

*“Sobering lessons on EU-phoria”*

Miklós Losoncz

## *The economic political challenges of Hungarian EU membership*

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**M***iklós Losoncz* is an unavoidable authority of Hungarian literature on European integration. As a scientific researcher, university lecturer and public writer, he monitors Hungary's catch-up process with the main economic trends of the European and world economy. His publications include studies analysing both the real and monetary processes of the economy and the economic political space, for professional forums, and popular scientific literature for the general public. It thus deserves special attention if, in addition to works spurred by current events, the author publishes summarising volumes from time to time. Just 3 years after the publication of his latest volume entitled 'EU challenges and Hungarian answers – The expected effects of EU accession on the international competitiveness of Hungary', in the year 2004, interested readers already have a book in the hand on the initial experience of accession and the expected perspectives. The

book is part of the author's earlier series of summarising works on similar topics. He directly 'continues discussing the issues raised in the latest book, from different angles, on the one hand, arranging what he has to say around the economic policy and, on the other hand, he processes the new events that have taken place since then.' (page 10) Besides, he wishes to provide useful reading not only for university and college students of economics but also for public administration and business professionals with theoretical knowledge and practical experience on the structure and operation of the European Union. Thus, the book is both a study book and a handbook, which contains directly useable information for those interested in macroeconomic issues, while business players 'may profit from the book through the evaluation of the economic political space and the expected effects of various economic political measures' and 'the author hopes the infor-



mation published in the book may indirectly contribute to the improvement of the standards of their everyday work'. (page 10)

The volume is divided into 4 main chapters.

■ The logically closely related first two chapters begin with the interpretations of the concepts of competitiveness and economic policy, followed by analyses of the economic political goals of the community and member states, including Hungary's scope of action and interest representation opportunities. Here the author comes to the conclusion that the current target system of the EU – formulated in the Lisbon Strategy – comprising 28 main targets and 120 secondary targets is overdimensioned on the one hand and partly laden with inner contradictions on the other hand, since increasing competitiveness and employment simultaneously and strengthening social cohesion are not well enough supported either by the community's readiness to sacrifice or by the implementation mechanism of the targets. The success of the Lisbon Strategy depends, at the same time, on the success of the economic policies of member states and it is therefore essential that Hungary formulate and follow an adjusted economic political strategy. When Hungarian targets are formulated, a target system narrower and more concentrated than that of the EU should be selected. The requirement of sustainability must be complemented 'by export orientedness following from small national economic dimensions and wide world economic openness. Sustainable growth in Hungary must therefore be investment- and export governed'. (page 65) A crucial concept of the target system is international competitiveness but organisational innovation is also required. While the liquidation of the institutional system of the planned economy has been a justified measure, the economic management has failed to preserve the strategic planning workshops for macroeconomic planning which have a place also in the market economy,

because of which the strategies for economic development are worked out within the public administrative framework for operative interest representation. The book suggests establishing an independent strategic centre within the government framework to conduct interdisciplinary analyses on long-term social economic processes, to make national economic prognoses and to participate in the negotiations on the economic political decisions of the government, since 'the overcentralised public administration is unsuitable for uniform strategy implementation; moreover, it increasingly endangers the competitiveness of the Hungarian economy.' (page 46)<sup>1</sup> The establishment of the strategic centre cannot be regarded a heretic idea, especially considering the fact that 'some experts have, for a long time, urged the establishment of a European Centre for Planning, meant to foster common action, which would determine and coordinate the strategic goals, measures and opportunities of the common European comprehensive economic-social cooperation and dynamisation as well as the relations with the USA and developing countries.' (page 42)<sup>2</sup>

■ In the three chapters forming the backbone of the volume, the author focuses on some of the less spectacular and rather neglected subfields of the economic policy as well as on some of its crucial segments, namely organisational and sectoral policies, R&D policy, salary policy, foreign economic policy and investment policy.

In the field of organisational and sectoral policies, the book underlines the significance of the major corporation sector, which is crucial for the Hungarian export capacity and is the driving force of the country's contribution to the international division of labour, and which is able to operate without subsidies or preferential treatment, requiring only transparency and accountability in the economic and legal environment. In addition, it emphasises the

employment role of the small and medium entrepreneurial sector which, by increasing the role of supplier clusters, may be able to help move the Hungarian economy from its follower position or shorten the following distance. This requires a better utilisation of the opportunities of the subsidisation policy, the reduction of employers' contributions and the abolition of the practice of minimum salary determination based on political and popularity considerations, which latter erodes competitiveness and strengthens the grey economy.

An interesting suggestion concerning the R&D policy is the introduction of a state subsidy meant to reduce the risk of participation in community R&D projects, which would provide contributions to the tender-related costs for Hungarian enterprises and institutions in shortage of capital, and it is exactly those winning the tenders that would have to pay it back. (page 102) This opportunity would really help those avoiding tenders due to the risk of being rejected, although it would probably be a force of attraction also for the masses of 'entrepreneurs' hanging around tender businesses. Another suggestion urging the transfer of the R&D plants of the high number of foreign-owned enterprises to Hungary, which is expected to have significant synergic and reverberating effects, can be unconditionally supported, however. The idea suggesting state subsidisation for the establishment and maintenance of innovation and technological bridge building institutions, which concerns the area that probably best suits the regulations of the community subsidisation policy, is similarly welcome.

Instead of the short-run pursuit of salary convergence, the author draws attention to a salary policy subordinated to the aspects of international competitiveness, which seems impossible to implement without a long-term consensus between the government and opposition. An agreement that does not generate

ungrounded salary demands motivated by political considerations may be more fruitful even from the point of view of an employment policy meeting employee interests than a continuous confrontation between social partners at the labour market.

In the field of foreign economic policy, the author underlines the fact that 'over 80 per cent of the exports are produced by companies with foreign shareholdings. In the majority of cases, these companies take business strategy decisions outside Hungary and there is a series of factors independent from the Hungarian economic policy that play a role in these decisions.' (page 114) In contrast to the period preceding EU accession, the majority of former foreign economic considerations have become subordinated to inner market mechanisms as a consequence of the single market, while extra-community foreign economic conditions are set at the community level. This has certainly made the Hungarian market less vulnerable and has strengthened the Hungarian negotiating position with partners outside the Community, which has beneficial effects on the conditions of foreign market access and the competitiveness of the Hungarian economy. Based on the more advantageous conditions established thereby which act as catalysts for investments, Hungary may aim for the role of a geographical and technological mediator centre towards the countries of the Balkans and the Middle East in the broader sense, for which role it competes with other countries of the Central-East-European region.

Within the framework of exploring the elements of international competitiveness, the book gives special focus to factors determining foreign operational capital investments from the point of view of foreign investors. Using the adjusted present value model, the author considers, in addition to the volume of investment and the discounted cash flow therefrom, also the discounted value of the financial

effects of the investment-related financial risks and it is on the basis of all these factors that he evaluates investors' development decisions. He establishes that, due to the common trade political regulations of the EU and the single market, it is hardly possible to gain competitive advantage over EU member states. In Hungary, salary on-costs are remarkably high, which is no competitive advantage, and the effects of the current short-term economic political measures make the already bad situation even worse. It is an adjustment to the tax competition in countries in its direct neighbourhood where Hungary may best use its competitive capacity, although community regulations are restrictive in this field. There may be a scope for action in the acquisition of subsidies aimed at reducing regional development differences and in decentralised (local government) subsidies.

■ The final part of the volume is devoted to monetary policy. There is no doubt that given today's sad economic political events, it is this field that may arouse the greatest interest. At the same time, the order of the chapters of the book once again confirms the undisputable fact that Hungary's financial perspectives are most strongly influenced by the results of the adjustment processes in the entrepreneurial sector and it is the catch-up produced as a result of the real processes that determines the pace of budgetary and monetary convergence, too. Hungary's scope of action is marked by the Stability and Growth Pact which, despite the fact that budgetary policy has been left within the authority of member states, very much questions the fiscal autonomy of member states even outside the Eurozone. Although the pact is attacked from several sides because of its lack of expedience and strictness, its theoretical bases are questioned and its practical consequences are regularly adjusted to meet the momentary demands of the influential member states that insisted on its introduction,

changing the basis of the system seems unlikely if the current contractual framework of the community is maintained, and it should therefore be considered an unchangeable factor for Hungary. The author warns against restricting public investments to make up for the shrinking scope of action and the unimplemented structural reforms in the budget, in an effort to meet the budget convergence criteria prescribed by the Maastricht Treaty for the sake of joining the Economic and Monetary Union, which would have unforeseeable consequences on economic growth. He regards it essential that political parties reach a consensus on joining the Economic and Monetary Union and on the desired exchange rates of the Hungarian currency, while admitting at the same time that 'the current tense atmosphere in domestic policy, based on confrontation, is unfavourable for consensus seeking, although this may be changed in a short time, however.' (page 217)

Keeping the independence of the national monetary policy is a decisive argument of those who do not want to rush Hungary's accession to the Eurozone. By analysing the current monetary environment and exploring the consequences of its contradictions, the author draws attention to the fact that the independence of the national monetary policy is restricted today already. Among the contradictions, the author notes that, through the implementation of the interest rate convergence, household savings have fallen to a critical level and the excessive indebtedness of the household sector is made worse by the low interest sensitivity of households, because of which rational loan habits are impossible to force out despite the unrealistically high interest burden. 'Euroisation', i.e. the spontaneous spreading of the use of the Euro, also decreases the efficiency of the monetary policy. The general widespreadness of the foreign currency borrowings of households, ignoring exchange rate risks, and the 70 per cent ratio of the foreign

currency borrowings of enterprises are signs of warning for the monetary policy against an overwhelming feeling of indispensability. 'All in all, from a technical point of view, there is a possibility that the use of the Euro reaches a critical level on the basis of which it is practically, spontaneously introduced without Hungary's joining the Economic and Monetary Union.' (page 138)<sup>3</sup> The restrictive monetary economic policy aimed at price stability has a paradoxical effect on the general government deficit, too, since the high interest rates increase the interest burden on public finances and thus maintain the high level of or even increase state debts. At the same time, the interdependence of the monetary and budget policies generates a cooperative strategic compulsion between the Hungarian National Bank and the Ministry of Finance. While this statement may fill readers with optimism regarding the future, 'the events of the past years indicate that the Hungarian National Bank on the one hand and the government, i.e. the Ministry of Finance, responsible for the fiscal policy, on the other hand have not taken the other side's intention of cooperation for granted; instead, both parties have assumed that they would have to attain their objectives despite the other party' decisions showing a lack of support for these goals.'(page 248)<sup>4</sup> The unfortunate consequences of this strife are just unfolding in front of readers' eyes these days.

In the economic considerations of the past two decades, the preparation for the European integration process has played a central role. Within the framework of this process, large-scale popularisation of information on European integration has followed. Innumerable books, publications, journals, studies and newspaper articles have focused on the operation of the European Union and on Hungary's accession chances. A significant part of these publications met the information demand of professional and civil circles, filling

the information gap that had been a consequence of half a century's isolation, and thus accomplishing a historic mission. Until the turn of the millennia, the popularisation of facts on the EU usually involved a longing for Hungary's participation in the European integration and was often characterised by uncritical enthusiasm. At the beginning of the new millennium, as Hungary's accession got realistically close, realistic considerations of the advantages and disadvantages of EU membership and even fears of the risks involved in the new type of competition were voiced. Today, in the Hungary that has become a member state of the European Union, acknowledging the fact and the challenge of European integration, accepting the historic compulsion of adjustment and ending the illusions related to EU membership are the only way to go. The book by Miklós Losoncz is exemplary also in this respect: by his calm and objective analysis of the real economy and the budget and monetary sectors as well as his balanced recommendations, he has a sobering effect on the European euphoria of readers laden with potentially ungrounded expectations.

A most important message of the book is that it is impossible to catch up with good EU performers without political and social legitimacy and wide-scale social support. 'This is unimaginable without a consensus between major political parties and economic players (the government, employees and employers as well as their interest representation organs) on the long-term priorities, principles and goals of the development strategy and the economic policy. Economic historical examples of the past decades have indicated that, in democratic political systems, the conditions for economic catch-up (Ireland, Spain) as well as various short-term correction and longer-term structural reform programmes (Sweden, Finland) can be established through social consensus. It is a consensus on the main targets and basic

principles of the economic strategy between economic players that replace the force-mechanisms that are meant to serve catch-up in dictatorial systems.' (pp 66–67)

The only thing a reviewer can add to the considerations of the author is that the positive example of the countries listed above, which used to belong to the European backyard before, is a sobering warning to the members of the (economic) political class captured by their

own selfish interests, i.e. that they have no right to destroy the social efforts of the past two decades, sacrificing the chance of catching-up on the altar of political battles for several generations more. The way to go is easy to see (also) from the sober account given in Miklós Losoncz's book, and EU-phoria is not a necessary travel companion.

*János Zsugyel*

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## NOTES

<sup>1</sup>The author here refers to an article by Tamás Sárközy entitled 'Kiút az állami labirintusból' (Way out of the state labyrinth), *Népszabadság*, March 5, 2005, Hétvége, p 4

<sup>2</sup>With reference to an article by Béla Kádár entitled 'A gazdaságpolitikai koordináció és a monetáris politika új dimenziói' (The new dimensions of economic political coordination and monetary policy), *Európai Tükör* (European Mirror), 2004, Issue 1, p 22

<sup>3</sup>Here the author refers to an article by János Kun

entitled 'Lopakodó euró. Az euró magyarországi bevezetésének lehetősége' (The creeping Euro. The possibility of introducing Euro in Hungary). *Élet és Irodalom*, July 28, 2006, p 6

<sup>4</sup>With reference to an article by László Antal entitled 'Hol volt, hol nem volt. Egyensúly, stabilitás a magyar gazdaságban az ezredforduló után' (Sometimes there were, sometimes there weren't. Balance and stability in Hungary after the turn of the millenia.) *Mozgó Világ*, Volume XXX, Issue 8, August, p 31