Péter Mihályi

Why is the Hungarian economy poorly?

Diagnosis and therapy

HVG Books, 2008

With the 2006 elections completed, there was first a debate on the desirable economic policy, followed by the events of 2007-2008, and it was after the conclusion of these events that *Péter Mihályi* published the book (2008) that I am supposed to write a review on hereby but which I can provide only an opinion paper on. The two main starting points of the debate following the 2006 elections and preceding the events or at least the decisive part thereof, was an article by *Lajos Bokros, Tamás Bauer, István Csillag* and *Péter Mihályi* (2006) as well as a book by István Csillag and Péter Mihályi (2006). Discussing the above article of the four authors, the reviewer published an opinion paper (Szakolczai, 2006a) – alongside with many others, whose articles are not to be discussed here not for lack of merit but for lack of space – to which articles there was no reply. The reviewer also published an opinion paper on the above book of the two authors (Szakolczai, 2006b), to which – what is very important – there was a reply (Csillag – Mihályi, 2007), which latter the reviewer, again, gave a due response to (Szakolczai, 2007). The two authors' reply and the reviewer's response to the reply were published in issue 2007/1 of this journal, whereby the debate of principle stopped. It was this debate of principle that the book of Péter Mihályi (2008) returned to, and the reviewer is to follow hereby by the current opinion paper.

The *response to the reply* that concluded the previous phase of the debate of principle summarised the *agreements of opinion* between the authors and the reviewer in ten points first of all. This agreement of ten points is most significant (for the exact quotations and sources, cf. the original). ❶ Individuals should be encouraged to make savings. ❷ Although we must preserve our traditions, we must radically modify certain elements of it, like the attitude of "leaving our debts to our grandchildren". ❸ We must be successful in the competition of winning over investors. ❹ The implementation of stabilisation and reform should not be drawn out at will: immediate action is necessary. ❺ The reforms require wide social support. ❻ The transparency of public finance is a requirement of primary importance. ❼ The general government should have an accounting system capable of monitoring not only current changes but also changes in assets. ❽ The Maastricht criteria are arbitrary rather than scientifically proven but, as long as these rules of the game are applicable, we must follow them. ❾ We must stick to the appropriations related to the convergence programme until experience and calculations prove it necessary to modify them. ❿ Without a plan made with a cool head and the implementation thereof, our problems cannot be solved. – This wide-scale agreement could have led to a successful policy based on wide-scale agreement; we know that, unfortunately, this has not been the case, however.

Despite these important and wide-scale agreements of opinion, there were also deep *disagreements of opinion* and the *response to the reply* first summarised those referring to the *timeframe of 18 months proposed for the reforms* by the two authors as also apparent from the subtitle of their book (2006). ❶ The 18 months were not justified by international economic considerations. ❷ The 18 months were justified by domestic political considerations. ❸ It was the subordination of economic policy to domestic political and election considerations that had caused the crisis which had developed by then and it is thus imperative to break with such practice. ❹ The implementation of the reforms did not appear to be feasible within 18 months from the very beginning. ❺ The latter lack of implementability within the timeframe was also confirmed by the unrealistic nature of the calculations published in the appendix of the book. ❻ The reforms could not be expected to accelerate economic growth. ❼ As the reviewer opined from the very beginning, due to the insistence on the 18 month timeframe, the reforms could not even lead to either stabilisation or a better international judgement of Hungary. ❽ The insistence on the 18 months, under the reviewer's above opinion, raised the danger of a political catastrophe. ❾ The insistence on the 18 months, under the above opinion of the reviewer once again, also raised the danger of a political identity crisis. ❿ This concept and policy, as similarly outlined in the above opinion of the reviewer in the very beginning, was furthermore counterproductive in the political sense because, instead of the hoped for success at the next elections, it was likely to lead to an unprecedented failure. – Advancing the conclusion of this article, predictions could not have come more true.

The above was followed by further *basic disagreements of opinion: is the major cutback on the welfare state justifiable and implementable?* Under the reviewer's opinion formulated in the very beginning already, it was neither justifiable nor implementable, for the following reasons.

❶ It was not proven and has not been proven until today that the reason for Hungary's lag is the relatively large-scale redistribution.

❷ It was not proven and has not been proven until today that the lower the tax rate, the more we are interested in its proper use – it is rather the contrary that holds true.

❸ The way out of the tax competition is extending legal harmonisation to the restriction of tax competition.

❹ There have been numerous arguments, not to be listed here, in favour of maintaining the welfare state. Under the reviewer's opinion, the positive result of cutting back on the welfare state and on the role of the state was and has remained a preconception unsupportable by facts or scientific arguments.

It should be emphasised here that, as the reviewer agrees, it is unavoidable to restore budget balance: this is a necessity well proven. What has not been proven, however, and it is thus, to put it harshly, a preconception, is that the only and the desired way to achieve this is by cutting back on the welfare state and on the role of the state.

The third *basic disagreement of opinion* referred to any form of a *reform dictatorship: should any idea, even a best one, be implemented against the will or even without the active contribution of those affected?* The reviewer believes it should not; it ought not even to be attempted. Society, as the authors also pointed out, cannot be made happy against their will. The original response to the reply included a lengthy quotation by *László Csaba* on this, who says the following on the issue: "It seems that in social sciences the day of experimenting with and implementing plans conceived at a writing-desk for societies as a whole, in brief, the day of *constructivism*, is on the decline." (Csaba, 2007a, p. 7)

• After summarising the main conclusions of the response to the reply, let us now discuss Péter Mihályi's new book (2008b). Right away in *Chapter 1,* the Introduction, the author makes his main postulate clear. He quotes *Márton Tardos* and Tamás Bauer who, in the early eighties, said that privatisation was impossible. Although Tardos discussed the impossibility of reprivatisation rather than that of privatisation, which former was indeed not implemented, Bauer explicitly wrote that "the elimination of capital ownership, a thirty years' practice, has become an irreversible process that could only be changed by outer colonisation" (p. 10), and yet, capital ownership has returned: privatisation has been implemented. What Tamás Bauer said on colonisation, on the other hand, is very much worth consideration. Mihályi also quotes *László Antal,* who says: "it is doubtful if, from a fully developed social security system with historical traditions, one that society has got accustomed to, it is possible to regress to a much narrower social welfare system, since this would generate an abrupt growth of inequality and social tension, i.e. this is not an open gate for Hungary." (p. 12) Mihályi, on the other hand, pointedly argues that this is not only an open gate for Hungary but this is in fact a gate to cross: "in an open, democratic market economy", we should not "provide incubator protection (….) for the premature infant" – the phrase clearly referring to the "premature welfare state" (pp. 11–12) –; on the contrary, the welfare state should be downsized: together with the issue of "general government balance, these are the key issues of the coming years" (p. 12). The author thus argues that privatisation was held impossible and yet it was implemented; so downsizing the welfare state should just as well be implemented even if some hold it for impossible.

With reference to the response to the reply quoted in length above, the reviewer must point out here in Chapter 1, the Introduction, already that, in his view, Mihályi's main postulate is not only not to be shared but, considering what has happened in connection with the health care reform, this main postulate should not even have been put down, let alone with the implication that it was something obvious and beyond doubt. What has happened in Hungary in the past two years spectacularly proves that "from a fully developed social security system with historical traditions, one that society has got accustomed to", it is not possible "to regress to a much narrower social welfare system". Yet, just as the agreements of opinion were listed in 10 points in the response to the reply, basic agreements of view should also be pointed out here, too. Mihályi is absolutely right saying that "there is approximately 10 per cent excess [domestic consumption] (…) to GDP" because of which "sooner or later, in one way or another, a correction of a similar rate will be (…) necessary" (p. 11). This is *beyond doubt,* as the reviewer has also pointed out in several works that are not to be referred to here, so in this respect there is an *absolute agreement of opinion* between the two of us. "Sooner or later" – sooner rather than later ; "in one way or another": the main question is whether in this way or another, i.e. what is the way; this correction, i.e. *ending domestic consumption beyond our means, is inevitable.* In this respect, I am in absolute agreement with the author, while, as pointed out before, I do not consider it proven, on the other hand, that the only alternative for this correction could be largely diminishing or almost eliminating the welfare state. This basic, conceptional difference of opinion must be underlined, pointedly and clearly, in Chapter 1, the Introduction, already.

■ *Chapter 2: Reform – why now?* – is devoted to the timing of the reform and this is where we should refer back to the antecedents. In their article entitled "Last Chance" (2006), Lajos Bokros, Tamás Bauer, István Csillag and Péter Mihályi say the following : "In the second third of the year 2006 (from May until the end of August), all important bills related to the public finance reform must be worked out. In the third third of the year (from September to New Year's Eve), Parliament must discuss and pass these bills." This article thus set out an eight-month timeframe for "all important bills" to be passed. The scheduling is somewhat more modest in the book of István Csillag and Péter Mihályi (2006), since the book bears the subtitle "The eighteen months of stabilisation and reforms", while political considerations are more overtly expressed here: "The question is if there will be a political situation, if there will be a government with ministers who, working together as allies, are able to carry out in 18 months what they know, deep in their souls, must be carried out. And then they will still have 30 months left to prepare for the next election battle." (p. 96) The above formulation thus reveals that the scheduling of the reform is clearly subordinated to election considerations: the reforms should be implemented within 18 months so that the 30 months thereafter could be enough for electors to forget it all and to re-elect the government. Finally, with not 8 or 18 months but as many as 26 months having passed, Chapter 2 of Péter Mihályi's new book (2008), under the title "Reform – why now?" begins as follows: "As dream books of politology suggest, it is not advisable to initiate comprehensive reforms in the middle of a four-year parliamentary cycle, let alone at a time of minority government. There is no need to discuss here the strong arguments supporting this. It is the opposite that would need an explanation." (p. 17) And there is an explanation to follow here, coming to the final conclusion that "it is only at times of crisis when society can be expected to accept genuine reforms. We have nearly got there already." (p. 21)

So here we are with a short deadline once again – as if we did not have the bitter experience of the past two years behind us. There is only one quotation that should be added to the above: "However, creating the proper size of a welfare state that is economically and socially acceptable is a task for which the designated time limit of 18 months for implementation is plainly inconceivable. The authors' approach (…) is (…) counterproductive, because their efforts aimed at incorporating in the 18-month timetable questions that cannot be resolved within such a short time actually represent obstacles to accomplishing the very measures that indeed belong among the tasks of this 18-month period. " (Szakolczai, 2006b, p. 509). The lesson of the Bokros package is also clear. While an 8 per cent import duty or crawling peg or – for further proof of commitment – some cutting back on certain welfare services of almost insignificant effect regarding the budget can be introduced within 8 months or in fact a time much shorter, in just 1-2 months, the reform of the welfare system cannot. It is incomprehensible how four noted authors in the first instance and two in the second case – including two and one former ministers respectively – could put down something like that. Finally: the "situation of crisis" described in Mihályi's current book (2008b, p. 21) would assumingly not exist, or would at least not be so severe, if the 8 and 18 months had not been formulated as a necessity and, more importantly, if these timeframes had not been attempted to be implemented.

The discussion of this chapter would not be complete, however, if *basic agreements of opinion* were not noted. While the reviewer does have reservations about the crisis index, one could not more agree that stagflation is a real danger and especially that the fall of the gross accumulation rate from 31 to 23 per cent in just six years is a real national catastrophe. It is thus indeed inevitable to "reverse (…) this bad trend" (p. 20).

■ *Chapter 3 – The unchanging model: welfare state from the cradle to the grave* – would be the theoretical basis of the book if it could really be qualified as such but one can certainly not strive for making a theoretical basis in just eight pages. It offers two postulates, both of which appear at the beginning of the book already and many times, repeatedly, later on. The one is that, "until today, we have failed to back out of the dead-end of socialism and of the centralised economy" because, while we have successfully implemented "national freedom, (…) the privatisation of major companies and the permeability of borders", the issue of "separating the two most important social welfare systems, pensions and health care, from public finances (…) has not even been raised." (p. 9) This in fact means that the welfare system, or at least the current form of it, is a heritage of "the dead-end of socialism, of centralised economy". (Ibid.) The other postulate is that the Hungarian welfare state – under the term introduced by *János Kornai* – is "premature" (p. 10).

The first postulate, in its current form and undisputable way, is wrong. The welfare state dates back to the time of *Bismarck*, when there was neither a "Great October Revolution", nor a planned economy, nor "socialism implemented", and least of all was there a *János Kádár.* Besides, today's problems of the welfare system – the financing difficulties caused by the ageing of society and the development of medical technology – are much the same in Western Europe, where there has never been socialism like in Eastern Europe. Thus the problem is a global one rather than a "post-socialist" phenomenon, even if there are no two countries alike and no two welfare systems completely alike: the German system and problem are not the same as those of Hungary, for example. The reviewer cannot even share Mihályi's assumption that there were five points that "planners (…) took as a basis" (p. 23), either. In the reviewer's opinion, what the planners took as a basis was the absolute correct realisation that individual and social preferences were different. If, under the Soviet conditions – and also under other conditions – the rate of payments in money had been higher and that of payments in kind had been lower, more money would have been spent on current consumption goods and less on education, health care and housing. To put it absolutely crudely, there would have been even more money spent on vodka and less on the improvement of cultural, health care and housing conditions, which would have hardly been favourable for society as a whole, let alone the development thereof.

As regards the second postulate, "the premature welfare state" as János Kornai formulated it, discussing it here would be somewhat impolite. On the one hand, it is impolite to discuss a term coined by such a distinguished author, which term is used not only nationally but almost all over the world, in a review on another author's article, as if in passing – but it is unavoidable to discuss it due to the series of references made to it by Mihályi. On the other hand, Kornai's relevant article was published in 1992, i.e. 16 years ago, and it is impolite to call somebody to account for something that, thank to the development of science, is widely known today but was not at the time.

The reviewer's first remark related to this term is that its formulation, its highly effective character and wittiness prompted authors to use this slogan contrary to Kornai's intentions. The term has had an independent usage, in Mihályi's book and elsewhere, and has been used to support intentions, proposals and actions – by Mihályi, too – that have not met Kornai's intentions. The second remark is that the postulate, as has become clear by today, is imprecise; under the current stance of science, we would put the emphasis elsewhere.

Let us begin with the second remark. Kornai's original formulation in question is as follows: "The Hungarian welfare state is »premature«. According to a general observation, there is a close positive correlation between the economic development level and the size of welfare services of a country. The level of development is not the only determinative factor but is undoubtedly one of the basic ones. In this respect, Hungary »ran ahead of time«." (Kornai, 1992, p. 507) The way we would formulate this today would be rather that the size of welfare services – using the term coined by *Douglass C. North* – is path-dependent: it depends on the historical traditions and earlier political decisions of a country. As was also pointed out in the elementary study book by *Samuelson* and *Nordhaus,* which I referred to in an earlier article: "the budget, the welfare state and state redistribution, and in fact the state as a whole have inevitably a lesser role in the colonial states, such as the United States, and a larger role in societies where traditions have a stronger part to play, like in Continental Europe." (Szakolczai, 2006b, p. 498). Certainly, both factors have a role. Kornai also underlines that "the development is not the only determinative factor but is undoubtedly one of the basic ones". The way we would formulate this today is that it is traditions and earlier political decisions that are central and their effects may be influenced by the level of development.

The above postulate is clearly supported by the figure published on page 27 of the Mihályi book currently discussed, which lists OECD countries according to their welfare expenditure as a percentage of GDP in the year 2003. If development was the factor of primary importance, the United States would be on the right hand side of the figure, among the states where the percentage of welfare expenditure is the highest. This is not the case, however. The United States – following Korea, Mexico, Turkey and Ireland – is number five from the bottom. Other countries on the left hand side of the figure – under the OECD average – are Canada, Australia and New-Zealand, i.e. English-speaking settler countries as well as – due to the high cultural similarity – the United Kingdom and Ireland. On the right hand side of the figure we can find the countries of continental Europe, on the other hand, Scandinavian countries being towards the right edge, with Sweden right on the edge. What is more, Hungary, considering the two factors simultaneously, is in its right place in fact: according to its continental European historical traditions, it is on the right hand side of the figure while, due to its relatively low development level, it is towards the left compared to Italy, Austria, Germany and France. This position does in no way justify a reduction in the rate of social expenditure; on the contrary, it would justify a continuous and gradual increase of the rate of such expenditure in the hope of catch-up towards the level of Germany and France. It should certainly be also considered that in these countries there are currently efforts to reduce this rate, so the target set should thus not be the current level of France or Germany but a level somewhat lower than that.

Let us now examine the same in a historical perspective. If it holds that social expenditure depends on the level of GDP, i.e. if higher GDP per capita involves higher social expenditure, then at around 1880, at the time of the Bismarckian reforms, Germany should have been the richest country in Europe. Everybody knows, however, that this was not the case. Under the figures published by *Angus Maddison* (2003), the actual situation was the following *(see Table 1)*.

Table 1

GDP PER CAPITA IN 12 WEST-EUROPEAN COUNTRIES IN 1880

1900 international Geary–Khamis dollars

United Kingdom	3 477
Belgium	3 065
Holland	3 046
Switzerland	2 450
Denmark	2 181
France	2 120
Austria	2 079
Germany	1 991
Sweden	1 846
Norvway	1 588
Italy	1 581
Finland	1 155

Source: Maddison (2003, pp. 60–61)

These figures need no explanation. At the time of the introduction of the Bismarckian reforms, Germany was among the less developed countries; to the reviewer surprisingly, even Austria was ahead of it in the list. Remarkably, it was the "poor, pitiable, beggarly" Scandinavian countries that were bottom of the list. Furthermore, there are no signs at all suggesting that it was richer countries to construct a welfare system. On the contrary: what can be established is rather that the introduction of the welfare system was *rather a means of catching up.*

Let us now examine Kornai's actual intentions and recommendations, which are most apparent from the following quotations. "We have heard some radical proposals aimed at diminishing the role of the state (…) in the [welfare] sphere to a great extent, at least to the level characterising e.g. the United States today, in short time. With the exception of a narrow band financed by the state, fast and far-reaching decentralisation and privatisation should be implemented in both health care services and the pension system. (…) The only thing I wish to underline in this respect is that (…) it makes a difference where we come from and we are heading. It is one thing to decide on whether the state should grant its citizens certain rights that they have not enjoyed before, and it is another thing to decide on the withdrawal of earlier acquired rights that citizens are accustomed to. (…) The wheel of history turns in one direction, but it cannot start turning backwards. If in Great Britain there had been no state-financed health care before the time of *Margaret Thatcher,* her government would probably not have decided for its introduction. But, since it had existed before Mrs. Thatcher, her government did not propose to liquidate it." (Kornai 1992, p. 508) "Citizens of post-socialist societies experience much uncertainty that they were not familiar with before. (…) It would severely shatter many people's feeling of social safety if, on top of the above, state-guaranteed health services, pension provision and several other welfare services collapsed around them. There is immense resistance against the fast and drastic reduction of state welfare services and the decentralisation and privatisation of welfare duties. What is more, it is exactly the economic difficulties of the transition that put new items of expenditure on the agenda." (Ibid.) Considering the above, it can in no way be argued that, using the slogan of the "premature welfare state", Kornai wished to suggest suffocating the premature newborn. It would have been fortunate if those referring to Kornai had not only taken over a single term by him that they had heard from a secondary or tertiary source but would have taken the trouble to read what he had actually said.

It is László Csaba (2005, 2006, 2007) who formulated the view in accordance with "the current stance of science" with reference to post socialist countries. According to his latest work (2007) presenting the latest data and the latest and presumably most precise conclusions drawn on the basis of the former, "the development of "post communist" states has taken permanently different courses" (pp. 258–259). "The transformed countries can therefore be put into the following four categories as regards content. 1, The "rest of Visegrád" plus Slovenia. (…) 2, Baltic states plus Slovakia. (...) 3, Southeast European countries, i.e. Bulgaria and Romania plus Croatia. (…) 4, Countries of the Community of Independent States (…)." (p. 266) "The common past does not haunt them; it is differences that are becoming permanent ." (p. 283). "Transformed countries constitute permanently different groups. Therefore, assumptions on a uniform and optimal way of transformation or on a more or less arbitrary re-allocation of certain countries from one group to another are both irrelevant. At the same time, the example of Romania and Slovakia prove that there is always some room for change." (p. 283) Accordingly, the "debates in many of the social sciences that have continued until today, considering "what sort of capitalism should we now choose?" lacks a material basis" (p. 278), since " the individual groups have been formed much rather along long-term path dependence than along the ideologies of the various periods and eras" (Ibid.). Mihályi's proposal that the welfare state should be most radically eliminated or at least diminished thus lacks a sufficient scientific foundation. In West-Central and East-Central Europe – comprising Germany and Austria as well as Poland, the Czech Republic, Hungary and Slovenia – the Bismarckian welfare traditions are deep rooted and are difficult to uproot through some radical ideological assault.

There is the case of Slovakia, on the other hand. In this country, the radical cutback on welfare expenditure has been successfully implemented – if one can speak of success in this respect at all. There is a high price to pay for it, however. As is presented by Győrffy (2007b, p. 141), regarding all Central-East European countries, the rate of people who prefer the old system to the new one from a financial point of view is the highest in Slovakia: in 2004, it was almost 70 per cent – followed by Hungary, with over 60 per cent. This, according to Győrffy, (2007a, p. 196) has the consequence that in Slovakia – like in Lithuania – "the low level of trust in the [political] regime provides considerable incentives for the erosion of the consensus" (Ibid.), and, consequently, "[economic political] sustainability can not be taken for granted" (Ibid.). Considering these consequences, this is a result of dubious value and does not justify the correctness of the radical cutback on social services in the only country where the latter has been successfully implemented. Besides, exactly because of the dissatisfaction, the government that implemented the reforms has failed, so there may arise justified doubts as regards the durability of the reform. It is a great lesson to learn, at the same time, that the reforms in Slovakia were implemented during two cycles, after due preparations, in a considerate way.

▪ *Chapter 4* bears the title *Changing reality* and is actually an introduction to Chapter 6 presenting the proposals, because of which it can be discussed only briefly. *Subchapter 4.1* has the title The interest alliance of employers and employees against the state, and discusses the fact that neither of these groups like paying tax and contributions. Subchapter 4.2, entitled Work is no obligation – and it is not worth working anyway!, is significantly more problematic. The essence of the problem is in fact what the author described as such: "The workforce of the 5 million employees registered at the time of the change has fallen by over 1 million" (p. 43), which means that, accordingly – as the author most precisely reveals – only 3,947 thousand people of the 7,719 thousand of employment age, i.e. just 51.1 per cent, are actually employed. The reason why the rate of employment is so low is, however, not that people do not want to work but that there is no work. The situation is perfectly described already in the title of *Subchapter 4.3* – The hopeless situation of undereducated employees: this is the sad reality.

In the rest of the subchapters, however, the author, following in the wake of *early globalization theorists* (Győrffy 2007a, p. 155), overestimates the actually existing tendencies, the reviewer believes. It is true that, as pointed out in *Subchapter 4.4:* "[There are] Hungarians abroad and foreigners in Hungary", and, as *Subchapter 4.5,* "No work place, no work time (…)" says, the rate of atypical employment is growing. It also holds that, as according to *Subchapter 4.6,* the rate of "intangible families", i.e. "atypical families" is similarly on the rise and finally that, as *subchapter 4.7* underlines, "Everything depends on your flat", i.e. housing property has wide-reaching effects. Yet, all the above does not mean that the traditional conceptual system of statistics, employment and labour affairs, taxation and the welfare system as a whole has completely lost sense and what we face now is an absolutely new situation, as the author seems to suggest. And even less does it follow from the above what is described in the beginning of *Subchapter 4.8* entitled Subsidy for the sake of subsidisation?, i.e. that this is a *"squirrel's wheel of zero efficiency"* (p. 65, italics in the original, Gy. Sz.). Irrespective of the above – to emphasise a basic point of agreement of great importance once again – it is true that in Hungary, just like in the United States before, a group of not insignificant size of people *living traditionally* on aid has been formed. This is indeed untenable; the aim of aiding in this case should be creating employment ability rather than sustaining the lack of it. This is, however, no argument against the system of the welfare state as a whole, as this chapter, very well written from a publicist's point of view, seems to suggest.

■*Chapter 5 – What has become of the health care reform* – is really what its subtitle promises: A *subjective account* (p. 73) of the events: a real novel to be read, which is difficult to be reviewed on. The reader learns first of all that the author has been engaged in the problem of Hungarian health care since 1997 and that former minister of finance *Péter Medgyessy* commissioned him to work out the health care reform (p. 73), moreover, the author has even written a study book on the issue (p. 74). It was at the time of the 2002 parliamentary elections that he became really close friends with *dr. Lajos Molnár* (p. 75). "When SZDSZ [Alliance of Free Democrats] was preparing for the elections, the complete preliminary version of the bill on health insurance companies was available to read on the party's homepage. Not a single line of it could be read on the homepage of the Health Care Work Group of MSZP [Hungarian Socialist Party], on the other hand. This is thus the way dr. Lajos Molnár became minister of health and dr. Ágnes Horváth became his deputy." (Ibid.) "It is a fact that (…) the situation of Hungarian health care could still be considered as good in the year 2006. (…) If (…) somebody goes to see a doctor or gets into hospital (…), he will get the basic treatment and medication even if he does not give the doctors any gratuities and does not have a private health insurance policy." (pp. 77–78)

"In autumn 2006, minister Molnár and myself consulted with economic experts close to both SZDSZ and MSZP, with László Antal, Tamás Bauer, László Békesi, Lajos Bokros, István Csillag and György Surányi (…), on the opening of the health insurance market several times." (p. 89) "In spring 2007, (…) the unexpected, voluntary resignation of Lajos Molnár left no choice for MSZP and made the situation of SZDSZ easier in the short run. (…) It was thus (…) that a compromise solution was made on June 30, 2007, the last work day of the spring parliament session." (p. 93) While this was probably an unexpected turn for the ministerial apparatus, "it was even a greater surprise for insurance companies. Insurance companies had been working hard for the previous 12 months, too. They had regularly attended the Ministry of Health for consultations, they must have held consultations with one another as well, and they had probably made numerous English and German-language summaries and records for the management of their parent companies. But because there were a huge project and a huge market at stake – some HUF 1,000 bn annually – they did not complain at all when invited to the negotiating table on the hot days of July and August." (p. 94). "The situation got more and more distressing day by day, which opinion was shared by the insurance companies attending the negotiations as well. Therefore, in the last days of August, I requested the head of the insurance consortium to express their concerns to the top leaders of the two parties. The message reached its goal. Prime minister Ferenc Gyurcsány summoned a meeting of the faction leaders and experts of the two parties as well as of the potential investors in Parliament, to be held on September 13." (p. 96) "Already in September 2007, the leaders of MSZP (…) opined they had no chance for success with the health insurance reform within their faction, either. From then on, all their efforts were merely aimed at saving what could be saved and minimising the loss of prestige for as long as six months – right until the national referendum held on March 9, 2008." (pp. 96–97)

"Would there have been investors?" (p. 97) "In the second half of 2007, some of the insurance companies really lost interest. (…) For some of them it must have been the last straw when, at the end of 2007, wisemen of MSZP and experts of the Ministry of Finance raised the base fee of the privatisation bid to HUF 12 thousand/ person. This means that every investor should have paid *at least* this amount when purchasing the minority share package of the 22 state-established health insurance funds. Calculating with the population of 10 million, this means an investment of HUF 120 bn or, when divided up for 7–8 funds, HUF 15–17 bn per fund. This was far more than what could be considered as profitable under the given boundary conditions." (p. 98) "The decisive question now is which of the measures already taken during the health care reform may be long-lasting and in the case of which should a fast and absolute restoration of the original state be expected." (p. 111)

▪ In principle, *Chapter 6 – What should be done?* – should be the central and most important chapter of the book. The Basic principles are to be found in Subchapter 6.1. ❶ "The change must begin in the social security system. (…) These systems must be privatised, their financing must be separated from the state and the direct feedback mechanisms between individual payment and eligibility must be made significantly stronger." ❷ Everybody must be granted "portability of eligibility, i.e. that, in whichever country they live and work (…), their insurance legal relation should be continuous and guaranteed". ❸ "The above does not mean giving up the social security principles as interpreted under EU norms." "State provisions (…) are guaranteed as subjective rights (…); social aid and subsidies (…) are available on the basis of eligibility." ❹ The creation of employment opportunities as a conceptual construction is something to forget. ❺ "Hungary (…) will be unable to resist (…) the temptation of one-bracket linear taxes referred to as flat taxes." ❻ "Social and welfare expenditure as a whole (…) should be cut back on as fast as possible." ❼ "It is inevitable to (…) revise and/or correct the wrong decisions made in the past 10 years." ❽ "The net migration balance (of minus 3 per cent) of university graduates characteristic today [must] be turned in the positive direction." ❾ "It is essential to present the reform of the tax and contribution system in an integrated package." (pp. 115–118)

The summarised review of this nine-proposal package can take place only at the end of the overall review, but the reviewer wishes to point out right away that the package is heterogeneous, with proposals of various weight, and that the reviewer does not support most of the proposals. The details are to be discussed briefly as follows. *Subchapter 6.2* discusses double grossing up, i.e. that nominal earnings must include all contributions. *Subchapter 6.3* bearing the title Solidarity and proportionality supports the idea of "fixed amount pension contributions" and "fixed amount patient insurance fees" (p. 126) adding that this latter "could be implemented only gradually" (Ibid.). The title of *Subchapter 6.4* is Making social security funds independent from the work place and the state. The main conclusion of *Subchapter 6.5* bearing the title Transition to sector neutral taxation is, the reviewer opines, that "in general and proportional burden sharing in Hungary, progressivity is hardly implemented even in principle" (p. 137), which suggests that this issue should rather not be dealt with at all. According to *Subchapter 6.6* focusing on the reform of general and proportional burden sharing, "reducing the relative significance of income-dependent taxation is an extremely urgent task" (p. 140). At the same time, this subchapter firmly supports progressive inheritance tax. The reason why this proposal is problematic is, however, that it would affect domestic capitalists only and – considering the almost absolute lack of savings by domestic households – would thus further increase foreign ownership ratio. The same subchapter demands the "reduction of social (welfare) expenditure" once again (p. 142). According to *Subchapter 6.7* discussing the question of local taxes and subsidies, "although the European Union has not found any fault with it, we should eliminate local industrial tax for our very own interest" (p. 143), while, at the same time, "easing old-age poverty is something that should rather be dealt with largely by local governments" (p. 146), which latter is a suggestion made without any reference to the source. Finally, according to *Subchapter 6.8,* "demands of West-European level are simply not to be met within the framework of small enterprises, at competitive prices!" (p. 149). The labour market subsidies designed and earlier introduced for small and medium enterprises have all proven counterproductive techniques generating corruption. These, too, must be cut back on". (Ibid.) "There is no need for any amendments in tax or contribution regulations targeted especially at the small and medium enterprise sector." (pp. 149–150)

■ As the closing *Chapter 7,* there follows the *Epilogue, or where did Ferenc Gyurcsány make a mistake?,* which raises two questions as a way of introduction: ❶ "What was the opinion of the leading officials of the social-liberal coalition headed by Ferenc Gyurcsány on the reform proposal outlined in this book? ❷ Why have these proposals failed to be implemented almost completely?" (p. 151) "I definitely know the answer to the first question" – the author continues. "Neither Ferenc Gyurcsány, nor János Kóka had a view on the problems of the Hungarian economy, on what needed to be done and on the main direction of progress different from that of the author of this book. This can even be proven by documents. " (p. 152) At the same time, "there are three main reasons to explain why the reform strategy of the prime minister-party president has failed." (Ibid.) ❶ "He is a liberal reformer leading a socialist party." (p. 152) ❷ "The question of order." (p. 153) Here the author lists the various tactical mistakes made by the prime minister. ❸ "The time factor." (p. 155)

As regards the time factor, Mihályi argues, without actually stating it, for the 18 months urged by the two authors (Csillag – Mihályi 2006) or much rather for the 8 months urged by the four authors (Bokros – Bauer – Csillag – Mihályi 2006), when saying the following: "In 2006, the government had Parliament pass five important health care-related bills at a very fast pace. The sixth and most important bill, referred to as the fund bill, could have been easily passed with the same impetus. The prime minister believed, however, that it was wiser to postpone that to a later date. He was very wrong. The delay gave an opportunity for persons not related to health care at all – within the Socialist Party and outside it – to join the debate, organise themselves (cf. the railway strike) and, through the thousand channels of social publicity and populist communication" – he says – "discredit the conception of government parties" (pp. 155–156) – which conception, as Mihályi unmisunderstandably pointed out earlier, was not and could in no way be the conception of the Socialist Party. Mihályi thus suggested that, with a single rush, that is before the bigger coalition party MSZP and the public could have understood what was going on, everything could have been passed – and he is probably right about this.

"Three is the Hungarian truth" – as they say – "and four is the extra on top". Among the three postulates of Péter Mihályi there is a fourth one, since this is an independent postulate due to its weight. This postulate is that the main reason of the slowdown was probably the hope of EU moneys – which was a vain hope that the reviewer had warned both political and economic leaders and the public against, in all his related writings. The last three paragraphs of the book – by which the author did not confute himself – describe a "Minimum package until 2010", i.e. another 8-months or 18-months or something similar, which begins by a "grossing up". (p. 158)

The discussion of the book being completed, let us now start the review part. The book bears the title Why is the Hungarian Economy Poorly? and the subtitle Diagnosis and Therapy. In the reviewer's opinion, the most important elements of the diagnosis are correct, but this diagnosis does not or does not necessarily lead to the therapy recommended by the author.

The right diagnosis is revealed in Chapter 4, and especially in subchapters 4.2, 4.3 and 4.7. Here the author clearly states the obvious, as has been quoted before. Following the political change, employment fell by one million; only just a little more than half of the population of employment age are employed; the situation of undereducated employees is hopeless and – as *Zsuzsa Ferge* has formulated it – "there are generations growing up (…) in aid culture" (p. 66). Why is the Hungarian economy poorly? – This is why. The diagnosis is perfect. The diagnosis could be continued at length: much of society is falling hopelessly behind – in fact such a great part of it that it may drag along the whole society. Whether the part falling behind is one third of society, half of it or even a greater part, is subject to discussions and definitions – it is hardly disputable, however, that only some one third of society, if any, is on the right path.

The wrong therapy, running through the

whole book, is downsizing the welfare state and cutting back on (p. 117) and reducing (p. 142) social and welfare expenditure. This therapy, however, as the reviewer has pointed out above, does not follow from the diagnosis but it suitable for making the patient more ill. If the diagnosis is that one million people of employment age do not have a work place and are not suitable for modern employment, either, then the only therapy may be to make them suitable for employment and through this way primarily, as well as by other means, to ensure their employment. This, however, requires strengthening the welfare state rather than diminishing it, and makes its restructuring also necessary in the sense that its primary goal should be not to sustain the hopeless situation of people in hopeless situation, making it at least bearable, but to eliminate the hopeless situation and make social rise possible. Restructuring the system is very different from diminishing it, however.

The most important element of the wrong therapy is making a closer connection between individual payment and eligibility to services, i.e. self care, although the author does not use this phrase explicitly. The basic assumption of the conception is that a closer connection between individual payment and eligibility, i.e. the realisation of the necessity of self care forces out self care, voluntary payment or at least the voluntary meeting of the obligation; moreover, even saving. If deduction is transformed to payment, force is replaced by voluntariness and what has been proven impossible to force out – cf. the one thousand methods of tax and contribution avoidance – will now be implemented voluntarily. This is an illusion, however, which does not become reality even in the upper third of society; the foresight of the individual is always weaker than that of the community. Twenty year olds have no way to know if they will live to be seventy or eighty but society must know that there will be old and ill people in fifty and sixty years' time, too. To assume fifty years' foresight and self care on the part of the lower third of society, however, is not an illusion any more but is self deception, which no social policy can be based on. Strengthening the connection between individual payment and eligibility in the lower third only leads to a decrease in eligibility, and in fact a major decrease, with all the tragic economic, political and social consequences involved. Thus, diminishing the welfare state, which necessarily deteriorates the supply of the lower third of society to the greatest extent, can only make the already hopeless situation of undereducated employees even more hopeless, increase the division of society and add to trouble. It is thus unmisunderstandably true that this therapy is contrary to the diagnosis.

The other critical element of the differences of opinion between the author and the reviewer is the reduction or increase of income, assets and social differences. While the author aims at increasing these by almost all of his proposals, the reviewer believes that all efforts should be made to reduce them. Differences are clearly increased by reducing the welfare state and cutting back on welfare services, and numerous other proposals of the author from emphasising the taxation of consumption to flat tax, fixed pension contributions and patient insurance fees all have a similar effect. In the reviewer's opinion, these proposals all make the diagnosed illness worse, fostering the fall behind of a great part of society and the division of society as a whole, because of which they are unacceptable or only certain elements of them may be acceptable after due consideration and within the framework of a complex programme.

So what will happen to the budget under such circumstances – this is a question that Péter Mihályi could justifiably raise. The answer, with reference to the Swedish example, can be found in Dóra Győrffy's book (2007, pp. 139–172). Sweden strongly committed itself not simply to sustaining a cyclically corrected budget balance but to attaining a 2 per cent surplus, i.e. to reducing the debt stocks (p. 159). This target was not reached by eliminating the welfare state, however, but by the complete transformation of the system of budget making. Instead of demands, Sweden took the framework figures made possible by national economic and macroeconomic considerations as a basis; they rejected the lawnmower principle, too, and made it every minister's own task – "every minister is his own finance minister" – to make the necessary savings within their ministries in the fields where this demanded the least sacrifice. The result is clear: the deficit has disappeared – the surplus has been attained – the welfare state has been sustained.

In the reviewer's opinion – going back to the beginning of this article – there are thus many things we must forget:

- we must forget the various 8-month or 18-month timeframes;
- we must forget the primary importance of domestic policy to economic policy;
- we must forget the elimination of the welfare state;
- we must forget the increase of income differences; and what is most important of all,
- we must forget constructivism, i.e. the conception of forcing through solutions constructed at the writing desk or imported from elsewhere.

After discussing the serious and basic differences of opinion, let us – like before – return to the views shared. As the reviewer earlier pointed out that it was inevitable to create a budget balance, it must be added here that the transformation of the taxation system is similarly inevitable, the transformation of social security systems is inevitable just the same; moreover, even a greater reliance on self care is inevitable. Mihályi is right about all these, the reviewer agrees, and several of his actual proposals are well-grounded and worth considering. The Swedish welfare state could be sustained not because it was left unchanged but because it was transformed, and also because the order of budget-making was also transformed. There can be hardly any dispute as regards the required direction of the transformation. Investment in human capital, i.e. expenditure on health care, education and especially further training and retraining, must be sustained or even increased – it is especially in the latter field where an increase is justified or even inevitable. At the same time, financial subsidies given to people without employment may be reduced, and some of it may actually become superfluous as a result of fruitful retraining and further training. Retraining and further training may become an investment with fast return; it is widely known that there is a shortage of labour in some professions. Therefore, the financing of the welfare system is problematic in countries where the welfare system has not been transformed and the system of taxation and the order of budget making have not been amended. It is thus not the reforms that the reviewer protests against: reforms are inevitable; he protests against reduction or elimination and – certainly – against unrealistically short deadlines. Yet, the protest against unrealistically short deadlines does not mean that the reforms should be postponed. Quite on the contrary, they must be urged, but with due preparation and with the greatest possible support of the profession and of society.

This is the point where we can return to the last chapter of the book, the failure of *Ferenc Gyurcsány's* attempt. The first element of the failure is clear: the theoretical construction – which, Mihályi claims (cf. p. 152), was the same as his, and this was probably the case indeed – was wrong, and a wrong construction must fail sooner or later. As regards the second unit, the following can be read about it in the book: "Gyurcsány (…) [was] obliged to accept also the reform rituals inherited from the past. One of these – for example – was the widely mentioned institution of social debate, the need for which is talked about as much in his party as if it was the most natural thing in the world. It is not that at all, however. In a representational democracy, all important debates, including debates on reforms, must be held in Parliament. "Social debate" is inherited from the time of the single-party state and is an institution contradicting the letter and spirit of the constitution in force; in the legal sense, it is in fact non-existent already." (p. 153)

In this review, quite a number of basic disagreements of opinion have been revealed already, but there is still an absolutely basic one. The reviewer des not wish to quote the Constitution, but it is widely known that the Parliament is only *one* means of exercising national sovereignty. More importantly even, a nation is not to be governed against their will, and especially, the basic principles of the social system of a nation are not to be formed against the nation's will. There is no political success, especially regarding basic issues, without a consensus – not even in a representational democracy. In this country, they have tried to force something upon the nation that the nation did not want to have, and it is very good that this attempt has failed. It would have had much worse consequences if this attempt, through cunning efforts, had brought temporary success.

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