

NÓRA KISS

## Crisis?! What Crisis?! Conversations with the management of Herend Porcelain Manufactory Ltd<sup>12</sup>

For generations of Hungarians, and of customers worldwide, the name ‘Herend’ has signified timeless elegance and beauty embodied in luxury fine porcelain. The Herend Porcelain Manufactory Ltd<sup>3</sup> craftsmen and craftswomen weave the values of traditional arts and crafts in over sixteen thousand shapes and four thousand patterns. Despite such highly skilled craft, the luxury porcelain market has been narrowing, over the years, and the global economic crisis has had severe impacts on porcelain manufacturers worldwide, including on Herend. On this unpromising backdrop, unlike most other manufacturers of luxury porcelain, Herend has actually improved its performance. This article stems from the author’s internship with the manufactory in June–July 2011 and from her MSc dissertation on the manufactory’s organisational culture (Kiss 2012), and sets to explain this counterintuitive state of affairs by looking into Herend’s long and convoluted history, through documentary evidence, and into its increasingly complex present, through conversations with the management.

Consumer habits have changed, over the years—and alongside the effects of the global economic crisis. Luxury substitute products have appeared, adding an increasing number of untraditional competitors to the competition traditional in the luxury porcelain market. In the last ten years, for example, the German luxury porcelain market halved. Moreover, ever since 2008, Meissen, Herend’s foremost competitor, has been heavily affected by the global economic crisis. Up to ten other large German manufacturers have had to close down altogether. Other, smaller European manufacturers such as the Austrian Augarten, the German

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<sup>1</sup> This article is part of Young Scholars’ Platform, a *Pannon Management Review* initiative aiming to guide and encourage masteral and doctoral students and fresh graduates to publish. Young Scholars’ Platform is particularly supportive of young scholars for whom English is not their first language.

<sup>2</sup> For their invaluable time and insights into Herend Porcelain Manufactory Ltd, the author is extremely grateful to Dr. Attila Simon, Chief Executive Officer (CEO); Dr. Zoltán Gaál, Chairman of the Board of Directors; Dr. Melinda Hegedűs, Finance Director; Dr. István Ködmön, Production Director; Mr. László Szesztay, Commercial Director; and Mr. Gyöngyi Pék, Human Resources Manager.

<sup>3</sup> Herendi Porcelánmanufaktúra Zrt., in Hungarian.

Ludwigsburg, Nymphenburg, and KPM, and the French Sèvres have shrunk, operating from only a handful of boutique shops.

At the same time, according to Dr. Attila Simon (2011), its Chief Executive Officer (CEO), Herend Porcelain Manufactory Ltd 'was again profitable in 2010 and achieved its best results in nine years, exceeding its own business plan and expectations. No other porcelain manufactory achieved similar figures. Furthermore, based on number of employees and export markets, we can safely say that Herend is the largest porcelain manufactory of the world.'<sup>4</sup>

With significant profits achieved in spite of an unfavourable foreign exchange market, the year 2011 was even more successful than 2010. Profit before tax rose by 10 per cent, in comparison, and domestic and foreign turnovers both increased. Herend paid 10 per cent dividends to its owners. In addition, a new, special brand outlet was established at Liszt Ferenc International Airport in Budapest, Hungary. The current (November 2012) financial indicators are equally promising, pointing towards further highest performance in recent years.

To understand its present and, possibly, its future too, the next section, based on Balla (2003), Szelényi et al. (2004), and Herend (2012b; 2012c), examines the manufactory's distant and recent past.

### **A manufactory 186 years young**

The beginnings of Herend Porcelain Manufactory Ltd go as far back as 1826, when the forerunner of the manufactory was founded by Vince Stingl (1796–1851?). Vince Stingl was a ceramist with knowledge of porcelain manufacturing and problems of financial liquidity. Mór Fischer, the next owner, was set on modernisation and expansion, and the manufactory became a porcelain factory in 1842 (see Illustration 1, p. 91).

A fire in 1843 led to changes in the owner's business philosophy. The manufactory started to produce porcelain which had formerly been manufactured by famous German, French, Italian, and Austrian factories such as Meissen, Sèvres, Capodimonte, and Vienna. Sales increased with consumer demand—and lack of competition.

This new, artistic direction was very successful not only in Hungary but also overseas. Herend won its first gold medal at the 1846 Industrial Art Exhibition in Pest, and the 1851 Great Exhibition in London brought it international recognition—Queen Victoria ordered a dinner set there, with a butterfly and floral pattern which has born her name ever since, and which continues to be in demand nowadays, all over the world. Herend's international recognition continued to

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<sup>4</sup> Translated from Hungarian.

grow with the 1853 International Trade Fair in New York and the top prize at the 1855 World Fair in Paris. Ming, Esterházy, and many other well-known patterns were created during this period. They often bore the names of the wealthy customers for whom they were initially created, as a sign of respect, from the manufactory, but also as a marketing tool, for the manufactory—an astute arrangement, mutually beneficial.

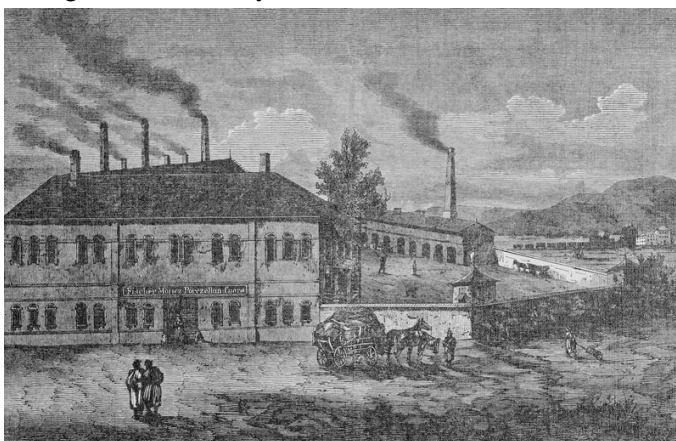


Illustration 1: Mór Fisher's porcelain factory before 1876

Source: Herend (2012c), courtesy of Herend Porcelain Manufactory Ltd

With strong industrialisation and numerous new factories sweeping away the old guild system, Herend, the pride of the Hungarian industrial development, almost came to a complete halt in 1873—mechanisation rendered Herend's traditional manufacturing methods obsolete. Herend's success at the 1873 World Fair in Vienna could not prevent the

manufactory's bankruptcy the year after. Some of the factors which contributed to the manufactory's severe decline—such as the economic depression, globally, and the lack of government support, nationally—were outside its powers. However, some others were well within its powers. Initially of a very great help, Fisher's artistic inclinations and preoccupations ultimately stood in the way of sound business judgement.

Fischer retired in 1876 and left the manufactory to his two sons. The Fischer brothers gave up their father's artistic line and focused on lower cost, and lower quality, products. Intriguingly, success failed to follow. Faced with constant liquidity problems, the Fischer brothers finally sold the manufactory to the state in 1884. Soon after, the state sold it to a public limited company. To increase profitability, the new management made an attempt at diversification and started to produce stoneware and earthenware. Again, intriguingly, success failed to follow. After one more attempt at domestic arts and crafts, the manufactory finally closed down in 1896.

Jenő Farkasházy Fischer (1863–1926), Mór Fischer's grandson, took over his grandfather's legacy, purchased Herend in 1896, and returned to an artistic

direction. The manufactory started to produce to order as well as to regain its reputation, nationally and at international trade fairs. Unfortunately, the manufactory was hit by the porcelain industrial crisis, in 1907, and, just a few years later, alongside everybody else, by World War I. Most manufactory employees were on the front, the demand for porcelain was low, the sales were down, and the manufactory hardly produced anything at all. The Austro-Hungarian Monarchy dissolved at the end of World War I, Hungary lost two-thirds of its territory, and Herend a sizeable part of its national market. Jenő Farkasházy Fischer transformed the manufactory into a stock company in 1923. At the peak of its economic difficulties, Herend was operating with only 23 employees.

Out of the devastation left behind by World War I and its aftermath, new lower-middle and middle classes emerged, soon recognised as valuable consumer markets by Herend's management. New lines, most notably of figurines, were introduced for these new markets in the 1930s. The number of employees rose, and reached 450 by the end of the 1930s. In addition, Herend acquired international recognition, once again. However, with the advent of World War II, success was relatively short-lived, and Herend became isolated from its export markets as well as from its import markets for raw materials.

After the socialist nationalisation of 1948, Herend recovered. Various developments were accompanied by changes in the management culture and by economic and artistic independence. The manufactory resorted to the strengths and energies embedded in its own past. The forms and patterns of old, including the famous Herend figurines, were given a new lease of life. At the same time, the search for new ways of doing things was restarted and the interest for modernisation renewed. As a result, Herend's artists were able to experiment with new ideas and create new masterworks. While harmonising tradition and modernity at Herend has always been challenging, more often than not, it seems, it has also been the key to success. The next section looks closely at Herend's present.

### **The manufactory today**

The manufactory was privatised, in 1989, and a new ownership structure was created, based on Anglo-Saxon principles. To attract and retain highly skilled staff, Herend offered company share ownership to its employees, under the XLIV Act of 1992 on Employee Ownership Programme<sup>5</sup> (MRP). Distribution of shares began in 1995—75 per cent of the shares are owned by employees, now, and 25

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<sup>5</sup> 1992. évi XLI.: Törvény a Munkavállalói Részvénytulajdonosi Programról, in Hungarian.

per cent by the Hungarian state. Of the 75 per cent shares owned by employees, 50 per cent are owned directly by them and 25 per cent indirectly, through the MRP established in 1992 to ensure a circle of member-owners among the prevailing employees of the company. Employees may retain their shares, on leaving the company (through retirement, for example), or they may sell them to MRP. Employees may also inherit shares, but if the inheritors do not work for the manufactory, then the shares are repurchased by MRP.



Illustration 2: Herend Porcelain Manufactory in 2012

Source: Herend (2012c), courtesy of Herend Porcelain Manufactory Ltd

Due to favourable market conditions, the manufactory grew steadily, after the implementation of the new ownership structure, and the financial loan Herend took in order to buy the shares from the Hungarian state in the first instance was repaid swiftly. The 1990s brought Herend a series of major achievements in the form of new, modern buildings (see

Illustration 2) and technology—including the Porcelánium, a museum and mini factory highly successful with visitors to the area. The events of 11 September 2001 put an abrupt stop to this growth. In the words of **Mr. László Szesztay**, the manufactory's Commercial Director,

*'the US market and the buying habits of well-off customers elsewhere overseas started to change, after 2001, as if in shock . The luxury porcelain market had been narrowing anyway, up to that point in time, due to social changes and changes in people's dining habits. The low-design consequence of modernisation had become increasingly popular, in Western Europe, and a real threat for Herend's intricate, rococo and baroque styles. Furthermore, changes in dining habits, such as the advent of fast food chains, and hectic lifestyles have ousted the traditional family meal from people's lives, and do not favour the luxury porcelain industry. Further narrowing of the market may also be caused by the increasing number of substitute consumer articles.'*<sup>6</sup>

<sup>6</sup> All the interviews in this article were carried out in and translated from Hungarian.

Exclusive holidays and expensive jewellery, to name just two examples, are attractive alternative options for costumers with disposable incomes—in the current economic environment, the options have become that much broader, and the market that much more dictatorial. Again, in the words of **Mr. László Szesztay**,

*‘the events of 11 September 2001 affected the entire world, not just us, and we had to rethink much of what we did. Tourists’ habits started to change—people did no longer dare to travel by airplane, and well-off customers preferred cruise ships. We realised that some previously very important markets linked in with tourism—some markets in the Caribbean Islands, for example—would be lost in a couple of months.’*

While market trends were changing, and the market demand for Herend products was dropping, the manufactory’s production rate was left unchanged, and a considerable amount of stock was accumulated fast. Distribution too collapsed with the changed market circumstances, and employee-related costs rose. The staff numbers had not been a problem before.

It was on this background that Mr. József Kovács retired as CEO and a new management team took over in 2003. In the words of **Dr. Zoltán Gaál**, the manufactory’s Chairman of the Board of Directors,

*‘the new CEO started with huge enthusiasm, but also, in my opinion, with no experience and little understanding of the luxury porcelain industry. Methods expedient in telecommunications and information technology simply did not work here. The new management team appointed by the newly appointed CEO were equally inexperienced in the luxury porcelain industry. Besides, they seemed unable to take advantage of the local knowledge and social capital of their predecessors. Our employees were working hard, they were doing what was expected of them, they were not responsible for the situation that developed. Difficulties could not be overcome, we were moving in the wrong direction, and we kept going down.’*

With the manufactory’s very survival at stake, in 2005, Herend’s Board of Directors had to take the difficult decision of appointing a new CEO, in the person of Dr. Attila Simon.

The cornerstones of his countercyclical strategy of stabilisation were market retention, cost reduction, increased effectiveness, harmonisation between demand and supply, advertisement of the manufactory aspects of the production process, and maintenance of the ownership structure. The new CEO set himself to implement this strategy in three stages. The first stage was a thorough analysis of the manufactory’s situation. The second stage was the establishment of long-term goals and short- to medium-term priorities. To this end, three-year general and functional programmes were defined, with extensive communication central to all these programmes—unknown, secret strategies are difficult if not outright

impossible to follow, and employees' trust and support was a critical success factor. The third stage consisted of measuring progress against targets, while taking into account the manufactory's internal culture and external environment. Field force analysis was employed to distinguish potentially beneficial influences from potentially harmful influences, including in terms of source and degree of influence.

Dr. Attila Simon called this normative management method 'the grand coalition'. The members of this grand coalition were the Hungarian State Privatisation Company<sup>7</sup> (ÁPV), MRP, the directors, the management, the works council, and the employees' trade union. This grand coalition was based on negotiation, cooperation, and sincerity—trust, morality, ethics, and honesty are all part of Herend's management culture.

#### The general programme

The general programme defined as part of the manufactory's strategy of stabilisation revolved around market retention, annual revenue stabilisation, and cost reduction. It required extensive examination and revision of activities which did not contribute directly to either production or sale. Outsourcing such activities became a distinct option. It also required rethinking the incentive system, to reflect the company performance—the wage system was analysed, and the social expenditure revised. With the Herend products as the manufactory's main strength, technology development and product quality became important parts of the general programme. Since rationalisation of the organisational structure can lead to increased flexibility and effectiveness, the number of directorial levels was rethought. Some aspects of employee share ownership and the manufactory's in-house training system were also revised.

This general programme generated aims and tasks for each of the five functional areas, financial, commercial, human resources, production, and quality assurance. To return the manufactory back to growth, each of these five areas had to implement their own functional programme. The next sections detail these functional programmes and present the views of the management with regard to the challenges they had faced, the measures they had taken, the results they had obtained, and the future challenges they envisage.

#### The finance programme

The Finance Department played a major role in returning Herend back to growth. To reduce costs and increase efficiency, the Finance Department had to

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<sup>7</sup> Állami Privatizációs és Vagyonkezelő Rt., in Hungarian.

analyse and compare the planned and realised costs; analyse the upper limit of sales, as determined by demand, and the lower limit of sales, as determined by costs; and determine the breakeven point, so that the manufactory produces sufficiently to at least cover its costs (although costs depend not just on the volume of production but also on the volume of production experience). In addition, the Finance Department dealt with the control of investments, the revision of stock and customer payment conditions, the formation of the planning system, the uniformisation of the financial reporting system, the identification of currency exchange risks, the supervision of tenders, and the introduction of the Systems Applications and Products in Data Processing (SAP) software. **Dr. Melinda Hegedűs** was appointed as the manufactory's Finance Director back in 2005.

NK: What were the challenges the Finance Department faced in 2005?

MH: *The manufactory was in great difficulty then. The situation could be characterised as a financial and economic crisis.*

NK: What had caused these difficulties?

MH: *A severe drop in tourism led to a significant decline in demand, and trade decreased drastically, both domestically and internationally, after the fall of the Twin Towers in September 2001. A change in CEO resulted in a change of direction for the manufactory, in 2003, but the new direction proved impracticable. Credits had been accumulating, resulting in layoffs in 2005, and peaking in February 2006. We reached rock bottom, in February 2006, but we have been recuperating gradually ever since.*

NK: What measures did the Finance Department take to overcome these difficulties?

MH: *It was a very serious, very deep crisis—crisis management was our overall number one priority, and financial stabilisation was one of our main priorities. We needed to reduce our costs—so, we set about by rethinking every process, and by implementing very strict cost reduction measures. We achieved decreases in almost all types of cost. In addition, all managers knew what they had to do. I remember there was one goal at the time, for the directors, that the manufactory does not go bankrupt.*

NK: When did the manufactory recover from these difficulties?

MH: *It was a very gradual process. A large company such as Herend is like a big ship. Due to inertia, the ship continues to move towards an undesired destination, even after applying the brakes. I think we recovered from these difficulties when we repaid our loan to the last penny. At the beginning of 2007, if my memory serves me right.*

NK: How did the global economic crisis affect the manufactory?

MH: *We were in the middle of our crisis management process, in 2008, when the global economic crisis started. It hurt, but we were perfectly prepared. If the global economic crisis had begun in 2005 instead of 2008, perhaps we would have*



*gone broke. Fortunately, however, we had already gained appropriate crisis management techniques, by 2008.*

NK: Will the global economic crisis have any spillover effects on the manufactory?

MH: *It definitely will. We have all the techniques which enable us to handle it, but we are not out of the crisis yet. Of course, it will all depend on how deep the crisis will turn out to be.*

NK: Export represents the major part of the manufactory's sales. How will the manufactory handle the risk from exchange rate fluctuations?

MH: *We apply for forward exchange transactions, and we are in a much better position now than we used to be—we have significant savings, and we manage our savings in foreign currencies.*

NK: Now that the manufactory has reached financial stability, are there any new investment plans?

MH: *We are implementing new investment projects continuously, and there are new investments projects this year too. Our car fleet has been completely replaced; our production, distributor, and computer system has been developed; a new glazing machine is arriving in November (2012); and there will be new control equipment for the kilns, which need regular maintenance.*

NK: Planning is very important to the manufactory. How does the manufactory monitor its planning activity?

MH: *The annual planning tasks and the realisation of plans are monitored regularly. Payment plans are made with the so-called rolling method—a planning method which requires continuous foresight based on financial and non-financial indicators, and which exceeds the confines of traditional annual planning. Our target is the rolling annual revenue plan. Fortunately, we have not had any causes for modifying our plans yet.*

NK: What do you think the biggest future challenge will be for the manufactory?

MH: *Market retention will be our biggest challenge. The global economy does not show signs of recovery yet—so, in the middle of a global economic crisis, market retention is the biggest challenge.*

### The commercial programme

The effectiveness of the Commercial Department is central to the manufactory. The Commercial Department was concerned with market retention and revenue stabilisation as well as with looking for new partners and building new distribution channels—in turbulent economic environments, markets and partners alike may disappear. In addition, the Commercial Department had to prepare different action plans for different scenarios and different outcomes. Developing the store network

was part of the commercial programme and meant not just looking for new opportunities but also maintaining the existing network, with the help of good communication and the establishment of good partnerships. The commercial programme established a price level policy and determined the market pricing as well as effective incentives for those responsible with revenue generation. Diversification, another part of the commercial programme, required thorough analysis and the (re)building of the Herend brand through effective marketing based on effective communication channels and styles. With the manufactory having to balance consumer needs, on the one hand, with its own style creation function, on the other, the commercial department was instrumental in product development. Last but not least, the commercial department elaborated the manufactory's Internet policy. The Internet has opened new opportunities for those who can use the advantages of information technology effectively. It offers a platform for the manufactory's cultural mission, and advertising space as well as new sales and communication channels. The manufactory's Commercial Director is **Mr. László Szesztay**.

NK: What were the challenges the Commercial Department faced in 2005?

LS: *We always have one main challenge: to sell as much as possible. We also have to build stable markets and then retain them. The former management did not really face the problems—they chose a 'forward escape'. Their oversized market plans proved to be desires rather than well established solutions. In one and a half years, a huge amount of debt was accumulated. When the new CEO took over, the manufactory was close to bankruptcy.*

NK: How did your partners react to the manufactory's difficulties?

LS: *Our representatives were anxious, and they were enquiring about our business policy and about our next steps. Quite understandably, our partners whose activities relied primarily on Herend's activity were the most concerned.*

NK: How did the manufactory succeed to reassure partners and customers?

LS: *Through the appointment of a new CEO and a new management team. The new CEO even invited Mr. József Kovács back, for a while—Mr. Kovács had been our last CEO bar one. His return was a kind of token that the manufactory will continue to build upon Mr. Kovács' previous business policies. In addition, by putting an end to unrealistic initiatives, our actions served as ultimate reassuring evidence.*

NK: How did the global economic crisis affect the manufactory's commercial activities?

LS: *Our customers—our market—represent a very special segment within the luxury consumer market. Consequently, there is just an indirect connection between the global economic crisis and its impacts on the manufactory. An economic crisis in the US or Japan will have an effect on the manufactory, of course, but not directly.*

NK: Had the global economic crisis actually have a positive effect on the manufactory, through the elimination of competitors?

LS: *There was such a perception. In the last ten years, the German porcelain industry roughly halved, in terms of manufacturing and sales—of closer concern to us, the German porcelain retail trade almost halved. Up to ten porcelain manufactories closed. In addition, Meissen, our main rival, was affected badly by the global economic crisis and transferred its emphasis to jewellery, fashion, and furnishings. It may well follow that some retailers will turn away from Meissen, as a result, simply because they can no longer identify themselves with their new product lines. This may constitute an opportunity for us, but it is far too early to say one way or other—we simply do not know yet how the market has reacted to Meissen's new strategy.*

NK: How does the manufactory respond to changes in consumers' needs?

LS: *We want—and can—respond to changes in consumers' needs, but the manufactory must not follow the changes in consumption patterns blindly. The drastic changes in the German market constitute a perfect illustration. Twenty years ago, traditional, handcrafted porcelain played a significant role in German furnishings and dining habits. Nowadays, traditional, handcrafted porcelain does not seem to appeal to the younger, better-off generation. This has resulted in a decrease in the German porcelain market. When I joined the manufactory, back in 1985, Germany was our largest market, while the American market was just starting to rise for us. Twenty years later, we were losing important German and North European markets, because the manufactory was not following the changes in consumption patterns. However, while addressing change, we need to remain loyal to our traditions. Thanks to our traditional lines, there are several markets where our styles are very popular, and the US is one of them. In addition, we are hugely successful in Japan, where European history is appreciated and respected. Of course, we are 'rejuvenating' our product lines. We are rethinking traditional, well-known patterns such as Rothschild, Apponyi, and Victoria, for example. The Royal Garden pattern (see Illustration 3)—a low-key, pastel representation of the*



Illustration 3: The Royal Garden pattern, a result of product development  
Source: Herened (2012a), courtesy of Herend Porcelain Manufactory Ltd

*successful in Japan, where European history is appreciated and respected. Of course, we are 'rejuvenating' our product lines. We are rethinking traditional, well-known patterns such as Rothschild, Apponyi, and Victoria, for example. The Royal Garden pattern (see Illustration 3)—a low-key, pastel representation of the*

*Victoria pattern—was only created last year, but it already proved a very successful product development. A Royal Garden dinner set was presented to Prince William and Princess Catherine on their wedding. As you may know, the Duke and Duchess of Cambridge did not generally accept wedding presents, but they did accept ours—Prince William had fond childhood memories of Herend porcelain. Their personal representative collected our wedding present from the Hungarian embassy in London.*

NK: Have there been any changes in the manufactory's major market emphasis in recent years?

LS: *There have been, but, fortunately, with no major negative impacts. The US and Japan, our two largest markets, continue to give us stability. We experienced losses in the Scandinavian and German markets, but Scandinavia has never been one of our strong export markets. With its mixture of European and US consumption patterns, the UK remains a good European market for us. The UK's role as a business and tourism hub results in a varied customer base for us. Our customers there include not only native British but also Middle Eastern and Asian tourists and business people. Italy remains our third or fourth largest European market. Of our new market base, Russia was the country where we were very successful very fast. Other former member states of the former Soviet Union followed shortly after. At present, we are most successful in Azerbaijan, but Uzbekistan and Kazakhstan look encouraging too. Taiwan and Korea are also prosperous markets in Asia. China, where porcelain was first manufactured, has become an export market for us, in the last few years. The Arab states of the Middle East are interesting markets for us. Establishing traditional, stable representations there did not prove possible, but being commissioned one-off projects did. Once we started to understand the Arabian culture, we soon realised that well-off Arabian consumers prefer ordering either directly from us or through their favourite London-based interior design company. For them, Herend porcelain holds a value too intimate to see it on display even in the luxury stores available to the wealthy Arabian audience, and I do not think we could be paid a compliment better than this. We have especially good relationships with Oman, where we supply directly to the ministry responsible for the maintenance and provision of the Sultan's Palace.*

NK: How successful is the manufactory in Hungary?

LS: *Compared with previous years, this year we are very successful, not least because of our dedicated sales employees, but also because of a number of changes in our approach. The new brand store at Liszt Ferenc International Airport brought us good results, so far, and we survey our customers there, to understand their knowledge of the Herend brand. According to the data we have collected so far, it would appear that the new brand store at Liszt Ferenc International Airport is a good advertisement for us.*

NK: What do you think the biggest future challenge will be for the manufactory?

LS: *Harmonisation between the need to change with changes in consumption patterns, on the one hand, and the need to preserve our core values and traditional, rococo and baroque styles, on the other, will be the biggest future challenge for us.*

### The human resources programme

The main task for the Human Resources Department was the efficient management of the labour force. Layoffs were inevitable, but the lawnmower approach was avoided. Dismissals were agreed upon after intensive consideration of market forecasts, technology developments, task systems, and efficiency increases. Early retirement became one viable solution, and a revision of activities helped to distinguish core activities from peripheral activities in order to facilitate outsourcing decisions. The Human Resources Department also had to deal with some financial aspects, such as share repurchasing, employer-granted loans, advances on salary, and the membership fund. Wages were revised and corrected, ceasing wage pressure and increasing the efficiency of the sliding wage scale. The elements and the levels of the manufactory's own social benefits system were also revised. Later on, and in conformity with the overall general plan, the Human Resources Department as well as the Quality Assurance Department ceased to belong at directorial level. The manufactory's Human Resources Manager is **Ms. Gyöngyi Pék**.

NK: What were the challenges the Human Resources Department faced in 2005?

GP: *The year 2005 was a very difficult year for us. We had sustained significant losses, and our primary concerns were cost reduction, loss minimisation, and the settlement of overcapacity. Layoffs, unfortunately, could not be avoided.*

NK: What were the reasons behind the drop in annual average numbers of employees shown in Table 1 (p. 102)?

GP: *Due to reductions in demand and internal inefficiencies, we were working at overcapacity, overproducing and accumulating a huge stock of products. The first wave of layoffs took place in 2005 and the second in the first quarter of 2007. Implementing shorter working hours also contributed to capacity reduction. It was all going reasonably well until the advent of the global economic crisis in 2008. Orders dropped even further, and employee numbers became a problem once again. Fortunately, however, we won two public tender opportunities at the right time for preventing further job losses. In addition, women were offered the opportunity to retire after forty years of service. Between eighty and one hundred*

people left us this way, in 2011, and harmony between orders and capacity was once again re-established.

Annual average number of employees at Herend Porcelain Manufactory Ltd							
Type of employee	Year						
	2005	2006	2007	2008	2009	2010	2011
blue collar	1,053.2	877.5	773.1	729.0	708.5	697.2	619.8
white collar	290.9	242.2	218.8	205.2	200.6	196.8	180.1
retired	13.1	11.5	12.5	12.3	8.4	7.7	5.9

Table 1: The annual average numbers of employees at Herend Porcelain Manufactory Ltd between 2005 and 2011

Source: Courtesy of the Human Resources Department, Herend Porcelain Manufactory Ltd

NK: What does the future hold for the manufactory in terms of employee numbers?

GP: *We do not plan to increase our employee numbers, in the near future, because orders have not been increasing at such a rate as to justify such an increase. However, if orders pick up, then we can rely on latent extra capacity at least to an extent. For example, employees returning from maternity leave, currently on six hours a day contracts, could be employed on eight hours a day contracts. In addition, paid overtime is always a viable and flexible option to increase capacity.*

NK: What did the manufactory's employees think about these changes?

GP: *Not much, at the beginning. Let me give you an example. It occurred to us that, towards the end of the year, there were fewer tasks to carry out than earlier in the year—employee, and task, optimisation through working method transfer was the obvious, natural solution. It was a difficult changeover, but more and more employees recognised that, if there was not enough work for them in their area of expertise, there was enough work for them in other areas. In our company, employers and employees depend on one another to a large extent—employees may be highly skilled in one area, but may not be able to find work elsewhere easily. All in all, these changes were very successful.*

NK: People are employers and, at the same time, employees, at the manufactory. Are there any conflicts between these two capacities? Is one of them stronger than the other?

GP: *In our experience, the employee is the stronger of the two. As employers, people rely on yearly dividends. As employees, people have the security of a guaranteed monthly income. Employer-employees also have the security of a stable workplace.*

NK: Employee recruitment is key to the manufactory's future. What attracts the young generation to the manufactory's own vocational school?

GP: *We collaborate with the local primary school and we introduce seventh grade pupils to the secrets of porcelain manufacturing and painting as part of their curricular drawing course. In addition, we participate in an increasing number of career days at schools throughout the region. Up to ten young people enrolled in our vocational school both in 2010 and in 2011, and five enrolled this year. With changes in conditions and the restoration of the former vocational training, we hope to increase our student numbers again, next year. Our aim is to win over not only the current young generation, but many young generations to come.*

NK: What do you think the biggest future challenge will be for the manufactory?

GP: *Continuing to adjust to a rapidly changing environment, and harmonising continuous development with traditional manufacturing methods and values.*

#### The production and quality assurance programmes

The Production Department was expected to satisfy orders in accordance with the contractual obligations, on time and of the high quality standards expected by the manufactory's customers. To increase internal efficiency and improve quality, the production programme included support and reorganisation of technology and compliance with technology developments. Technology developments had to adjust to market requirements. In this context, the Production Department had to define investment goals and expectations, and had to keep investments and staff numbers under control. Just like the Human Resources Department, the Production Department too had to rethink its incentive system. The manufactory element of the production required revision and rationalisation of the process, to reinforce expertise and to comply with health standards, safety procedures, and environmental regulations. The manufactory had an independent Quality Assurance Department, and the quality assurance programme provided for the creation of a single quality control unit for both in-process and finished products, independent of production. Their further duties were reducing scrap costs, maintaining ISO specifications, and securing a professional relationship between technology and quality assurance. Herend quality means not just product quality but also appearance, orderliness, cleanness, discipline, regulation, and documentation. The manufactory's Production Director is **Dr. István Ködmön**.

NK: How does the manufactory determine the optimal production volume?

IK: *My colleagues and I had worked hard at determining this optimal production volume—this year in particular, requirements and possibilities are in harmony. Our work was preceded by working method transfers and employees learning new skills in areas other than their area of expertise in order to enhance*

*capacity as and when required by the market. As a result, the manufactory did not have to dispense with its employees during the global economic crisis. On the contrary, the management's primary aim was to preserve its employees' jobs.*

NK: Women took the opportunity to retire after 40 years of service. Was this disadvantageous for the Production Department?

IK: *We had several months at our disposal to prepare for this eventuality, for instance through working method transfers.*

NK: How did the global economic crisis affect the manufactory's production activity?

IK: *Our premium products may be classified into three categories. The global economic crisis did not affect two of these three categories, the most expensive and the least expensive. Only the demand for our medium-priced products was affected negatively by the global economic crisis. The situation has been stabilising ever since, but this was particularly the case in the years 2009 and 2010. To protect our employees' jobs, we were working to a very tight work schedule, at the time. Our operational culture had to become much more regulated, disciplined, and less tolerant. From a democratic leadership we had to turn into an autocratic leadership, to match the circumstances. Flexible working hours were no longer sustainable, in the Production Department. However, by July 2011, everything returned to normal. We are now confident that the manufactory will not be affected by spillover effects from the global economic crisis. With 50–60 export markets worldwide, the ripples of the global economic crisis cannot affect them all at one and the same time—a much better position to be in than if we had concentrated all our efforts in just one particular segment.*

NK: Have there been any perceptible changes in consumer demand?

IK: *Over the last ten years or so, we have witnessed an interesting trend: the demand for figurines has declined alongside changes in family patterns and home furnishings.*

NK: What determines product development?

IK: *Product development is the direct result of inputs from several sources. Firstly, inputs from wholesalers are paramount in markets such as the US and Japan, for example, where wholesalers have exclusive rights and expect intensive product development. Secondly, our own, internal needs and ideas are another source of inputs for product development. The results of a whole year's intensive, hard work are then presented at the Annual International Trade Fair in Frankfurt. Thirdly, the absolute pillar of product development is the individual needs, needs which my colleagues transform into ideas and then into new products.*

NK: By ignoring machine technology, is the manufactory at a competitive disadvantage?

IK: *In a way, indeed, it is more difficult to compete without the use of machine technology. However, the real value of—and demand for—our products lies in its*



*handcraftsmanship. Intriguingly, the market—especially the Japanese market—does not tolerate the almost inevitable handicraft differences which give products individuality and uniqueness. Consequently, we had to develop our skills to the highest professional levels, manifest in consistent colours, sizes, and patterns. Since such products are made in relatively large numbers, this is a serious challenge.*

NK: How do you secure the quality of your products?

*IK: Each and every one of our products goes through a multi-round quality control system. In-process controls are installed at different stages on the production line, to avoid further work on deficient pieces. Before its delivery to the customer, the finished product constitutes one of the key control points. We continue to improve this system. Over the last several years, we have overhauled the entire production process, production philosophy, and quality control system. As a result, we save about HUF 30–40 million (EUR 130,000, approximately) annually.*

NK: Does the traditional manufactory production system coexist easily with modern management sciences and techniques?

*IK: Of course. While respecting the past, we have to wink towards the future. Management's foremost challenge is to imagine the future of the manufactory based on the values of its past. If the manufactory wants to stay the same, it has to change day after day.*

NK: What do you think the biggest future challenge will be for the manufactory?

*IK: Maintaining harmony between commercial requirements and available capacity and strengthening our labour force. In so doing, we have to take into consideration the fact that some of the skills involved in the production process cannot be learned overnight—they may take several years to acquire at professional level. This is a major challenge for the management, and for the manufactory as a whole.*

### **The manufactory's future**

The manufactory succeeded in implementing the overall, general plan and the five departmental plans. Its costs decreased by HUF 2 billion (EUR 7–7.5 million, approximately), compared with the year 2005. All bank loans were repaid, and the manufactory accumulated significant savings. Repurchase of shares also restarted. Indoor unemployment was wound up, due to proper labour force management, and incomes and social benefits went up again. Its annual revenue and profit before tax increased year by year. New markets were opened, and the volume of sales stabilised and, then, rose (see Table 2, p. 106). Net export turnover increased by 10

per cent in 2010 compared with 2009, and by a further 3 per cent in 2011 compared with the previous year. The figures for the net domestic turnover demonstrate that the manufactory is becoming more and more successful nationally as well as internationally—a remarkable achievement, considering the surrounding domestic economic difficulties. Recalling Mr. László Szesztay's words, this year (2012) may be more successful still.

Net annual turnover at Herend Porcelain Manufactory Ltd (million HUF)			
Type of net annual turnover	Year		
	2009	2010	2011
export	2,774	3,048	3,135
domestic	1,172	1,173	1,266

Table 2: The net annual export and domestic turnover at Herend Porcelain Manufactory Ltd between 2009 and 2011 (in million HUF)

Source: Courtesy of Herend Porcelain Manufactory Ltd

Nowadays, the manufactory maintains low levels of stock of its most popular products and produces on demand according to a pull production system. Efficiency gains can be deduced from developments throughout the manufactory. Despite the very tough times the manufactory went through, the Herend brand remains strong. To focus on its main activities, and following organisational restructuring, the manufactory retains three of the previously five directorial departments (Finance, Commercial, and Production). The grand coalition continues to exist—it helped the manufactory get over challenges, and it will remain a strong, positive force in the future. The manufactory's financial indicators continue to rise, and the manufactory preserves its market leader position in the luxury porcelain industry. The manufactory's Chairman of the Board of Directors, **Dr. Zoltán Gaál**, is very satisfied with the results.

NK: What was the primary task of the management newly appointed in 2005?

ZG: *The manufactory was in a very critical condition, in 2005, due to major financial losses and significant bank loans. 'With such huge debts, will the manufactory remain independent?' was the question in everyone's mind. This gem of a luxury porcelain manufactory became a target for takeover attacks. In addition, the state could sell its shares—the legislation allowed it, at the time. The newly appointed management had to overcome this situation fast. To steer the manufactory towards more hospitable waters, significant collaboration was required and, indeed, established, to fend off such attacks. It was a really hard period, with many injured parties, but retaining the ownership of the manufactory was at stake, alongside the manufactory remaining a stable workplace up to the*

year 2020 and beyond. By the way, with their loyal and hard-working people, the communities of Herend, Báánd, Márkó, and Szentgál, of which some are Swabian settlements, have won my respect and admiration. The changes necessary to overcome this situation could not have been implemented by force, without their cooperation and support. The manufactory is back in good hands, now, as well as on the right track.

NK: What does the Board of Directors do, and what are your duties as its Chairman?

ZG: *In my opinion, there is a good division of labour between management and the Board of Directors. The members of the Board of Directors do not intervene in affairs of operational management, but carry out strategic activities such as formulating goals, outlining possible pathways to the targets to be achieved, and performing strategic controls. To this end, we have a very good reporting system in place. Reports based on considerable analyses of data inform our decision making on a monthly, quarterly, and particularly half-yearly and yearly basis. I am particularly interested in efficiency indicators—how much net profit does a sales revenue figure of HUF 1 generate, for example, or in how much sales revenue does a wage figure of HUF 1 result. Efficiency indicators and financial ratios such as the capital intensity ratio show how competitive we are.*

NK: How is the manufactory doing now, and what do you think the future will hold for it?

ZG: *The manufactory is growing—this is an undeniable fact. Our wages increased to a level nationally respectable, dividends of 10 per cent were paid out in 2012, and we usually provide one-off grants too. All in all, we continue to climb, and we may climb even higher this year (2012) than we did in recent years. In the luxury porcelain industry, Herend is in a better position than both Meissen and Augarten. Of course, the countries' national economic environments influence our manufactory as well as anyone else. Therefore, for the manufactory to grow, first the economies have to grow.*

*In a stable or slightly diminishing luxury porcelain industry, our manufactory can still find opportunities for expansion. I see opportunities in Russia and China, where the markets are particularly large but our stakes are particularly small—to respond to these opportunities, we have to invest. Diversification and new partnerships are also possible future directions for the manufactory. To avoid redundancies and to avoid loosening the manufactory definition, there are other, more convenient opportunities, such as investing in a press in order to improve the quality of our white goods—which is what we call our products before decoration by painting, but after burning and polishing. We will not move towards mass production—we want to remain a manufactory where beauty and handcraftsmanship are both integral parts of the definition. Changing our*

*organisational culture in order to enhance performance will be the manufactory's next challenge.*

**Dr. Attila Simon**, the manufactory's incumbent CEO, believes that, by definition, a good quality status implies the existence of a better quality status, and that the manufactory's duty is to achieve it, through a realistic growth strategy. Future goals and possible ways to achieve these goals are defined by management and the Board of Directors in cooperation. The manufactory has a 3–7 year long-term strategy, annual business plans consisting of detailed programmes, and detailed departmental action plans containing concrete operational measures. Several management techniques are used in this thorough strategic planning: PESTEL analysis, Porter's analysis, resource analysis, comparative analysis, portfolio analysis, stakeholder analysis, and SWOT analysis. In addition, as evidence of continuous development, the manufactory has been applying lean management techniques, since 2007, when the production process was rationalised with assistance from the consultancy firm Hexolut. Following a thorough analysis, the concept of 'improving island' was developed and implemented. Stocks and accounting activities between different functional areas were reduced drastically, as a result. In addition, production efficiency was increased and classification mistakes during the quality control process were reduced. The production time was decreased drastically. Furthermore, a Kaizen list was put on display, to allow for the collection and implementation of employees' ideas and suggestions respectively (Hexolut 2012).

The future organisational philosophy of the manufactory consists of three elements, according to the manufactory's strategy: its environmental philosophy, its mission, and its achievable status. The environmental philosophy refers to maintaining Herend's manufactory status, its presence in the luxury porcelain market, and its current ownership structure. Herend is an inalienable brand as well as a Hungarian manufactory which rejects foreign capital. The mission refers to the manufactory's social and environmental responsibilities and to its openness to the outside world. The manufactory aims to establish an organisational environment where employees are flexible, loyal, action-oriented, skilled, committed to improving their competences, have salaries nationally competitive, and can envisage their future with the manufactory. The manufactory also aims to undertake the cultural mission of looking after and preserving the arts and crafts traditions and of educating the domestic and European markets to this effect. The manufactory has achieved its previously appointed status. The manufactory leads the luxury porcelain market, is profitable, is operating without any external capital, and is able to fulfil all the customer requirements. Among others, the Herend brand epitomises excellent product quality, customer service, and human and professional relations.

## Conclusion

Is there a general recipe for all companies facing difficulties? Surely, there is not. Enterprises are all different. A recipe successful somewhere may be unsuccessful elsewhere. Nevertheless, there must be common recipe elements just as there are specific and unique ones. Hard work and persistence must be on any such recipe, for example. All in all, however, there is no general recipe, but Herend Porcelain Manufactory has found its own, unique success recipe. The manufactory is more prosperous now than it has been in many years, and the opportunities for future growth are numerous.

NK: What is the secret?

MH: *The product.*

LS: *Especially in a continuously changing world, a business policy loyal to the manufactory's core values and basic principles. High quality, wide range of products, and customer-friendly service are also important, but remaining loyal to traditional, handcrafted porcelain manufacturing is the most important of all.*

GP: *Local people, local knowledge. People's affection for both products and manufactory. The solidarity typical of this manufactory—the manufactory is about each and every one of its employees. A common goal, and trying to pull in the same direction. The CEO and the management sharing a common interest in maintaining the current ownership structure and the company's operation as a manufactory.*

IK: *If anybody unravels Herend's secret, the secret will then be lost. Herend's secret is just . . . Herend . . . .*

ZG: *Collaboration, hard work, and persistence in achieving the right goals. The CEO, his personality, and his exemplary behaviour.*

AS: *Commitment to handmade porcelain and manufactory production. High quality. Uniqueness. Preservation of values derived from the past. Faith in the revalorisation of porcelain. Strong product development activity. Balance of economic, social, and cultural aspects. Finally, as stated in our social mission, looking after and preserving domestic and European values as precious inheritance for future generations.*

Art at Herend is not just about exceptional porcelain but also about exceptional management. Without proper steering, the ship that Herend Manufactory Porcelain Ltd represents would still be in the eye of the storm. Just like the art of porcelain manufacturing, leadership is not just a discipline but also an art with its own complexities.

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