

THE EFFECT OF DOING COMMISSION WORK ON THE DEVELOPMENT OF THE HUNGARIAN KNITTING INDUSTRY

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Looking back

The origins of the Hungarian Knitting industry, as regards the setting up of factories, dates back to the latter years of the 19th century. The first true knitting factory was established in 1885. However, only the twenties of the 20th century was the period when this industry began to develop on a larger scale. The economic upswing after World War I involved establishment of many smaller and greater knitting mills, too. During World War II the emerging knitting industry sustained massive damage but following the post-war reconstruction and the nationalisation in 1948–1949 large-scale reorganisation of the production was executed. The many smaller knitting mills were merged into several large ones and their production profiles were unified. These new enterprises worked mainly with machines that were left here from the pre-war period.

In the early 60's the textile industry was reorganized again and still larger state-owned enterprises were established for specialized but bulk production of relatively limited choice of goods. Each company had at that time more plants throughout the country. During the 70's general reconstruction of the textile industry was carried out which meant typically the change of out-dated machines. However, also two new knitting companies were established at that time. Large-scale modernizing of the technological level was the result of this action, though, unfortunately, not all goals could be reached.

Political and economic changes in Hungary at the end of the 80's and the beginning of the 90's resulted in serious consequences for the whole economy and, of course, for the knitting industry as well. The huge state-owned companies were unable to adapt themselves to the new economic environment. Most of them became bankrupt and out of the ashes many smaller private ventures came into being. In parallel with this, capital import was looking up. Many knitting mills were established with help and partnership of German, Austrian, French, American and other foreign investors.

According to official statistics 57 knitting factories worked with more than fifty employees in 1997 but much more than this is the number of mills where 5 to 10 people work. Totally round 8500 employees work in the Hungarian knitting industry the importance of which must not think little since knitwear export plays important role in the Hungarian foreign trade.

Motives of doing commission work

Since the middle of 80's doing commission work has kept getting more important for the Hungarian textile and clothing industry. The main motive of this was at first that companies grappled with lack of sources and it seemed to

be obvious solution to make products for which ground materials need not to be purchased and financed by themselves but they were supplied by the customer. Later, with collapse of Comecon in 1991, loss of huge markets hit this industry, followed by falling back of capacity utilization and employment, which forced the companies to do as much commission work as possible. This is why the clothing industry, which makes highly labour-extensive products, sells still now about 90 % of its total capacity. This ratio is only 30 to 40 % in the textile industry. Commission work in export of clothes made of woven or knitted fabrics represents round 80 %.

Advantages for the Customers coming from commission work made by Hungarian companies

Costs of labour in Hungary were much lower than those in developed Western European countries, so it was worth to have commission work made in Hungary, even if additional costs of transportation had to be taken into consideration. Labour costs in Hungary came to US \$ 1,38 in 1991 comparing with US \$ 22,49 in Germany [1], so the ratio was 1:16,3. This ratio is definitely much smaller now because wages and salaries as well as overhead expenses have become significantly higher since then but it is still about 1:5 now.

However, in addition to the large difference between labour costs, foreign customers take some further aspects into consideration:

- Knitting industry has great tradition in Hungary. Many companies existed in this section with a great number of skilled workers. It gives not much trouble to them to learn new manufacturing methods and working practices which are required to fulfil the customer's demands. The only problem was perhaps that speed of work and utilization of working time was lower than in Western Europe so productivity of labour was worse than accustomed to the customers. However, significant improving can be registered on this field for today, not at last just as result of doing commission work.
- Thorough technical education had been a fruitful tradition in the textile industry, both on medium and on higher levels. Many well-educated technicians and engineers work in the factories to whom it gives not much trouble to adopt and to adapt the technological and organization methods which are supplied by the customer in form of know-how. Many examples prove that the technology offered by the customer could be improved by the Hungarian specialists when adapting them in their factory and this modification led to better result than expected. This was profitable also for the customer.
- The Hungarian knitting industry was always able to manufacture products of higher than medium quality level. This makes easier to these factories to comply with the quality requirements that Western European customers demand. Most factories had the proper instruments, laboratory equipment as well as qualified staff thus continuous quality control did not raise problem. If necessary, the service of internationally acknowledged accredited Hungarian institutes could be employed. These possibilities exist today, too.
- Because of Hungary's geographical position and good traffic connections transportation routes between the customer's site and

the Hungarian factory are relatively short which means that costs of transportation as well as delivery times are quite prosperous.

- Hungarian companies had also previously good export contacts with Western European customers which led to good personal contacts between managers and specialists of both sides. This made it easier to realize of doing commission work for these customers.
- Additional costs like, for instance, expenses connecting with environment protection are much lower in Hungary than in highly developed countries and also environment protection rules are lighter than to which Western European companies in their own countries should be respectful.

Advantages for the Hungarian knitting industry coming from commission work made for foreign customers

Within production costs in Hungary material costs are two or three times more than wage costs. This is the main reason that companies strove for structure of manufacturing where material costs play as little role as possible. This tendency led to forging ahead. Expenditures allotted to fulfil commission work orders are recovered in about three months and these amounts are much less than in case of other products. Moreover, also very important fact is that continuous doing of commission work enables the more or less continuous utilization of manufacturing capacity and the continuous employment of the employees.

Besides, the advantageous effect of some more facts must not be neglected:

- The foreign customer is usually interested in giving assistance to manufacture the goods on as high quality level and as economical as possible. He gives know-how to use advanced technology and sometimes gives special machines to use if they miss from the subcontractor's equipment. These machines may not meet the latest technology level and may not be the newest ones, however they enable to use and to learn new methods and technologies thus they help technicians of the factory to learn something new. They get acquainted with advanced technologies and machines and this new knowledge can be used also in manufacture of the company's other products.
- The high quality level required by the foreign customer moves the Hungarian company to use these prescriptions and methods in the manufacture of other products as well. This leads to the raising of the general quality level, covering also the company's own products.
- Similarly, doing commission work requires higher productivity level than used to be at the company. This forces improving of working practices as well as using of methods and tools which improve the productivity also in manufacture of the rest of products.
- It was advantageous, too, that through commission work Hungarian companies and their managers were able to build up direct contact with well known foreign trading companies which proved to be very useful later, in the period of privatization and also in further development of the private companies.

- Through doing commission work for well known brand holder company the Hungarian enterprise is able to make itself known and acknowledged since a respected order placing company is a good reference for making other businesses.

Further outlook for the Hungarian knitting industry concerning commission work

Commission work represents about 20 % in Hungary's export today. Most of this is done by the textile and clothing industry from which 90 % is made for customers in the European Union. Roughly half of this is ordered by German customers but Austria, Italy, the Netherlands, France, the UK and the USA play important role too [3, 5].

The Hungarian knitting industry has, unfortunately, only few own brands which could be competitive on the markets of highly developed countries. This fact makes difficult to export real Hungarian creations. For this reason our industry will be compelled to have recourse to do commission work for foreign customers for long time.

However, large-scale commission work has definite disadvantages:

- It happens that companies are forced sometimes to take uneconomical commission works upon themselves.
- Low profitability of the commission work does not enable to reach enough profit for continuous technical development. The result is that technical level of companies that carry on too much commission work falls behind the desirable rate.
- Commission work is an activity which is sensitive to economic trends. This is why extension of orders is possible only in case of economic upswing and a period of recession causes decay.
- Own product development at companies that settle upon first of all doing commission work goes back. The consequence of this is that the company's own collection grows poor and its market position worsens. Members of the staff whose work is product development, usually highly educated persons with reach professional experience (engineers, designers) cannot choose but to leave the company and this fact makes the company's position even worse.

Commission work carried on by Hungarian companies has invariably advantages for Western European customers, however continuously increasing expenses and the strengthened Hungarian currency against Western currencies (USD, EUR) undoubtedly puts this country in disadvantageous position, concerning commission work, comparing with other Eastern and Central European regions. Chart 1 shows the labour costs and their expected tendencies in some Eastern and Central European countries [2]. Coming rules are expected to make prescriptions stricter in the interest of environment protection and also expenses ensuing from these rules are presumably going to increase.

All these and, in addition, the fact that orders to do commission work are in some extent limited by the European Union, admonishes the Hungarian textile and clothing industry for preparing themselves to the danger that these orders may go back but in any case their expansion hardly goes on.

Chart 1

<i>Country</i>	<i>Expenses (€/min)</i>	<i>Expected trend</i>
Ukraine	0,06	stagnant
Albania	0,08	unforeseeable
Lithuania	0,08	stagnant
Romania	0,09	stagnant
Bulgaria	0,11	stagnant
Czech Republic	0,13	stagnant
Poland	0,13	increasing
Slovakia	0,13	stagnant
Hungary	0,14	increasing
<i>European mean</i>	<i>0,15</i>	

References:

- [1] DRI McGraw-Hill, Morgan Stanley Research
- [2] Bráz, Szilvia: Ruházati cégek marketing tevékenységének kialakítása. (Shaping of the marketing activity of companies in the clothing industry.) Cél-Iránytű, February 11, 2002
- [3] Világgazdaság, September 24, 1998
- [4] A bér munka és az EU kapcsolata. (Relation of commission work and the EU.) ITD Hungary, 2001
- [5] Textil-felsőruházati termékek magyarországi piaca. (The market of textile outerwear in Hungary.) Kopint-Datorg, September, 1997