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# HITEJINRO
# SUSTAINING SUCCESS IN THE KOREAN BEER MARKET

**HEHJIN LEE [1] & SEUNGHO CHO[2]**

[1] *English Literature / Ewha Woman's University, Seoul, South Korea*

[2] *Business Administration/ Ewha Woman's University, Seoul, South Korea*

***ABSTRACT***

***Hite Brewery was founded in 1933 and became the first beer company in Korea. It managed to achieve its success with 'Hite' beer, and became the top beer company in 1996(HiteJinro, 2010). Hite beer was so successful that the company, which was formerly named "Chosun Brewery", changed its name to "Hite Brewery" in 1998(Hite Jinro, 2015). HiteJinro's main strategic issue is whether it should focus on the imported beer market through licensing and direct import, or focus on recovering the domestic beer market. This issue is crucial to HiteJinro as the decision would have long term impacts; its domestic beer market will shrink if they focus on imported beer, but it will also lose revenue from the rapidly growing imported beer market if it focuses on domestic beer***

***KEYWORDS: Strategic Issue, Long Term Impacts, Imported Beer***

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## INTRODUCTION

### History of HiteJinro

HiteJinro, now one of top liquor companies in South Korea, was the result of a merger between Hite Brewery and Jinro in 2005(HiteJinro, 2015). HiteJinro was established in 1924 and started its business with soju. Jinro achieved its success as the top soju company in 1970, winning against its rival, SamHak. In 1998, Jinro launched "Chamisul", and this immediately became popular for its clean taste, with 14 billion bottles sold by 2008 (HiteJinro, 2010).

Hite Brewery was founded in 1933 and became the first beer company in Korea. It managed to achieve its success with 'Hite' beer, and became the top beer company in 1996(HiteJinro, 2010). Hite beer was so successful that the company, which was formerly named "Chosun Brewery", changed its name to "Hite Brewery" in 1998(Hite Jinro, 2015).

In 2005, Hite Brewery acquired the insolvent Jinro Company, resulting in the merger to form HiteJinro. The company is now a global company and is exporting its products to more than 50 countries. Currently, HiteJinro has several divisions in the alcohol industry. Other than beer and soju, HiteJinro also sells whiskey, wine and Korean rice wine. This term paper will only focus on HiteJinro's beer division.

## HITEJINRO'S BEER PRODUCTS

### Domestic Beer

HiteJinro's most popular brand of beer, 'Hite' became successful for its smooth and fresh taste, capturing over 50% of the market share for beer in 1999(HiteJinro,2010). 'Hite' was brewed from barley malt and rice using a range of brewing methods. An ice point filtration system was used for the entire process from fermentation to filtration (HiteJinro America, 2015), thus allowing Hite to be branded as Korea's first non-heat treatment beer. After the success of Hite beer, HiteJinro wanted to launch differentiated beers to capture more market share. It launched 'Prime Max' in 2006 and 'Dry Finish D' in 2010.

### Imported Beer

Aside from selling domestically manufactured beers, HiteJinro also imports foreign beer brands to provide more variety of beer to consumers. Among the brands HiteJinro imports, "Kirin" has the most sales (Yoon, 2015) and recently, "Kronenbourg 1664" sales have been increasing (Park, 2015). There are two ways that Korean companies can sell imported beer: direct import and licensing. Currently, HiteJinro imports beers directly from foreign countries. Some modifications could be made to the beers to suit the local conditions, but these modifications would be done within the foreign countries. Even though HiteJinro is not licensing beer now, it could explore this option in the future. Licensing is a contract permitting the licensee to use the intellectual property of the licensor and the licensee would need to pay royalties to the licensor. The licensee could then modify the foreign product and produce it in its own country. There could also be strict rules in place for the licensee to follow; otherwise, its license could be stripped off by the licensor.

## EXTERNAL ANALYSIS OF HITEJINRO

### Porter's Five Forces Model

### Threat of New Entrants

The threat of new entrants of South Korea beer industry is high. There would be new imported beer tax policies introduced in the coming years. In the past, the imported beer producers faced a cost disadvantage from the import tariff that was set by the government. For example, American beer has a 12.8% import tariff when it is exported to South Korea (Oh, 2015). However, new international agreements signed by Korea and other countries helped to reduce the barriers of entry into the Korean market. In 2012, Korea and United States signed the 'United States-Korea Free Trade Agreement (KORUS FTA)', which stated that American beers can be exported to Korea duty-free in January 2018 (Oh, 2015). The existing 30% import tariff on European Union countries' beer will also be phased out in July 2018 under the "Korea-EU Free Trade Agreement" which was signed in 2011 ("S. Korea-EU FTA to come into full force Sunday", 2015) . These government policies can thus lower the entry barrier for new imported beer brewing companies and encourage potential competitors who want to enter the Korean beer industry.

### Bargaining Power of Buyers

The bargaining power of buyers is high. The bargaining power is formed by three components: wholesalers, retailers and individual consumers. Since the beer industry is huge in South Korea and the demand for beer is high from the general public, there are wholesalers to distribute beer to middle and small-sized retailers and consumers. The wholesalers have more bargaining power than retailers and individual consumers because they can affect the market share significantly through bulk purchase. The wholesalers can also influence the sales of beer though their own promotion campaigns and price discounts to their consumers. For the retailers and individual consumers, they face few switching cost. For one pint of beer in South Korea, it costs around US$ 3.39 (Numbeo, 2015). The price difference between different brands of beers is small, so retailers and individual consumers can easily switch their choices of beer if they want to. Furthermore, beers do not require specific huge-invested machines, knowledge and human resources to store and drink. With the influence of wholesalers in the industry and the low switching cost for retailers and individual consumers, it can be concluded that the bargaining power of buyers is high.

**Bargaining Power of Suppliers**

The bargaining power of supplier is moderate. A famous general manager of a beer brewery company said that the cost and availability of raw materials are major concerns for the beer brewery industry overall (Briggs et al, 1981). For example, raw materials such as barley, sugar, water, malt, rice, hops, corn, grains and other ingredients are all the important inputs to the beer industry. The slight change in raw material's quality and species may result in a huge difference in taste. Therefore, Korean beer industry's companies could rely heavily on the suppliers and this enhances the suppliers' bargaining power. For instance, in 2011, Oriental Brewery was forced to increase its beer's selling price by double digits due to the rising costs of specific raw materials (Aldred et al., 2014). The beer brewery company had to accept the rise in costs of raw materials as it would not be able to find alternatives within a short period of time. However, globalized raw materials network helped to reduce the bargaining power of suppliers to an extent. For the Korean beer industry, most of the industry players are doing global procurement which means purchasing ingredients from all over the world. For example, they are purchasing malt from Australia, Canada and Spain, and purchasing hop from United States, Germany, New Zealand and England. Global procurement allows companies to find suppliers who provide similar type of raw materials more conveniently. This industry practice prevents the few Asian and local Korean suppliers from dominating the raw material industry. The bargaining power of suppliers could be concluded as moderate as companies would still find some difficulties in sourcing for their respective suitable suppliers.

**Threat of Substitutes**

The threat of substitute products is high, mainly due to the large variety of alcohol beverage products in the Korean market. This limited the potential returns of Korean beer companies by placing a ceiling on the prices of beer that the companies can potentially charge. In 2013, soju, beer's main substitute in Korea, has around 30% of the alcohol beverage market sales (25% in terms of volume), (Oh, 2015). Soju's market sales and volume sales are behind beers in the local market (Figure 1 & 2). Individual consumers can freely choose between these two alcohol beverage products as the switching cost is nearly zero and the cost of buying beer and soju are affordable from the public's point of view. At the same time, distilled spirits, rice wine and fruit wine are other substitutes for beer in South Korea. These alcohol beverage products can also satisfy the needs of alcohol drinkers and be commonly found in the market. From both figures, these products make up a quarter of the total market sales. Therefore, although the market share of beer in Korean alcohol beverage market is the highest, it could still be substituted by other alcohol beverage products.

**Intensity of Rivalry**

The rivalry among existing firms is extremely high. The competitive force mainly comes from two factors:

slow industry growth and numerous existing competitors. From 2008 to 2013, the growth rate of beer delivery and personal consumption remain between 3.5% to -4% (Figure 3). The small increase in industry growth every year induces existing companies to compete intensely for market share. The slow growth rate limits breakthroughs in the industry and traps the competitors in the red ocean. Intense rivalry in the beer industry becomes avoidable.

Moreover, domestic Korean beer industry is an oligopoly industry (Figure 4). Korean domestic beer industry is driven by two giant local breweries, Oriental Brewery Company Co., Ltd and HiteJinro Co., Ltd over a long period of time. Oriental Brewery has around 60% of local beer market share from 2013 to 2015 while the rest is taken by HiteJinro. Furthermore, a new industry player, Lotte Group, entered the industry by launching 'Kloud' in 2014. The industry believes that 'Kloud' will achieve around 3% of market share in late 2015. An insignificant amount of market share shared by microbreweries.

## EXISTING COMPETITORS OF HITEJINRO

### Oriental Brewery (Ob)

It is the largest local brewery company in South Korea, with production scale being 930 million litters in 2013(Oh, 2015). OB owns some famous beer brands in Korea: Cass, OB and Cafri. From 2011, it dominated more than half of the domestic beer market. In 2014, OB was acquired by Anhueser-Busch InBev. Therefore, OB has licenses to sell some foreign beers such as Hoegaarden and Budweiser in Korea (Flanders Investment and Trade, 2014) and at the same time, it also imports beer directly from Anhueser-Busch InBev to Korean local market.

### Lotte Group

Lotte group is a corporate group in South Korea that owns departmental stores, restaurants, convenience stores, hotels and even theme parks. In 2014, Lotte started selling 'Kloud' with a production capacity of 50 million litres per year (Flanders Investment and Trade, 2014). The group announced that when 'Kloud' is successful in the market, they will further invest USD $545 million to future expand the production scale (Jung, 2015). Moreover, Lotte directly imports Asahi, the bestselling imported beer in South Korea since 2010 (Figure 5), to South Korea.

## IMPORTED BEER MARKET

In South Korea, domestic Korean beer accounted for 91.8% of total beer sales in 2013 while imported beer accounted for the rest. Imported beer in Korea is booming at a rapid growth rate due to consumers' high demand for products of different tastes and high quality. Imported beer mainly comes from Japan, Germany, Netherland, Ireland, China, and United States (countries are listed according to the market share of imported beer in South Korea) (Oh, 2015). Korea's beer imports increased around 180% between 2010 and 2014 (Figure 6). In 2014, imported beer reached the highest amount of USD$ 111.7 million, which increased around 25% when compared to last year. For the total imported volume, it also reached the highest amount of 119.5 million liters with around 25% increase (Figure 7). Based on these statistics, it can be forecasted that the imported beer market can maintain a rapid growth rate in the coming years.

Apart from the two 'nearly equaled in size and resources' competitors who dominated the market, the steady growth of microbreweries and the booming of imported beer added to the intense competitive environment, where existing competitors are competing with each other in this zero-sum competition to sustain and increase their influence in the industry.

## GENERAL ENVIRONMENT: SOCIO-CULTURAL

Consumer trend is shifting from local beer to imported beer nowadays. According to a managing director in San Miguel Korea (Arirang news, 2015), "Tastes have broadened too as more people travel and study abroad so they become fond of the beers they tried overseas". This means that people are more willing to try foreign beers rather than limiting their choices in the Korean market. People also tend to like imported and foreign beers because of taste difference. For Korean local beer, the products skimp on using barley malt to brew. However, they will use rice and corn to replace the use of barley malt in the brewing process ("Fiery food, boring beer", 2012). As a result, Korean domestic beer's tastes much lighter when compared to the traditional beer. According to 'The Economist' in 2012 ("Fiery food, boring beer", 2012), Korean beer was named as "boring beer" because it is tasteless, which resulted in less usage of barley malt. Therefore, by following the new trend, people are willing to seek for heavier taste in imported beer rather than the local beer, which increases the demand for imported beer.

## INTERNAL ANALYSIS OF HITEJINRO

### VALUE CHAIN ANALYSIS

The processes that give HiteJinro its competitive advantages could be understood from the analysis of the value chain.

**Primary Activities**

**Inbound Logistics**

Inbound logistics include activities related to purchasing, storing and managing inputs to the product. The main raw materials of beer are malt, hop, yeast and water. HiteJinro usually obtains these ingredients from clean countries that produce a large quantity of beers. Malt is mostly from Australia, Canada or Spain, and hop is from the United States, Germany or New Zealand (Hitejinro, 2015). Above all things, they have put a great emphasis on water. Water makes up more than 90% in beer and thus plays a significant role in making beer. Indeed, "Hite" had started to show an upturn in 1990s since HiteJinro had emphasized on 'clean water'. It was possible because the main competitor, OB, had a serious problem due to the 'phenol incident', which was the inclusion of phenol in the water of OB products at that time (Choi, 2009). Since then, Hite has continuously focused the most on using clean water in its beers.

**Operations**

Operations are related to all processes of manufacturing which transform ingredients into the final product. Most of beer products are produced through the process of mashing, lautering, boiling, fermenting, conditioning, filtering and filling ("How beer is made: the brewing process", 2015). For these processes, HiteJinro considers adjusting suitable technologies for each product as an important issue. For "Hite" product lines, it uses ice point filtration and air blocking system. "Ice point filtration" is a method that keeps temperatures below zero in all processes. This method makes it possible to eliminate impurities and make the taste fresher. "Air blocking system" is a technology which minimizes the air contact to keep the beer fresher (HiteJinro, 2015). For the "Dry D" line, HiteJinro set up a cooperative system to release a new product with Danbrew Alectia in Denmark, one of top beer laboratories in the world (Lee, 2010). They developed 105 quality processes, conducted consumer taste tests for more than two years, and invested five years with huge amounts of cost. In addition to these, HiteJinro has other various technology systems such as FTK (Fresh Taste Keeping) system. Hite Jinro has tried to develop distinct systems to differentiate their products from other competitors in the operations part.

**Outbound Logistics**

Outbound logistics means distributing to the sales point and includes activities such as management of warehouses and delivery of finished goods. Usually in Korea, beer is distributed from manufacturers such as Hite Jinro, OB or Lotte to wholesalers, then from wholesalers to retailers such as supermarkets, convenience stores or restaurants and then finally to consumers (Figure 8).

As most companies have similar distribution channels, SCM (supply chain management) is much more important to beer manufacturers to differentiate themselves from others. HiteJinro has tried to create a real-time system that can provide faster updates on its inventories. Unlike other companies, HiteJinro also manages its distribution system through ‘fresh 365 campaign’ (Lee, 2010). This system exchanges products that have passed the period for good quality. It was implemented since 2006 and it was the first trial in Korean beer industry.

**Marketing and Sales**

In the Korean beer industry, it is important to give specific brand identity to products because most consumers do not recognize the exact difference between various products. From 1990s, the “Hite” line emphasized ‘the purest water’ image, while OB had suffered from the ingredient problem. However, this image of clean water does not attract consumers anymore. Since 2012, HiteJinro has also used a famous actor, Hyun Bin, as the main model of “Hite”. Nevertheless, major consumers from 20s to 30s are still not aware of the distinct identity of “Hite”, “Max” or “Dry D”.

In addition, sales are also significant, especially in processes connecting from retailers to consumers as many retailers are affected by salespeople. However, HiteJinro does not have an effective system to train and reward their salespeople compared to OB. Besides, HiteJinro had labor problems including salespeople for a few years. HiteJinro is also aware of this problem and has tried to reorganize their sales groups after their market share rapidly decreased in 2011 (Lee, 2014). These marketing and sales problems mean that even if HiteJinro has products in a good quality, they cannot sell their products effectively.

**Supporting Activities**

**Technology Development**

HiteJinro has endeavoured to develop R&D to make better tasting beers, using systems such as “Q-UP”, “Fresh Taste Keeping” and air blocking system. More significantly, HiteJinro has used “Q-UP” to manage most primary activities consistently, from choosing ingredients to delivering to stores and consumers. Not satisfied with only internal development of their systems, HiteJinro has also collaborated with international partners, such as Danbrew Alectia. Based on these relationships, HiteJinro has made international alliances with renowned beer companies, and made a ‘WBA (World Beer Alliance)’ in 2014. WBA includes major beer making and consulting companies such as Hanse Beverage, Weihenstephan and VLB Berlin in Germany (Shin, 2014).

## STRATEGIC ISSUE

HiteJinro's main strategic issue is whether it should focus on the imported beer market through licensing and direct import, or focus on recovering the domestic beer market. This issue is crucial to HiteJinro as the decision would have long term impacts; its domestic beer market will shrink if they focus on imported beer, but it will also lose revenue from the rapidly growing imported beer market if it focuses on domestic beer. As mentioned earlier, HiteJinro currently only imports through direct import, while other domestic competitors use both licensing and direct import. The most popular brand of HiteJinro is "Kirin Ichiban" while others only have a small market share.

In order to decide which market to focus on, it is important to understand HiteJinro's position in both markets. HiteJinro currently has a low market share for both domestic and imported beer brands. In the domestic market, the gap between OB and HiteJinro is decreasing and HiteJinro has recently increased their revenue in 2015 due to its aggressive marketing which led to the increase of sales for "Max" and "Crown". This shows that there is a place for improvement in the domestic beer market.

On the other hand, the imported market is growing rapidly since 2011 and it is predicted to grow faster due to the cancellation of import tariff, which lowers the entry barrier. However, HiteJinro currently lacks competitive advantage compared to its competitors because its imported beers are not in the top preferred brands. There are also other factors to consider regarding importing beer brands such as the threat of becoming future competitors which would cause cannibalism in the domestic market. Considering the current environment, which market is the best choice for the future of HiteJinro?

## SOLUTIONS AND RECOMMENDATION

According to the analysis, it is better for HiteJinro to diversify its imported beer brands due to the booming imported beer market and changing customer preferences. However, at the same time, HiteJinro has to strengthen its domestic beer brands with competitive advantages. Although the imported beer market has been growing, HiteJinro has to continuously focus on domestic beer since its main revenue stream is from domestic beer products (Figure 9). Imported beer could also be a future competitor of domestic beer. This means that focusing on imported beer could have both risks and benefits simultaneously. Therefore, considering this situation, our team has come up with a two-part solution: diversification of imported beer brands in the short-term and strengthening the domestic beer brands in the long-term.

### Short-Term: Diversification of Imported Beer Brands

In the short-term, HiteJinro needs to decide which importing way is suitable for it to diversify its imported beer brands. Since HiteJinro has five brands of imported beer which are not included in the top 10 list, it has to have more contracts with other imported beer brands which could potentially be popular in the Korean market. Compared to OB and Lotte, which have some of CVS best-selling brands "Budweiser" and "Asahi" (Kim, 2013), HiteJinro's main imported beers are "Kirin Ichiban" and "Kronenbourg 1664".

### Analysis of Licensing and Direct Import

There are advantages and risks of licensing. For example, "Budweiser" and "Hoegaarden" are licensed by OB. OB made these products in its Gwangju factory, which helps OB to have imported beer at lower costs as it is cheaper to produce the beers domestically with reduced tariffs and delivery costs. It can then get higher profit margins as the selling price would be the same as directly imported beer. In addition, knowledge transfer can occur as OB would know the whole process of “Hoegaarden” and “Budweiser” production.

However, customers believe that the imported beers made in Korea do not taste the same as the original ones, so they avoid buying them. For example, “Hoegaarden” is called “Ogaarden” (Segyeilbo, 2013), which is the sarcastic name combining OB and “Hoegaarden”. Another risk is that to get a license, sophisticated technology is needed and the process could get more complicated due to annual factory tests and qualification tests by the licensor. The main reason why OB could get the licenses was due to AB InBev acquiring OB in 2014. Compared to licensing, directly importing could be an easier way and could be used in fast diversification. However, the company would not be able to avoid the cost of tariff (Table 1). There would also be increased delivery costs.

***Table 1: Tax Formula of Imported Beer***

| |
|---|
| Tariff 30% + Liquor Tax 72% + Education Tax(Liquor Tax x 30%) + Additional Tax 10% |

***Table 2: Advantages and Risks of Licensing and Direct Import***

| | **Advantages** | **Risks** |
|---|---|---|
| **Licensing** | Reducing delivery and tax cost, get more revenue<br>Knowledge transfer | Consumer’s negative perception<br>Complicated test for licensing |
| **Direct Import** | Easier way than licensing<br>Fast diversification | Delivery cost and tariff |

**Long-Term: Strengthen the Domestic Beer**

**Risks of Focusing on Imported Brands**

In the long-term, HiteJinro should focus on developing domestic beers and not just depend on direct import of international brands. If it only focuses on imported brands, there are high risks. First, it is not a safe way to just have a few international brands as trends of imported beers are constantly changing (Figure 5). This means that even if a company has products with high sales, sales could decrease as soon as consumers’ preferences change. The company might also lose competitiveness without its own brands as imported beers can be future competitors. Most importantly, in most restaurants and bars, domestic brands such as “Hite”, “Cass” and “Kloud” still have a large proportion of 60~70% ( News dive, 2015). Therefore, they have to sustain and strengthen their own domestic brands continuously.

**Strategies for Developing Domestic Brands**

This strategy of developing domestic brands in a long term would be possible if HiteJinro focuses on two main issues: developing R&D and aggressive marketing.

**Improving Domestic Brands Based on R&D**

As HiteJinro has competitive advantages in technology, it could use this strength to improve domestic product lines from existing ones such as “Hite” to new products such as “Queen’s Ale”. For example, HiteJinro released “New Hite”, which is a new version of “Hite” in 2014. It changed everything from taste, alcohol degree, and product design to manufacturing processes, except the product’s name. It was the first result of a newly developed R&D center, which was a joint research with Hanse Beverage under the World Beer Alliance. With “New Hite”, HiteJinro has succeeded in increasing its sales volume by 24.7% compared to the previous year (Lee, 2015).

Another good example that shows HiteJinro’s potential to succeed in the domestic market based on their R&D is “Queen’s Ale”. In addition to improving existing products as in the case of “New Hite”, HiteJinro can target the domestic market through new products based on technologies. “Queen’s Ale” was released in 2013, and HiteJinro applied a new technology named ‘triple hopping process’ to differentiate its taste. As a result, this technology development for a new product won best awards in renowned international competitions such as a gold award in Monde Selection and IBC (International Beer Challenge), and a silver award in WBC (World Beer Cup) (Jung, 2014). Consumer responses for the taste of “Queen’s Ale” were also highly positive. This resulted in the product having higher market share of 80~90% in the ale beer market, while the market share of OB’s “ALESTON” has decreased continuously (Lee, 2015). While OB considers stopping the production of “ALESTON”, HiteJinro has started to export “Queen’s Ale” to China and other countries. Therefore, HiteJinro should strengthen their domestic brands based on their own R&D and international alliances in the long term.

**Aggressive Marketing**

Another strategy for developing domestic brands is ‘aggressive marketing’. As mentioned in primary activities in the value chain analysis, HiteJinro had not conducted distinct marketing activities to improve their obsolete brand images. However, it is trying to do more aggressive marketing than before recently, and this increased its market share in the first half of 2015. Although they suffered from the increased marketing cost temporarily in 2014, this brought sales increase in the next year (Chang, 2015). This means that if HiteJinro puts more efforts in marketing based on its qualified products, it could win back the first place in the domestic beer market. Currently, it is targeting the 20s to 30s consumers by SNS campaigns and limited editions, and consumers have shown more positive responses than before.

With these marketing activities, popup stores can also be an additional way of aggressive marketing. From 2013, HiteJinro has opened popup stores to promote its international beer, “Kirin”. In these stores, consumers can experience products in various ways such as food shows with famous chefs, or self-design of beer label. HiteJinro made a large success in the first year, so it continued to open them every year with more than 50,000 visitors (Kwon, 2015). HiteJinro also opened popup stores for soju, and made consumers participate in managing stores by themselves. Popup stores gained popularity in these ways, so if there are other popup stores for domestic brands, it could be an opportunity to attract more 20s to 30s consumers and recover HiteJinro’s brand image and then finally recover market share.

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Seungho Choi is a corresponding author (Tel: +82-2-3277-4138, choise@ewha.ac.kr).

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