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Consolidating Economic Reforms: the Hungarian Experience with Lessons for Poland

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1. Introduction

"Transition to what?" – this major puzzle of the transformation studies appears to be solved in Hungary. In 1998 the Hungarian social system is democratic capitalism. Viewed in the perspective of the country's own past, this outcome is a success. Between 1989–98 the longest and most democratic period of Hungary's post-World War I history coupled with the most radical episode of economic liberalization it ever experienced.

How to assess Hungary's present situation in the broader context of overall economic and political developments in post-socialist Eastern Europe? The regional perspective suggests that in terms of parting with state socialism and building market democracy Hungary – and a few other countries including Poland – represents the maximum any former socialist state could achieve between 1989–98. While in this respect no country succeeded in getting farther, most other states have struggled with the peaceful or forceful formation of national identity or a new, independent state, which often dominated over and conflicted with, the issues of economic reforms and democratization on the transformation agenda. Another key to success is that Hungary –similar to Poland, but to a much larger extent – became a major target for foreign direct investment. This is due to a number of factors: from Hungary's strategy for debt, macroeconomic management and privatization, to the foreign investors's and creditors's own expectations. However, the resulting large capital inflow had a major impact on the features of Hungarian capitalism. While everywhere in East the new ownership structure displays various combinations of foreign owners, "national capitalists", and the scattered property rights of workers, the proportions dramatically differ. In much of the East the cohort of foreign investors is entirely missing, while national capitalists of often doubtful origin, skills and strategies acquired overwhelming share and influence. At the other extreme, in former GDR virtually the whole business elite is "foreign": West-German or of other Western origin. On this scale Hungary, with a one-third of its largely private economy in foreign hands [Hegymenet, 1998: 163] in 1997 is closest to the former GDR – and at the same time farthest from the other extreme exhibited by Eastern "national capitalisms". This location makes the Hungarian case specific and hints both at the risks the country avoided and the ones it took.

Where does the secret of Hungarian success lie? I believe that both past, and present matters: the success is both due to the favourable legacies of socialism, and the patterns of resolving the conflicts between the capitalist and democratic components of transformation. Hence in section 2 of my essay I shall ask how has democratic politics affected the process and the outcome of capitalist transformation? Given that the pattern of interaction between politics and the economy was also shaped by the risks and opportunities of the international environment, external factors are going to get ample weight in my explanation too. While my analysis covers the whole transformation period, in section 3 I take a closer look at the second half of the decade, and at the politics of consolidating economic reforms. Section 4 is devoted to the assessment of the political and economic costs and worrisome side-effects of Hungary's road to freedom. Finally I conclude, and offer a few lessons.

2. 1989–98: Ten Years of Social Patience

The implementation of the market-oriented strategy in Hungary was difficult throughout the whole decade. On one hand, macroeconomic tensions reflecting the harsh initial conditions, the collapse of the Soviet markets, and policy failures meant ever-present challenges for politicians and policy makers. On other hand the political and social legacy of the socialist system, and the rules, institutions and conflicts characteristic to democratic politics had an immense impact on the transformation and gave support to the idea that creating capitalism after the breakdown of socialism is an eminently political project [Kornai, 1988]. Hence to understand how and at what cost Hungary has become a market society the best is to ask how it succeeded in balancing the political and economic dimensions of social change.

Let us recall first that initially most observers did not give much credit to the viability of democratic capitalism after state socialism. Indeed, scenarios of destabilization or breakdown under post-socialism have become more profoundly elaborated than those of the collapse of socialism ever were. Often, these gloomy prophecies contradicted to each other, but neither their contrasts, nor their criticism got too much attention. Firstly, a number of liberal economists and policy makers worried that delays or deadlocks of radical economic reforms could lead to political and economic destabilization and, even to a new turn to populist authoritarianism. But secondly, on the Left, social scientists and politicians argued the opposite: that it is excessive economic liberalism, where the danger to freedom and democracy ultimately comes from. Thirdly, many historians and political scientists believed the political, cultural, and social legacy of state socialism had been almost entirely negative, and could become a massive obstacle to the emergence of the new social system. Finally, there were fears, that democracy came "too early", and political competition could undermine state capacity to radical reform.

Contrary to these latter views my argument is that both a number of important socialist legacies, and the democracy itself, did contribute to stability rather than to destabilization in the first period of the Hungarian transformation. They did so in three ways: (1) by creating winners who supported (or at least did not oppose) the transformation; (2) patient losers who granted reformist politicians with relatively long "grace periods", and (3) by leaving behind domestic and external constraints to irresponsible economic adventurism.

2.1. Empowered Winners

Firstly, Hungarian socialism improved the chances of powerful economic elit-groups, whose behavior was important if democratic capitalism was to survive, to become winners of privatization. Thus for them, both capitalism paid, and democracy was acceptable: they were not interested in derailing the transformation process [Ost, 1992]. I refer to the empirically well-documented argument that the last Hungarian socialist governments created and left behind the legal and institutional infrastructure – laws regulating the commercialization, and privatization of public firms – helping the most competitive elements of the managerial stratum to become powerful in the emerging capitalist elite [Urbán, 1991]. There were other factors of their legacy which both enhanced their competitive advantages against domestic rivals – small private entrepreneurs, and "expectant" client-capitalists – and enabled them to easier ally with external challengers: foreign direct investors. It was their skills inherited from Hungarian reform socialism: in part their experience as "public entrepreneurs" in mixed formal-informal, state-market strategies, organizations and institutions which "got the job" of keeping economic activity afloat "done" [Róna-Tas, 1997; Stark and Bruszt, 1998: 128]. Their other skill was their familiarity with foreign markets, investment, licensing contracts, partnerships, and joint ventures which became a common practice by 1980s, and explain the remarkable openness of the Hungarian managerial elite to foreign capital, and specifically to alliences and cooperation with foreign investors. As a consequence the emerging business elite exhibited a more moderate and less insatiable domestic managerial element, whose acquisition strategies considered privatization less as a zero-sum game, than actors of other Eastern "national capitalisms". Secondly, unlike in other countries the state did not collapse in Hungary by 1989–90 [see also Murrell, 1996], and the most powerful cohorts of Hungarian administrative elite – the policy-making and financial bureaucracy – was in a relatively good shape and favorable position to enforce the administrative changes required to the conduct of the market-oriented economic strategy: a point to which I shall return later.

2.2. Patient Losers

Other elements of the socialist legacy contributed to the overwhelmingly patient attitude of losers of transformation. I believe it was mainly due to them, that the political dynamics of the Hungarian transformation exhibited a different pattern than the disruptive social response to the first wave of radical crisis-management and adjustment in late 1970s and early 1980s in many Third World countries [1]. Fears of similar developments have frequently been expressed in the Eastern context by politicians, political analysts and social scientists alike. However, these fears missed two important points. One is that the "IMF-riots" of Latin America typically challenged authoritarian regimes, and signalled the turn to democracy, rather than to dictatorship [2]. Another neglected aspect was that the post-socialist countries differed from the more rebellious societies of the Third World in a number of structural, cultural and institutional aspects. These in "East" have become a basis for political patience even in critical situations when explosive political protest was the more probable response in "South". To put it differently, in part, the socialist legacy have had a demobilizing, and, consequently, politically stabilizing effect. The explanation that socialism left behind societies characterized by a relative lack of the structural, cultural and institutional factors associated with violent collective action seems to be especially powerful in the Hungarian case. It is the following legacies and effects that deserve particular attention.

When the changes began large popular sectors in Hungary had yet at their disposal relatively substantial reserves to survive hard times. To be sure, their resources were modest in absolute terms: but at least they had not been devoured by hyperinflation or confiscation of the population's forced savings held responsible for the "monetary overhang" [3]. In this sense the fact that the state did not "whither away", and did not lose control over the macroeconomic fundamentals was another positive element of the socialist legacy. As a consequence, the absence of extreme income inequality and of poverty of a Third World type – that is, concentrated in overpopulated and politically

[1] Often, the initial response to crisis and adjustment in Latin America and elsewhere in the Third World was severe, massive and violent protest: food riots, general and political strikes, clashes with the armed forces, and escalation of guerrilla-warfare resulting in declarations of state of emergency and imposing of martial law, or, alternatively, in withdrawing economic reform measures, replacing key ministers, ousting governments, or returning to civilian rule [Walton, and Seddon, 1994].

[2] Also, the violent economic revolts lost momentum by the late 1980s: in this sense many new Latin American democracies appeared to be more crisis-proof, than the old military regimes.

[3] Obviously, Poland where the changes were preceded by gallopping inflation, was less fortunate in this respect which partly explains why Polish society was somewhat less "patient" than the Hungarian.

explosive informal urban settlements – may have contributed to weakening the threat of violent political mass actions. Even if poverty and inequality dramatically increased during the last decade, it continues to be far below Third World standards both in terms of its extent, and concentration. To be simple, Budapest has not yet become Lima, Sao Paulo or Djakarta. These effects could be reinforced by cultural factors such as the substantially higher education standards, or by a characteristic element of Hungarian political memory: the experience that – as it happened in and after 1956 – revolutionary violence breeds horrifying counter-revolutionary retaliation.

Such structural legacies as the country's demographic characteristics certainly mattered as well. The Hungarian society is more aged and less urbanized than most of the rebellious Third World nations. Elderly people in general, and pensioners in particular, could not strike or riot, even if they felt aggrieved, and typically neither could members of the rural society who lived dispersed in the countryside. When urban socialist industries in Hungary collapsed redundant labor migrated back to villages and other small-scale settlements and got stuck there contributing to the emergence of "pockets of rural poverty": of economically depressed and marginalized regions lackig any public infrastructure and jobs as well as the chances and resources for collective protest. Consequently, major social groups, like the poor, the pensioners, and much of the rural population have had to tolerate economic hardships. If they have associated their grievances with the strategy of economic transformation, their only avenue of protest has been to vote against the reformist governments [4].

Labour protest, the contentious political action of the lower, and lower-middle classes of the Kádár-regime, did not significantly shape Hungarian transformation politics either. At the beginning this could have been, because the potential organizers, the ex-communist National Federation of Hungarian Trade Unions (MSZOSZ) and its allies, were suffering both from a dramatic loss of union rank and file, and credibility problems. Their lost credibility was due to their socialist legacy: their intimate ties with the communist party. It is also true that the few new unions that were credible, among them the League of Democratic Trade Unions – similar to Poland's Solidarność – initially

[4] There was, however, rural protest in Hungary, organized by the Smallholders Party, and, in 1997 by the emerging new association of better off agricultural producers. Also, with respect to the political behavior of Polish peasants I am aware of the fact that they – or at least their representatives in politics – were in general less patient than rural population in Hungary. Clearly what matters is not just the geographic dispersion of the population, but its interaction with other – organizational and cultural – factors of mobilization. As far as the pensioners are concerned, it is also interesting to think about to what extent the policy of early retirement widely used for solving employment problems and conflicts in Poland, and dramatically increasing the share of retired seniors in the society might have contributed to the dominance of overall social patience during the Polish transformation.

favored reform. Later, however, the transformational recession [Kornai, 1994] – the decline in living standards, and the loss of job security associated with rapidly growing unemployment – has curbed the rest of labor's contentious mood. Finally, one more institutional factor, also originating partly in the Hungarian socialist past – the tradition of collusion between labour unions and management – may have contributed to the cooperative rather than confrontational stance adopted by most unions [5].

Finally, in different forms and to different degrees, all population groups, including the workers, the poor, the elderly, and the rural population have had an important alternative to protest: "going informal". Led by cultural and behavioural norms left behind by socialism – e. g. that laws do not matter and theft from state is morally permissible – one-third of Hungarian population (and not only the poor) retreated to the second economy: another socialist legacy, also revitalized by the crisis and massive social dislocation. Noncriminal exit forms may also have had a positive stabilizing effect, at least in the short run [Sík 1994] [6].

All in all, instead of protesting violently and directly, Hungarians remained patient and either went informal or exploited their employers' capacity to enforce protective state intervention until this was still possible. Whatever social tensions remained effective, their direct influence was neutralized either by government tactics aiming at dividing losers by partial compensation, or by the democratic political institutions. Both Hungarian democratic governments abundantly used pre-emptive partial compensation: from political side-payments to unions to politically targeted pension-, wage- or social benefit-increases. However, I believe it was even more important, that democracy institutionalized protest-vote as the standard weapon to express economic grievances – it became much more popular (and was less costly) than riots, strikes, or violent demonstrations. In politics, Hungarians typically preferred protest votes, and channelling their demands through democratic institutions to more disruptive tactics. Thus the democratic system contributed to the success of economic transformation by providing a safety-valve for socio-economic tensions.

The characteristic political dynamics presented above – the alternation between extended periods of political patience with protest and retaliation only during elections – is one of the keys to the politics of the Hungarian economic transformation. On one hand, society's overwhelmingly patient and democratic attitude has provided democratic

[5] This, again, is to some extent different in the Polish case, where labor was more contentious, although according to the data available strike activity in Poland did not reach critical levels and did not paralyze the economy, and its intensity fell throughout the last decade [Ekiert, and Kubik, 1996].

[6] Another similarity between Poland and Hungary: data show a large extent of informalization of the economy.

reformist governments with longer grace periods and longer time horizons in which to implement difficult reforms [7]. On other hand the politicians' fear from protest vote mostly (but not only) before elections was still there, which is a partial explanation for why reforms were sometimes delayed, "watered down", or lost radicalism in other ways. Finally, the fact that social discontent was expressed mostly in democratic form contributed not only to the success of economic transformation, but also to the stabilization of the main institutions and actors of democracy, e.g. the political parties.

Was the protest expressed by votes effective? Were electorates able to radically change the transformation strategy? Did the economic hardships of Hungarian population substantially decline during the past decade? My answer is rather negative. What mostly happened was that Hungarians voted out economic policies injurious to their immediate interests, only to witness their recurrence under different party banners: in Hungary first in Christian-Democratic, then ex-communist Socialist, and Liberal, and most recently, center-right and Liberal ideological colors [8].

2.3. Constraints

Finally, I believe the fact that the main stream of the transformation strategy could be maintained is partly explained by the – external and domestic – constraints left behind by socialism. Specifically, in the early period of Hungarian transformation the economy affected politics mainly by the constraints posed by its critical shape. Although Hungary started its transformation with a relatively less devastated economic landscape than most other post-socialist states, its macroeconomic situation in 1991, 1992 and 1993 was far from permitting any populist or social democratic "deviation" from the main stream of stabilization and structural adjustment policies. From the beginning, the effect of domestic macroeconomic constraints had been reinforced by external constraints: the international "rules of the game" to which Hungarian politicians became increasingly committed during the 1990s. While keeping all the above said in mind let us now take a closer look at how politics affected economic policy making and vice versa in the period of consolidating Hungarian democratic capitalism.

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[7] Mainly for political institutional reasons – the initial absence of minimal threshold of political support required to entering the parliament – the Polish political process was more "hectic" in this respects: and policy makers were granted much shorter "grace periods" than in Hungary [Balcerowicz, 1995]. However, after the threshold was introduced, Polish politics in this respect became more similar to the Hungarian.

[8] This seems to have happened in similar ways in Poland where not only center-right and liberal, but also ex-Communist coalitions parties implemented largely market-oriented economic policies.

3. Four Years of "Rush Towards Capitalism" (1994–98)

One important approach to the political economy of policy reform offers a number of suggestions about why and how the political dynamics of sustaining economic transformation under democratic rule differs from the initial reform phase [9]. In this view sustaining economic transformation may face growing difficulties and even harder political challenges than initiating the departure from the old system [10]. Specifically, it is suggested that in the consolidation phase the pace of reforms has a tendency to slow down, and their initiation and implementation requires new government tactics representing a shift from "imperative" to a more "interactive" style [11], implying negotiation and cooperation with a wide array of political and bureaucratic actors and diverse social interest groups.

Let us test the above propositions on the Hungarian case – specifically the politics of policy making in the areas of restructuring and privatization of large SOEs, and the banking sector, foreign trade strategy, debt-management, and state household reforms – under Gyula Horn's government based on the supermajority coalition between the ex-communist Hungarian Socialist Party (MSZP), and the liberal Alliance of Free Democrats (SZDSZ) in 1994–98.

To begin with, in all above areas, the period of consolidation, especially between 1995–98) witnessed an acceleration, rather than a slowing down of the pace of economic reforms [Kornai, 1995a]. Secondly, although political protest certainly intensified after the initiation of the Hungarian "Balcerowicz-plan", Finance Minister Lajos Bokros's stabilization and adjustment package on March 12, 1995, it was far from being excessive, or becoming a serious obstacle to implementation [12]. Thirdly, while the government had several

[9] My summary is based on Nelson (1994; 13–18).

[10] This may happen for the following reasons. (1) While the social costs of transformation rapidly increase after the first reform measures, it takes much longer time for the benefits to materialize. Reformers may face losers' opposition, while they may not count yet on the winners' support. (2) Later stage reforms – such as financial sector reforms, privatization and restructuring large SOEs, liberalization of labor markets, and reforms of the social welfare system – are administratively more complex, and require more legislative and institutional preparation than e.g. subsidy cuts, price liberalization, or foreign trade liberalization. (3) Finally, the political context shifts as well: times of "extraordinary politics" [Balcerowicz, 1995; 311] are followed by periods of "politics as usual", characterized by dwindling willingness to sacrifice, and the consolidation of the political sphere in terms of "a wider and more pushy array of interests" [Nelson, 1994; 15].

[11] These terms are used by Hausner (1993).

[12] In this respect the repeated intervention of the Constitutional Court which declared many (although neither all, nor the most important) measures anti-constitutional posed a more formidable challenge to Bokros and his men.

attempts to apply an "interactive" approach in forms of encompassing socioeconomic pacts, or political and bureaucratic consultations and negotiations, most (though not all) of those attempts failed, and actual implementation typically exhibited the "imperative style".

Apparently we have a few puzzles to solve: how and why could the transformation accelerate, and why did all this happen under the above mentioned political and bureaucratic conditions? I demonstrate below that the pace of economic transformation between 1995–98 could accelerate, and the reforms could stick not least because of both the positive, and negative legacies left behind by József Antall's government. In this sense there are reasons to stress the aspect of continuity, rather than of rupture between the first and the second Hungarian governments [13].

3.1. New International Political and Economic Commitments

Firstly, in continuity with the late Kádár-regime, but maximally taking advantage of the new situation the Antall-government made crucial political commitments, reinforcing Hungary's wish to reintegrate into the world economy and outlining increasingly concrete agendas for Hungary's return to the West and, specifically, to Europe. As far as foreign affairs and economic diplomacy is concerned, by signing the Association Agreement with the EU in december 1991, creating the CEFTA with the Visegrád-countries in early 1993, maintaining and intensifying Hungary's memebership in The World Bank, IMF, WTO and GATT, expressing Hungary's wish to become full members of the NATO, and the EU completed the country's departure from socialism, increased the cost of deviating from the chosen path, and paved the way for later steps of integration such as Hungary's OECD-membership in Spring 1995, or the forthcoming successes of getting closer to both NATO, and EU. All these steps followed a rather similar path in Poland.

However, with respect to international integration the most crucial difference between the Hungarian and Polish strategy was Hungary's different approach to its external debts: the Antall government opted against asking for rescheduling and debt-forgiveness [14]. This choice might explain much of the later divergence between the

[13] In this respect my interpretation is different from János Kornai's who in terms of the pace of economic transformation demonstrates the continuity of economic gradualism between the late Kádár regime, and the Antall-government, but mainly stresses the aspect of discontinuity between the latter, and the radicalism of the Horn-government [Kornai, 1995a]. I accept his view on the faster pace of reforms under Horn, but I highlight how this acceleration originated in the measures under Antall.

[14] To be sure, Hungary had minimal chances to follow the Polish road for the different structure of its debts, and because of its relatively modest political importance for the West. However, Hungary did not even push strongly for debt-relief.

Hungarian and Polish performance in privatization and foreign direct investment, and, as a consequence, of the ownership dynamics and pattern of their emerging capitalisms. On one hand, Hungary, from the starts was highly dependent on hard currency cash receipts from privatization, which implied aggressive strategies of selling-off state property to foreigners. Specifically neither could Hungary "afford" systematic delays in privatization, nor could it widely apply methods of free property distribution, or labor inclusion in the privatization process. Poland applied both latter forms more extensively. On other hand, it is partly for the Hungarian way of debt-management why foreign investors might have had a more positive view of Hungary than of Poland initially, and why Hungary could count on much larger capital inflows from the beginning [15]. However, selling for hard-currency cash was not easy: on one hand there was an intensive process of "spontaneous privatization" was underway, and on the other, the Hungarian state-owned enterprises (SOEs) were suffering from excessive bad debts, and the banking sector from crippling problem-loans in early 1990s [16]. All this posed the Antall-government the difficult tasks of both regaining control over the spontaneous processes, and improving the financial standing of both the SOEs, and the banking sector. I argue below that a number of important administrative and institutional reforms and structural measures and institutional reforms implemented between 1990–94 paved the way for accelerated marketization later.

3.2. (Re)centralized Privatization, and Restructuring the SOEs and Banking

Firstly, right at the beginning of its term the Antall-government (re)centralized privatization by rendering the State Privatization Agency (SPA) under government control [17].

[15] A similar view is expressed in Brada (1996; 78).

[16] The bad debts forced by non-payments of the debtors to their suppliers, the social security system, and accumulating as problem loand in the banking sector had multiple negative effects: they delayed structural change, slowed down the effect of macroeconomic stabilization measures, and became an obstacle to both financial stability and privatization both in the firms' sector, and the banking system.

[17] While these measures got passionate criticism for their statist and centralizing features, and for allegedly slowing down privatization, looking back from the perspective of the past decade, and also assessing the Hungarian case in a regional context I believe this move had been reasonable: it was arguably wise to reinforce state control over spontaneity and state capacity against the tendency of loss of control experienced in many other cases in East.

Secondly, from late 1991 till 1994 the Antall-government took several controversial steps implying first methods of "creative destruction", and later state structural policies to cope with the above challenge. In December 1991 the government implemented the law on financial institutions, which "brought Hungarian practice up to those of the European Union. This was the first serious legislation on banking in the region, and...uncovered much of the financial strain inevitable under restructuring and recession [Csaba, 1995: 224]. This was soon followed by the implementation of the law on accounting ripping off much of the fictive revenues which had helped the firms to cover their losses before. As a combined effect both the banks and the SOEs became more interested in enforcing payments from their debtors [Jelentések az alagútból, 1994; 74–5]. The institutional vehicle of enforcement was provided by the implementation of a severe bankruptcy legislation which between April 1992 to December 1993 produced 16000 cases of bankruptcies: a number unprecedented in the whole region. Some analysts argue that the combined and shockwise implementation of the three laws had been "wanton" but not "creative destruction" [Stark-Bruszt, 1998; 131], especially because the timing was unfortunate – the firms' budget constraints were hardened just at the moment when their Eastern markets collapsed – and because the bankruptcies had a domino-effect: healthy firms were made insolvent by the decline of their debtors [Jelentések, 1994; 35] [18]. From 1992 the enforced processes of structural change were both shaped and mitigated by two other sets of structural policy measures: between 1992–94 several packages of consolidating the banking sector, and consolidating and reorganizing a number of large SOEs – including 14 large firms and until 1994 55 other companies (later their number substantially increased). Especially in 1993–94 in the framework of the sole large public "investment program" of the period the government bailed out the largest state banks while requiring them to clean their balances and implement crucial, efficiency-enhancing changes in their organization, financial structures, and business strategies. Large debtor SOEs, in turn had to contract reorganization plans with their creditor banks and other large creditors, the Social Security Funds, and the Tax Office. In exchange they were granted debt forgiveness and new capital injections recycled from the privatization revenues [19] (see Table 1 in Appendix).

[18] While these claims are justified, and the structural policies of the Antall-government indeed had an element of "overkill" I wonder whether better solutions had been in sight, and specifically whether they had been feasible under the Hungarian conditions. Specifically, I belive that the Czech attempt to solve the problem favored and conceptualized by Stark, and Bruszt (1998) as restructuring by "deliberative associations" was neither superior to the Hungarian solution, nor feasible under the Hungarian conditions of heavy indebtedness, and macroeconomic instability.

[19] The programs of bank-consolidation and firm reorganization got severe and justified criticism for their high costs, the dirigist and protectionist style of state intervention, and the rent-seeking and moral hazard involved.

To sum up the combined positive effect of the measures above: the cleaning up of their balances and their improved capitalization subsequently made Hungarian SOEs and banks more attractive for foreign strategic investors. There was another development originating in the structural policies of the Antall-government, which – while it was worrisome from the viewpoint of indigenous firms, had a positive effect on greenfield foreign investment. Both the recession accompanying the wave of bankruptcies in 1992–93, and the hardening of the Hungarian banks' budget constraints implied that Hungarian companies had to withdraw from their traditional markets both in Hungary and abroad [20]. The gaps were quickly filled by both the acquisitions, and greenfield investment of export-oriented foreign multinational corporations, and intensified operations of fully foreign owned subsidiaries of large and small banks on the Hungarian domestic market of financial services. All in all I consider the policies and results of the Antall-period as "investments" into privatization and financial restructuring under the Horn-government [21].

3.3. Politics of Accelerated Reforms in 1995–98

Finally, there was a third legacy, and this was negative: while the Antall-government bore substantial economic and political costs for its measures in terms of skyrocketting unemployment, decreased state revenues, increased public expenditure, and collapsing exports, in macroeconomic terms it also left behind a close-to-financial-meltdown-situation for its successor. For Hungary, then, similar to the period of parting with socialism, the next phase of consolidating capitalism started in economic crisis. Nine months were wasted with rivalries between Premier Gyula Horn, and his top policy maker Finance Minister László Békesi [Greskovits, 1998b], until further dramatic deterioration of the country's external and domestic balances,

[20] By 1991 the Antall-government also completed trade liberalization by mastering its most difficult phase, and exposed the most sensitive parts of Hungarian economy to import-competition. However, the bankruptcies had especially severe effect in the Hungarian export-industries. Of course, the loss of external markets was not a simple outcome of the policies implemented: clearly the most important factor was the collapse of the Soviet economy in 1992–93. What brought especially hard times for Hungarian firms was the simultaneity of the above processes.

[21] In this sense, I believe the tasks of economic and political consolidation cannot be mechanically rendered to the second democratic Hungarian government. Rather the periods of initiating and consolidating both economic and political transformations had been overarching, and the tasks had been shared by both governments. This is why the politics of Hungarian transformation was in part different from what the political economy of policy reforms would expect: in both periods, and, specifically, under the Horn-government.

increasing capital flight, and the pressure of external actors made decisive steps imperative: Békesi resigned, and the new Finance Minister Lajos Bokros initiated a drastic stabilization and adjustment package on March 12, 1995 (see Table 2 in Appendix).

Bokros advocated sustainable, fast and balanced, primarily export-led growth based on domestic savings [Bokros, 1996; 825]. His package consisted a combination of stabilization measures including a sharp devaluation, the introduction of a crawling peg for Hungarian Forint (HUF), and a surcharge for imports. It also was an attempt to maintain macroeconomic stability without recession and facilitate growth by the deep restructuring of the composition of GDP, by less consumption, more investment, and more exports [22]. The specificity of the Bokros-package was its focus on the fiscal expenditure side of the budget, where restructuring implied drastic cuts, and a strategic attack against wages and salaries, welfare transfers and public investment.

Thus the social and short-term economic costs were no less impressive than the results, and in general, the Bokros package once and for all changed the expectations of Hungarian society, and "spending bureaucracy".

How was this package implemented, and why was it politically feasible? I answer these questions by sketching a few characteristics of policy style under the Horn-government, and by identifiyng the broader political factors of the acceleration of systemic change.

3.4. Failed Attempts at Policy Interaction, and Successful One-man-shows

As to the governments tactics, the Horn-government experimented with diverse policy styles – ranging from negotiated to imperative strategies – in a variety of fields: from fiscal adjustment, and institutional reform, to privatization. Most typically the Horn-administration started with negotiation, failed, and resorted to more imperative styles: to pressure and force rather than persuasion, improvization more than preparation, to individual decision making rather than institutionalized compromise. Hence "imperative" strategies became dominant, because the "interactive negotiated" strategies failed, and in the atmosphere of recurring crisis the Premier gave free hand and strong political backing to a few top policy makers whom he trusted. Moreover, to resort to imperative strategies also was possible, because social protest against the

[22] In it's philosophy, the Bokros's program was similar to the strategy advocated by János Kornai (1995b).

methods and their consequences was either moderate, or ineffectual [23]. These shifts in the policy-style of the Horn-government could be observed in the case of the failed Socioeconomic Pact of 1994–95, the style of the implementation of the Bokros-package, major privatization strategies, and the legislative decision on how to use the unexpected huge inflow of privatization revenues in late 1995.

Initially, the Horn-government seemed to prefer negotiation and cooperation to pressure: in accordance with the coalition's electoral promises, and using the framework of Hungary's major tripartite corporatist forum, the Interest Reconciliation Council, extensive negotiations with the major trade unions and business associations started right after the new government was enacted. The negotiations aimed at a Socio-Economic Agreement on the transformation strategy for the next three years. The parties were to come to agreement on the major stabilization measures, the reform of state household, the principles of privatization, the extent and ways of further labor-market liberalization, of real-wage losses, and their compensation. In early February 1995 it was officially declared that the Pact had failed. Most participants and a few observers stressed factors such as the missing long-term strategy of the government, or the rigidity of the trade unions to accept short-term losses in exchange for long-term gains [Héthy, 1996] [24]. While pacting was impossible, outright pressure still seemed to be a feasible way of enforcing the breakthrough of stabilization and adjustment. Actually, this is what had happened.

The Bokros-stabilization plan avoided negotiation and consultation from its birth. The package was prepared in secrecy by Bokros and a few other economists, and was put to the agenda of the coalition-parties and the legislation with a strong political backing by the Premier: this was one important reason why it got almost unanimous approval from the coalition parties which had a supermajority of about two-thirds of the parliamentary votes. While implementing his program, Bokros similarly preferred outright pressure and force to convincing, and collaboration with other administrative agencies. I believe this policy style mostly originated in the logic underlying his program. While his original plan

[23] The reasons in part can be found in "old" factors of political patience mentioned in section 2. But the other part of the explanation is closely connected to the consolidation period: the economic and social structural changes induced by the chosen transformation path, and becoming more and more accentuated by the mid-90s, further impaired the capacities for collective action of its losers (see section 4).

[24] I believe that, in part, the Pact was not to be signed because this would have increased the political capital of the Premier's both main rivals, Békesi, and Sándor Nagy, the Chairman of the largest trade union MSZOSZ. On his part, Békesi invested in the success: he was actively participating in the negotiations and was ready to concessions in terms of both softening, and delaying some of his adjustment measures. Similarly, Nagy much more than other union bosses was moderate: in principle he was not against accepting real-wage losses in exchange for compensation in organizational and political issues. There is a sense that Horn did not really support that these two men would come to an agreement, rather it was the failure of the pact which entailed gains for the Premier in terms of his own relative political standing [Kohegyi, 1995].

envisaged comprehensive rationalization plans for the public sector, enabling an "ordered retreat" of the state with substantial savings as a result, those plans were not available, and could not have been prepared without time-consuming bargaining and coordination. Bokros opted for an offensive method of trial and error rather than preparation and negotiation [25]. He drastically cut fiscal expenditures in many budgetary areas, and granted wage-increases only in exchange for downsizing employment. No wonder, that his strategy left Bokros with little support in administration. Still, the Bokros-package in its most important elements could break through.

Similar to macroeconomic stabilization, and fiscal reforms, in the issue of privatization and privatization-control, the Horn-government initially took a consultative and negotiating stance. Negotiation in this area was to ease the conflicts both within and outside state administration on issues such as: (1) who should control privatization – the Finance Minister or other bodies such as the State Property Agency and the branch ministries (2), which interest groups and political parties were going to get access to the headquarters of the privatization strategy and practice and in which way (the trade unions showed hyper-activity in this debate), (3) what were the correct strategies to be pursued: those maximizing cash-receipts or those creating more jobs, or more Hungarian owners, and finally (4) how privatization should be (re)organized and legislated. In 1994 Finance Minister László Békesi tried, and initially succeeded, to expand his control to the legal framework, strategy, government agencies, and receipts in this field [Sárközy, 1996]. But according to some observers the Finance Minister's time-consuming administrative and legislative preparation to overtake the control over privatization could be itself one of the factors why privatization was practically brought to a halt in 1994, at least this was used against him later. All in all, around late 1994 the Premier personally nullified one large privatization contract, fired Békesi's man responsible for privatization, and nominated his political and personal intimate, Tamás Suchman as a Minister of Privatization without portfolio.

Although nobody initially believed that the committed Socialist Tamás Suchman will become the heroe of Hungary's property sell-off, under his leadeship privatization dramatically accelerated. Cash receipts both in HUF and foreign exchange were looming [26] (see Table 3 in Appendix). Suchman in his own field fought the same "Blitzkrieg" with the same controversial success as Bokros in the field of public finance. His criterion for

[25] His decision might have been influenced by the failure of earlier attempts to reform public finance. Whenever the task of elaborating their own reform and rationalization plans was delegated to the ministries themselves, those reforms failed to happen.

[26] Suchman himself explained his commitment to fast methods and decisions in truly leftist ideological terms. He said, "The reason why we have to privatize fast is not that the state is an inappropriate, or incapable owner in general, but because at the moment it lacks the financial resources to restructure its firms". He also said, "I shall do my best to avoid that one would introduce a new austerity program claiming that the receipts from privatization are missing" [Kocsis, 1996; 55–6].

his own success was to sell public property, which often involved quick personal decisions without much consultation or negotiation, and he had the Premier's full support to do it. Hence in terms of policy style he performed a "one-man show", with little attention to institutionalized procedures and control, as is attested by the late 1996 large corruption scandal.

Thus paradoxically in 1995 – against the prevailing expectations – the challenge to Bokros's stabilization policies originated not in the fall-out, but in the unexpected, large inflow of cash receipts from privatization. One had to decide about a sum which according to various estimates was in the range of 260 to 400 bn HUFs, and in principle, the outcome could have been a "negotiated" solution. Bokros's view also supported by the SZDSZ and a wide consensus of professionals was, that the extra-receipts should be used for servicing the country's foreign debt. Premier Horn, however, took the lead in arguing that at least a part of the cash was to finance infrastructure, firm reorganization, and other development projects. The Socialists, the largest party in Parliament were taken by surprise by the revenues of that magnitude [27], they were neither prepared to produce and assess alternative plans, nor to act in a cohesive and coordinated way. Finally, 60 Socialist MPs in alliance with the SZDSZ and the opposition, voted against Horn, and favored fast legislative decision to negotiation and bargaining with various spending lobbies and bureaucracies [28].

The Horn-government had two more policy-packages which are generally considered as successes in the literature: the first is the privatization of the banking sector at a tremendeous pace, and to a remarkably large extent. As a result by 1998 the Hungarian banking system is to 75% private, and – reflecting both the effect privatization, and of the expansion of foreign greenfield operation in banking – to almost two-third foreign owned [29]. The last reform success story mentioned here is the breakthrough of the pension reform. While the politics of this reform is detailed in Joan Nelson's comparative study (1998), I mention here only one that while rebuilding the pension

[27] Note that this sum was between one-quarter to one-third of the total cash-receipts from privatization accumulated between 1990–97.

[28] Negotiation could partly be avoided, because for spending the unexpected cashthere were no credible programs available Other explanations are that there were too many competing priorities, or that MPs in MSZP still had been under the shock of Hungary's external imbalance.

[29] As I argued above the expensive consolidation of the banks and their debtors under the Antall-government was and important condition of this success: earlier attempts at privatization mostly failed because of the banks' precarious financial standing. However, this large share of foreign ownership in banking is rather unprecedented in all Europe: there are only three more countries – Belgium (45%), Luxemburg (60%), and the U.K. (91%) – where foreign ownership was around or above 50% in 1990 [Törékeny stabilizáció, 1997; 103]. Interesting enough, this unusual feature of Hungarian capitalism and the risks and opportunities inherent in having a foreign-owned banking sector – also accompanied by a 100% foreign ownership in the insurance sector – remained, for the time being, undertheorized in the literature. Nevertheless, the first analyses report on intensive investment activity and improvements in financial services.

system the Horn-government indeed followed the tactic of consultation, negotiation, and political and bureaucratic alliance building.

Let me finally come back to my earlier question on the political factors behind the acceleration of reforms between 1995–98. I believe, in addition to the important "preparatory reforms" undertaken, and the crucial new political commitments made by the Antall-government, at least two other factors more characteristic to the Horn-period had an important role. One is the consolidation of both the political institutions, and the state institutions by the second phase of the Hungarian transformation. The other is the coalition building tactics inherent in the Horn-government's privatization strategy.

3.5. Consolidation of the Political System, and Coalition-building by Privatization

While the argument about the positive effect of the consolidation of political and democratic institutional system on the process of Hungarian transformation is convincingly made by Haggard, Kaufman, and Shugart (1998), I shall highlight only two aspects of this development. One considers the fact, that by the mid-1990s Hungary's important political parties, on their part, fully internalized the constraints and opportunities inherent in Hungary's actual economic situation, and the country's old and new international economic and political commitments both in their election and coalition programs, and the Horn-government to some extent could count on this. Specifically, the parties were much more keen on collecting protest votes than seriously suggesting or implementing policies satisfying the short-term demands of aggrieved constituencies. Rather than making too bombastic economic promises, or challenging the path of international integration, the parties of the entire Hungarian political spectrum from the right to the left end, de facto proved to be capable of governing and building legislative majorities, or even issue-specific alliances transgressing the divide between government and opposition around quite similar major political and economic policy objectives [30].

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[30] Save for the communist Workers Party, and the racist extreme right Party of Hungarian Justice and Life which however until 1998 could not mobilize significant political support. However, Even the Smallholder Party, which is generally termed "populist" in the Hungarian political discourse, and used both aggressive rhetoric, and political mobilization against the Horn-government and its policies, did embrace many suggestions of the Washington-consensus in its 1995 party-program. Smallholders campaigned on a moderate economic platform in 1998, and did I believe, as the junior member of Hungary's recent government, will either prove to be "bait and switch populist", or will leave the coalition. The latter term is coined by Paul Drake characterizing Latin American personalist leaders who campaign on a populist platform only to switch abruptly to market-oriented policies following election [Drake, 1991; 36]. Economic populism, then, was "the dog, which did not bark" in Hungary. A similar phenomenon in the Polish context was pointed out by Leszek Balcerowicz (1995; 300).

Secondly the economic transformation strategy was also embedded in the emerging new structure of bureaucratic power. Due to the long traditions of Hungary's relative external openness – stemming, irony of the ironies, not least from the heavy external debt, and Hungary's resulting early IMF, and World Bank-membership – Hungarian policy making and financial bureaucracy from the early 1980s became involved and integrated in international professional, policy-making and financial networks. This created skills – experience with IMF and World Bank staff and policy programs, negotiating and bargaining with foreign creditors [31] or investors – which were not less, but more badly needed when the changes came. Rather than losing with economic transformation this reform bureaucracy consolidated its influence in politics and policy making. By the mid-1990s their power was also institutionalized in the dominance of the Ministry of Finance and the Hungarian National Bank over rival bureaucratic strongholds, and the leadership of the Finance Minister over the "spending ministries". Also supported by the consensus of most economists on "what was to be done" the reform-bureaucracy had become a strong advocate of fast roads to capitalism, and decisive steps in economic hard times.

Finally, a closer look at Table 1 and 3 reveals one more factor of the acceleration of privatization. By using a wide variety of methods from compensation-vouchers to cheap existence-building loans (E-loans), and direct sales for HUF or foreign exchange, and by an intensified recycling of substantial amounts of privatization revenues into firm-reorganization, Premier Horn built up the largest possible coalition of beneficiaries of his policies [32]. A broad range of economic actors – from the clientele of the Antall-regime (the owners of the restitution vouchers), to foreign and domestic investors, and would-be-private firms expecting bailout and capital for reorganization – became directly dependent upon, and interested in fast privatization, and large inflows of privatization revenues, and in part this is why privatization could accelerate.

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[31] These skills even might have entalied capacities of outmaneuvernig the external actors by domestic bureaucrats [Csaba, 1995], or designing policy programs with a large domestic intellectual value-added. Greskovits (1998) concludes that Hungarian, Polish and Czechoslovak policy makers enjoyed higher degrees of relative autonomy of policy formulation than their colleagues in the less integrated Romania, Bulgaria, or for that matter, the Baltic States.

[32] For an excellent and detailed analysis of ex-communist Socialists' coalition-management in Hungary, Poland and Slovakia, and the interaction of social coalition-building with external constraints see Silitski (1998).

4. What Kind of Democracy, and What Kind of Capitalism Has Consolidated?

Against the gloomy expectations Hungarian democracy survived the transformational recession and also contributed to the success of economic transformation. But the crisis left behind much political damage. Democracy in Hungary could take root only at the cost of some of its qualitative aspects, such as its representativeness, inclusionary features, and its capacity to evenly provide and protect civil liberties. Many important ingredients of fully developed Western-type democracies continue to be in short supply in the new Hungarian political system.

Throughout the past decade it was all the time obvious that – because of the dire economic situation left behind by socialism and aggravated by the transformational recession – the emerging system would be incapable of meeting even some of the most justified demands for acceptable living standards and security of large social groups including those of the lower and lower-middle working classes of the Kádár-regime. Thus the major dilemma the political system had to face was the political representation of the millions pushed to the margin by the crisis and the transformation strategy. If their demands had got immediate, strong political representation, and were to become major issues on the agenda of economic transformation, they had paved the way to economic chaos, and short-lived populist democracy. Conversely, if the essential democratic institutions and capitalism simultaneously were to taking root under economic stress, the political system had to exclude justified but unfeasible economic demands from the discourse as political non-issues. In this sense with a bit of exaggeration: the emerging Hungarian democracy had to simultaneously perform the democratic agenda of political integration, and the authoritarian agenda of political exclusion. It succeeded in both: and got consolidated as a democracy with strong exclusionary features [33]. This is the price Hungarian democrats paid for building capitalism in democratic settings after socialism. As to the institutional and organizational consequences of the above political logic I mention only two: (1) there is a pervasive lack of both civil organizations representing various losers's groups, and channels – other than voting in elections – for civil control over state policy in general. (2) While the elite-echelons of ex-communist labor unions were to some extent included in power, and used their allliance with elites to defeat rival

[33] Hungarian democracy is, to some extent, "undemocratic" not only in terms of the tension between its exclusionary, and inclusionary dimensions. To use Guillermo O'Donnell's and Phillippe Schmitter's famous concept (1986) Hungary also represents a case of democracy building by "undemocratic means": specifically by exclusive elite pacts. See for these milestones of Hungarian transformation Greskovits (1998a).

civil organizations and the new non-communist trade unions, labor at the shop-floor is mostly left alone, and unrepresented. The victory of the ex-communist unions, and the transformational recession in combination resulted in the decline or dissolution of all new trade unions: the Solidarity Workers' Alliance, the League of Democratic Trade Unions, and the Workers's Councils. Based on the evidence of these developments in Hungary, and according to the concept elaborated by Acuna and Smith (1994) in the Latin American context I classified Hungarian democracy as a "dual democratic regime" where the system's stability is based on the alliance of political and state elite with a strategic minority of the potential opposition to economic policies, where the purpose of the alliance is to exclude "the majority of the remaining social actors by disarticulating and neutralizing their capacity for collective action" [Acuna and Smith, 1994, 47; Greskovits, 1998; ch. 9]. As a consequence large sectors of the Hungarian society continue to be both marginalized in the economy, and excluded from political representation. Moreover, those who are on the margin economically, and are largely unrepresented in politics typically lose in terms of provision and protection of their human and civil rights as well.

Is this new market sociey durable? Is the "low-level equilibrium" between the incomplete democracy, and the type of the emerging market economy stable? How long will the tension between the integrative and the exclusive, antidemocratic features of the political system prevail? Can economic transformation further advance in the atmosphere of social patience in the next decade? These are big questions, and I have only tentative suggestions.

Hungarian democratic capitalism seems to be consolidated in the sense that while there is an ongoing debate on its details no robust political challenge to either its democratic or capitalist component is in sight. Moreover, as I streesed above the past decade brought about crucial international political commitments which magnified the costs of abandoning the chosen path. Thus there are good chances that the new system will prevail in the medium term as it is now: without much probability of an authoritarian turnabout, but also without automatic guarantees of development towards a democracy of better quality. On one hand, reform elites need not be enticed by authoritarian temptations to defend their interests because the transformation strategies they favor will not be effectively challenged by the society. But on other hand – and for similar reasons – I think there will not be strong societal pressure for more inclusion, and more liberalism either. Hence politicians have a great responsibility.

I base my above hypotheses on emerging evidence of the economic and social structural impact of the transformation strategies implemented throughout the decade, and at an accelerated speed during the past four years' rush towards capitalism. In brief my argument is that the structural changes induced by the chosen transformation path further impaired the capacities for collective action of its losers, particularly large segments of labor, and other lower-income groups. I think, in the Hungarian context it is the following changes that deserve particular attention.

One of the most visible structural adaptation processes is the dramatically increasing share of private non-industrial employment, and a rapid decrease of the average plant-size [34]. One dimension of this process, the emergence of many hundred-thousands of small or medium size firms and their growing role in output and employment [Laki, 1997] is visible not only in Hungary, but elsewhere in Eastern Europe too. But it is a Hungarian specificity, that at the opposite end there has been a rapid rise in the scope of operations of the local subsidiaries of large multinational corporations which by now led to their clear dominance in a number of important sectors (see Törékeny stabilizáció, 1997, and Hegymenet, 1998 for the forthcoming details of the Hungarian multinational export sector). Both above types of economic organizations prefer forms of employment with limitations on institutionalized representation of interest or collective protest (for the description of the Hungarian labor relations below see Ladó, 1996, and Ellingstad, 1997). As to the first matter: about one-third of Hungarian employees are covered by collective agreements – mainly the employees of the shrinking public or semi-public industry and services. Roughly a second third of the workers – including those employed by the multinational corporations – have individual contracts, while much of the rest – including migrants – do not have any: they are hired and fired under precarious conditions by the small-scale firms of the (mostly informal) economy. The presence and activity of trade unions in the firms and at the shop-floor level is in conformity with the above pattern: specifically about two-third of Hungarian labor force is not (or at least not directly) represented by unions: they are mostly absent in the sectors dominated either by the small-medium firms, or by the multinational corporations. Where the unions are, however, present, they are mostly very silent: in striking contrast with the vocal and noisy elite-unionism in the political parties, parliamentary factions, national tripartite corporatist forums, and a number of important redistributive centres of the governemnt administration such as the self-governing bodies of the pension, and health-care funds. Apparently, dual democracy, and dramatic economic structural change, in combination, resulted in a dual system of labor representation and industrial relations. As far as the work conditions of those employed on the "margins" by the small- and medium-scale economy is concerned, there is a strong sense that the absence of both collective representation and state control and, in general, the defenselessness of labor allows and maintains low levels of job stability, dependence upon income from piecework, poor working and health-conditions, little access to training, impediments to collective

[34] See for the negative effect of similar processes on labor in Western Europe Pontusson (1995).

negotiation, and often subjection to authoritarian relations or outright oppression in the workplace. As the case of Chile, the most advanced neoliberal reform-country in Latin America shows, such anomic and unhappy situations may long prevail provided that the strategic export-sectors of the economy – in Chile 8–10 large, export-oriented and internationally integrated conglomerates – consider the low cost, and "flexibility" of labor employed under precarious conditions by their suppliers – the domestic semi-informal small and medium-scale firms – as a major factor of their international competitiveness [Díaz, 1993]. The lesson from Chile's above pattern of integrating its dual economy is: a more cohesive, more integrated and efficient capitalist economy does not automatically lead to better work- and life conditions. It may lead to the opposite if the improved cohesion and international competitivity of the national economy occurs in part at the cost of oppressing large segments of labor.

In the above respect the level of internal cohesiveness and integration of the Hungarian economy apparently has not reached the Chilean standards yet. For instance there is little contact and, even less cooperation between the MNC-dominated leading export-sectors, and the Hungarian firms oriented to a larger extent towards the domestic market, including the small and medium size companies. Instead the most powerful and influential, largely foreign, cohorts of Hungarian capitalism reside in an – economic and political – "off-shore" status. They operate off-shore, mostly in the more developed Transdanubia or Budapest, enjoy tax-reliefs, low-price real estate for locating their plants, and other incentives provided by the central and local governments. Rather than acquiring inputs from domestic firms they typically buy foreign: their suppliers are either firms abroad, or foreign firms setting up their Hungarian production facilities next to their buyers, and likewise in off-shore status. These firms have their own associations, but neither are they members of Hungarian business organizations, nor are they participating in the national tripartite corporatist bodies and negotiations. Supposedly they are able to reach the government with their economic policy preferences, but they apparently do not use the more or less formalized and visible channels of interest intermediation for these purposes. They are almost exclusively export-oriented, hence it is not the conditions of the Hungarian, but of their export-market upon which they ultimately depend, and which govern their decisions on investment, production and sales. Consequently, they are also largely autonomous vis-a-vis government policies shaping the domestic economic conditions – be their effect recessionary, or expansionary. Their autonomy resulted in benevolent effects in 1995–96, when notwithstanding the recessionary impulses of the Bokros stabilization and adjustment plan the foreign multinationals completed massive investment projects [Töréspontok, 1996]. But what about the opposite situation: how to balance the Hungarian economy in case of a larger recession abroad? The latter situation could cause really big troubles given that the

Hungarian export-sector became more concentrated, and thus more vulnerable, than it was: its most strategic part, manufacturing essentially means ten firms and ten products. To deal with the effects of a recession abroad seems to be substantially more out of the reach of Hungarian economic policy than ever before. Let me finally conclude, and also ask the question: is there anything that politicians and policy makers in other countries, and, specifically, in Poland can learn from the Hungarian experience?

5. Conclusions, and Lessons for Other Countries, and Specifically, Poland

(1) By 1998 Hungary's social system is democratic capitalism, which is a success both in terms of its own past, and in comparison with many other countries in post-socialist Eastern Europe. This success is the combined result of many factors.

(2) One factor is nothing but "virtue of lack" [35]: unlike in many other countries of the post-socialist region neither the peaceful or forceful formation of national identity nor of a new, independent state were important items on the Hungarian transformation agenda, and they could neither seriously conflict with, nor dominate over the issues of economic and political transformation [36].

(3) Another important factor was that even if the Hungarian economy did not always perform much better than other economies, by the actors of international capital and financial markets it has more or less constantly been perceived as a would-be success story. To the extent that this was important, then, the Hungarian success, in part, can be attributed to "the power of path-finding expectations" abroad [37].

(4) Still as a third set of advantageous preconditions: Hungary inherited relatively favourable legacies from state socialism: one of them was that the Hungarian state did not collapse by the time transformation speeded up. Other legacies contributed to stability rather than to destabilization in the first period of the Hungarian transformation. They did so in three ways: by creating winners who supported (or at least did not oppose) the transformation; patient losers who granted reformist politicians with relatively long "grace periods" to implement economic measures, and by leaving behind domestic and external constraints to irresponsible economic adventurism.

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[35] The expression, in a different context is used by Grant (1998).

[36] See Bunce 1998 for similar thoughts.

[37] And, of course, to many other, partly domestic, political and economic factors, which I shall highlight later in my essay. I borrow the above expression from Federowicz (1997).

(5) In part, these or similar legacies played a role in a number of other countries of North-West Eastern Europe, but I believe it was Hungary where their positive effect was the strongest, and thus the political dynamics of transformation was most stable. Specifically, from a bird's-eye-view Hungary and Poland seem to be similar, their legacies were not unfavourable, and their results are among the best ones states of the East could achieve. They both have more or less stabilized, expanding, internationally integrated economies, and fairly stable political systems characterized by several successive, fair, and competitive elections, and other democratic institutions. Civil rights, in general are observed in both countries. Hungary and Poland, with one-tenth of the population of the whole post-socialist East succeeded to acquire roughly one-half of both the foreign direct investment, and institutional credit granted to the region altogether.

(6) But, clearly, the success is not a pure reflection of the legacies and of the initial conditions: policy choices and the continuous balancing between the democratic and capitalist aspects of transformation were extremely important, and in these respects Hungary and Poland seem to be rather different. Specifically, Hungary opted for disciplined debt-management, while Poland chose its opportunity of debt-forgiveness and rescheduling. Hungary's choice dramatically increased its dependence upon international integration including its export-orientation, dependence upon hard-currency cash from privatization, foreign greenfield direct investment, and financial integration. As a consequence – also explained by the much smaller size of its national economy – Hungary became much more internationally integrated than Poland. with all the risks and opportunities inherent in such a situation.

(7) As a first step, Hungary drastically – and in part wantonly – decimated its economic capacity, then invested huge amounts into restructuring, and, finally selling off both its SOEs, and banks: mainly to foreigners. As a result in all East it came closest – much closer than Poland – to the case of former GDR where virtually the whole business elite is "foreign". At the same time Hungary got farthest – much farther than Poland – from the other extreme exhibited by Eastern "national capitalisms". Thus Hungary and Poland in the beginning of their second decade of democratic capitalism face rather different structure of opportunities and risks: Hungary's risks are inherent in its remarkable dependence upon its foreign capitalists, an the global international system, while for the time being Poland still seems relatively more dependent upon its national capitalists, and state ownership.

(8) The processes leading to the above outcomes accelerated under Hungary's second democratic government. The politics of consolidating reforms exhibited less consultation and negotiation, less political protest, and more imperative and fast decisions than one approach of the political economy to policy reform would have expected. An important lesson, for other countries, and for Poland than, is, that if consultation and

compromise fail, imperative strategies and outright pressure can still offer a feasible – although socially traumatic – way of enforcing the breakthrough of stabilization and adjustment. Imperative methods will work especially if the external pressure is intensive, if the enforced measures are well prepared by the previous administration, and if influential social interests are accommodated and "payed off" including the government's tolerance to their unbridled profit- and rent-seeking, as exemplified by the Hungarian case [38].

(9) However, a next lesson offered is that, privatization – including the Hungarian practice of fast sell-off to foreigners – is very expensive. We might conclude that – in the medium or longer run – revenues from privatization as such do not exist. Instead, in Hungary – in a self-propelling process – revenues from privatization were largely spent for (more) privatization: either for preparing firms or banks for privatization by restructuring, reorganization, or bailout, or for creating support for privatization (by restitution and cheap credits), or, finally for attracting foreign investors either by one of the above methods or by mintaining their trust and interest by accelerated debt-repayment [39].

(10) As to the political effect of the road to capitalism Hungarian democracy proved to be crisis-proof, but consolidated as dual, exclusive democracy with a weak capacity to provide equality and evenly protect civil and human rights. Losers of Hungarian economic transformation are losers in political terms as well: they are hardly represented, their rights are not sufficiently protected in democratic politics. Thus the democratic capitalist system in Hungary is stable but Janus-faced. Its consolidation also brought about the emergence of contradictory and dualistic features in polity, economy, and society.

(11) For the foreseeable future Hungary's major risks lie in its economic and social dualism and vulnerability resulting from (a) the chosen export-oriented strategy largely based on its off-shore multinational companies, and characterized by an overconcentration of its exports on only but a few firms and products, a few regions, and heavy dependence on imported inputs; (b) from its large but largely informal small and medium-size firm, sector; and (c) from its dualistic political system, and labor relations.

(12) The major lesson for Hungarian politicians and policy makers, then, is: there is much yet to be "democratized" in Hungarian democracy, and more to be done – not least by the Hungarian government – for a more cohesive, more integrated economy and society. Moreover, an efficient, integrated, and dynamic economy does not automatically

[38] For an original approach to the problem of rent-seeking in the context of neoliberal transformations in Latin America see Schamis (1998).

[39] For a similar argument on the former GDR see Brada (1996; 71), and on the Czech Republic Hayri, and McDermott (1998).

result in more equitable and liberal democracy. The corrective and inclusive function of the political system cannot be substituted for pure economic strategies, rather there is a separate need for institutions of more generous political inclusion, and for mechanisms of sharing the gains when they materialize.

(13) Finally, the major lesson for other countries including Poland, which have not made as strong strategic commitments as Hungary did is to think seriously in the trade-offs between the risks this country avoided and the ones it took. The balance can turn out to be both positive, and negative. Which will be the actual case in the medium run is hard to tell for the time being.

Table 1. Debt Relief and Equity Capital Provided to Banks and SOEs, and Bad Debts in 1992–97 in Hungary

Year	1992	1993	1994	1995	1996	1997	Total
Debt relief and equity capital to banks (bn HUF)	104 (1)	129.5 (2)	24	12 (3)	15.9 (3)	n.a.	285.7
Expenditures for firm reorganization, investment, and guarantees due (bn HUF) (4)	14.5	17.3	15.0	21.1	34.9	46.6	149.4
As a % of cash revenues from privatization (4)	11.3	44.8	38.9	4.8	34.9	14.4	13.7
Problem-loand held by banks (bn HUF) (5)	173.0	549.0	534.0	435.0	398.0	n.a.	n.a.
As a % of total outlays (5)	7.6	28.5	21.3	15.0	12.8	n.a.	n.a.

Sources:

(1) Fordulat és folytonosság 1995; 98.

(2) Fordulat és folytonosság 1995; 96. and Töréspontok 1996; 90. The major beneficiaries were: Magyar Hitel Bank, Kereskedelmi Bank, Budapest Bank, Takarékbank, Mezobank, Dunabank, Agrobank, Iparbankház. Actually, the banking sector got even more than this. Even after the consolidation program was concluded in 1994, several banks continued to receive further capital injections.

(3) Granted to Budapest Bank in early 1995 [Töréspontok 1996; 91], and in 1996, to Magyar Hitelbank, Konzumbank, Magyar Befektetési és Fejlesztési Bank Rt in 1995–96 [Törékeny stabilizáció 1997; 96–7].

(4) Hegymenet 1998; 150.

(5) Fordulat és folytonosság 1995; 98, and Törékeny Stabilizáció 1997; 96.

Table 2. Hungarian Macroeconomic and Social Indicators Before and After the Bokros-package

Year	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**
Budget deficit as a share of GDP (%)	0.0	-4.9	-7.0	-5.7	-7.5	-5.4	-2.3	-4.1
Current account balance as a share of GDP (%)	0.4	0.8	-2.9	-9.6	-9.4	-5.7	-3.7	-2.0
GDP growth rate (%, previous year=100)	-3.5	-11.9	-3.1	-0.6	2.9	1.5	1.3	4.0
Consumer price index (%, previous year=100)	29.0	35.0	23.0	22.5	18.8	28.2	23.6	18.3
Real wages (%, previous year=100)	-3.5	-7.0	-1.4	-3.9	7.2	-12.2	-5.4	4.9

Sources:
Törékeny stabilizáció 1997; p. 8, 11, 17, 18, 22, and Hegymenet 1998; 11–22.

Table 3. Government Revenues from Privatization (bn HUF), and Foreign Direct Investment (bn USD) in Hungary in 1990–1997

Form of revenues	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**Total**
bn HUF	0.14	4.81	17.55	27.61	25.71	25.71	25.09	108.78	235.40
Foreign exchange (in bn HUF)	0.53	24.61	110.67	10.95	10.95	412.05	77.50	208.39	885.65
Total cash	0.67	29.42	128.22	38.56	36.6	437.76	102.59	317.17	1091.05
Compensation vouchers	n.a.	n.a.	2.26	14.56	64.2	18.48	41.63	22.66	163.79
E-loans	n.a.	1.01	9.07	21.72	29.27	3.92	2.44	0.30	67.73
Foreign exchange loans and other	n.a.	n.a.	n.a.	n.a.	16.84	n.a.	5.16	3.80	25.80
Dividends	n.a.	0.93	7.41	5.41	7.80	13.81	8.15	5.77	49.28
Total revenues in current prices	0.67	31.36	146.96	80.25	154.77	473.97	159.97	349.70	1397.65
Total revenues in 1997 prices	3.0	105.4	401.3	178.9	290.3	693.4	189.4	349.7	2211.4
FDI (mn USD)	**1200** (1989-90)	**1614**	**1641**	**2481**	**1320**	**4570**	**2040**	**2107**	**16973**

Sources: Hegymenet 1998; 148, and 48, and Törékeny stabilizáció 1997; 20

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