

January 2003

## Survivorship in International Chain Restaurant in Korea

Woo Gon Kim

*Oklahoma State University*, null@okstate.edu

Kye-Sung Chon

*The Hong Kong Polytechnic University*, null@polyu.edu.hk

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### Recommended Citation

Kim, Woo Gon and Chon, Kye-Sung (2003) "Survivorship in International Chain Restaurant in Korea," *Hospitality Review*: Vol. 21 : Iss. 1 , Article 3.

Available at: <https://digitalcommons.fiu.edu/hospitalityreview/vol21/iss1/3>

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# Survivorship in International Chain Restaurant in Korea

## **Abstract**

Several western chains have done well in Korea, while others have withdrawn from the market. The authors summarize the current operational results of western chain restaurants in Korea, report positive impacts of western foodservice firms, and analyze the key elements leading to their survival and non-survival. Some lessons could be used as tools to establish entrance strategies of western chain restaurants in Korea as well as in other Asian markets

## **Keywords**

Woo Kim, Food and Beverage

# Survivorship in international chain restaurants in Korea

by Woo Gon Kim  
and Kaye Chon

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The food service industry in Korea has grown considerably in size and changed significantly in composition over the last several decades. Within a decade the number of restaurants increased more than three times, compared to the figure of 154,000 units in 1988. Many of them are family-owned and are small commercial restaurants.

Food away from home (FAFH) expenditures per household in 1990 represented 21.6 percent of total food spending expenditures, while that figure

in Japan was approximately 25 percent in the same period. In the U.S., FAFH expenditures per household in 1996 were approximately 45 percent compared to 35 percent in Korea.<sup>1</sup>

## Western chains enter

It was not until the 1980s that Korean food service became a modern enterprise with strong management emphasis. In 1982 Burger King signed a franchise contract and started operations in Korea. In the following two to seven years, American chain restaurants such as Wendy's and Kentucky Fried Chicken (KFC), both in 1984, Pizza Hut in 1985, McDonald's in 1986, Denny's in 1987, Coco's in 1988, and Domino's Pizza in 1990 penetrated the Korean food service market.

In the 1990s, the Korean food service firms that made joint ventures or franchising agreements with western food service

firms shifted from their previous concentration on fast-food operations toward more diverse concepts such as family restaurants and dinner houses. Some of those restaurants are TGI Friday's that arrived in 1991, Ponderosa in 1992, Sizzler in 1993, Popeye's in 1994, Tony Roma's, Bennigan's, and Planet Hollywood in 1995, Chili's and Hard Rock Cafe in 1996, Outback Steakhouse in 1997, and Starbucks in 1999. By providing casual and friendly service and a nice atmosphere not usually found in Korea, western restaurants became the food service equivalent of Levi's Jeans or Coca-Cola.<sup>2</sup>

#### **Chains are varied**

There were also some successful chains that are non-western restaurants. Lotteria, a Japanese hamburger restaurant chain, was the first chain restaurant company introduced to Korea in 1979; its performance is ranked at the top of the fast-food segment in terms of the number of units and sales. Skylark, a successful family restaurant in Japan introduced in 1993, emphasized a lower-end market positioning strategy by maintaining a lower average check of US\$10. The average check of most western family restaurants in Korea ranged from US\$13 to US\$18. Marché, introduced in 1997 from Switzerland, became a strong competitor against the rapidly expanding American food service chains.

Table 1 summarizes the status of American food service chains operating in Korea at the end of 2000. Of the top 25 restaurant chains ranked by *Nation's Restaurant News* in terms of U.S. sales, only 10 were represented in Korea.<sup>3</sup> Baskin-Robbins had the largest number of units in Korea, but most were very small. In terms of the number of units, McDonald's with 244 units was the second largest U.S. chain in Korea, followed by KFC and Pizza Hut, with 206 and 199 units, respectively.

Within the segment of family and dinner house, Coco's with 29 units was the leading restaurant, followed by TGI Friday's and Bennigan's with 17 units and 10 units, respectively. In terms of sales volume, McDonald's was the number one chain with US\$206.4 million, followed by Pizza Hut and Kentucky Fried Chicken with US\$156.3 and US\$145.3 million, respectively. Among family and dinner house restaurants, TGI Friday's was the leading chain with US\$46.9 million, followed by Bennigan's and Coco's with US\$31.5 million and US\$23.4 million, respectively.

It is interesting to note that Coco's, which commands a relatively tiny market share in the U.S. restaurant industry and which falls behind TGI Friday's and Outback Steakhouse in terms of the number of units operating in the U.S. was ranked as one of the top 10

chains in Korea. In fact, Coco's, the first U.S. family restaurant to open in Korea in 1988, enjoyed the leadership position before other well-known, high-profile

U.S. chain restaurants penetrated the Korean food service industry. Sizzler, Ponderosa, and Chili's operated only a few units in Korea in 2000.

**Table 1**  
**U.S.-based food service chain**  
**restaurants in Korea in 2000**

Brand	Rank in number of units in Korea	Number of units in Korea	Korean sales volume (US \$Millions)	U.S. units rank	U.S. units number	U.S. sales rank	U.S. sales volume (US\$Mil)
McDonald's	2	244	\$206.4	2	12,629	1	\$19,006
Burger King	8	93	67.3	4	8,139	2	8,659
Hardee's	10	23	15.6	16	2,673	13	2,139
KFC	3	206	145.3	8	5,182	6	4,300
Popeye's	6	160	108.6	32	1,165	35	986.4
Pizza Hut	5	199	156.3	5	8,084	5	5,000
Domino's Pizza	7	149	39.1	11	4,629	9	2,560
Little Caesars Pizza	14	6	NA	12	3,850	26	1,200
Coco's	9	29	23.4	88	NA	NA	NA
Ponderosa	17	3	NA	56	465	58	560.2
Sizzler	15	4	6.3	76	253	90	315
Tony Roma's	15	4	9.0	85	157	100	297
Bennigan's	12	10	31.5	79	237	71	460.3
Chili's	18	2	NA	43	626	21	1,555
Pizzeria Uno Chicago	18	2	NA	86	155	94	308.4
Outback Steakhouse	13	8	11.7	47	574	18	1,729
TGI Friday's	11	17	46.9	58	452	24	1,334
Dunkin Donuts	4	200	19.5	13	3,650	15	2,007
Baskin-Robbins	1	460	29.7	18	2,438	57	573.3

Source of units and sales in Korea: Korean Restaurant Association, 2000

Source of U.S. units and sales data: Nation's Restaurant News, (June 26, 2000). The NRN data reported are for the top-100 food service chains only. Data for firms outside the top 100 are shown as "NA."

Managers of the three different segments of Korean restaurants, traditional Korean food, fast food, and family and dinner house, were selected for an interview. The 12 restaurants included one traditional Korean food restaurant, two hamburger fast food restaurants, two pizza restaurants, two chicken restaurants, and five family and dinner house restaurants. The majority were western chain restaurants.

### **Positive impact recognized**

Managers participating in the focus group interview recognized the following positive impacts of western food service firms on the Korean food service industry:

- **Enriching dining out:** The entrance of western restaurants enabled local diners to get new exposure to diverse choices in dining-out experiences, while encouraging local restaurant managers to benchmark from western restaurants. Many Korean restaurant managers recognized that they were not able to compete with their traditional management style. They thought that food taste and quality were the keys for success, but they underestimated other important factors such as atmosphere, interior design, service, cleanliness, etc. They eventually recognized that restaurants existed to cater not only to hungry people, but for social activity purposes as well.

- **Stimulating growth:** The average square footage of restaurants tended to increase. Many

mom-and-pop establishments found they could not compete effectively against a huge local restaurant, international chain, or domestic chain restaurant. Regardless of the rapid increase in the number of stand-alone restaurants, the proportion of restaurants whose owners directly participated in management decreased from 22.3 percent in 1982 to 12.9 percent in 1991.<sup>4</sup> This fact reflects that many small eating places had become large local restaurants affiliated with prominent local restaurant chains.

Some larger corporations entered the food service industry as a diversification strategy by becoming master franchisers of mostly western restaurant companies. The conglomerate's motivation to participate in the food service industry with multiple brands was the positive cash flow created by restaurant operations and real estate investments. Wealthy individuals, conglomerates, and institutions tend to invest in land to benefit from the appreciation of real estate, while they have to pay large amounts of tax for unused land. By building restaurants on the vacant land, landowners were able to take advantage of both the constant cash flow and significantly reduce their tax burdens.

The three typical firms participating in the food service industry were food-related companies, retail companies, and hotels. Food produc-

tion, manufacturing, and supplier firms already had some business relationships with the food service industry; therefore, it was relatively easy to establish new firms. Hotels had the expertise in operating upscale food and beverage outlets; it was therefore a natural strategy for them to expand by establishing free-standing restaurants outside the hotels.

- **Effective management:**

When western food service firms entered the Korean market, they were initially perceived as a threat to traditional Korean restaurant operators. Korean food service enterprises learned western ways of efficiently operating restaurants. Franchising played an important role in seeking replications of advanced management techniques and strategies. Management innovation became an important ingredient for successful restaurant operations even though Korean food service managers traditionally did not place much emphasis on it.

Included among the most successful local chain restaurants was Nolbu Korean traditional restaurant. Its history started with a small Korean restaurant selling boiled pork in 1987, and within two years it launched its first franchise operation. Currently Nolbu operates and franchises more than six different concept restaurants featuring traditional Korean cuisine. Menus consist of purely tradi-

tional Korean fare that is rooted in traditional home-style recipes.

Nolbu Korean restaurant's success is attributed to the application of western scientific management techniques into Korean traditional food operations. Its expansion in terms of the number of franchised units and sales has skyrocketed. Since Nolbu is not competing against many western chain restaurants, its market position among Korean restaurants is superior.

- **Manuals and technology:**

Traditional Korean food service operators were astonished by the introduction of manuals that clearly explained the overall operational processes.<sup>5</sup> Stimulated by international chain restaurants' sophisticated operating manuals, traditional Korean restaurants started developing their own. In addition, many Korean conglomerates entered the food service industry with franchise contracts with famous western restaurants because they considered food service as a profitable business. In order to survive the competition of famous western restaurants, many local restaurants developed their own brands and expanded with local franchising. Technological advances of western restaurants have led to sophisticated business controls and established franchise systems. In addition, well-organized manuals of employee training, food production, menu design and layout, and store opening were important lessons for local operators.

- **New market niche:** Since western food service chains introduced the take-out concept, the take-out business became more popular and a variety of foods were developed for take-out. Traditionally, Chinese restaurants used to be the provider of most popular take-out or delivery food in Korea, but fast-food restaurants serving pizza, chicken, and hamburgers expanded rapidly by offering take-out or delivery services. In addition, diverse local cuisines such as Kimbap, a kind of California roll, and a variety of noodle dishes were developed and served more often by take-out.

- **Reduced labor costs:** Traditionally small eating places were considered as one of the least popular places to work. The restaurant industry was often perceived as a gateway for unskilled workers; as a result, the employee turnover rate in the food service industry was known to be one of the highest. However, this trend was reversed when western food service operators started offering effective training programs, with trainees exposed to various functions related to the management of operations, sanitation, service, human resources, basic equipment maintenance and operations, restaurant cashing out, and record-keeping. The adoption of these ongoing employee training programs aided in reducing the high turnover rate. A dramatic increase in the percentage of part-time employees reduced labor

costs and improved the bottom line figure.

### **Survivor cases presented**

Despite the difficulty of identifying primary reasons of success, some key factors of survival of western and local chain restaurants could be identified by restaurant managers.

- **Localization of services:** TGIF translated more than 100 operating and training manuals into Korean to take full advantage of the expertise of the parent company. TGIF succeeded in localizing its service standards by adjusting to local customs and culture. For example, TGIF created a new ordering method, “kneel-down” service, rather than the traditional western stand-up ordering method. TGIF developed many local menu items to appeal to Korean guests. Kimchi rice pilaf, the Bulgogi set menu, and Bibimpap (a dish with rice and several vegetables) are the most popular items developed by TGIF in Korea and sold throughout TGIF outlets in other countries. The success of Marché, introduced from Switzerland, could be partly attributed to the effort of catering to local taste preferences. Marché has been very flexible in developing and changing its original recipe in order to improve guest satisfaction.

A success case as a local brand was Spaghettia, an Italian-style restaurant. Its primary reason for success was the trade secret of its recipes that changed



original Italian flavors with some major adaptations, including developing its thin sauce and serving larger portions of sauces to cater to local preferences. In addition, Spaghettia consistently used the best quality ingredients regardless of the relatively high food cost ratio.

BBQ Chicken, Inc. originated from a fast food concept that specializes in providing quick, convenient, varied chicken entrees such as fried, hot wing, barbecued, smoked, Cajun-style, nuggets, gold fingers, burgers, and side dishes. The BBQ name does not represent the traditional western-style barbeque restaurant theme, but more of a combination of several western style operations such as KFC, Popeye's, and others. BBQ achieved enormous growth since 1994 and became the leading Korean chain restaurant in the number of units offering fast food chicken items. Its success was mainly attributed to the development of its appealing spicy hot sauce which met the taste preferences of local guests, thereby attracting repeat customers.

• **Cost controls:** With the completion of a central kitchen in 1992, TGIF reduced food costs from 40 to 30 percent. Marketing activities such as sending birthday cards, using coupons, and issuing mileage and point cards were very successful. Nolbu Korean restaurant is a typical example of success by adopting an American management technique, which led to a

dramatic food cost reduction. Nolbu was able to reduce food costs from 30 percent to 20 percent by developing a database of recipes of Korean cuisines. Previously, local restaurateurs adopted best practices from the excellent western operational systems.

• **Product and service quality:**

*Mister Pizza*, a typical success story of a local chain with sales of US\$13 million in 2000, has built a good reputation based on its tasty pizza. By implementing an extensive research and development program to better serve the local taste, Mister Pizza succeeded in developing hand-toasted dough, which was less greasy and tasted fresher. The chain also introduced a new potato pizza menu that became a popular item, and was later imitated by Pizza Hut and other competitors.

All foods of Marché are selected and produced in front of guests so most employees have cooking skills as well as the ability to function as wait staff. The primary goal of Marché is to serve fresh food and to have a consistent supply of fresh food items. The atmosphere is very casual with old market style; a variety of people like the open atmosphere. Marché offers a wide variety of items including fresh salad and baked goods, as well as Japanese, Chinese, Korean, and other ethnic foods. Marché is well known for keeping the menu lifecycle as short as possible and taking advantage of a wide variety of menus as compared to other western family chains.

- **Finding good locations:**

Starbucks' success was attributed to its strategies in locations, capitalizing on locations with high traffic flow and easy access from mass transportation such as subway and bus, which appealed to younger customers. A similar strategy worked well for other chains.

The BBQ chain was known to be good at finding the right locations and utilizing a unique positioning strategy. BBQ opened many small units in residential areas and others were located close to educational institutes, while Kentucky Fried Chicken (KFC) opened spacious units in relatively established locations with a high volume of traffic. BBQ expanded very rapidly in terms of number of units, but the average size of the unit was very small compared to its major competitor, Kentucky Fried Chicken. In 2000 BBQ operated 1,320 units while Kentucky Fried Chicken had 206 units.

- **Effective investment strategy:** The success of Spaghettia was partly attributed to its relatively efficient investment strategy. In order to minimize costs, most units chose basement locations with savings of almost half the rental costs, while most other family chains were located on the first or second floor. Spaghettia offset its location disadvantages with massive marketing and promotion efforts.

#### **Non-survivor cases presented**

Managers identified some key factors for the failure of western restaurant chains.

- **High pricing strategy:**

Denny's concept adjustment efforts with a high pricing strategy conflicted with its original American concept. Many local guests had dined at U.S. outlets and their perception of reasonable prices did not match the high pricing strategy in Korea. Denny's price positioning in Korea was close to the range of other U.S. family and dinner house chains. Many clients preferred to go to other restaurants after their first visit to Denny's in Korea because its price-value relationship was much lower than what they expected.<sup>6</sup>

- **Poor management:** Wait staff's service and cooking skills in the production area were not up to par partly due to lack of a consistent employee training program by Denny's. Employee morale was quite low due to ineffective compensation and a promotion policy that was based on seniority. The capabilities of management staff were not sufficient enough to compete against other major U.S. chain restaurants in Korea.<sup>7</sup>

- **Poor marketing strategy:** Denny's marketing effort was not creative and often imitated other competitors. The special events Denny's prepared were not popular due to lack of creativity. Failure of its promotional effort was partially due to the lack of harmony between employees in the marketing department and each outlet's guest contact employees.

- **Poor location:** When Planet Hollywood was first introduced in Korea, it had the mass media spotlight even before

opening with large crowds gathering for the ceremony. An inappropriate location without a subway line and with heavy traffic congestion was key in the failure of Planet Hollywood. This was a good example for U.S.-based chains to learn from since it withdrew from business within seven months. Many guests visiting Planet Hollywood complained about insufficient parking spaces which inconvenienced guests and prevented many from becoming repeat customers.

- **Lack of thorough feasibility study:** Excessive capital expenditures without a thorough feasibility study implied the foreseeable failure of Planet Hollywood in Korea. Its initial investment was approximately US\$7 to 8 million. In order to attain break-even sales, daily revenue should have been at least US\$50,000 or the equivalent to 10 turnovers. Extremely heavy initial opening costs and normal operating costs caused the high break-even point.

- **Failure of cost control:** Planet Hollywood management failed to control labor costs at the outset. The restaurant opened with approximately 300 full-time employees, and labor productivity declined as customer counts decreased. It failed because of inadequate cost controls and lower-than-expected sales.

- **Failure to adjust to local taste:** Cooks in the production area failed to adjust to local tastes because most food recipes were benchmarked from the Planet

Hollywood in Hong Kong. Korean customers have very different food tastes from those of Hong Kong even though they are located in the same Pacific Rim area. Most foods were too salty and contained too much oil for local taste preferences, but management did not catch the problem in a timely manner.

### **Competition exists**

The Korean food service industry showed dramatic growth over the last several decades. Up to 1996 all segments of the food service industry grew because of the significant increase of food-away-from-home expenditures, increased incomes, and people's increased interest in food. In the 1980s western fast food chains were forerunners in launching brands in Korea, and in the 1990s many western family steakhouse and dinner house restaurant chains entered the market. Western restaurant chains provided clean facilities, quality services, great atmospheres, and systematic management that was astonishing to local customers who had never experienced them before. Beginning in 1998 the Korean economy went through an economic recession and the food service industry faced stiff competition. Some segments still show strong growth, but some exhibit a decline.

Even though the overall food service market is more competitive than ever before, there is still enough room for new chains to introduce concepts. Since most

western restaurants were fast food or dinner house chains, new concept restaurants such as theme restaurants are expected to have great appeal if introduced. Many other top American chains such as Applebee's, Olive Garden, Red Lobster, and International House of Pancake (IHOP) have not yet been introduced. The reason may be that some of those chains still have ample growth opportunities in the United States, giving them little motivation to expand into Korea. In addition, since they are very successful chains, their royalty fee structure may be too high for local partners. However, American chain restaurants may still have more expansion opportunities in Asia. Coco's and Tony Roma's found new life in Asia when the brand's popularity began to decline in the United States.

A number of premier U.S. chains keep dominating market share, while others are not market leaders; some chains have withdrawn from the market entirely. The key elements of survivors were localization of services and operations, effective management leading to cost control, product and service quality, good locations, and an effective investment strategy. The key elements of non-survivors were inappropriate concept modifi-

cation with a high pricing strategy, poor management and lack of consistent employee training, poor marketing strategy, poor location, lack of thorough feasibility study, failure of cost control, and failure to adjust local taste.

Understanding the key non-survival elements could help western food service firms reduce their chances of business failure during their expansion movement in Korea as well as in other Asian markets. Even in the same Pacific Rim regions, for example, some chains succeeded in Hong Kong and Singapore, but could not succeed in Japan and Korea. It is important for western restaurant chains to do a more in-depth analysis of each country, even within the same geographic regions. A more comprehensive understanding of unique cultures, food habits, and local tastes of each country will be helpful for western chains to successfully expand into Asia. Another important factor for Korea and other Asian markets is the extent to which newcomers can or should modify original concepts and recipes to meet local needs and tastes.<sup>8</sup> Reviewing more accurate and comprehensive success and failure cases could be invaluable resources for those restaurant firms planning to expand into foreign countries.

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**Woo Gon Kim** is an assistant professor in the School of Hotel and Restaurant Administration at Oklahoma State University, Stillwater, and **Kaye Chon** is chair, professor, and head of the School of Hotel and Tourism Management at the Hong Kong Polytechnic University, Hung Hom, Kowloon Hong Kong.