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# Liberal Reformism and Declining Capital Formation in Hungary:

## *The Developing Capitalist Sector Is Its Only Frontier But This Threatens the Party Dictatorship*

By JOHN B. HALL\*

ABSTRACT. Of countries noted for having an Eastern type of *economic system*, Hungary is commonly touted for the successful, market-type *reforms* applied to the management of its economy. The commonly held notion that these reforms have been successful is challenged. It is argued that the reforms have never been implemented as was intended, and this has consequently resulted in macro and microeconomic *planning* policy to be administered in a varying fashion; also that the new direction in planning policy is seeking to implement fundamental changes regarding the formation and growth of *private enterprise* as a response to the problems facing Hungary's State-owned sector. This development is noted to be causing profound changes in Hungary's economy, while also having a disequilibrating effect on the composition of classes in Hungarian society.

### I

#### Introduction

OFFICIAL ECONOMIC REFORM in Hungary owes its existence to the New Economic Mechanism (N.E.M.) established as law in Hungary beginning on January 1, 1968. The N.E.M. sought to reform Hungary's industrial sector which, up until that time, was organized and managed according to the Soviet-type model that Hungary inherited after World War II. The 1968 Reform made enterprises autonomous and profit-maximizing economic units. Central determination over resource allocation was replaced with the indirect controls of an enterprise regulation system which was to operate under conditions of uniform State control.<sup>1</sup> This meant that the economic regulators: wages, subsidies, and taxes, were to be centrally determined and uniformly enforced by the central planning offices

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in order to coerce enterprises to produce efficiently and in accordance with central macroeconomic planning objectives.

The 1968 Reform sought to alter the vertical character of the centralized economic planning that had been used up until then in the management of Hungary's economy. The preconditions were created for initiating freer exchange in materials and products between and among enterprises. In effect a market system was brought into being; yet, a system which had to operate within a defined set of institutionally imposed constraints.

An additional and equally important dimension of the Reform was committed to strengthening the multisector character of Hungary's economy by effectively removing obstacles which had slowed the development of the cooperative sector and small-scale private activities. In principle, the Reform sought to encourage development of a complementary relationship among the State, cooperative, and private sectors, so that one might foster the development of the other. A final and often under-emphasized dimension is that the Reform intended that, concomitantly with the increasing of enterprise autonomy, there would also be an ". . . expansion of the democratic rights of workers in determining the operation of enterprises."<sup>2</sup>

The 1968 Reform effectively altered the management of Hungary's economy since it sought to decentralize control over production through making enterprises autonomous from the Center.<sup>3</sup> Independent enterprises would decide their own production profiles and produce with the motivation of enterprise profitability in mind. The Center would maintain its centralized role in appropriating surplus from the enterprises by using as economic regulators the setting of wages, subsidies, and taxes. After the 1968 Reform, any surplus produced in the industrial sector could effectively be appropriated from the enterprises through selective policies, the most direct of which was taxation of enterprises' profits. In short, an enterprise would pay a percentage of profits as tax revenues to the Center. A significant contribution of the 1968 Reform was that capital accumulation would take place through a developing financial system.

Though Hungary's 1968 Reform is an important contribution to institutional change and socialist innovation, the Reform's success is questionable. Criticism has been directed against its comprehensiveness. It is argued that, at best, the Reform was only partial, since the capital and labor markets were essentially unaffected. Also, the institutional hierarchy characteristic of the pre-reformed, Soviet-type planning remained intact and prevented the Reform from realizing the full benefits of economic decentralization.<sup>4</sup>

From a different perspective, it has been argued that the 1968 Reform, as promulgated, was not effectively implemented. Contributors to the discussions

surrounding the Reform have taken the position that a recentralization actually occurred during the 1970s, and thus both the intentions and practical implementations of the Reform were rescinded. One variant of this position argues that the aspirations of enterprises came to be expressed through the interests of higher echelons of the planning administration. This resulted as the Council for Mutual Economic Assistance (CMEA) contracts continued to be arranged by top administrative officials. Since CMEA trade is often based on bilateral trade and commodity quotas, microeconomic decision criteria of the enterprises were thus subsumed under higher level, ministerial interests.<sup>5</sup> A second variant argues that a recentralization occurred as enterprises were assigned "responsibility for supply" for producing commodities for the domestic market in accordance with administrative requests.<sup>6</sup>

The Reform's failure to alter the traditional institutional hierarchy, combined with an unofficial recentralization program that began in 1972, effectively left Hungary's economy in reform limbo. However, even to this day, the 1968 Reform has never been officially dismissed in Hungary as it was in some other Eastern countries.<sup>7</sup> This gives rise to the important question: "If the Hungarian economy is not operating by the principles of the landmark 1968 Reform, how, or by what design, is the economy currently functioning?" In attempting to answer this question, what will be noted is that significant changes are taking place in Hungary. The institutional conditions under which a surplus is being produced, appropriated, and reallocated are changing. Also, accompanying such changes are observable changes in the social relations of production and the composition of class in the society.

## II

### **Regulator Bargaining**

WHILE THE 1968 REFORM intended central determination and uniform enforcement of the enterprises' income regulation system, the outcome in the latter part of the 1970s is that economic planning in Hungary came to be supplemented by a case-by-case, or enterprise specific, regulation system. That is, the determination of the economic regulators, wages, subsidies, and taxes, became the subject for negotiation between the Center and the enterprises.<sup>8</sup> In other words, the economic regulators became the important variables negotiated and bargained in planning agreements between the Center and the enterprises.

This phenomenon is related to the institutional nature of Hungary's economy. Hungary, since its founding as a peoples republic, has sought a planning system which promotes the rapid expansion of industry. Even though the accounting

category, enterprise profitability, was introduced in Hungary with the 1968 Reform, it is not used as is the concept of profits in the West. Indeed, enterprise profitability plays a negligible role in determining the success or failure of an enterprise. There is no bankruptcy rate to speak of in Hungary.

This is related to the political nature of Hungary's socialist system which has effectively integrated State and economy into one unit. In this marriage of State and economy, if one partner fails, the other stands likely to fail as well. Given the circumstances of Hungarian socialism, the proclivity for an enterprise to become insolvent is far greater than for the State to face insolvency. Thus, the implication of this marriage is that if enterprises are failing by bankruptcy and closing their gates, problems are created for the State. Consequently, we can observe that enterprise survival is inextricably intertwined with the State's attempt to make good its program of ensuring stable employment with rising real incomes, and increasing levels of consumption for the population. Enterprise insolvency threatens such a program.

In an attempt to preserve face, the State, acting through the system of economic planning, has consequently fallen into a case-by-case financing approach to enterprise management so as to prevent insolvency. The result is that the economic regulators are not uniformly determined, but are negotiated instead.<sup>9</sup>

The economic situation changed somewhat as the world recession, beginning in 1981, produced a serious stagnation in Hungary's economy, a stagnation from which the economy still shows no signs of recovery. The world crisis can be traced to policy measures taken by the United States which concomitantly combined high Federal Reserve discount rates and a restrictive monetary policy. High interest rates and "tight money" effectively precipitated the general downturn of the World's economy and brought about the shrinking of some of Hungary's important export markets. Particularly affected were agricultural exports to the European Economic Community. The loss of some important hard currency-export markets, combined with tight international credit, created a foreign liquidity crisis for Hungary. At this crucial time, planners found themselves with limited resources to distribute even though enterprises' need for subsidies increased. Consequently, the bargaining system as it had been known in the late 1970s effectively fell apart as enterprises pushed for subsidies which the State, because of the crisis, did not have.

Also during the early 1980s, a major price reform was adopted. However, the unconscious consequence of the situation at that time was for policy-makers in Hungary to opt for a solution by which enterprises would have to be financed by other individual enterprises and not the State, their traditional source. This meant that industries would have to pay higher prices for their purchased inputs

into production as costs were passed on through increasing output prices. Thus the situation changed from one of State subsidization of industry to the case in which enterprises adjusted (raised) their prices, thereby passing on costs to their customers, other enterprises.<sup>10</sup>

What must also be considered is that in the early 1980s, there was adopted a policy of parallel pricing as an integral part of the price reform. This policy meant that export products would be priced according to a world market formulation, essentially meaning that the prices of Hungarian export products were set in relation to the average of world market prices for identical products. While this occurred, prices for the exact same goods produced for and sold in Hungary's domestic market would fluctuate parallel with the enterprise's export prices. However, problems began to emerge as Hungary's export prices were forced downward during the world recession in the early 1980s, in the attempt to keep these products price competitive in world markets. In addition to this, and in accordance with the rules of parallel pricing, domestic prices were reduced along with export prices. In principle there should be no discrepancies with such an arrangement, but in practice, prices were reduced in Hungary's domestic economy even for goods that faced chronic short supply. The consequence was a pricing rule which went completely against the logic of market principles. Such an irrational system of parallel pricing occurring during the time of a worldwide recession, effectively undermined the application and enforcement of Hungary's price reform.<sup>11</sup>

### III

#### **Crossing the Capitalist Frontier**

THE LEGITIMATIZATION OF A PRIVATE SECTOR is one significant dimension of the liberal reform tendency in Hungary.<sup>12</sup> Ever since the founding of the Peoples' Republic of Hungary in 1948, there have always been some small shopkeepers and agriculturalists who were allowed to operate independently of the State sector. Accompanying these few legally sanctioned activities, some gray and black market activities have profited by providing goods and services against the general wishes of the State, as expressed in its legal codes. What is new and different about the establishment of an "official" second economy is that the State has now given legal sanction and protection to small capitalists activities. Thus the law enacted in January of 1982 has brought what previously might have been black and gray market activities into the open, making some of them legitimate and also subject to government taxation.

Hungary's private sector can be broadly divided into rural and urban activities. The growing of food on private plots and the selling of these products in free and open markets is one common rural second economy activity. In the urban setting there has also arisen numerous small, independent enterprises that specialize in performing tasks for the service sector. These include the running of restaurants and catering, taverns, car repair, and language instruction, to name the general categories of activity.

By design, second economy activities can generally be noted as jobs which, by their economic nature, are best performed by small, independent enterprises. For example, the growing of many specialty vegetables, a common rural activity, is done more effectively by flexible, independent producers, who, working under the influence of the profit motive, can provide the quality care and timing needed for producing marketable vegetables. In the case of language teaching, a common urban second economy activity, private tutors and small language institutes employing a few language teaching specialists, can accommodate the teaching needs and time schedules of the working population, more effectively than can the State educational system. For the largest part, second economy activities supplement activities already provided by State-owned and managed institutions.

One important exception to the second economy rule is the construction of private flats and houses. This is probably the single most important and least researched second economy activity in Hungary today. The emergence of construction businesses has been spurred by a recently adopted policy which frees the State from the responsibility for building apartments and houses for individuals and families. Such a policy has effectively created a dynamic market for fledgling construction industries which are quickly changing the face of some parts of Budapest and some smaller cities.

However, restrictions limit the expansion of Hungary's second economy. State policies do not allow the capital market to develop to the extent necessary for raising investment and operating capital sufficient for fledgling firms to expand at a scale which would bring them in a position to effectively out-compete State-owned enterprises in important areas of the economy. After some years, the private construction industry may emerge as a group of dynamic and capital rich companies, but this still remains to be seen. Currently, second economy firms tend to participate in peripheral operations that make some contribution towards the performance of the service sector. For example, in Budapest one now has a choice between riding in a taxi owned by a State firm and driven by a State employee, or in a taxi owned by a "socialist entrepreneur" and driven by an employee of a private, second economy firm. Likewise, one may choose between having one's automobile repaired in a shop owned by the State and repaired

Table 1  
 NATIONAL INCOME (NET MATERIAL PRODUCT)  
 BY SOCIAL SECTOR

<u>Sector</u>	<u>1970</u>	<u>1980</u>	<u>1983</u>	<u>1984</u>	<u>Percent Change From 1970-1984</u>
Socialist Sector	97.4	96.5	94.9	94.5	-2.8
Of which:					
State	70.7	69.8	67.3	66.1	-6.5
Cooperative	23.6	23.0	23.2	22.9	-3.0
Subsidized Farms of Employed Persons	3.1	3.7	5.1	5.5	77.4
Private Sector	2.6	3.5	5.1	5.5	111.1

Source: Statistical Pocket Book of Hungary, 1985. Budapest:  
 Statistical Publishing House, 1986, p. 97.

by a State employee, or in a private shop and repaired by a mechanic with no employment connection to the State. Creating a competitive relation between some State enterprises and second economy firms is done with the intention to encourage better resource allocation, while also promoting a better performance of State-owned activities. To date, there are no noted cases in which second economy activities have driven State-owned companies out of business.

Statistics indicate that in 1985, private economic activities from both private plot farming and urban activities produced 11 percent of national income measured as net material product. Though 11 percent is relatively small when compared to the 66.1 percent produced by Hungary's State sector, what is crucial to note is that private activity is the only growing sector in Hungary's economy. From the years 1970 to 1984, private economic activity, as percent contribution to national income, increased 111.1 percent, while the contribution from subsidized farms of employed persons increased 77.4 percent (see Table 1).

This marks a rapid growth in Hungary's private sector both in terms of its respective sectoral growth, and its growth as an increasing percentage of the total sectoral contribution to national income. Also, if we examine the differences in employment between the socialist and private sectors during the fifteen year period from 1970 to 1985, we find that the total number of employed persons in the socialist sector decreased from 4787.6 thousand in 1970 to 4684.3 thousand in 1985, a decrease of 103.3 thousand workers, which is a 2.2 percent decrease (See Table 2). As the number of workers in the State sector decreased, the



number of workers in the socialist sector increased from 201.1 thousand in 1970 to 228.6 thousand in 1985, an increase of 27.7 thousands workers, that is, a 13.8 percent increase (see Table 2). Though this group is only 0.60 percent of Hungary's total working population in 1985, the relative weight of this group makes it especially significant because it means that almost 28 thousand more workers are earning a portion or all of their income independent of the State. Moreover, since 1982 this group of private sector income earners has a degree of official sanction and protection in the form of legal statutes. Thus, what we find in Hungary currently is the emergence of a new capitalist class earning, in many cases, significantly higher incomes. Perhaps as important, this group has a degree of real autonomy from the State with respect to consumption. Those earning higher incomes through the second economy are also the main consumers of the new houses and flats built by the emerging second economy construction firms, as well as the main consumers of services offered by other second economy firms.

Though the second economy is still small with respect to its percentage contribution to national income and as a percentage of total employment, it is, nonetheless, the fastest growing sector. This is occurring while the socialist sector, as a whole, is not only stagnating, but is actually declining both with respect to its total contribution to net material product and to employment. The second economy is the only sector which shows any signs of expansion since 1980 (see Table 2).

#### IV

#### **Class and Socialist Development**

TWO DISTINCT PHASES of socialist development can be differentiated in the case of Hungary. The 1968 Reform officially ended the first development phase that was based on economic expansion by means of material appropriation, organized through the method of material balance planning. The second phase is somewhat more difficult to discern, because the reform was incomplete in that it failed to alter the institutional hierarchy or change, in any significant way, the capital and labor markets. In addition, this incomplete reform was unofficially rescinded in 1972. This unofficially rescinded and partially revived, half-way reform has resulted in a system of economic management operating under an unofficial and unsanctioned system termed regulator bargaining.

What remains to be examined is how the relations of production have been altered during the two respective phases of socialist development discussed above. Yet, a discussion which ties the relations of production and the notion

Table 2

ACTIVE EARNERS BY BRANCHES OF THE NATIONAL ECONOMY  
(IN THOUSANDS OF FORINTS)\*

	<u>1970</u>	<u>1980</u>	<u>1985</u>	<u>Percentage Distri- bution of 1985</u>
Industry	1813.2	1697.3	1539.5	31.3
Construction	370.0	403.6	356.4	7.2
Agriculture and Forestry	1216.9	1038.9	1035.1	21.1
Transport, Post and Telecommunications	363.1	407.3	396.1	8.1
Trade	394.7	488.1	508.8	10.4
Personal and Economic Services	137.8	196.5	214.8	4.4
Sanitary, Social, and Cultural Services	382.4	535.5	560.5	11.4
Public Administration and Other Services	251.5	229.7	223.5	4.5
TOTAL	4988.7	4900.2	4684.3	95.3
Of which:				
Socialist Sector	4787.6	4900.2	4684.3	95.3
Private Sector	201.1	173.4	228.6	4.7

Source: Statistical Pocket Book of Hungary, 1985. Budapest:  
Statistical Publishing House, 1985, p. 26.

\*One forint is equal to slightly less than U.S.\$ 0.50 in 1985

of class to the phases of socialist development is much more difficult to undertake. This difficulty arises because the "real existing socialism," as can be observed in the case of Hungary, deviates sharply from the principles outlined in the classical political economy literature on the subject of socialism.

Critiques of Hungary's real existing socialism can focus on the perpetuation of commodity production, the survival of a centralized and powerful bureaucracy, the national framework, and the degree to which these features effectively restrict the development of institutions through which the "proletariat" might express their will on the direction of Hungary's socialist system.<sup>13</sup> The degree to which the voice of labor as expressed through soviets and labor unions has been controlled by the interests of the centralized bureaucracy is worth noting. What has

resulted is that the system of economic planning has been used to restrict market relationships in an effort to lessen the economic alienation associated with commodity production. This strategy has essentially failed to lessen alienation, since an observable class hierarchy effectively prevents the "proletariat" from realizing their power.

Classes in Hungary can be broadly disaggregated into the industrial working class; the peasantry working on State farms, agricultural cooperatives, and private farm plots; persons in intellectual, that is, non-manual professions; retired persons; small capitalists; and those in the bureaucratic strata.<sup>14</sup> At the top is a bureaucratic strata working through the offices of the central planning system. This class attempts to perform the task of regulating the rate of exploitation, surplus appropriation, and the division of the surplus between and among uses such as consumption and investment. The bureaucratic class also determines wages and the largest share of commodity prices, and thus the levels of consumption for the population. In addition, the bureaucratic class regulates the system of privileges which are discriminately allocated in exchange for individual and class allegiance to the perpetuation of the status quo.

Important contributions have been made towards analyzing the class structure of existing socialist societies. Leon Trotsky, writing as early as 1923, was moved to criticize the problems facing Soviet socialism associated with the rise of an omnipotent bureaucratic strata intent on entrenching itself at the top of the Soviet system.<sup>15</sup> Referring to this group as the "new" class, Milovan Djilas cited its rise both in the Soviet Union and in his independent communist homeland of Yugoslavia.<sup>16</sup> Inspired by the intellectual tradition established by György Lukács and the Budapest School, György Konrad and Ivan Szelenyi have extended Djilas's analysis by arguing that the origins of this "new" class stems from the intelligentsia.<sup>17</sup>

Also in the tradition of the Budapest School, a recent contribution by Ferenc Feher, Agnes Heller, and György Markus argues that the bureaucratic strata in the "real existing" socialist countries survives by maintaining a dictatorship over the needs of the population.<sup>18</sup> This is observable as a bureaucratic strata engages in regulating the rate of exploitation through wage and price policies and influencing the composition of the labor force participation through such mechanisms as keeping wages at a level which requires that both husband and wife must enter the labor force and continue working. Consumption levels are also regulated and were noted to be unbearably low during the early phase of socialist development in Hungary in the 1950s. While the consumption levels were kept low, it is also noted that between 1949 and 1955 20 percent of gross output was wasted in the heavy industrialization program. In the earlier phase

of Hungary's socialist experiment, the high investment rate sometimes approached 30% of national product. However, the generally low rate of return combined with the wastes associated with State investments are a dimension of socialist history which now tends to be downplayed by Hungary's leadership.<sup>19</sup> Such mismanagement and waste of precious capital have kept the consumption standards of the population so low and the sphere of civil liberties so restricted, that only the hardest pressed of countries would deem such a program enviable.

The important question to ask regarding Hungary's socialist program is: Why have the goals outlined in the classical political economy literature not yet been achieved? In seeking to answer this, it would be useful to consider the argument that the transition time between underdeveloped capitalism and pure socialism is going to be longer than four or five decades. However, this fails to acknowledge that Hungary's socialist program is effectively moving in the opposite direction, that is, towards a mixed economy composed of a State sector run by the bureaucracy and a private sector run by independent entrepreneurs.

In Hungary, the primary goal of the State is really not economic development, but, rather, the maintenance of political hegemony by the bureaucratic strata, which can be seen to express itself through a ruling faction of the communist party. Admittedly, economic development plays a role in class preservation since it serves to stabilize the economic and social system. If there arise problems in the economic program which become translated concretely into falling consumption levels, this tends to create a crisis for the whole system. This is especially observable when nutritional standards decline. The political uprising in Hungary in 1956 was related to many factors, but declining nutritional standards played an important role. It can be observed that the subsequent reforms in 1957 intended, as an initial solution to the 'economic' problems, to alleviate the bottlenecks in food deliveries which peasants either failed to produce because of the negative consequences of overcentralization on production decisions, or actually withheld because of the peasants' general discontent with the heavy industrialization program advocated by Matyas Rakosi, the leader of the Communist Party at that time.<sup>20</sup> We can also judge the case of Poland as symptomatic in this respect. The rise of Solidarity and the independent trade union movement there was jolted into direct action by the rising meat prices in Poland in the summer of 1980.

The Hungarian case, though, remains somewhat unique. The sovietological literature uses the term "Kadarism" to characterize the compromise program in Hungary.<sup>21</sup> Kadarism is based on a compromise between the government and the population in an unofficial contract drawn up after the uprising in 1956 in which an estimated 20,000 civilians were killed. The core of the compromise

seeks to ensure the population with steadily rising incomes and improving consumption standards, provided the populace refrains from active street politics which threaten the geopolitical alliance with the Soviet Union. One point which provoked the Soviet invasion in 1956 was the declaration of neutrality which went against the principles of the Warsaw Pact Alliance.

Given the nature of the compromise which has kept peace in Hungary from 1957 onwards, there can be observed some potential tensions building up in Hungary's social system related to emerging economic difficulties. Statistics indicate a secular decline in total investments. Measured at constant prices, the level of total investments put into operation has fallen at an average rate of 5.3% every year from 1980 to 1985 (see Table 3).

While this has occurred, consumption measured in constant dollars has remained at parity, and actually shows a small increase in the service sector (See Table 4). Though consumption standards have been maintained, we can observe,

Table 3

CAPITAL ACCUMULATION AS MEASURED BY INVESTMENT  
IN THOUSAND MILLION FORINTS AT CURRENT PRICES

<u>Year</u>	<u>Investment of Socialist Or- gans</u>	<u>Investment of Population</u>	<u>Investment Total</u>	<u>Total Invest- ments Put Into Operation</u>
1980	189.7	23.7	213.4	202.8
1981	182.8	26.6	209.4	196.7
1982	185.5	29.8	215.6	196.8
1983	188.1	36.1	224.2	223.1
1984	188.8	42.7	231.5	223.3
1985	190.8	45.8	236.6	215.7
PREVIOUS YEAR = 100.0 (AT CONSTANT PRICES)*				
1981	93.6	104.0	94.8	94.8
1982	96.9	104.0	97.8	95.9
1983	94.8	111.3	97.0	108.1
1984	95.2	107.1	97.1	98.6
1985	95.6	97.7	95.9	86.3

Source: Statistical Pocket Book of Hungary, 1985. Budapest:  
Statistical Publishing House of Hungary, 1986, p. 100.

Table 4  
 PER CAPITA CONSUMPTION  
 (PREVIOUS YEAR = 100.0 AT CONSTANT PRICES)

<u>Year</u>	<u>Total</u>	<u>Of which: Food Stuffs</u>	<u>Beverages Tobacco</u>	<u>Industrial Goods</u>	<u>Services</u>
1981	102.6	101.5	100.9	103.5	104.0
1982	101.3	101.0	101.5	100.2	103.1
1983	100.7	101.4	98.7	99.4	102.6
1984	101.4	100.0	101.0	101.6	102.8
1985	101.2	100.3	102.3	100.7	102.2

Source: Statistical Pocket Book of Hungary, 1985. Budapest:  
 Statistical Publishing House of Hungary, 1986, p. 33.

according to the officially published statistics, that the declining investment program indicates that the Hungarians are essentially consuming (eating up) their surplus, causing a real decline in new investments.

## V

### Discussion

THIS RAISES some very important questions regarding Hungary's future. In the not too distant future, we can expect that the effects of declining investments will be realized as out-moded production capacities cause a serious technological lag and hence a decline in labor productivity, thereby causing real incomes and consumption standards to fall, especially for those persons employed in the State sector. Provided that the world economy retains its slow rate of growth and world trade remains as competitive as the current level, both of which will likely continue, the important question then becomes whether the Kadarist compromise, which is essentially the glue holding Hungary's society and political program together, will fail. If this be the case, then one of three policy postures is likely to be observed.

In the first policy posture, the government would implement austerity measures while simultaneously limiting civil expression of the discontent. This would keep the populace compliant with a deteriorating economic situation resulting from falling real incomes and declining levels of consumption.

A second policy posture might choose to quicken the pace of economic reform. This would include adopting such proposals as a full reform of the banking system and the creation of capital holding institutions which would base in-

vestments on profitability as opposed to other goals.<sup>22</sup> The hope is that such a reform program would increase the rate of economic growth. Capital could then be reinvested so as to offset effectively the current problem of declining capital formation in the State sector.

A third policy posture would promote a more rapid development of the second economy, which since its legitimation in 1982, has provided an important outlet for workers caught in stagnating industries in which real wages are tending to fall. The Hungarian Socialist Workers' Party (H.S.W.P) is courting the second economy because it provides one easy way to take some of the heat from the unsettled compromise between the population and the powers in the Party without having to endorse official, reformist solutions. Essentially, controls on economic activity can be relaxed, thereby allowing the socialist entrepreneur to use his or her own clever initiative to increase real household incomes.

This leads to the concluding point about Hungary and its economy. The growth and dynamism of Hungary's State sector at this conjuncture of the postwar world economy are literally at a dead end. There currently appears to be no possibility of further economic growth and expansion in that sector. This is related to a larger systemic problem related to socialist development, generally.

The extensive phase of socialist development which was based on rates of investment reaching as high as 30 percent of national income and growth rates as high as 10 percent is now history. Such a high rate of investment and double digit growth rates could occur concomitantly with the world expansion in the 1960s. This extensive phase of socialist development mainly involved moving the feudal or petty capitalist activities into relatively modern production systems. Also small scale peasant producers were incorporated into State farms and co-operatives, while artisans were incorporated into a system of factory production. The already large production organizations were nationalized and expanded further. Hungary's economy simply latched on to the postwar economic growth phase in the 1960s.

However, the extensive phase of Hungary's economic growth, has never recovered from the effects of the oil crises beginning in 1973, and the general slowdown of the world economy since that time. Moreover, since the mid-1970s, its economy has essentially been stagnating, while periodically contracting from the effects of ever recurring and ever deepening world recessions. Chronic slow growth has caused the intensification of protectionist tendencies on international markets in which Hungary's agricultural products and industrial goods must compete. Combined with this foreign exchange bottleneck, the foreign indebtedness, and the bureaucratic nature of Hungary's socialist system, the

prospect of an intensive phase of industrialization is highly unlikely, at least for the State sector.

The standing solution rests on the fact that the developing capitalist sector is Hungary's remaining economic frontier. The degree to which it will be used in the future will have profound implications with regards to the social relations of production under which capital formation is to take place in the economy, and this, in turn, will continue to have a disequilibrating effect on the composition of classes in the society.

#### Notes

1. Marton Tardos, 1984. "The Development Program for Economic Control and Organization in Hungary," *Eastern European Economics*, 22 (3-4): 7.

2. *Ibid.*

3. The term "Center" appears in an article on mathematical programming by J. Kornai and T. Liptak [*Econometrica*, 1965]. In this article, the Center, though not clearly defined, represents the administrative unit assigning the allocations to the sectors. Teresa Laky [*Acta Oeconomica*, 1980] developed the notion of "Center" to a greater degree by describing it as a complex inter-relationship of the higher levels of administration in Hungary. She includes institutions such as the Council of Ministers and National Planning Office in her use of the term. Laky's conception of "Center" is being used in this paper.

4. Both of these points are argued by János Kovács in "Reform Bargaining in Hungary: An Interview with János Mátyás Kovács," 1986. *Comparative Economic Studies*, 28 (3): 25-6.

5. Thomas Bauer, 1976. "The Contradictory Position of the Enterprise Under the New Hungarian Economic Mechanism." *Coexistence*, 13 (1): 65.

6. László Antal, 1979. "Development with Some Digression: The Hungarian Economic Mechanism of Recentralization in Hungary," *Acta Oeconomica*, 23 (3-4): 255.

7. The case of the German Democratic Republic provides one useful example. The G.D.R.'s economic reform of the late 1960s intended to decentralize the system of economic planning and management. In 1972, this reform was completely rescinded and the planning returned to the orthodox Soviet-type, command model.

8. John B. Hall, 1986. "Plan Bargaining in the Hungarian Economy: An Interview With Laszlo Antal." *Comparative Economic Studies*, 28 (2): 50.

9. These ideas which appear in the interview with Antal (fn. 8) are more thoroughly elaborated in his book *Gazdaságirányítási és pénzügyrendszerünk a reform után (The Changes in Our Economic Policy and Monetary System in Connection with the Reform)* (Budapest: Közgazdasági és Jogi Könyvkiadó, 1985). The interview was conducted shortly after the book's publication. A review of Antal's book appears in English in *Soviet Studies*, 1986. 38 (3): 445-6, by the present author.

10. *Ibid.*, p. 51.

11. *Ibid.*

12. The most comprehensive and recent study of Hungary's second economy to date is by Péter Galasi and György Sziráczyk, eds., 1985. *Labor Markets and Second Economy in Hungary*, Frankfurt and New York: Campus Press.

13. Thomas Bauer, 1984. provides a penetrating analysis of some of the short-comings of Hungary's "real existing socialism" *vis-à-vis* those goals found in the classical political economy



literature. The points expressed in this paper are borrowed from Bauer's article. See Thomas Bauer, "The Second Economic Reform and Ownership Relations: Some Considerations for the Further Development of the New Economic Mechanism," *Eastern European Economics*, 22: (3-4): 33-87.

14. *Statistical Pocket Book of Hungary, 1985* defines social classes roughly in this way, p. 36.

15. Leon Trotsky writing in 1923 noted: "Thence, in large measure, the bureaucratization of the apparatus, which threatens to separate the party from the masses." "Bureaucratism and Revolution," Chapter 4 of *The New Course* (Ann Arbor: Univ. of Michigan Press, 1965), pp. 39-46.

16. Milovan Djilas, 1957. *The New Class: An Analysis of the Communist System* (New York: Frederick A. Praeger).

17. George Konrad and Ivan Szelenyi, 1979. *The Intellectuals of the Road to Class Power* (New York: Harcourt Brace and Jovanovich).

18. Ferenc Feher, Agnes Heller, György Markus, 1983. *Dictatorship Over Needs* (Oxford: Basil Blackwell).

19. *Ibid.*

20. For a detailed and recent account of the changes taking place in Postwar Hungarian agriculture see: Z. Edward O'Relley, 1986. "The Changing Status of Collectivized and Private Agriculture Under Central Planning," *The American Journal of Economics and Sociology*, Vol. 45, No. 1 (January): 9-16.

21. After the 1956 uprising in Hungary, Janos Kadar became Hungary's key political leader. He is noted for ruthlessly dealing with the fates of those who participated in the uprising and also beginning the liberal reform tendency which continues until this day. After the 1956 uprising, Kadar is noted to have made the conciliatory statement: "Those who are not against us are with us."

22. Tardos, pp. 3-32. Bauer, *Eastern European Economics*, pp. 33-87.

### ***Academic Directories of Members***

MEMBERSHIP DIRECTORIES are one of the benefits one receives as a condition of membership in most academic associations. Some of these are more useful than others. The degree of usefulness is largely a matter of the amount of information conveyed and the way it is conveyed. Some directories give breakdowns of members on the basis of state, province and country only. Others give much finer geographical breakdowns. Some indicate departmental chairpersons, others do not. Some give a considerable amount of bibliographical data while others may list only addresses, etc.

It might be time for some organization to take the initiative and have a conference of directory editors and lay out the most desirable kinds of listings. In light of the great deal of change in the means of communication which has occurred, such a conference might produce an electronically available and easily up-dateable listing. There might even be grant money available for such a project or money to be made as a result of it.

F.C.G.