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The liberalization attempts in the early 1980's in Eastern European countries attracted western car manufacturers. Thus for example, the Japanese Daihatsu began negotiations in Poland while Suzuki targeted Hungary. However, owing to the longer local involvement of Fiat and a stronger governmental backing behind it, Fiat won and Daihatsu failed to get the deal [10]. On the other hand, Suzuki, though after long negotiations, established a joint venture car assembly factory in Hungary which is up to date the largest Japanese direct investment in Eastern Europe. During the first year of its operation Magyar Suzuki successfully developed the network of Hungarian subcontractors by inviting Suzuki's Japanese partners to help them upgrade. Exports were also started in 1993.

## The Market

Although the potential Hungarian automobile market may seem small because Hungary's population is only 10 million, it is really quite substantial as the result of the need for a quick renewal of Hungary's aged car stock. The average age of Hungarian cars is roughly 10 years and roughly 1 million of Hungary's 3 million cars ought to be immediately replaced because they are more than 10 years old or have a high-polluting 2-stroke engine. In 1990 about 40 percent of all Hungarian cars, including Trabant and Wartburg made in the former GDR, had a 2-stroke engine and their share did not decrease substantially even after many western used cars were imported as a result of car import liberalization in 1989-1990 [7].

Hungary's high demand for automobiles is also demonstrated by import data. In 1989 car imports totalled 204.345 of which 136.280 (67 percent) were imported by state car trading companies and 68.065 (33 percent) were imported by private individuals. In 1989, imports by private individuals were particularly high as a result of the temporarily low import duty of only 10 percent. However, even in 1990, when the import duty rose to 35 percent, 30 thousand cars were imported by tourists.

In 1992 36,000 new cars were sold in Hungary, by the end of 1993 this figure reached 45,000. Anyway, earlier estimations for the Hungarian market in the range of 120 to 140 thousand cars have not come true yet. Suzuki's management is considering boosting production to 50 thousand cars by 1995, of which half could be sold in Hungary and half in Western Europe.

The world market strategy of Suzuki is to establish regional manufacturing and marketing centres for its various products. Three categories of car are in play. The mini Maruti is produced in India. The subcompact category Swift and the bigger sedan version will be made in Hungary. The third type, an off-road vehicle is the product of the Santana factory in Spain.

Until recently, Suzuki's main office maintained a marketing strategy of supplying Western Europe by cars made in Japan while to sell the Hungarian made cars in Hungary and the Eastern region. From 1994 this strategy has been basically changed: Suzuki wants to supply Europe from the Hungarian factory (in 1993 altogether 60 thousand Suzuki cars were sold in Europe) [15].

## Capital Sharing and Conditions

The agreement was negotiated almost 10 years long and finally it was signed in 1990.

The basic agreement with Suzuki specifies that the five door model of the Suzuki Swift, with both a 1 and 1,3 liter engine will be produced beginning from 1992. An output of 15 thousand is planned for 1992 with production reaching 50 thousand by 1995 and eventually reaching later a maximum of 100 thousand per year.

The Magyar Suzuki was founded in April 1991 with US$ 70 million, then, after production started, capital was increased by another US$ 90 million in December 1993.

**Table 1 Capital sharing**

| | | 1991 | | 1993 |
|---|---|---|---|---|
| Total project value: $ | | 70 million | | 160 million |
| Japanese share: of which | | 51% | | 65.5% |
| Suzuki | 40% | | 49.9% | |
| C. Itoh | 11% | | 15.6% | |
| Hungarian share: Autokonszern | | 40% | | 30.2% |
| International Finance Corporation | | 9% | | 4.3% |
| | | 100% | | 100% |

In the initial figures (1991) Suzuki's share is somewhat overrepresented because in reality 20 percent of its share is contributed in the form of foregone licence fees.

After the project was opened, some financial troubles appeared mainly due to changes in exchange rates. As Suzuki imported car parts from Japan and took a yen-credit, it is quite understandable that exchange rate impacts were felt quite strongly. In 1993 the Japanese yen was overvalued, the Hungarian forint was devalued which meant a double-negative impact [13]. For instance, the Yen 17 billion loan equaled at the beginning a Ft 9 billion but as a result of new exchange rates this repayment burden grew to 15 billion. In addition, one more new car type, the Sedan was introduced into production which required additional investment. Therefore, mainly in order to escape from the grip of yen-credit, Suzuki decided a considerable capital increase which was realized in December 1993 primarily with Japanese contribution. After this the Japanese share increased from 40% to 65% and the earlier Hungarian director was also changed for a Japanese one.

The Hungarian government has decided to promote the joint venture by granting a series of preferences. Land upon which the car factory is constructed was sold to the joint venture at a price considerably below its market value. The joint venture will also enjoy a full exemption from the income tax during the first 5 years, after which a preferential reduced taxation will be applied. Furthermore, imported machines, equipment and parts used to cars to be exported will be exempt from import taxes while parts used to cars to be sold on the Hungarian market, will be subject to an import tax of only 5 percent.

As the ioint venture approached completion, the government's support was felt less. Mr. Shinohara, general-director of the Magyar

Suzuki claimed that in the beginning the Hungarian government promised financial support to the car industry but subcontractors were suffering from shortage of capital. Also, the full-fledged import liberalization left the developing car industry without any protective umbrella. Therefore, in his opinion, a consequent industry-policy would be necessary [14]. On the other hand it must be mentioned that Suzuki tried to involve Hungarian authorities as much as possible into taking over additional (external) costs of the plant. One example is the infrastructure where Suzuki wanted the Hungarian side to build a special service road to the site. Or, in another case Suzuki found the local environmental norms as being too severe and bargained a compromise with Hungarians reducing thereby the costs of environment protection.

Mr. Suzuki, Suzuki's president when visiting the Hungarian factory in 1993, also proposed a Japanese-style domestic market protection package to the Hungarian government: to increase tax for imported cars, to prohibit the import of used cars, to increase the price for gasoline with lead and to start a budget-supported program for exchanging cars with 2-stroke engines [1]. These requests contradict the free-trade, free-market principles and also several international agreements that were signed by the Hungarian government. As a compromise, Hungary prohibited the import of used cars being older than 6 years.

## Subcontracting, local content

The Suzuki project requires wide *cooperation with Hungarian supply industry*. While Suzuki will provide the important engine and gearbox components, within the first year of operation 50 percent of all work on the project - 25 percent in assembly and 25 percent in parts supply - was contributed by Hungary. In future years the Hungarian share will rise to 55-70 percent. As can be seen from the following draft of the value composition, the Hungarian share consists of two parts, that of the base assembly factory (Magyar Suzuki, Esztergom) and that of other subcontractors. According to the draft, the share of the base plant is not going to increase, therefore involving more subcontractors will become a crucial issue when increasing the total Hungarian local content (see Table 2).

Originally about 50 Hungarian companies were targeted as subcontractors. During the project's realisation Suzuki had to face mainly two problems when trying to involve subcontractors. One was that the ambitious program of privatizing state companies was started, which generally made the legal status of enterprises unsure. The second was that the government struggled with aggravating budget deficit and thus was unable to give financial support needed for restructuring. Potential subcontractors need an investment in the range of Ft 15 to 100 million ($ 180 thousand to 1.2 million) for restructuring and modernizing in order to supply Suzuki the

**Table 2 Subcontracting as value composition of the car** (%)

| | 1992 | 1993 | 1994 |
|---|---|---|---|
| Suzuki Japan (imports) | 65 | 45 | 35 |
| From W-European subcontractors | 5 | 5 | 10 |
| Hungarian share | | | |
| consisting of | | | |
| Magyar Suzuki (Esztergom) | 20 | 25 | 25 |
| Other subcontractors | 10 | 25 | 30 |

Source: Magyar Suzuki. 1993

parts of the quality required. At the beginning Suzuki could contract only slightly over 20 subcontractors. According to a tender survey 130 companies would be able to supply parts provided they can obtain a restructuring injection. It is in the interests of Suzuki to increase the Hungarian share over 50 percent as soon as possible, because in this case the joint-venture-made car can be qualified as of Hungarian origin and can be exported to the EC thus surmounting the EC's car import quota imposed on Japanese-made cars. Almost during one year the number of subcontractors increased to 35 (as of October 1993), but owing to some shadows in marketing partly because of the increasing competition on the Hungarian market and partly because of the depressed western European markets, Suzuki does not plan at present a dramatical increase in the number of subcontractors.

Several subcontracting deals are successfully running. For example, the Precision Instrument Factory of Eger and Showa of Japan signed a licence agreement to manufacture shock-absorbers. The Hungarian firm has bought the necessary licence and expertise and began production in June 1992. Bakony Works of Veszprem has also formed a joint venture with Suzuki to buy the licence for windscreen wipers and wiper motors. The Sumitomo Wiring System signed a technical cooperation agreement with the IMAG-factory of Ikarus bus factory. The Japanese partner provides the manufacturing technology and helps to train the workforce. IMAG has several contracts with Magyar Suzuki for supplying cable harnesses and seat frames. In early 1993 a subcontracting joint venture of a larger scale was concluded. The Daikin-company, being one of the largest suppliers for Suzuki in Japan, established a joint venture in

Hungary for the production of transmission compartment. The base capital is Y 115 million with a participation of 50% for Daikin, 10% for Itochu and 40% for Bakersz (a Hungarian private company). While at the beginning the elements will be imported, within two years all of them are to be produced in Hungary [9]. At present there are joint-ventures with altogether 18 Japanese companies [14].

However, the present state of affairs in subcontracting cannot be qualified as satisfactory. There are two reasons for this, which come mainly from Suzuki's approach. One is the inflexibleness of the cooperation of Suzuki with the Hungarian government, the other is the lot size problem. In the following we will go into more detail.

First, as for the inflexibleness, Suzuki never disclosed its feasibility study to Hungarian governmental organizations. There was a general study made regarding the possibility of an assembly plant in Esztergom, but it lacked main indicators such as development of output, profitability, etc. No estimations were drawn up for the subcontracting background. Suzuki never turned to Hungarian officials to consult on these issues; only before the plant's opening did it present a rough calculation on investment needs in order to upgrade subcontractors. According to information from the Ministry of Industry (Budapest), in order to reach a subcontracting share of 20 percent of the car's value in 1993, a total of 25 subcontractors that had been suppliers for the IKARUS bus factory would need a total of a Ft 2.8 billion ($ 35 million) capital injection. Of this, Ft 1.8 billion would be in credits. In order to help, a special credit construction has been arranged with a 15 percent interest rate, which is only half of the usual rate. The Industrial Development

Bank (Budapest) informed all 25 subcontractors about the credit line, out of which 12 sent in their application, of which 4 remained after screening, the rest not being able to prove credibility. These latter subcontractors could either be upgraded by Suzuki through Japanese bank credits or by joint ventures with other Japanese companies. The joint venture solution would also be a good opportunity since a new joint venture can get the so-called job creating credit amounting to a maximum of Ft 100 million. (Likewise, when Ford's subcontractor came to Hungary in 1992, it also used this joint venture from and could immediately enjoy this Ft 100 million credit line.) Therefore, efforts would be needed on Suzuki's side to attract other Japanese companies to boost subcontracting in Hungary.

Secondly, the lot size problem was obvious from the beginning though, but became prominent again in the subcontracting. That is, the maximum output volume pegged at 50, 000 cars yearly is in fact much lower than the generally accepted optimal level of over 100, 000 cars. President Mr. Suzuki says, anyway, that the minimum is 10, 000 cars for the assembly plant in Esztergom below which production would be unprofitable [6]. A renowned professor from Hitotsubashi University means that the main reason for Suzuki's continuing loss is evidently the low output volume, however, as it was consciously set at a low level, it can not be excluded, that Suzuki gets a compensation from the Japanese government through some "behind-the-scene" arrangement.

There are already several new parts manufacturers in Hungary supplying mirrors, plastic parts, wires, etc. to western European car makers. As they are supplying in large enough lots to be profitable, Suzuki's low volume orders are disadvantageus, and they cannot be combined with western European ones because of Suzuki's standard specifications. Only recently there seems a breakthrough in this problem since Suzuki finally agreed to accept Hungarian made parts to be supplied to other Suzuki assembly factories. Further, in the case of Western European carmaking, the maker usually helps the subcontractor by providing the initial equipment freely.

## Labor management

Magyar Suzuki will inevitably contribute to *employment and labor skill*. The Suzuki factory employs 1200, almost all of which are inexperienced. Through subcontracting, Suzuki will generate an additional 17 to 18 thousand jobs in other companies.

Quite interestingly, Suzuki assembled a totally new labor force, even though in Hungary there was already a skilled labor force in bus production and related factories. Nevertheless Suzuki took the harder way by bringing Hungarians to Japan for training.[1] Suzuki's conditions for employing new laborers were [8]

1. to hire primarily farmers's sons but not individuals with work

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[1] This was also the case in the U. S. where Japanese auto manufacturers such as Honda and Toyota hired totally inexperienced workers at their facilities in Ohio and Kentucky, even though many GM employees etc. were available. This was usually theorized as a move by the Japanese companies to avoid having to retrain workers, who may have poor work habits, etc., or may not do things 'their way.' Also, average age was lower, thus they needed lower salaries for more energy (productivity) and later pensions.

experience in the automotive or machinery industry

2. to hire mainly males in their 20's
3. not to hire ex-communists.

Why does Suzuki attach importance to one's values and behaviour rather than his knowledge and skills? According to Kasahara [8] "whereas knowledge or skills can be taught relatively easily, values or behaviour are in the realm of culture that is difficult to teach. Changing one's values or behaviour would also require extensive time and energy".

Both managers and workers were trained in Japan for several months, about half of the starting staff receiving training. The other half is being trained successively in Japan. Trainees had to sign a contract with Suzuki obliging themselves to repay the training costs if they quit within 2 years. Experience showed that only a modest number of 15 trainees left complaining of working conditions. It is interesting to compare employee benefits at Suzuki and Hungarian Opel. Managers at Opel, both foreign and Hungarian, are provided with an Opel car at their disposal, while at Suzuki only the Japanese managers have such a car.

Another special feature in Suzuki is the equality between blue-collar and white-collar employees. They wear the same uniform, make the same morning gymnastics, dine in the same cafeteria and executives share the same large room with their subordinates.

Suzuki introduced the so-called sandwich pattern in management, appointing alternately Hungarians and Japanese to managerial posts. Thus, the president was a Hungarian, the vice executive president Japanese, vice president of engineering Hungarian and the plant manager Japanese. This pattern helps the smooth adaptation to the

Hungarian environment.

There is no labor union at Suzuki. As the work council is merely a consultative body, the management acquired a dominantly powerful position. Because of the lack of an interest-harmonizing mechanism between management and workers, the opposition of workers being discontent with low wage mounted to serious tensions in 1993 [8].

## Marketing

The Suzuki agreement leaves most of the marketing responsibility with the Hungarian partners. Although the joint venture company is given the exclusive right to sell the assembled cars and parts on European markets, Suzuki is required only to advise the venture and promote sales through its marketing network. No specific obligations are imposed on Suzuki. Furthermore, although Suzuki is required to recommend the parts made in Hungary to Western buyers, it is under no obligation to sell the joint venture's products on Western markets [5]. Probably because of such stipulations of the funding agreement, among Suzuki's Japanese management staff the engineering orientation dominates while the marketing side is not strong. After initial production increases, however, it seems probable that Suzuki will target both Eastern and Western markets, helping increase sales through its West-European network. Such a change in marketing approach will also be necessitated by a competition on the Hungarian market which is stronger than Suzuki could have anticipated (see later).

According to the project-draft, during the first two years the marketing will target Hungarian consumers and only starting in 1994, when production substantially increases, will exports be activized, reaching nearly 50 percent of total production by 1995 (Table 3).

**Table 3 Production and sales (number of cars)**

| | 1992 | 1993 | 1994 | 1995 |
|---|---|---|---|---|
| Production | 1,000 | 20,000 | 40,000 | 50,000 |
| Sales | | | | |
| in Hungary | 1,000 | 18,000 | 30,000 | 30,000 |
| exports | — | 2,000 | 10,000 | 20,000 |

Source: Magyar Suzuki, 1993.

A sign for a new sales strategy it was when in the spring of 1993 Suzuki unexpectedly launched on the market a third new type, the Suzuki Sedan with the obvious aim to acquire a greater portion of market through type-diversification. The composition of production according car-types is depicted in Table 4.

**Table 4 Composition of production according car-types**
(as of 1993)

| | share in production |
|---|---|
| Hatchback 1.1 l | 50% |
| Hatchback 1.3 l | 30% |
| Notchback (Sedan) 1.3 l | 20% |

Source: Magyar Suzuki, 1993

As for Eastern export markets, Suzuki set up a sales office in Moscow, and began exporting to Russia and Ukraina toward the end of 1993. Also in 1993, exports started to China, reaching a volume of 3000 cars by March 1995. Suzuki's main target is, however, the EC market. Since Hungary became already associated member of the EC and was granted practically tax-free imports for manufactured industrial goods, Suzuki can use this opportunity as soon as the Hungarian made share in the car exceeds 50%. From April 1994 Suzuki exported the first few hundred cars to Italy and the Netherlands [2]. That Suzuki prefers entering the EC-market from a third country to direct export is further illustrated by its recent decision to export 20,000 Marutis from its factory in India to the EC [11].

## Competition

Since the initial years when the Suzuki Project was devised, market conditions have changed considerably. On the one hand, another joint venture car factory opened production in 1992, while on the other several Western car makers began operating sales outlets.

The other joint venture car factory is that of General Motors for production of Opel cars and engines. This contract was signed at the same time as the one with Suzuki [4]. General Motors invested DM 80 million into an assembly factory and DM 440 million into an engine factory. Yearly 15,000 cars will be assembled and 200,000 engines manufactured (the maximum capacity is targeted at 400,000 engines). The cars will be sold partly in Hungary, partly in Western Europe, while most of the manufactured engines will be exported to other Opel plants in Western Europe for use in assembly. The Hungarian supply-share is 15 percent. After a 3-month experimental run the joint venture started production in July 1992

[3]. Furthermore, the U. S. manufacturer Ford is also present on the Hungarian market with its car-part factory opened in April 1992.

The German Audi decided to set up a fully German owned daughter company in Györ for the production of a new engine-family. The total value of the investment is going to be DM 320 million and opening is scheduled for 1994. The new factory will provide job for over 1,000 Hungarians. The Hungarian government helped the investment by granting a full tax exemption for the first 5 years and a 60 percent tax cut for a further 5 years period thereafter.

In addition, in the past two to three years several Western car makers opened up sales agents points in Hungary, selling 1,000 to 2,000 cars each annually. Some of them provide consumer credit facilities to attract new customers. Now sales offices of over 20 foreign firms are already present in Hungary [16].

In 1993 Suzuki's share in the Hungarian car market was 25% as compared with Opel's 20% share. (Of other countries with the Japanese firm, in India Suzuki's share was 76%, in Pakistan 66%.)

**Notes**

[1] A Suzuki (The Suzuki), Figyelö 1 July 1993.
[2] Aremelésre késül a Suzuki (Suzuki wants to raise price), Népszabadság 28 May 1994.
[3] Az Opel motorja (Opel's engine), Figyelö 23 July 1992.
[4] Bakos, Gábor: Japanese Capital in Hungary: the Case of Automotive Industry, in: In Search of a new Relationship between Japan and Europe, JAES, Tokyo 1991.
[5] Figyelö 1987. No. 48.
[6] Inter-Japan Magazin, 1992. No. 1.

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[9] Magyar Suzuki Swiftek indulnak a FAK-ba (Hungarian Suzuki Swift to the CIS), Népszabadság 1 March 1993.

[10] Morita, Ken: Daihatsu-FSO kesu no keizai bunseki (Economic analysis fo the Daihatsu-FSO case), Otaru Shoka Daigaku "Shogaku Tokyu," 1989. 10.

[11] Nihon Keizai Shimbun, 1 Oct. 1993.

[12] Not so Swift, Tözsdekurir, 29 Aug. 1991.

[13] Shihonkin baizo de saimuhensai isogu (With capital increase rapid credit payback), Nihon Keizai Shimbun, 11 Nov. 1993.

[14] Shinohara úr nem panaszkodik (Mr. Shinohara does not complain), Népszabadság 4 Aug. 1992.

[15] Uj ember ül a volánnál (New man at the wheel), Figyelö 3 May 1994.

[16] Verseny a magyar autópiacon (Competition on the Hungarian car market), Népszabadság 15 July 1993.