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A Fictitious Discussion by Financial Experts About Hungary's Position in the Changing World

Review of the Book Entitled *Hungary in the Changing World*

Summary
A collection of interviews with Mihály Patai, Chairman of the Hungarian Banking Association, László Parragh, Chairman of the Hungarian Chamber of Commerce and Industry, and Professor Csaba Lentner, Head of the Institute for Public Finance of the National University of Public Service, has been published by Éghajlat Kiadó under the title *Hungary in the Changing World.* In the book, Hungary's economic policy is discussed from the change of regime and the collapse of the Socialist planned economy to the present day, seen from the perspective of the three above-mentioned leading economists. This original and unconventional book examines problems in a complex manner and provides proposals worthy of consideration by political and economic leaders.

Journal of Economic Literature (JEL) code: B10, D6, E6, F01, F34, F5, F6, I2, G01, H6, N13, N5, Y3
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Éghajlat Kiadó has published an extraordinary book with Klára Lengyel as editor: the participants include moderator and interviewer Lajos Péter Kovács, and three interview subjects and discussion partners: Mihály Patai, Chairman of the Hungarian Banking Association, László Parragh, Chairman of the Hungarian Chamber of Commerce and Industry,

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and Professor Csaba Lentner, Head of the Institute for Public Finance at the National University of Public Service. The novelty of the book's content lies in the moderator-interviewer's discussion over the course of nine chapters of Hungary's economic and financial problems, and breakout and development opportunities with the three experts, followed by separate conversations with each of the three interview subjects to enable them to expand upon the deeper interrelationships of their views.

The first topic, *called 'mischief', is about Hungary,* where – as the respondents show – people were able to secure their livelihood by various semi-legal means that were tolerated by and evolved during the Kádár regime. At that time, the state not only put up with these ways but it even supported them. As the interviewees also mention, these means included various economic and corporate economic partnerships and moonlighting performed during or after official working hours, in the course of which company employees in cahoots with one another could obtain additional private income using the material and equipment of state-owned companies. It was under these conditions that spontaneous privatization and official government-controlled privatization occurred before and after the transition to democracy. The experts around the fictitious roundtable of the book also established that the application of various techniques and methods of corruption prevented the government from realizing considerable revenues from either spontaneous or government-controlled privatization, as the majority of foreign companies liquidated the bulk of the companies sold to them and reorganized during the 1980s from loans; in other words, their goal was market penetration rather than the continuing operation of these companies. The speakers also mentioned that Hungarians (with notable exceptions) also acquired considerable business assets through corruption, although most of them were squandered instead of being turned into businesses. This was also characteristic of the newly-established commercial banks, which granted a considerable quantity of long-term loans nearly free of charge to people within the orbit of the former Socialist political elite so that they could make a success of their businesses; for the aforementioned reasons this success was not realized. The commercial banks that went bankrupt because of this had to be replenished from public assets, and due to the government's sales activity they ended up in the ownership of foreign banks and continued their operations as subsidiaries.

In the chapter on this topic, the three specialists mention that after the Soviet Union had run short of funds to support the loss-making provinces of their overgrown empire, Hungary was compelled to take loans from the IMF and the World Bank, and so started to go into debt. In this context it is worth stressing the words of Mihály Patai that after the transition to democracy, negotiations were held about Hungary repaying only the principal amount of the loan, without any interest being accrued. Patai merely stated that "József Antall simply stopped the negotiations". He did not mention the weight of either direct pressure by the US or the indirect pressure placed on him through the Social Democratic Party. In my opinion, the Social Democrats and

József Antall, who cooperated with the US and the Social Democratic Party, are completely responsible for the fact that, unlike Poland, we are still burdened by debt servicing.

Quite rightly, Csaba Lentner pointed out that after the transition, there was only one option: the adoption of a market economy. However, according to the professor of economics, the problem was that adoption was extremely fast, and the Hungarian population was unprepared for it. As the other speakers also noted, the overwhelming majority of the population wanted to get rich quickly and were incapable of using the partly illegally-obtained wealth in a moderate, disciplined and professional manner, which was manifest in the operation of Hungary's manufacturing, services and banking sectors. Being far more disciplined and capable of rationally enforcing their self-interest, foreign companies and financial institutions could use this for their own benefit and to the country's disadvantage.

Finally, a few words were said about the unconventional economic policy that helped Hungary free itself of dependence on the IMF. In relation to this, Mihály Patai noted that Matolcsy's achievements in central banking and the government's results in financial policy should be termed 'new-orthodox' rather than 'unorthodox'. Everyone agreed, however, that today's generation of middle-aged and older economists still follow the anachronistic neoliberal policy that their instructors taught them.

The second topic essentially carries on from the previous one, and is entitled "MNCs and the friendly zoo". In this chapter the moderator investigates how aggressively the multinational corporations that have come to Hungary are enforcing their interests, to what extent they suppress Hungarian businesses and how much of their operating profits they take away and how much they leave in Hungary. During the conversation it was made clear that, in the course of their operations, foreign manufacturing and trading companies, in the same way as the subsidiaries of foreign banks, provide insufficient help for Hungarian businesses to develop, with most of them only taking care of their own interests and extracting their entire profits from the country. For this reason, though to different extents, the interviewees are positive about the state taxing foreign companies and about it introducing the bank tax. The debaters also pointed out the social problems caused by unfair procedures adopted by foreign banks, as well as by the Hungarian OTP Bank, in the course of forex lending, and by the irresponsible propagation of this lending by the former left-liberal regime, and how the incumbent government and the central bank were able to solve a significant part of the social problems by conversion into forints and derecognition of forex loans.

These government actions led to serious tension between the current centre-right government and MNCs, which the interviewees considered natural. They think the government must take note that companies coming from abroad will primarily consider their own interests but at the same time, these companies must also recognise that the host state and society have expectations of them. For this reason, Hungary's economic policy must attempt to reach a compromise with the companies operating in the country, while respecting each other's interests, in order to secure their long-term presence. This is the only way to develop, on one hand, the useful cooperation between small, mid-sized and large corporations and, on the other hand, the good relations between Hungarian and foreign companies,that will make the allegorical "zoo" become friendly.

In the third topic, entitled "In the wake of global developments", the talk centred on how this current evolved in the past and today, and Hungary's place in this current, specifically its place within the present day global centres of economic and political power. The discussion partners set out from the fact that with the collapse of the Soviet Union, the two power centres, namely the eastern Soviet and the western American, ceased to exist. Consequently, a unipolar economic and political centre evolved with US dominance. At the same time, as László Parragh brought up during the discussion, this unipolar power centre is increasingly being changed into a multipolar one by the economic rise of China and India. The moderator leading the discussion suggests that in this emerging power centre, once again heading towards a multipolar system, a place is being demanded by a renewed Russia that is regaining strength and does not wish to give up its imperial status. Russia and the US are, it is pointed out, fighting a tough battle for the Ukraine, which has been brought into the sphere of interest of the US. At the same time, the Crimean Peninsula, which previously belonged to Russia, has been annexed by it. Located in the buffer zone is the European Union, which placed Russia under embargo at the request of the US. The EU and its Member States will come out badly from this, while the USA profiteers, since – as was established during the discussion – the goods missing because of the EU's embargo will be supplied by the US.

During the discussion the debaters raised the point that in this process of realignment, the EU is becoming weaker despite the fact that the centralisation that began in the US has also started there both in the banking and insurance sector and in industry and services. It also emerged in the discussion that both the oil crisis and the banking crisis that started in 2007 hit Europe harder than the US. The discussion partners provide excellent analyses of both. The relevant professional financial analyses by Patai and Lentner are worth special attention, while the effects on industry and trade are explained by Parragh. Mention is made again of forex lending, which also appeared in certain Western European states, but caused serious financial and social problems mainly in Central and Eastern European post-communist countries. While discussing Hungary's case, the interviewees mention that the transformation of this form of lending through conversion into forints was, from a social point of view, an appropriate solution by the government acting in concert with the National Bank.

Returning to the lines of force, it turned out during the discussion that Hungary, among all of the member states of the EU, is in the most difficult situation vis-à-vis the Russian–American conflict, as it lies on the borderline of the historical cultural areas of the Catholic Western Roman Empire and the Orthodox Eastern Roman Empire, just as has been the case in history going back a thousand years. This was one of the reasons why Hungary had significant markets in the Slavic east, which were lost partly during privatization and partly through the embargo resulting from the Ukrainian conflict. The discussion concluded that the emphasis of Hungarian economic policy should fall on regaining these markets, which is justified by the country's economic geographical situation. All I wish to add is that it was a mistake to incarcerate József Stadler twice for his habitual offending for tax evasion, as he had excellent contacts in the Russian and Ukrainian markets, which were lost after his two periods in gaol. In my opinion, the financially- and politically-sound solution would have been the imposition of a large fine in the first case, and a suspended sentence, a fine and the enforcement of the payment of the unpaid taxes in the second case. Thus the country could have continued to benefit from him and his activities.

In the fourth topic the discussion partners dealt with the benefits of the adoption of the euro for the countries that have joined the euro area and the disadvantages, or possibly benefits, for those who have not. The related analyses focused heavily on Hungary. The various governments of Hungary put accession to the euro area on the agenda, and then extended its deadline on several occasions due to failure to meet the requirements. As this failure became permanent, the country has not joined the euro area. The reasons for Hungary not meeting the accession criteria are explained in detail and at length by Csaba Lentner, and the consequent disadvantages are summed up by Mihály Patai. During the discussion of the related correlations, further mention is made of the Russian–Ukrainian conflict and how the EU built a trap for itself with the embargo, weakening the euro with respect to the US dollar.

Lajos Péter Kovács mentions that highly conflicting developments are taking place in the euro area because the strengths of the participating economies vary. Csaba Lentner points out that the European Central Bank endeavours to strengthen economically weaker states by purchasing the sovereign securities they issue. In László Parragh's opinion, the problem in these states is that, due to the weakness of central authorities, structural reforms have been postponed, and this has resulted in a very high unemployment rate. In order to strengthen the euro, the debaters believe that this situation must be changed.

The fifth topic of the fictitious discussion tackled *the question of the revival of regions.* László Parragh thinks Hungarian foreign policy has "led to a dead-end" in this respect. He explained that Poland has adopted a maverick economic policy, and has markets of its own, although Galicia is its only region that once belonged to the Austro-Hungarian Empire. For this reason Hungary does not belong to the same region as Poland. Hungary would form a region with Romania, Slovenia, Serbia, Croatia, Slovakia and Austria. However, Austria, which can be classified as part of this region, would regard Hungary and the other aforementioned Central European countries as if they were colonies. Romania represents an opposing position to Hungary and most of the other Central European counties on the migrant issue and in other respects. Moreover, as referenced in the book, due to the suppression of the rights of Hungarian minorities living in the neighbouring countries, Hungary has serious conflicts with Romania and – on this question – with Slovakia. As for Serbia and Croatia, there are no problems in relation to the Hungarian minorities living in these countries, but there are considerable differences in approach to stopping the pressure of migration, as was also alluded to during the discussion. It should be noted, however, that since the publication of the book (in the summer of 2015), a favourable change has taken place in this respect in Austria, Croatia and Serbia.

Lentner and Parragh established that Hungary does not cooperate, or try to cooperate, with the countries in its own region. Nevertheless, the roundtable also ascertained that there are considerable differences in the standards of the various countries classified in this region, and that these should be levelled out. Here, the conversation partners alluded primarily to the advantage of Slovakia, a member of the euro area, over Hungary, which is outside the euro area. The discussion partners arrived at the conclusion that Hungary should first and foremost close the gap by reducing these drawbacks, analysing foreign solutions and taking them into consideration. The banking system, tertiary education, the management of unemployment and the promotion of employment should be reformed to a certain extent on this basis. Regarding the promotion of employment, all of them were of the opinion that the significant proportion of community work areas which still remain unproductive should be channelled in a useful direction, primarily towards production. They went into more detail about the proposals affecting the economic and financial system and already mentioned in the previous topic.

The sixth topic of the roundtable discussion concerned *bank loans, growth* and *opening to the east.* The conversation started with a historical reference to the transformation of a single-tier centralised Hungarian banking system into a two-tier one in the second half of the 1980s, with the second tier, called commercial-economic, initially lending to consumers and the business sector alike. It was also mentioned that due to irresponsible lending made with all-too-favourable conditions, second-tier banks, with the exception of OTP Bank, went bankrupt and needed recapitalisation before they were sold to foreigners. OTP Bank was also sold, but the internal management was given a significant role. The Hungarian subsidiaries of banks sold abroad – as mentioned several times during the discussions – sent a considerable part of their operating profits to their parent banks. The problems caused by forex lending were repeatedly mentioned, as the foreign parent banks do not assume any liability whatsoever for such transactions.

As to the character and role of Hungarian capitalists, the debaters find them rather uncreative, as they came into existence through state support rather than with their own resources. An argument developed about the political affiliation of the new Hungarian capitalists. Csaba Lentner is of the opinion that over the longer term they are shifting towards the right, which is, however, contested by the other two discussion partners based on the assumption that this layer of society is always rationally attracted to the side that can best serve its interests. In relation to this, László Parragh suggested, and Mihály Patai agreed, that a Hungarian business stratum should be created. In response, Csaba Lentner mentioned that in the framework of the Funding for Growth Scheme, the National Bank of Hungary has invested several thousand billion forints into Hungarian businesses, primarily SMEs and small agricultural producers.

The discussion also covered the issue of a correlation between company subsidies and corruption. The question was raised of whether the assignment of the majority of public procurement tenders to a single company should be considered as corruption. In Mihály Patai's view the misgiving related to this are unfounded. Csaba Lentner thinks that corruption is ruled out when the majority of public procurement tenders are granted to a proven company that seems to be the most suitable for fulfilling the mandate.

Opening to the east and the efforts made at penetrating eastern markets were raised as final topics, covering not only Russia, but also a more extensive area including the Middle East. In relation to this, the Russian contribution to the renovation of the Paks Nuclear Power Plant was mentioned, the soundness of which is not disputed by several of the older EU Member States, as they have realized that this is the most efficient solution for securing Hungary's long-term energy supply. The discussion partners also agreed that Hungary needs an economic policy which places equal emphasis on maintaining western economic relations and opening to eastern markets.

The 'fictitious meeting' convened for the seventh topic included a discussion by the three interviewees and the moderator who channelled their conversation about *Hungary's international judgement.* According to Lajos Kovács Péter, the West has a very low tolerance of Hungary, and he asked why this was so. Mihály Patai thinks the West does not blame Hungary for its interest in eastern markets, but they disapprove of the management of the Norwegian Fund, the tax on advertising, the comparison of Moscow to Brussels and its illiberalism. He thinks the most serious problem is the atypical articulation of Hungarian politicians towards the West. On the other hand, Csaba Lentner is of the opinion that the West has no moral basis to criticize us as they are competing against us in eastern markets. László Parragh attributes Hungary's negative image in the West to the fact that Hungarian economic policy broke with mainstream economic policy, and chose to become independent of the IMF through loan repayment, stopping forex lending and the PPP programme. In addition, he thinks that any measure taken in the national interest is a thorn in the flesh for westerners, because they hamper the integrationist goals of Brussels and the US. The discussion arrived at the conclusion that for the West the main problem is that Hungary sympathizes more with an economic system close to social market economy rather than the relentless competition-driven market economy supported by Brussels.

The last discussion was held about *the starting points for the market economy of the future.* To launch the conversation, the moderator asked about the most important factors that need to be considered for planning the future economy. Taking the floor first, Mihály Patai pointed out that the European Union has less than 8 per cent of the world's population but produces 25 per cent of the global GDP, and this situation is untenable over the long term. Consequently, a change is expected and will begin from an "extraneous environment". (Since the time of the discussion, the said change has already started: it is the migration threatening Europe with an invasion. – *T. P.*) Another factor in fast and constant changes is the movement of multinational corporations towards more favourable commodity and labour markets, which has a positive impact on employment when they arrive, although their departure causes serious economic and employment policy problems. In order to avoid the latter, compromise must be reached with MNCs, but efforts must also be made to enable Hungarian companies to expand and take roots abroad. In Csaba Lentner's opinion, primarily agriculture and the food-processing industry should be developed, while László Parragh considers the harmonization of social resources as important in enabling us to manufacture high-level technical devices (e.g. sensors and navigation software) to replace low-level assembly jobs. All three agreed that a positive direction for Hungary's future depends on high-level business and supplier activities. This, however, requires reforms in education, vocational training and healthcare, and improvements in infrastructure.

The second structural part of the volume contains *separate conversations using the same methodology* with László Parragh, Csaba Lentner and Mihály Patai. All three of them gave their opinions about the topics discussed during the roundtable meeting, this time placed in context. For this reason it is unnecessary to repeat them, and only the most important points of view are highlighted below in a synthesis. A discussion conducted with László Parragh is published under the title *Let's Not Stop Halfway,* and with Csaba Lentner as *Compromise in the middle ground...* In the chapter entitled *The Western Roman Empire and Fault Lines,* Mihály Patai went into further detail about the topics he had explained during the fictitious roundtable meeting.

During the conversation with László Parragh, he said that the change in the structure of industry during the Antall regime had a negative impact due to the unwise and sneaky privatization. Whatever the Hungarian elite obtained on the cheap was bankrupted. There was no capital to invest, however they withdrew and used up the companies' capital, and during privatization the overwhelming majority of foreign capital was merely invested to gain market share and consequently ended up in company liquidation. SMEs were unable to develop due to lack of capital. Low revenues flowed into the state budget due to tax evasion, tax allowances granted to MNCs, and chicanery with offshore tax havens. The role of the state was abortive, as illustrated by the government's contribution to forex lending. As a positive development, however, he mentioned the onset and completion of the long dragged-out structural reforms. In relation to their continuation, he notes that a closer link must be established between research, which costs the government a lot, and the economy, and the significant resources need to be harmonized with government cooperation. In addition, small businesses should participate in the economy primarily as suppliers, and should excel in handicrafts, a sector that is currently in an upturn. He thinks that vocational training and trade schools can be efficiently operated to high standards if they are linked to large corporations. So he would welcome the restoration of the system of training workshops and training places.

In the course of the conversation with him, Csaba Lentner explained that the success of the incumbent government results from the unorthodox and good economic policy, which put an end to dependence on the IMF. This is the reason for the attacks from the European Union and from foreign and Hungarian left liberals. However, the government's economic policy, which uses non-conventional instruments, enjoys the support of Hungarian society. With the exception of the Internet tax, this also applies to the new taxation system, as the majority of multinational manufacturing companies are increasingly satisfied with its calculability. Although the Hungarian subsidiaries of foreign banks are unhappy with the bank tax and are threatening to move out of the country, once the Hungarian economy takes a sustainable growth trajectory, they will return, as they may find safe internal markets and business opportunities. Until then, the gap may be bridged with the help of OTP Bank, other banks of Hungarian affiliation and the central bank, which is focusing on growth. Loans for investment in rational production will always be needed. Lentner made a positive statement about the activity of the National Bank under Matolcsy's control. He reminded us that similarly to the US Fed, the MNB has targeted not only cutting inflation, but also reducing unemployment and getting economic growth moving. In an analysis of the current community work scheme he, quite rightly, notes that its current, mainly unproductive, character should be transformed towards the productive. I believe an example if this could be the involvement of community workers in the production of agricultural raw materials. The professor appreciates the MNB's activities in education, foundations and research institutions, and I share his appreciation, as economists are still advocating the orthodox economic thinking learnt from the professors of the previous generation. Regarding tertiary education, similarly to László Parragh, he also presses for the closure of subjects, faculties and tertiary educational institutions with low student numbers and/or offering non-marketable qualifications. However, I would be careful with radical action, and instead of abolition, I find placing humanities (e.g. archaeology, art history, Assyriology, Egyptology) on the back burner a happier solution, even if a low number of students are taught. This is essential, among others things, for maintaining the country's overall cultural standard.

During his interview, Mihály Patai explained that from the 1980s onwards huge financial pyramids were made, first in the United States and then in Europe, and this process stopped somewhere between 2003 and 2005. These giant monsters enabled the financial elite to gain independence from the political elite. In the past three or four years, however, an opposite development has begun: the political elite has retrieved the initiative from the financial elite. He criticized the European political elite for being unable to adequately respond to the American challenges, because the financial concept behind the euro clearly includes political, budgetary and tax union, areas that are experiencing numerous problems, resistance and a deficit of consensus-building capacity. Patai said that to be fair to Swiss franc-based lending, which has spread in the past decade, one must add that it also had a positive role, as 1.2 million families are now living in better homes than they would be without these loans. He added that several independent factors also contributed to the collapse of CHF-based lending, and this relieves the government and the customers, but not the banks, of responsibility. As a criticism, he recalled the political promise that Hungary would join the euro area in 2007. Had employees been paid in euros by the time of forex loan repayment, no problem whatsoever would have been encountered. The chairman of the Hungarian Banking Association considers the government's consolidation measures as the opening up of a new era in banking, and the process of globalisation, which also includes Hungary, as a continuing "process" that cannot be concluded.

All the reviewer wishes to add in summary is that this original and unconventional book examines problems in a complex manner and provides proposals worthy of consideration by the government. The book sheds light on numerous interrelationships.

The English version of the book is forthcoming in 2017.

Mihály Patai – László Parragh – Csaba Lentner: Hungary in the Changing World. Éghajlat Könyvkiadó, Budapest, 2015, 325 pages.