

## **THE ANALYSIS OF FINANCIAL SITUATION OF LEATHER INDUSTRY IN POLAND IN 2000-2005**

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**Abstract.** The paper presents the estimation of financial situation of leather industry in Poland. The analysis of assets and capital as well as chosen ratios of liquidity, debt, profitability and efficiency were used. The period scope of research included years 2000-2005.

**Key words:** financial analysis, liquidity, debt, profitability, efficiency, leather industry

### **INTRODUCTION**

In conditions of market economy, at increasing national and foreign competition, enterprises more frequently perceive the necessity of executing financial analysis. This analysis is synthetic treatment, which allows for fast determination of result and estimation of financial situation of economic subject. It indicates economic results of earlier undertaken decision and allows for estimation of such results and indicates the direction of future operations [Finanse przedsiębiorstw 2007].

The estimation of financial activity of an enterprise can be performed applying various kinds of methods. Majority of them are based on analysis of data from financial reports. The most general method is ratios analysis, relying on formulating financial ratios. It allows to establish the condition of chosen area of activity of enterprise as well as to identify weak and strong part of activities [Finanse przedsiębiorstw 2007].

During several years, the leather industry in Poland suffered from a considerable decrease of production and employment. After the great crisis, when export to eastern neighbours had fallen dramatically, the leather industry improved its financial condition with time. However, the property structure has been changed. Alongside with the firms which emerged from transformations in the state industry, the private enterprises of

leather industries can be growing. They have been strengthened on market with time and their quality is known by Polish receivers. Presently, competition of cheap far-eastern products provides big threat, because the price of these products is often lowest than the cost of raw material. The growth of competitive position requires capital expenditure, which very often surpasses capabilities of the sector [Ostapowicz 2007].

The purpose of the paper was the analysis of financial situation of the leather industry in Poland. The scope of research included years 2000-2005.

## MATERIALS AND METHODS

Data for the investigation were taken from GUS papers: “Financial results of economic subjects” and “Financial ratios of economic subjects” from 2000-2005 (Fig. 1).

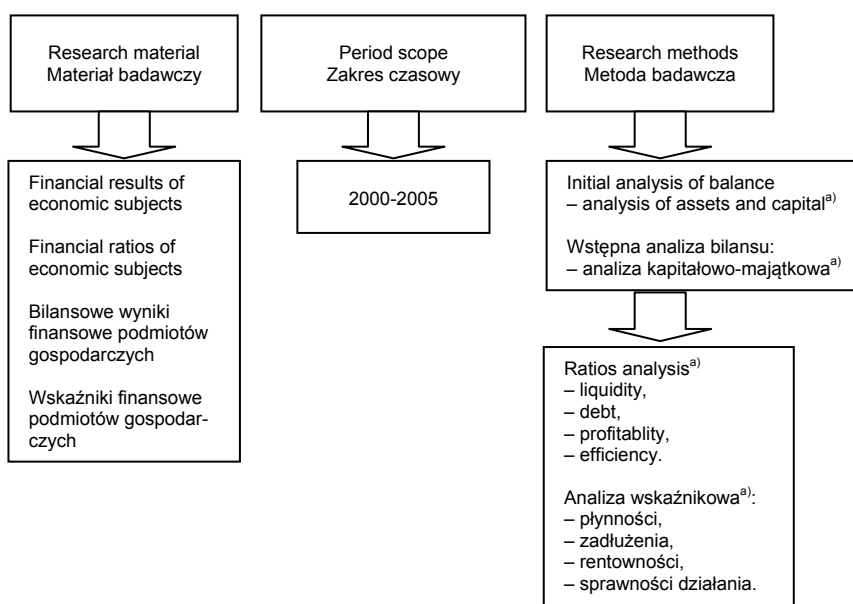


Fig. 1. Research scope

<sup>a)</sup> Description of ratios construction using in work were presented in: Sierpińska and Jachna [2004], *Finanse przedsiębiorstw* [2007], Szymańska [2007].  
Source: own elaboration.

Rys. 1. Zakres pracy

<sup>a)</sup> Opis konstrukcji wskaźników wykorzystanych w pracy przedstawiono wcześniej w: Sierpińska i Jachna [2004], *Finanse przedsiębiorstw* [2007], Szymańska [2007].  
Źródło: opracowanie własne.

Income of each firm and incurred cost as well as achieved effects are expressed in categories of value. So, for the research of efficiency and competitiveness of firm, it is possible to use financial analysis. Basing on the analysis of balance, the initial estimate

of financial condition of leather branch was prepared. Besides, using ratios analysis, it was examined if leather industry owned the ability to fulfil short-term liabilities in 2000-2005 (Fig. 1). The next step of research was the estimation of possibility of repayment of industry's liabilities. Besides, the profitability and efficiency of using of components of industry assets was analysed (Fig. 1).

## RESULT

The years 2000-2005 were not easy for the leather branch. The change of number of units in this sector of economy evidence it. In 2000 there were 264 enterprises of leather industries. After a year, the number of units in this branch grew to 277, but at the end of 2005 remained only 204 enterprises (decrease about 26%) (Fig. 2).



Fig. 2. Number of units of leather industry in Poland in 2000-2005 (according to employment)

Source: own elaboration based on Bilansowe wyniki... [2000-2005].

Rys. 2. Liczba jednostek przemysłu skózanego w Polsce w latach 2000-2005 (według wielkości zatrudnienia)

Źródło: opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005].

Except the decrease of the total number of firms in branch, unfavourable changes in structure of enterprises were observed. The number of the biggest enterprises has fallen down. From 38 firms in 2000 18 firms remained in 2005. They have not been closed.

Because of the limitation of the number of employees, they were ascribed to the group of average enterprises employing from 50 to 249 workers. Over a half of big enterprises of leather industry have dismissed workers and limited production, because of the economic situation (Fig. 2).

The next worrying phenomenon in the branch was limitation of the importance of an average enterprise to the benefit of small firms, employing up to 49 workers. The average firms were the most numerous group in the structure of leather industry enterprise in Poland in 2000 (about 47%). From 125 average firms in 2000 remained only 89 units in 2005 (Fig. 2). A part of these firms limited production and employment, as in the group of big enterprises, have been classified as small firms.

The number of units in the group of the smallest enterprises, employing to 49 persons, fluctuated in 2000-2005. Such firms were most numerous in 2001 (136 enterprises) (Fig. 2). This situation was value to arising of new enterprises of this branch as well as limiting of employment in average and big enterprises. However, the number of these units systematically decreased and there were only 97 small firms.

The market has eliminated weak enterprises of low production efficiency as well as these, which could not adjust their production to European Union requirements. Now, only strong developing firms have remained, which are modernizing their plants. First of all, these enterprises invest in buildings, machines and other industry facilities as well as in specialist transport. The modern production lines will allow to reduce the total cost, that can affect to reduction of the price of the final product. These enterprises can extend sale of their products on the domestic market.

Besides, opening of market of the European Union can also considerably improve sale and profitability of production in perspective of the next few years. Possibilities for sale to eastern border countries exist, too. But the real chance of considerable increase of export to these market need opened policy of the country against eastern neighbours.

The productivity of the branch was not used fully in 2000-2005 because the decrease of value of sold production was greater than decrease of number of units in percentage. Difficult situation on market forced the limitation of production on producers. Businessmen had problem with sale of fabricated goods, despite of growth of technological level and qualities of products. It was the result of the import of cheaper products from Asian developing countries [Cygański 2007]. Value of sold production of leather industry fell from 532.68 million PLN in 2000 to 370.75 million PLN in 2005 (Fig. 3). However, in case of the improvement of the situation on the leather market, the branch is ready for the start of currently unused capabilities of production.

In 2000-2005 small decrease of total balance sheet was observed (except 2003 year). Decrease of this value indicates the insignificant decrease of the production potential of the branch. The ratios of endowment of enterprises of specific economic means have basic meaning in research of structure of assets. The most important ratios of them are ratios of endowment of enterprises of fixed and current assets.

Decrease of share of fixed assets against current assets (from 44.3% in 2000 to 34.0% in 2005) shows the improvement of elasticity of enterprises of branch to fitting to market changes (Fig. 4). Low share of fixed assets allows for the easier reaction to prosperity changes and the level of sale which are interconnected. The most important components of structure of current assets were inventory and due [Bilansowe wyniki... 2000-2005].

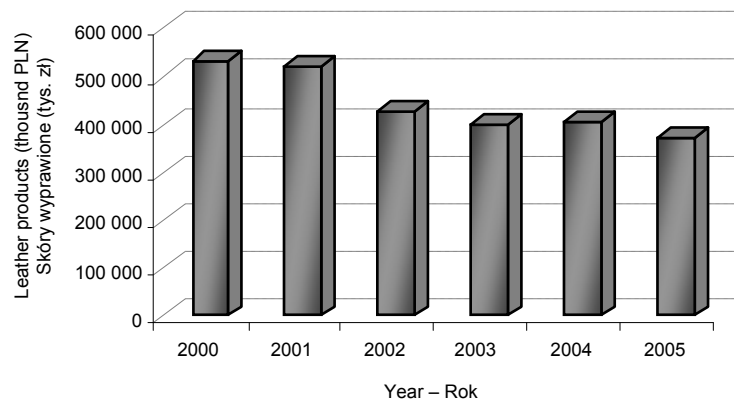


Fig. 3. Value of sold production of leather industry in Poland in 2000-2005 (thousand PLN)

Source: own elaboration based on: Produkcja wyrobów... [2000-2005].

Rys. 3. Wartość produkcji sprzedanej w przemyśle skórzanym w Polsce w latach 2000-2005 (tys. zł)

Źródło: opracowanie własne na podstawie: Produkcja wyrobów... [2000-2005].

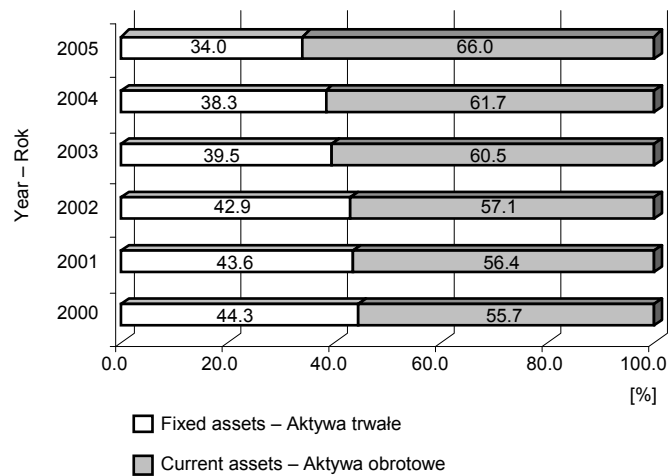


Fig. 4. Structure of assets of leather industry in Poland in 2000-2005 (%)

Source: own elaboration based on: Bilansowe wyniki... [2000-2005].

Rys. 4. Struktura majątku przemysłu skózanego w Polsce w latach 2000-2005 (%)

Źródło: opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005].

The structure of liabilities has improved, because the share of equity capital in total value of liabilities grew from 27.1% in 2000 to 41.8% in 2005 (Fig. 5). The high share of equity capital in total liabilities assures enterprises sovereignty and constancy in the face of environment as well as assures solvency of creditors. Besides, increasingly favourable relation of equity capital to foreign capital can stop collapsing of liquidity of leather industry enterprises. Primarily, the foreign capital was concentrated in the form of short-term liabilities [Bilansowe wyniki... 2000-2005]. It is an adverse situation for firms of branch, because it shows deterioration of possibility of enterprises to fulfil current liabilities.

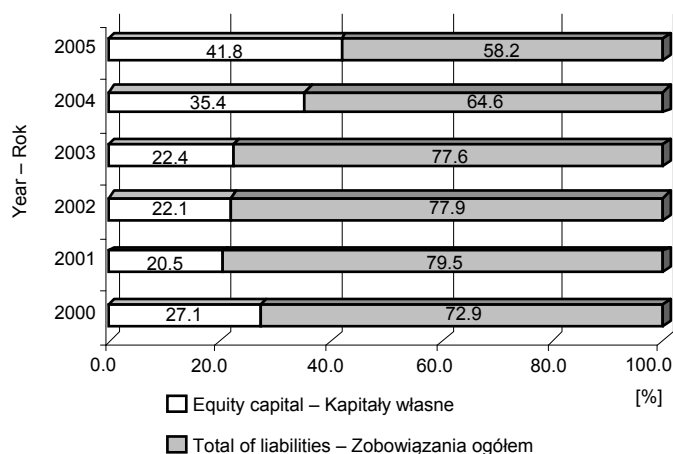


Fig. 5. Structure of capital of leather industry in Poland in 2000-2005 (%)

Source: own elaboration based on: Bilansowe wyniki... [2000-2005].

Rys. 5. Struktura kapitału przemysłu skórzanego w Polsce w latach 2000-2005 (%)

Źródło: Opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005].

The ratios of structure of assets and capital inform, that the golden rule of finance has not been granted. This rule informs that the fixed assets should be completely sponsored by long-term capital, which does not require fast refund. In this situation, the activity of enterprises of leather branch in Poland characterised big financial risk. It is possible to ascertain, during analysis of the general trend changes of values of ratios of assets and capital structure, that the financial situation of leather industry undergoes some improvement (Fig. 6).

Current ratio characterized growth tendency in 2000-2005. This ratio should accept values from 1.2 to 2.0. In 2005, due to favourable change of this ratio, current ratio managed to surpass bottom value of its optimal level (Fig. 7). Quick ratio also grew in research period, but his value strayed from optimal level, which should be 1. The value of quick ratio grew from 0.5 in 2000 to 0.8 in 2005 (Fig. 7).

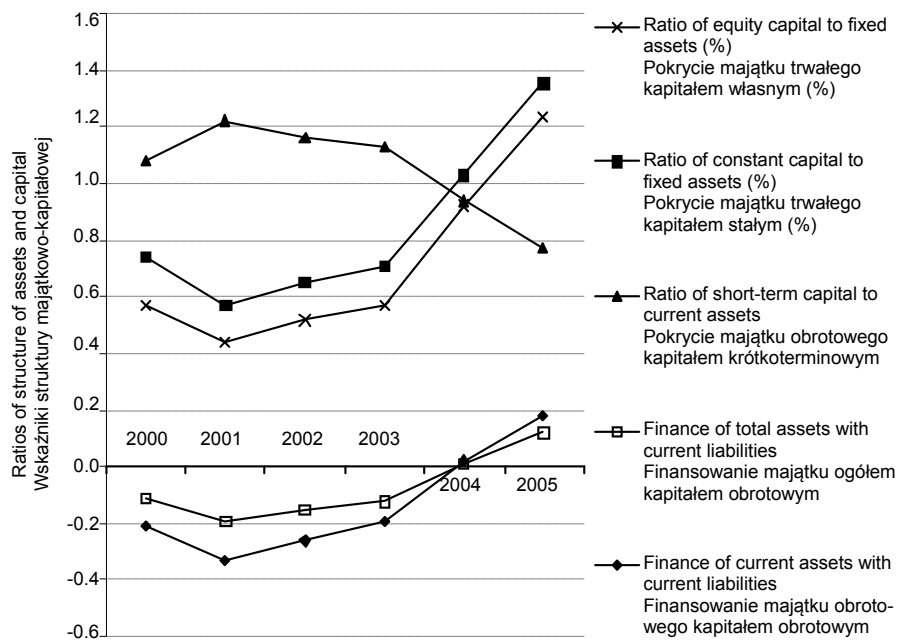


Fig. 6. Ratios of structure of assets and capital of leather industry in Poland in 2000-2005

Source: own elaboration based on: Bilansowe wyniki... [2000-2005].

Rys. 6. Wskaźniki struktury majątkowo-kapitałowej przemysłu skórzanego w Polsce w latach 2000-2005

Źródło: opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005].

Analysing together current and quick ratio, it is possible to ascertain, that in leather branch too high level of inventory is kept. So the working capital is frozen. Observing tendency of forming these ratios, it belongs to underline, that in the case when quick ratio will still grow, serious problems with fulfil current liabilities of enterprises of branch can lose.

Ratio of totality of debt fluctuated in the research period from 67.90% in 2000, 77.55% in 2003 to 58.23% in 2005 (Table 1). In 2000-2003 the situation of the leather industry was unfavourable, because too high level of this ratio was observed. It informed about problems of enterprises to fulfil liabilities. In 2004 and 2005 the ratio of totality of debt for branch reached optimal level (Table 1). It must be noticed that the balance between foreign capital and equity capital in leather branch was not kept. The fact that the contribution of foreign capital derived almost entirely from short-term finance is unfavourable.

All ratios concerning profitability of branch characterized very favourable changes in 2000-2005 (Fig. 8). They changed their values to positive sign in 2003, which shows obtainment of possibilities for generating profit by enterprises of leather sectors. This situation can be influenced by the elimination of weak and unprofitable enterprises from the market of leather products.

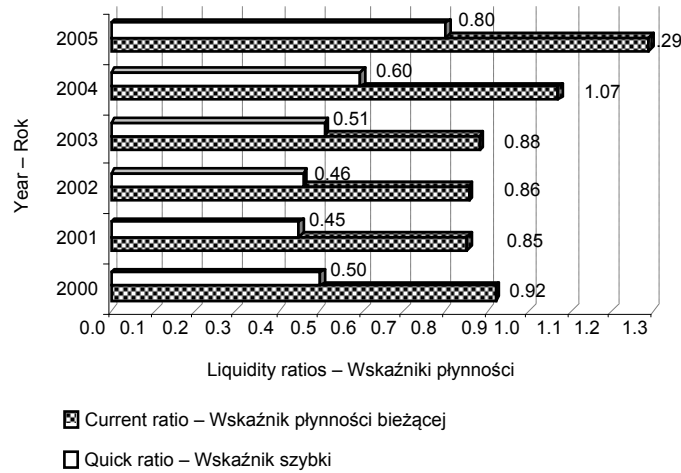


Fig. 7. Liquidity ratios of leather industry in Poland in 2000-2005  
Source: own elaboration based on: Bilansowe wyniki... [2000-2005] and Wskaźniki finansowe... [2000-2005].

Rys. 7. Wskaźniki płynności finansowej przemysłu skórzanego w Polsce w latach 2000-2005

Źródło: Opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005] oraz Wskaźniki finansowe... [2000-2005].

Table 1. Ratios of debt of leather industry in Poland in 2000-2005  
Tabela 1. Wskaźniki zadłużenia przemysłu skórzanego w Polsce w latach 2000-2005

Specifications Wyszczególnienie	Years – Lata					
	2000	2001	2002	2003	2004	2005
Ratio of totality of debt (%) Wskaźnik ogólnego zadłużenia (%)	67.90	74.37	77.83	77.55	64.61	58.23
Ratio of equity debt Wskaźnik zadłużenia kapitału własnego	2.69	3.87	3.52	3.45	1.83	1.39
Ratio of long term debt Wskaźnik zadłużenia długoterminowego	0.30	0.29	0.27	0.25	0.12	0.10

Source: own elaboration based on: Bilansowe wyniki... [2000-2005] and Wskaźniki finansowe... [2000-2005].

Źródło: opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005] oraz Wskaźniki finansowe... [2000-2005].



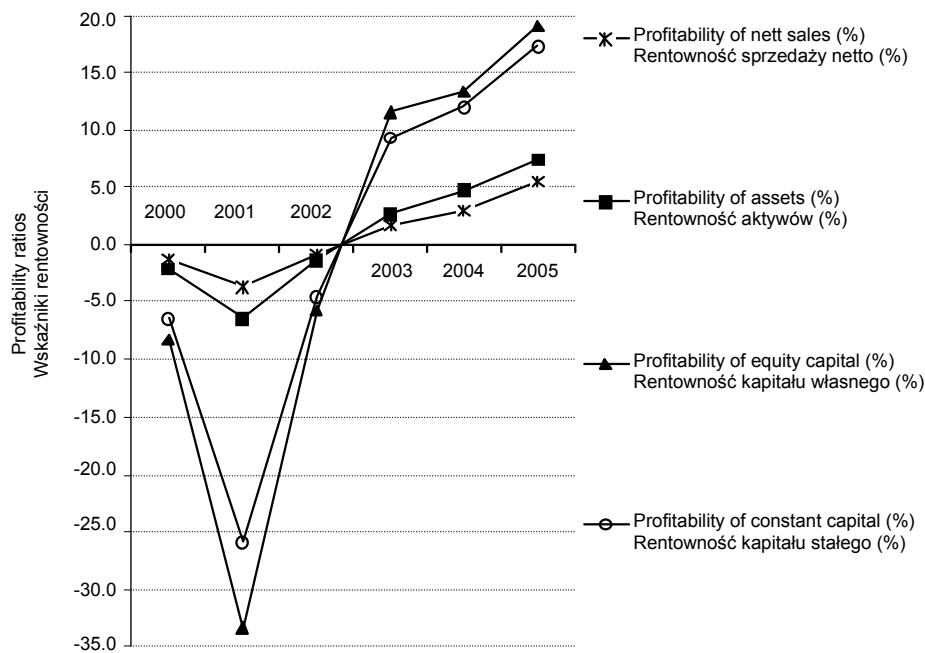


Fig. 8. Profitability ratios of leather industry in Poland in 2000-2005

Source: own elaboration based on: Bilansowe wyniki... [2000-2005] and Wskaźniki finansowe... [2000-2005].

Rys. 8. Wskaźniki rentowności przemysłu skórzanego w Polsce w latach 2000-2005

Źródło: opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005] oraz Wskaźniki finansowe... [2000-2005].

Ratios of turnover of total assets and current assets were decreasing in 2001-2005 (Fig. 9). It shows, that firms in branch had difficulties with generating incomes from the capital invested to assets. Enterprises badly used available current assets in the researched period. Decreasing values of ratios of turnover indicate deterioration of payment situation of firms of leather branch. Ratio of turnover of fixed assets grew slightly from 3.89 in 2001 to 3.92 in 2005 (Fig. 9). It shows good utilization of fixed assets.

Efficiency ratios concerning rotation, alike turnover ratios, were decreasing in researched period, too. Ratio of rotation of due reduced its value from 6.76 to 5.81 in 2001-2005 (Fig. 9). This ratio informs, that due were reaching the branch enterprises more slowly. Decrease of ratio of rotation of inventory indicates too long cycle of their turnover, in consequence affecting the engagement of more and more money in inventory. In this way, the branch incurs additional costs related with storage. Then, decrease of ratio of rotation of liabilities informs about elongation of cycle of repayment of liabilities. It shows deterioration of relation incomes from sale and liabilities.

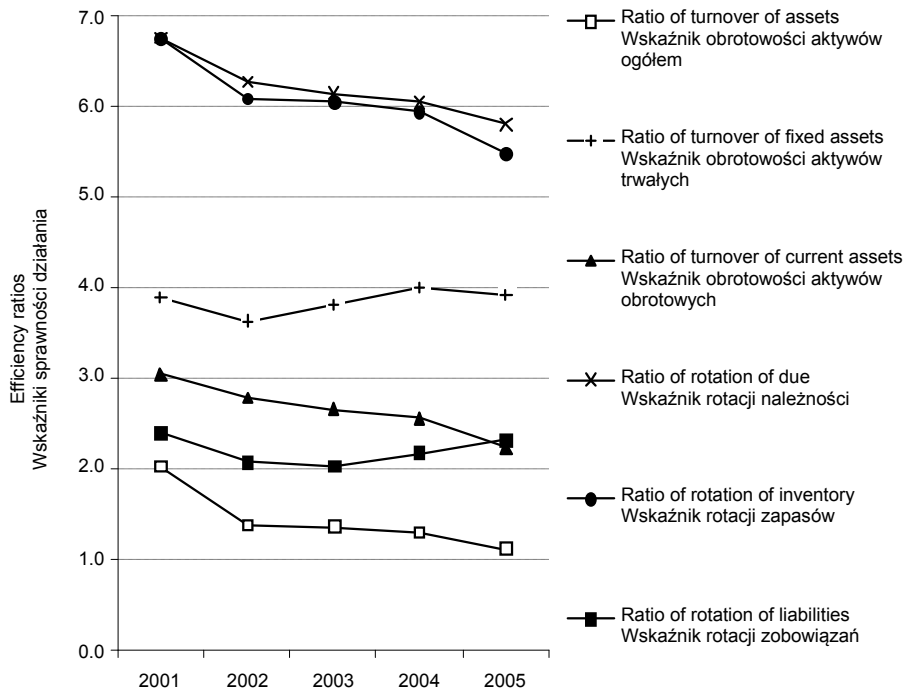


Fig. 9. Efficiency ratios<sup>a)</sup> of leather industry in Poland in 2000-2005

<sup>a)</sup> Ratios was calculated for years 2001-2005; year 2000 was omitted because of incomplete data.

Source: Own elaboration based on: Bilansowe wyniki... [2000-2005] and Wskaźniki finansowe... [2000-2005].

Rys. 9. Wskaźniki sprawności działania<sup>a)</sup> przemysłu skórzanego w Polsce w latach 2000-2005

<sup>a)</sup> Wskaźniki policzono dla lat 2001-2005; rok 2000 pominięto ze względu na niekompletne dane.

Źródło: opracowanie własne na podstawie: Bilansowe wyniki... [2000-2005] oraz Wskaźniki finansowe... [2000-2005].

## CONCLUSION

Observing the leather industry in Poland one should pay attention to the plurality of factors affecting its development. Situation in leather market underwent continuous changes in 2000-2005. Basing on carried out research it is possible to ascertain, that:

1. Number of units of leather branch has fallen, and the existing firms limited their production. The changes concerned the structure of enterprises of leather industry, too. First of all, the number of the biggest enterprises has decreased.

2. Improvement in structure of assets and the sources of their financing has followed. Share of fixed assets to current assets has fallen, that shows improvement of elasticity of enterprises of branch to fitting to market changes. Then, the share of equity

capital in total value of liabilities has grown. This situation assures branch sovereignty and constancy towards the environment and also assures solvency of creditors as well as can stop collapsing of the liquidity of leather industry enterprises.

3. Based on analysis of ratios of structure of capital and assets it has been ascertained, that the golden rule of finance has not been granted in enterprises of leather industry in 2000-2004. In this situation, the activity of enterprises of leather branch in Poland characterized big financial risk. In 2005 situation began to improve.

4. Estimating liquidity of enterprises of leather industry showed that, in leather branch too high level of inventory is kept. So the working capital is frozen. It should be underlined, that in the case when ratios still grow, serious problems with fulfilling current liabilities of enterprises of branch can disappear.

5. In leather branch the balance between foreign capital and equity capital in leather branch was not kept. It is worrying, that contribution of foreign capital derived almost entirely from short-term finance. In 2000-2003 enterprises had problem with fulfilling liabilities. In 2004 and 2005 the ratio of totality of debt for branch had optimal level.

6. All ratios concerning profitability of the branch indicate that, enterprises of the leather sectors have obtained the possibilities for generating profit since 2003. It could be influence by the elimination of weak and unprofitable enterprises from the market of leather products.

7. Majority of efficiency ratios concerning rotation and turnover were decreasing in the researched period. Enterprises of the leather industry had difficulties with generating incomes from the capital invested into assets. They also badly used available current assets. As a result deterioration of the financial situation of the leather industry followed.

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## ANALIZA SYTUACJI FINANSOWEJ PRZEMYSŁU SKÓRZANEGO W POLSCE W LATACH 2000-2005

**Streszczenie.** Celem pracy była ocena sytuacji finansowej przemysłu skórzanego w Polsce w latach 2000-2005. Materiał badawczy stanowiły dane pochodzące z opracowań GUS, jak: Bilansowe wyniki finansowe podmiotów gospodarczych oraz Wskaźniki finansowe podmiotów gospodarczych z lat 2000-2005. Wstępną ocenę kondycji finansowej branży skórzanej sporządzono na podstawie analizy bilansów. Ponadto, stosując wskaźnikową analizę danych, zbadano płynność finansową, zadłużenie, rentowność oraz sprawność działania przedsiębiorstw przemysłu skórzanego. Na podstawie przeprowadzonych badań można stwierdzić, że zmieniła się liczba oraz struktura jednostek w branży. Nastąpiła poprawa w strukturze majątku oraz źródeł jego finansowania. Jednak działalność przedsiębiorstw przemysłu skórzanego była obciążona dużym ryzykiem finansowym. Oceniając płynność finansową stwierdzono, że w branży utrzymuje się zbyt wysoki poziom zapasów, w których jest zamrożony kapitał obrotowy. Ponadto przedsiębiorstwa przemysłu skórzanego miały trudności z generowaniem przychodów z kapitału zainwestowanego w majątek, a także źle wykorzystywały dostępne aktywa obrotowe. W przyszłości istnieje jednak szansa na zniwelowanie problemów związanych z regulowaniem zobowiązań bieżących. Od 2003 roku przedsiębiorstwa branży skórzanej osiągnęły zdolność do generowania zysku.

**Słowa kluczowe:** analiza finansowa, płynność finansowa, zadłużenie, rentowność, sprawność działania, przemysł skórzany

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