or a wholesaler may enjoy his monopolistic position on a particular design of fabric is very short.

As to the problem of sales promotion, all the interviewed weavers believed that creation of a new "hit design" was the key for promoting sales. Without it, no sales promotion was thought to be effective.

No weaving companies of silk fabrics have ever advertised their products through any kind of mass media. They believe that advertisement forces considerable expenditure without contributing much to their sales.

That the weaving company's sole policy to increase sales is the change in the design of fabric is an important point to be considered. Because the silk fabric is non-branded good, favorable brand image or company image can not be established among consumers. The producer's promotional activities, therefore,

(8) The term "hit design" used in the fabric industry designates the design of fabric which is new and very popular in the market.

are directed only toward wholesalers, and they are forced to rely on wholesalers and retailers for the increase in ultimate consumption.

Dispatchment of market researchers to overseas to collect market information concerning fabrics is impossible for almost all the weaving companies in the Kyongpook area. The structure and design of export fabrics are usually designated by oversea importers and the weavers in Korea are only in a passive position. Since their products are exported through trading companies, a trading company also has strong influence on the design. Thus for design, market research, and sales promotion for export fabrics, weavers have to rely on overseas importers and Korean trading companies. The weavers just receive orders from trading companies and weave designated fabrics.

But as is the case with domestic marketing, export marketing also must be conducted under the leadership of the producers of the product. More effective export activities by the producers are necessary. In order to solve this problem, cooperative overseas market research may be carried out through the Korean textile Cooperative Association.

VIII. Collection of Credit

In general, three methods are used for collecting credits. Of the three methods, credit sales occupies larger part, as shown by Table-11.

(Table-11) Collection Methods used in the Sale of Fabrics

Collection Method	1 9 6 3	1 9 6 7
Cash	23.4%	15.4%
Bill or Check	41.8	67.2
Credit sale	34.8	17.4
Total	100.0	100.0

Note: 1. The data for 1963 are derived from "Present and Future of Taegu Textile Industry" Dept. of Commerce, Chung-gu College, 1963, p. 33.

2. Check is not considered as each because the word "check" usually denotes deferred check" and the period of deferment varies from several days to several months.

Table-11 shows that in 1963, cash sale was decreased while sales on deferred check or bill increased markedly. But pure credit sale without mortgage decreased. This means that although credit sale was increased, sellers prefer

deferred check or bill to pure credit sale in order to facilitate collection of credit.

In 1967, cash sale occupies about 15% of the total sales. When a wholesaler wishes to monopolize a newly designed fabric with good probable marketability, he pays the weaver in cash even before the production is completed. Therefore, we may say that the producer sold his product on very good term because the interest for the prepaid cash becomes additional revenue and expenses for collection is avoided. But then, the extra profit caused by the change in the price which usually is manipulated by the wholesaler after he monopolized all the quantity of the product adds nothing to the producer of the presold product but to the wholesaler who bought the product.

All the interviewed companies said that they allowed up to one month of deferment period for the deferred check they received, and they also allowed the duration of one month when they sold on pure credit. It is found that except for the "hit design" which is usually presold to a monopolistic wholesaler, sales of fabric products are usually made on one-month credit. If a customer pays in cash, he receives 5% deduction from the weaving company, the amount of which is market rate of interest on borrowed money. The five percent deduction system is recognized by almost all the weaving companies. Since deferred cash may also become bad check, weaving companies seem to be willing to give five percent deduction for the cash collected one month ahead.

A big problem with the credit sales is that the credits are often not collected even when the date matured. This was shown by the fact that in both surveys made in 1963 and 1967, the biggest problem in fabric marketing was "collection of credits". Many weavers complained that their wholesalers often delay payment for two or three months even if they had already collected payment from their retailers for the products. Since no interest may be collected for the delay in the payment, the wholesaler takes advantage of it and utilizes the collected money for other purposes for several months, making the weaver's financial situation more difficult, without having to pay interest for the fund so used.

IX. Brand

Strictly speaking, all silk fabrics produced in the Kyongpook area are marketed

as non-branded goods. Each 40-yard bundle merely carries a small piece of paper which shows the weaver's name. This paper is taken away for retailing. Some weavers insert their trade-mark papers on the surface of each 40-yd. bundle of fabrics which is packed into transparent bag. But consumers do not see the trade-mark paper because it is also taken away when the bundle is unpacked for retailing. As the producer's name can not be identified by consumers, their decision to buy and their evaluation of fabrics depend largely upon the sales talk of wholesalers and retailers. Therefore the relationship between the consumer and the producer is very remote whereas the merchants are closely related with the consumers. The fact that silk fabrics are non-branded is one of the important reasons for the middleman, especially wholesalers, having the biggest say in marketing of the silk fabrics.

In order for the producers to take control of marketing and promotional activities of their products, it seems necessary to have silk fabrics branded. Technically there may be several ways of attaching trade-mark or brand name on fabrics. One reasonable method might be to weave brand name on the both edges of fabric. If brand name is woven into the fabric on its both edges, consumers may be able to identify the producer even when the fabric is sold piecemeal.

The branded goods do not have to be of high quality, like most of the Korean silk fabric weavers believe. It will be sufficient to be a branded goods if the quality specified or implicitly understood by the brand name, can be maintained.

So the problem is whether the producer is willing to be responsible for the quality of his branded product. It is quite common practice in the silk fabric industry that initial quality is hard to be maintained because of price competition among producers and rising inflation which causes high production costs. Even if a producer wants to maintain the quality of his product, his wholesalers and retailers force him to reduce its quality to win in their very short-run selling competition. Therefore the weaver weaves his product with slightly thinner yarn so that when woven with designated weight of raw yarn, the length of the fabric would be longer than were the yarn with designated size is used. Usually consumers can not distinguish the slight difference quality and are just glad to buy at cheaper price. Therefore if a trade-mark or brand

name is attached or woven on fabrics, it may be utilized as the sign of untrustworthy producer in case a consumer finds out that the quality became poor.

In order for the weaving companies to succeed in branding policy in such environments, continued efforts seem necessary for a prolonged period of time. But once the product is branded, it will become an initial stage for the producer to regain leadership in the marketing of his products.

X. Conclusion

In the industrially advanced countries, goods are produced by giant monopolistic or oligopolistic enterprises or competitive firms who have much greater capital resources than most of the middlemen. Therefore the middlemen in these countries can not match against the producers because of relatively weak capital position, and naturally they are under the control of a producer in marketing the producer's goods. Thus all marketing activities are conducted under the direction of the producer and the middleman is a kind of commission merchant who receives a share for his creative service rendered to the distribution of goods.

But in the underdeveloped and developing countries, the merchant's capital is usually larger than most of the small-scale producers. This enables them to control the market, capital-wise at least. Numerous small manufacturers can not market their products without relying on the wholesalers who are small in number. In other words, a monopolistic relation exists between the two groups. When the wholesalers sell their merchandises at the market, they deal with a numerous retailers who have to rely for financial support on them. Thus a oligopolistic relation is established between them.⁽⁹⁾

This argument is at least partially confirmed by the result of this study. The purchasing channel of raw yarn is unnecessarily round-about because of the monopolistic buyer's intervention. The supply and price of yarn are largely influenced by their marketing policy. For the marketing of fabrics, a producer is forced to surrender his leadership to his wholesaler and he can not establish an effective marketing plan for his products.

There are at least three reasons for the wholesaler's domination of the whole

(9) Hee Bum Park; "Theory of Price in the Underdeveloped Countries", *The Seoul Kyungje Press*, April 19, 1967.

marketing process. The first reason is, as mentioned above, the existence of monopolistic relation between producers and wholesalers and oligopolistic relationship between wholesalers and retailers. The second reason is that the wholesalers' capital is larger than most of the small-scale producers, and the producers must rely on their wholesalers for partial financial support. These two reasons were also confirmed by a study conducted by the Medium Industry Bank of Korea.⁽¹⁰⁾

Another important reason is that all information concerning markets is collected through wholesalers because wholesalers are experts on the market while producers have scarce knowledge of the market of his products. The fact that silk fabrics are marketed as non-branded goods is another important reason for the wholesaler's domination of market. Because silk fabrics are non-branded, ultimate demand depends upon the promotional activities of wholesalers, and producers have to rely on them for the increase in the ultimate consumption.

The problem, therefore, is how to set up a marketing system under the control of the producers of the product so that whole process of marketing activities may carried out according to the plans established by the producer of the product to be marketed. If such producer-dominated marketing system is established, the unproductive and wasteful activities of the wholesalers will be eliminated, and the wholesalers will receive their shares for the productive service they render.

(10) "Distribution Structure Analysis of the Products of the Small Business", *The Medium Industry Bank, Monthly Statistical Review*, May 1967, pp. 5-16.