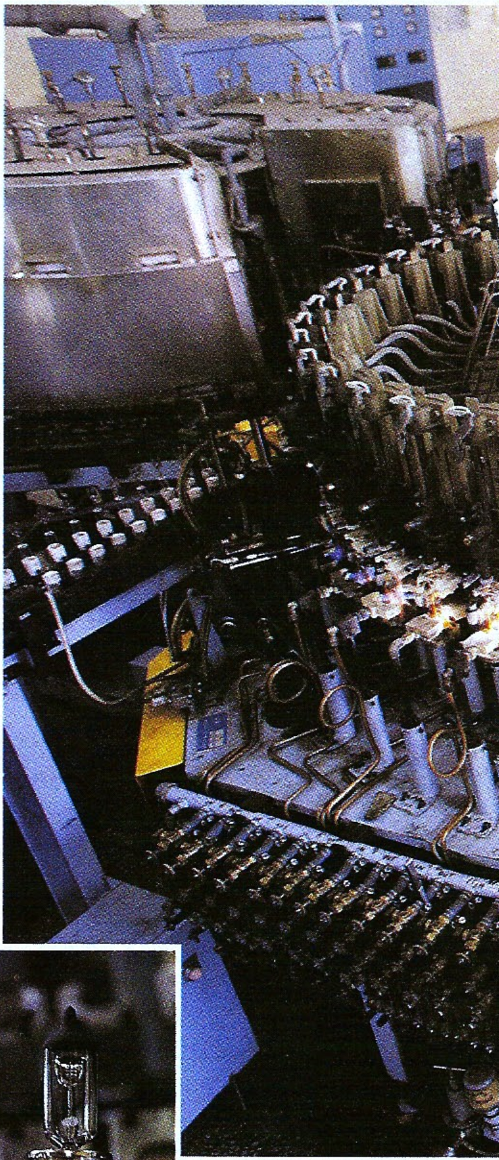
International

HUNGARY

GE CARVES OUT A ROAD EAST

But cleaning up Hungary's Tungsram will be a daunting task



George F. Varga was born and raised in Hungary. But even this onetime émigré was unprepared for what greeted him soon after he arrived back in Budapest last January to run Tungsram Co., the declining, state-owned light bulb maker that General Electric Co. had just taken over for $150 million.

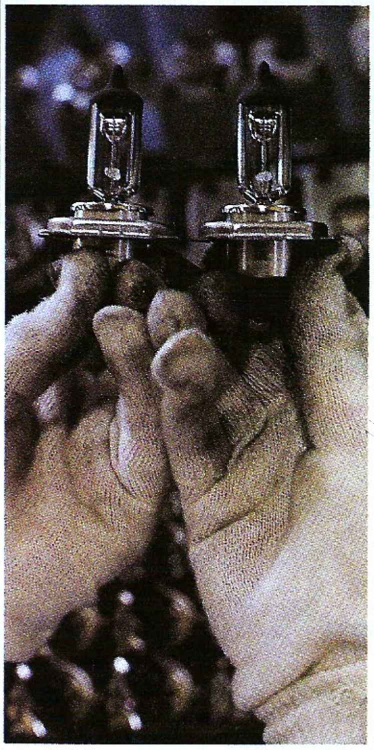
The bloated payroll and aging factories were about standard for Eastern Europe. But then came the books. Digging into Tungsram's accounts, Varga's team discovered that many bills were unpaid. Bulbs and other products that the company had reported as sold were piled up in warehouses. Worse, workers at some of Tungsram's 12 factories had been lining cartons of bulbs with rocks so they could collect bonuses for upping the volumes they were shipping. Such "shenanigans," says the veteran GE executive (page 20), accounted for half of Tungsram's $22 million reported profit last year.

BIG BET. Welcome to the world of Eastern European investing. As communism has faded in the former East bloc, more than 1,800 Western companies have rushed to Hungary to set up joint ventures in everything from automotive parts to advertising billboards. But few have as much riding on Hungary as GE.

For GE, Tungsram is more than a chance to get in on the East's rebirth. It is one of the biggest bets yet on using the East as a low-cost backdoor to the West. "To go after Western Europe—that's why we're there," says John D. Opie, GE's senior vice-president in charge of lighting. Indeed, General Motors Corp. and Ford Motor Co. have also moved into Hungary to serve the West. But unlike Ford and GM, which already are giants on the Continent, GE is a midget in Europe's $2.5 billion-a-year lighting business now dominated by archrivals Philips and Siemens' Osram unit (chart). Tungsram's 7% market share gives GE a ready-made springboard at a time when its competitors are busy consolidating their positions. Without the jump-start from Tungsram, "we'd be locked out," says GE Lighting's European marketing chief, William A. Woodburn.

In buying control of Tungsram, GE has taken on a living laboratory of socialism in transition. Tungsram's labor force will have to be slashed by thousands, and those who remain will have to learn how to think and work like their Western counterparts. On top of that, Tungsram's factories, computer systems, and management ranks will have to undergo a wrenching overhaul.

Still, for all its shortcomings, Tungsram is topnotch by Eastern standards. It is perhaps the West's best test of how good Eastern European industry can be. GE figures it will need to invest as much as $50 million over the next four years to bring Tungsram up to Western standards. Others say the tab may reach $200 million. Whatever the outcome, GE's success in reshaping Tungsram's destiny could set the pace for scores of other Western investors.



A BRIGHT SPOT: TUNGSRAM HEADLAMPS ARE HIGHLY REGARDED

Varga hopes to make GE's investment pay off by 1995 by introducing new technologies and higher priced products, raising production of components Tungsram now buys partly from others, and boosting the two companies' Western European market share to 14%. The Western European increase will be essential to Chairman John F. Welch Jr.'s plan to remain a dominant player in the lighting business worldwide. Now No. 2 globally behind Philips, GE can never become No. 1 without a strong presence in Europe. Increasing its world market share "is GE's game," says Varga.

In taking over Tungsram, GE has inherited a hodgepodge of technology spanning many decades. Among Tungsram's factories, there is everything from Japanese-made computer-controlled machinery turning out car headlamps to 30-year-old assembly lines grinding out filaments. The productivity of the work force of nearly 18,000 is one-seventh that of GE workers in the U.S. Despite all the inefficiencies, Tungsram still manages to compete. Some 70% of its $300 million in annual sales comes from Western Europe, the U.S., and other hard-currency markets.

GE, which has tried to gain a toehold in the European lighting business for years, was attracted to this long shot

PHOTOGRAPHS BY BANKUTI/BLACK STAR

well before Eastern Europe's regimes started to crumble. GE's relationship with Tungsram—largely patent licenses and component sales—dates back to 1913. The two companies talked over a possible linkup in 1987, but nothing really concrete began happening until 1988, when Tungsram's deteriorating financial straits forced its state owner to search for a partner.

DESPERATION. To support its teetering economy, the Hungarian government had been skimming off larger and larger shares of the hard-currency earnings of Tungsram and other exporters. By 1987, taxes were taking 85% of Tungsram's earnings, cutting the amount of money the company had to invest in new plants and equipment to $1 million a year.

In 1988, Tungsram's biggest creditor, the state-controlled Hungarian Credit Bank Ltd., exchanged its $83 million in debt for 91% of Tungsram's stock. Then it turned around and sold 49% of the company for $110 million to a consortium of Austrian banks. That was the opening GE needed. At a Vienna restaurant one night last August, GE Lighting's Woodburn drew up a plan on the back of a napkin and handed it over to Tungsram's bankers. By December, he had a deal. The Austrians would sell their shares back to the Hungarian bank. Then GE would buy 50% of the company, plus one share, take an option to buy an additional 20% from the Hungarians, and assume full control of Tungsram's management.

Now, it's up to Varga, a 53-year-old Stanford University economics graduate with long experience in new markets, to make sure the deal bears fruit. Varga boasts that Tungsram now produces a standard incandescent light bulb 30% cheaper than any Western competitor because a Hungarian lighting worker's $2,000 pay is a tenth of that in the U.S.

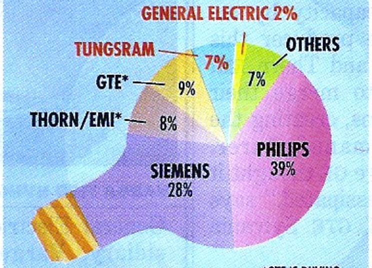
Varga thinks this advantage will last as long as five years. But that depends on how adroitly he maneuvers through some treacherous crosscurrents. GE's 18,000 lighting workers produce more than $2 billion worth of products a year, while Tungsram's similar-size work force only does $300 million. Thus, Varga will be pressed to slash jobs while bringing up the productivity of those remaining. In fact, even before GE, outside consultants were warning Tungsram that its staff was too large. Despite that, Tungsram's union is now demanding 30% higher wages, twice what GE is offering. Yet as Hungarian unemployment rises, Varga is under pressure to refrain from making it significantly worse.

Varga says he is targeting 2,700 job cuts this year through attrition and early retirements. But some outsiders say Tungsram ultimately will need to lay off more than half of its workers to remain competitive. Understandably, such talk has plunged morale to rock-bottom.

ROADBLOCKS. Many workers say they doubt higher wages pegged to higher output will breed the higher productivity Varga expects. Constant devaluation of the Hungarian forint undercuts any incentive to work harder. And like Laszló Kóhan, a 33-year-old engineer at Tungsram's Budapest auto headlamp factory, many Hungarians already work 10 or more hours a day or hold down two or three jobs to make ends meet. "What more can we do?" asks Kóhan, who supports his wife and four children on his $6,350 annual salary. "We're scared."

WHO LIGHTS UP EUROPE

SHARE OF WESTERN EUROPEAN LIGHT BULB MARKET



*GTE IS BUYING THORN EMI'S LIGHTING BUSINESS

DATA: BW, INDUSTRY ESTIMATES

CHART BY ALBERTO MENA/BW

Indeed, how much leverage workers have is perhaps the biggest wild card in Varga's plan. Under a holdover of Communist law, trade unions have a veto over management actions affecting employees. But how effectively the unions will use their clout will only unfold as their leadership remobilizes after 40 years of dormancy. Citing Hungary's 30% inflation, Union Secretary György Selmeczy says: "We want GE management to understand that increased purchasing power is a real expectation of our employees." Nonetheless, even Selmeczy concedes that job cuts are inevitable. "We have to accept the fact that to have a working economy we need working companies," he says.

Tungsram's cost-cutting drive will be mitigated by a number of other pressures. The price of Soviet energy, which accounts for about 12% of Tungsram's total costs, soon may shoot up 40% as soon as Moscow slashes subsidies for its allies. Tungsram's computerized accounting network is a tangle of incompatible systems. And upgrading Tungsram's manufacturing technology promises to be a tough slog.

Long past are the prewar days when Tungsram's patents for tungsten filaments and other achievements were the envy of the global lamp industry. Since then, Tungsram's R&D has been spotty at best. One of its few coups is making auto headlamps good enough to satisfy even finicky Mercedes-Benz and BMW. But auto lamps aren't enough. To build up Tungsram's strength in commercial and industrial lighting, which accounts for the bulk of GE's target market in Western Europe, GE will have to remake Tungsram in its own high-tech image.

Tungsram's fluorescent-tube production lines now waste 30% of their raw materials, more than four times that of an American GE line. Other assembly lines run 40% slower than Western ones. To cut waste and get new product lines going, GE has submerged 32 Tungsram executives in management-training programs in Hungary, while a handful of others have been sent to the U. S.

BEST CHANCE. Varga also plans to slim down Tungsram by selling or consolidating some divisions. But his job won't get any easier as GE's rivals shape up for the elimination of the EC's internal trade barriers in 1992. Seeking low-cost factories to maintain their lead, Philips recently took over Poland's leading lamp producer.

Osram plans to add capacity by acquiring an East German producer this summer. And GTE Corp. and Thorn EMI PLC soon are expected to merge their European lighting divisions, creating the region's third-largest manufacturer. "The short-term advantage GE thought it had bought has sort of dissipated," says Greg Rice, president of GTE Sylvania Lighting Europe.

Many observers think GE's best chance of breaking into Europe's big leagues is to maintain Tungsram's low-cost brand. But GE's Woodburn has other ideas. He plans to double Tungsram's ad budget next year and gradually raise prices as GE helps Tungsram bring on more high-end products.

As GE tunes its strategy, all eyes are on Varga, who says he returned to his hometown with "a bit of a missionary zeal to do this right." In plunging headlong into Hungary, "we're trying to mesh two cultures," he says. Making that culture clash pay off even as GE's rivals close ranks will be a test of the East's potential.

By Jonathan B. Levine, with Gail E. Schares, in Budapest, Zachary Schiller in Cleveland, and bureau reports

GOING BACK TO BUDAPEST TO WHIP A GIANT INTO SHAPE

As a teenager, George F. Varga was an up and comer in Hungary's major soccer league and aspired to a career on the national team—one of the world's best in the 1950s. But the Soviet invasion in 1956 changed all that. At age 19, he fled his homeland, leaving behind his family and his hopes of becoming a sports star.

Now, after 34 years in the West, Varga is back home and in the limelight again, this time as president of General Electric Co.'s Tungsram subsidiary. Varga's office guest book reads like *Who's Who,* from U. S. senators and European royalty to GE Chairman John F. Welch Jr. If Varga can remake the dowdy light bulb maker, with its aging factories and low productivity, he'll score a big one for Welch and for the home team, too.

WHIZ KID. Tough assignments don't seem to faze Varga. Landing in the U. S. knowing only 200 words of English, he entered Western Maryland College, muddling through his freshman year with an ever-present dictionary. With a Rockefeller Foundation fellowship, he went on to Stanford University where GE recruited him for a three-year training program in finance. Thus began a 28-year climb through posts in Spain, Mexico, Switzerland, and the Netherlands that left Varga speaking six languages and earned him a reputation as a manager with a knack for making businesses grow.

Then, in 1989, GE made its $150 million offer for Tungsram. Varga was running a $500 million-a-year international plastics unit in January when he got the call for the Budapest job.

From his spare office in the company's concrete and glass headquarters, Varga recalls childhood impressions of Tungsram as a gleaming centerpiece of Hungarian industry. Now that he is CEO in a new era, reality is closing in. He finds the unrelenting pessimism of the company's employees to be a constant drain on his emotions. He also finds all the cars and smog in Budapest hard to get used to and something he doesn't remember from before.

But there is something comforting about being back, too. Varga is getting to know parts of the city he never knew as a child, and he is back among friends and family. "Sometimes I feel like I never left, other times it's like I've never known the place," he muses.

For now, Varga's future is inextricably linked to Hungary. With Tungsram and its suppliers touching the lives of nearly 500,000 Hungarians, coming home has become a mission in itself.

By Jonathan B. Levine in Budapest

VARGA FLED HUNGARY AT 19 DURING THE 1956 UPRISING AGAINST SOVIET RULE

BARNETT/BLACK STAR