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Return of activist state in a former transition star: the curious case of Hungary

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ABSTRACT

European governments have become more active in economic affairs since the great financial crisis of 2008; the Covid-19 epidemic and Russia's war in Ukraine have triggered a variety of government interventions. What is less obvious is the increased non-customary state activism in the form of 'patriotic economic policy' in EU periphery, particularly in Hungary, in and out of crisis times. The successive Hungarian governments under PMV. Orbán have systematically eroded checks and balances in order to enlarge their room of manoeuvre while practicing a self-styled illiberal, pro-sovereignty policy. The paper revisits the earlier development phases of the Hungarian transformation, trying to identify antecedents to the later Hungarian backsliding in market competition and liberal democratic order. Aspects of state capacity, size and composition of the state sector, and key policy directions are investigated in order to make sense of the differing transformation paths in Europe's eastern periphery with a focus on Hungary, a onetime space setter in the transition process. Populism seems to be a misnomer for Orbanism which might be better understood as "cronyism with a cause": government budgetary measures are self-serving but they also attempt at rebuilding the state. The paper concludes with an overview of possibly outcomes.

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Introduction

Hungary under the premiership of Viktor Orbán, the European record holder as longest-serving prime minister in a parliamentary democracy, intrigues policy analysts as well as social scientists. Once a front runner in the transition from plan to market, present day Hungary has become a problem case in the EU. Such a serious case of democratic backsliding had not been foreseen by scholars of post-socialist transition and of

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Motto: Orbán's Fidesz government has been on a mission since coming to power in 2010 to return key foreign-owned parts of the economy to Hungarian control, using often sharp-elbowed tactics. Hungary's premier is not alone in such ambitions. Especially after the financial crisis, many central European states fretted that sales of communist-era assets in the 1990s had left their economies too much at the mercy of foreign owners. But for Orbán, repatriation of ownership is part of a broader effort to extend his political dominance into the commercial sphere – and to create a socio-economic system that endures even if Fidesz loses power. (Financial Times, 24 August 2022) comparative politics. The ongoing clash between the Orbán regime and the EU institutions baffles students of political science. Even the classification of the Orbán regime is a contested topic in the literature as the regime's policies are rather personalised and improvised.

The research assumption here is that a lasting and established rule like that of Orbán cannot be simply explained by masterly use of populism and demagoguery; there must be genuine social needs that the regime caters for. First, this article aims at distinguishing the recent return of industrial policy in core EU countries and the re-activation of the state in the peculiar Hungarian case. It is demonstrated that state activity in Hungarian is only partly similar to that of a proper development state. High public spending mainly serves to enlarge the room for manoeuvre of the central government, and secondly, to strengthen a politically loyal domestic business class.

Concerning the assumed social needs, not declarations and policy statements but fiscal indicators will be scrutinised. The main part of the article deals with budgetary data to identify the priority areas of the regime and to understand the role of the state under Orbán's premiership. Analysis reveals that social protection is, perhaps surprisingly, systematically underfunded, together with health and education. In contrast, areas related to identity politics (culture, sport, religion, media) are funded much more generously than is customary in EU countries. Economic affairs are also prioritised but not in the fashion of development states in emerging markets. The article raises whether selective government intervention in the working of an EU member state economy is reconcilable with the norms, rules and culture of the Union.

Being a particular and personalised country case, the concluding part does not attempt to generalise the Hungarian development path into a new or modified classification. Yet the case offers lessons about the diverging tendencies in the periphery of the European Union.

Drivers of state activism: politics, ideas – and economic crises

The case below, the particular regime of PM Viktor Orbán, stands out as a refutation of accepted wisdom about an eventual institutional, structural and performance convergence of new(er) member states to the core of the European Union. As a country case it has limits in defining development patterns, yet the length and structural consequences of Orbán's rule may offer useful arguments for the academic and policy-analysis debates about the development paths in the EU's eastern periphery.

Before exposing the particular government policy case, it is useful to look at the general picture, for similarities and differences in states' roles in the EU. There are clear theoretical justifications for a government to intervene in the working of the market such as correcting market imperfections. In real life, however, government interventions are driven by a variety of non-economic factors: war efforts, yielding to public expectations, the ideological stance of the political classes or simply the motives of those in power. Methods and intensity of government interventions are rather path-dependent: history matters. Scope and size of governments differ across countries even at similar levels of development – a phenomenon that the Varieties of Capitalism literature applies to the Central Eastern European (CEE) region (Farkas, 2011, 2016; Lane, 2005; Szelényi & Mihályi, 2020).[1]

The CEE region has, even after three decades of politics-driven convergence, remained different from the European core in some key aspects. History casts a long shadow on the region which had experienced an *extreme version of government activity* under a regime labelled (rather misleadingly) a *planned economy*, for decades before 1990.[2]

The sudden disintegration of the Socialist/Communist regimes unleashed a swift transformation towards a market-based economy in a process that is customarily referred to as *transition*. Its initial phase took quite various forms, not always following the assumed pattern of *state retreat*; reality beat widely shared expectations that all national paths would lead to the reduction of the size and scope of the state.

At the very start of the transition, *privatisation, deregulation, liberalisation, promotion of entrepreneurship and competition, and rolling back of the state* constituted the main blocks of the transformation blueprint that Western advisors offered Czechoslovakia, Hungary and Poland, as frontrunner transition countries (Blejer & Coricelli, 1995). Cutting down direct state presence in a market economy was certainly a logical task in post-1990 CEE, as all countries had inherited an oversized and inefficient public sector; the process, importantly, was also driven by the then dominant *free-market ideology*. International financial institutions also preached a leaner state under the *(post-) Washington SLIP consensus*: stabilisation, liberalisation, institution building and privatisation (Szanyi, 2019).

As so often in public policy, corrective measures are prone to *overshooting*. Deregulation, trade and price liberalisation, privatisation and similar pro-market corrections are no exceptions: they could go too far or too fast. Retreat of the *old state* may easily outpace the creation of a *new institutional order* whose existence would be a vital precondition for flourishing entrepreneurial activities and adequate social protection throughout the transition process. The astonishingly deep output contraction that former command economies had experienced right after the regime change was ascribed to regulatory chaos, weak social protection, declining level of public services – in general: *poor functioning of the state* in critical times (Kornai, 2015).

State capacity is an obvious factor in macroeconomic (in)efficiency but a political aspect is at play, too: voting patterns are shaped, among others, by the *public perception of state capacity*. The perceived weakness of the state may undermine the support for a new, pluralistic political regime and reinforce nostalgia for the old order.

At this point, however, it is important to distinguish between those who notice and criticise *premature state retreat*, on the one hand, and those with entrenched *anti-market position and reactionary attitude*, on the other. As an entrepreneur or as a taxpayer, you may complain about poor state performance, yet you do not wish the return of the omnipresent state, nor would you demand the restoration of public ownership.

In the initial phase of transformation, the way the state as a vital institution worked – or failed to work – differed a lot in the region. The progress from an oversized state to a leaner state was peppered by halts and fits, including temporary reversals.

A pulsating process is a unique CEE phenomenon: borders between the state and the market had also changed significantly in advanced Western countries. The 1980s was the decade of privatisation, whether Thatcher-type or gradual; later the demarcation between the public and the private sector in Western countries remained rather stable up to the great financial crisis of 2008–2010. The GFC, importantly, was a turning point also in this respect. The consequences of the crisis led to increased government intervention into the functioning of the economy, particularly of financial markets. Even nationalisation, albeit mostly of a transitory nature, took place in some Western countries.

GFC, it is claimed here, challenged the ideological-professional stance in the European semi-periphery. A pro-market consensus had been dominant in the 1990s, the formative years of the regime changes, but the financial crisis undercut the dominance of the 'marketeers'. Views on the proper size and scope of the state diverged even in the European core. This fact should be acknowledged when one wants to reconstruct the diverging paths in CEE that havenow led to such distinct development models as that of Estonia, on the one hand, and Orbán's Hungary, on the other.

General macroeconomic statistics would not easily reveal the major differences in the functioning of different regimes. As far as the ratios of income centralisation (state revenues/GDP) and redistribution (state expenditure/GDP) are concerned, the new member states are not much different from the EU core – typically somewhat below the EU average. A detailed breakdown of budget data is needed to scrutinise particular country cases. For the present analysis of a particular political regime, structure of the budget is chosen as a key aspect: what politicians do will matter more than what politicians say. The real preferences of any government are revealed by which selected taxpayer segments are being taxed heavily and who are the happy recipients of public expenditures.

This is the logic behind the analysis below. It is advisable to take a medium- to long-term view, as budget structure will change with time lags; trend data help distinguish 'normal times' and episodes of 'emergency'.

Hungary's income redistribution ratio has remained high in regional comparison in after-GFC years, indicating an active, spending state. Aggregate budget data, however, would not say much about the idiosyncratic policy line that Orbán took when he returned to power with a landslide victory in spring 2010, just months after the trough of a deep contraction. Certain initial non-customary policy measures of the incoming Orbán government were out of tune with the then policy mainstream, yet they did not provoke strong criticism. The reason, arguably, is policy slippages were also taking place both in core and periphery countries of the EU in the years following 2008: unorthodox policies in new member states did not cause much consternation at EU institutions that were busy managing Eurozone tensions (Bod, 2012).[3]

The shocks of the GFC took many years to dissipate, to be followed by a rather advantageous business cycle with low inflation and interest rates, and favourable terms of trade. For the whole CEE region, the year 2010 through to 2019 was a decade of growth, this time without serious accumulation of fiscal imbalances.

Soon the COVID-19 epidemic hit the world. Governments became active again in facing new challenges, and not only in sectors closely related to health issues (OECD, 2020).

It took over a year for Europe to digest the socio-economic shocks of the pandemic, and then only partly. Increased market uncertainties and new rigidities led to a sudden upsurge of inflation in 2021. The Russian invasion in February 2022 made things worse; the energy situation called for government measures. The security aspect of the war on Ukraine also justified a wider scope of state intervention.

Given the complexity of recent changes in socio-economic structures, ideas and policies, one must be cautious in making strong statements about assumed deviations in some member states from the Weberian ideal-type of European liberal democracy, rule of law, and a state limited by institutional checks and balances. Still, students of public affairs noticed cracks in the common understanding about the modern liberal state soon after the GFC in the European peripheries, in particular in Hungary, and some years later in Poland.[4]

It took a long time for EU institutions to admit having a systemic problem with particular member states, and to declare that Hungary was not a proper democracy any more (European Parliament, 2022). The Hungarian government were censured for documented breaches of fundamental principles of the rule of law. Yet Orbán's economic policy practice remained less exposed to explicit criticism even if the shift to 'patriotic economic policy' in Hungary, or a strong stand for 'national sovereignty' in Poland, have certainly gone farther than just a natural correction of the assumed previous excesses.

The Hungarian government has been frequently labelled as populist, illiberal and pro-sovereignty in the mainstream media, or, as the *Financial Times* put it in an editorial, *crony state capitalism* (Financial Times, 2022). Academic studies had already classified the emerging regime under PM Orbán's leadership as a *crony state* (Martin, 2017; Olejnik, 2020; Toth & Hajdu, 2018), even theterm *re-feudalisation* has been applied (Ádám, 2020).

Below, we will look at the long process that has led to Hungary's divergence from the accepted European concept of limited state toward an emerging model of a market-substituting state. Arguably there is much more here than simply a case of policy 'over-shooting'. Also, it is more than a temporary backsliding. The budgetary trend will be scrutinised as a key feature of a socio-economic regime.

Academics assumed 'different paths but same destination'

A heterogeneous region, once defined as *Eastern Europe* by Cold War logic, suddenly changed around 1990. It is hard to tell, even with the benefit of hindsight, what was more important in initiating the change: geopolitical shifts or the build-up of internal tensions. Transformation of social and political superstructures took a historically short period of time. Regime changes started in earnest in April 1989 when the Solidarity movement in Poland came to an agreement with the ruling party to share power; that summer East Germans escaped to freedom through Hungary where the Iron Curtain was removed in its physical reality. A key event of the year was the Malta Summit between US President George H. W. Bush and Soviet General Secretary Mikhail Gorbachev in December, just a few weeks after the fall of the Berlin Wall and before the Romanian dictator was executed. In 1990, the Baltic states declared their independence, and free elections were held in CEE countries. In the following year the Soviet Union ceased to exist.

The fact that countries in the eastern periphery of Europe experienced a political watershed at roughly the same time, despite their varying levels of socio-economic advancement and the different degrees of accumulated social tensions, implies that the main driver, or at least the trigger, must have been external. Political regimes from Warsaw to Tirana to Baku underwent transformation, irrespective of the local material conditions.

Yet, external impact is not enough to explain why the changes turned out to be so deep-going and fast, even in countries not experiencing financial chaos or a debt trap. Centralised regimes seem to start breaking up from the top, not so much yielding to revolutionary forces emanating from below rather than by loss of faith and spread of opportunism among key agents.[5]

If that was the case with the Soviet Union, it was even more so in its reform-communist dependencies where a large part of society suddenly recognised an opportunity to *return* to a still familiar system of the pre-war past (Bod, 2021).

Thus, the collapse of the old order, in the absence of any 'grand design' by external forces, was a result of the sudden implosion of autocratic (Party-State) rule. Once the establishment party's hegemonic position was questioned, its legitimacy instantly evaporated.

As an important consequence, the state stopped functioning adequately. Fiscal data register a decline in tax collection capacity: public sector revenues started to shrink. The budget expenditure side was forced to contract accordingly. States in transition suddenly faced a hard budget constraint with limited or no access to external debt finance as financial markets stopped regarding them as risk-free.

As later research established, fiscal adjustment during transition typically came less from concerted efforts to rationalise spending priorities than through non-payment and expenditure arrears in the public sector (Hare &Turley, 2013, p. 26). This is perhaps the least efficient method to roll back the State – but that is what happened when the *state capacity* vastly deteriorated.

The sudden retreat of the once omnipotent state came as an ideological shock to many of the former nomenclature but also among the simple folks, eliciting the 'Putin effect': a deep regret for the loss of the omnipotent state – an Empire, in the case of Russia. Its sudden disintegration delivered an ideological shock to millions who had been socialised to live a life set and controlled by a bureaucracy.

The events took place too fast. History did not allow enough time to erect another state before the old, Party-State, stopped functioning. Western policy makers, as documented by memoires and accessible sources, were also puzzled by the speed of the changes; they did not encourage the new political forces in 1989 to accelerate the disintegration progress (Cloud & Sandler, 2021).[6]

Perception is a key component of the explanation as to why the communist nomenclature gave up so easily even in relatively calm, non-violent situations. Those were the years of a swing of global balance in favour of the geopolitical West, led by the USA, at the expense of the Soviet Union; still, the geopolitical power aspect provides but a partial explanation. The Soviet leaders could have taken a stiff position domestically and externally as a nuclear power – but they did not. They gave up early. The point here is that it is not so much the geopolitical shift itself but its *perception* in the ruling classes and also in the broader society of Eastern Europe what mattered most.

The public perception of the existing situation (disintegrating state of the 'old order') was more negative than the perception of the incoming 'new system'. Both sets of perceptions matter, but for those in a position and with a mindset capable of considering policy options (in particular the *old* and *new political elite*) the contours of the future must have mattered more than their judgement about the past. While the old guard and the pro-democracy new forces vied for political influence, in some instances quite antagonistically, many among them identified upward risks in the changes to come, while others remained simply *sceptical* and *compliant* (Rose & Mishler, 1994).

Field research revealed that the general public was not totally naïve: not all citizens believed the promises of the new era at the crucial time of the political changes. The majority view in many transition countries was not much positive about the new order in 1991, and a sizeable portion of the public rated the old regime higher than the emerging new one – the proportions differed greatly across countries (refer to the article, the source of data: Rose and Mishler (1994)).The educated, the young and the better-off felt generally more positively about the new regime, and more critical of the old order.

It may sound paradoxical but many of the party nomenclature looked forward to the emerging regime. Those with proper training, endowed with social and pecuniary capital, or those in the secret services with a particularly valuable informational capital recognised promises in the future order. A significant part of them entertained positive expectations about the emerging new regime, or to put it differently, few people wanted or imagined a return to the old (and 'good') regime.

This aspect depends a lot on certain *personal continuity* of top level managerial and governmental staff during the regime change. To take one example, the Orbán regime may sound devotedly anti-communist and pro-Christian/conservative, yet many among its cabinet members and top officials had been Communist party members.

Here, there is a peculiar aspect concerning the generation of Viktor Orbán and the original Fidesz, established as a party in 1988. The received wisdom is that the founders and members of Fidesz (meaning 'young democrats') were the first 'new generation in politics'; hereby the argument is that this was the *last generation of the reform-communist era*. The youth (Fidesz had originally an upper age limit of 35) had been fully socialised in the former regime. It does not take any malice to assume that if the regime had not collapsed, most present senior Fidesz personalities may have been in the same or similar political jobs at present.

The Fidesz party members, and young Orbán himself, were textbook economic liberals and progressive democrats. At the time of the political regime change, TINA (there is no alternative) was the zeitgeist. The 'old' and the 'new' elite in CEE shared, to a similar degree, the feeling of inevitability of the new, liberal, market-based, pro-Western order.[7]

Spirit is an important factor in understanding public support for a return to the market order at that time. Pro-market and pro-democracy spirit stands in stark contrast to the mood in the region two decades later, particularly following 2008, when other shocks, notably the refugee crisis, hit society, and populist and anti-market discourse became the accepted norm in Europe. One may even speak of a populist Zeitgeist (Mudde, 2004). If that is true for the West, at least partly, it should not come as a surprise that illiberal ideologies have emerged (re-emerged) also in the CEE region – while illiberal political and government *practices* had never fully disappeared.

Back to the early phase of transition: given the characteristics of the *soft Communist regime* of Hungary (Kádárism, named after the then first secretary of the Hungarian establishment party for decades), it is easy to see why half of the Hungarians polled thought positively of the past, the previous regime in the early 1990s – in sharp contrast with the polls in all other countries, particularly in Romania. Yet as for the emerging new regimes, the overall perception (slightly positive) did not differ much across the sample of the five countries polled. If at all, the rather high share of the Polish negative answers may surprise us – this is probably a reaction to the 'shock therapy' of those months.

There is an interesting contradiction here: the mixed to positive expectations of what may come (that is: market order and multi-party politics) made it feasible for all new, democratically elected governments to go on vigorously with transition policies; yet in countries where the past was not strongly rejected, the popularity of the same governments waned quickly, resulting in slim or zero re-election chances. Certainly, that became the fate of the first, democratically elected centre-right government led by PM Antall in Hungary (Hieronymi, 2013). The former ruling party, the reinvented Socialists, allied to the Liberals, returned to power in 1994, with populist promises, supported by a mostly friendly left-leaning public media, and discretely, by business people with roots in the previous Socialist system.

Yet, the winning Left managed to remain in office for one term only, to lose to a moderate-right coalition led by a liberal-turned-conservative V. Orbán in 1998. Then the pendulum returned again: the first Orbán government was to be defeated four years later by the Left. Young Orbán seems to have learnt that populism works, and media is powerful, and it helps if the party in power has a business hinterland.

The *pendulum of parliamentary power* indicates that Hungarians consistently voted out incumbents – at least in the first four parliamentary elections. Meanwhile, Fidesz, a formerly *youth-alternative party* on the left at its inception, having sensed the waning public support for (peripheral) capitalism, decided to take a rather anti-banker, anti-market and pro-sovereignty stance. Having lost two consecutive general elections, and nearly dumped by his party, Fidesz chairman Orbán identified a golden moment to win big in the 2010 election held just after a deep economic crisis, taking the position of the political right in ideology, an anti-globalist stance with promises of a more efficient, active state that would protect the 'working men'.

He did manage to mobilise voter support for 'more than a "simple" change of government' in the words of Orbán (Martin, 2017, p. 3). What came after is a much commented on story of a government taking control over public media and an important chunk of the economy through unscrupulous use of state power. Arguably Hungary has gone the farthest on the particular 'national way' as Orbán has won four consecutive parliamentary terms since 2010.

The Hungarian case, to be discussed below, has become a paradigmatic one for hybrid regimes. Its evolution may offer an example to copy for other politicians also intent on securing political power for a long term – but also raises questions about the internal sustainability and international fit of a personal-authoritarian regime in Europe.

Convergence – divergence – national path

Transition is the stock term for the transformation of the former centrally planned countries which is, however, loaded with finality. It implies that the countries concerned are destined to advance from their starting position to an assumed future state. But the existence of an implicit common path is highly questionable, particularly taking into account the variety of the initial position of, say, the V3(4) countries, on the one hand, and Ukraine and other former Soviet republics, on the other (Bod, 2014). Against earlier expectations in media and international development agencies, significant differences (i) in the starting position, and (ii) in the speed of changes have substantiated the varieties of paths taken by nations (Douarin & Mickiewicz, 2022).

But not only that, policy orientations may also differ greatly, for various reasons. Business analysts have a tendency to somewhat overlook the differences in initial positions. True, the gap between the 'old democracies' and the 'new democracies' at the time of the regime change was larger than differences within each group – or at least it looked like this. Three decades later it is visible that national transition paths have differed, and their future courses may also be very different from each other.

Below, a review of the budgetary redistribution will highlight the particularities of the Orbán experiments in Hungary. The rational of putting national budget into our focus is that the political preferences of a political regime boil down to that: who pays tax and who benefits from public funds. As we will see, such a review does reveal significant trends.

As for relative size of the public budget, Hungary is not far from the EU average; the increased politicisation of the economic life in Hungary in not much reflected in aggregate statistics (Figure 1).

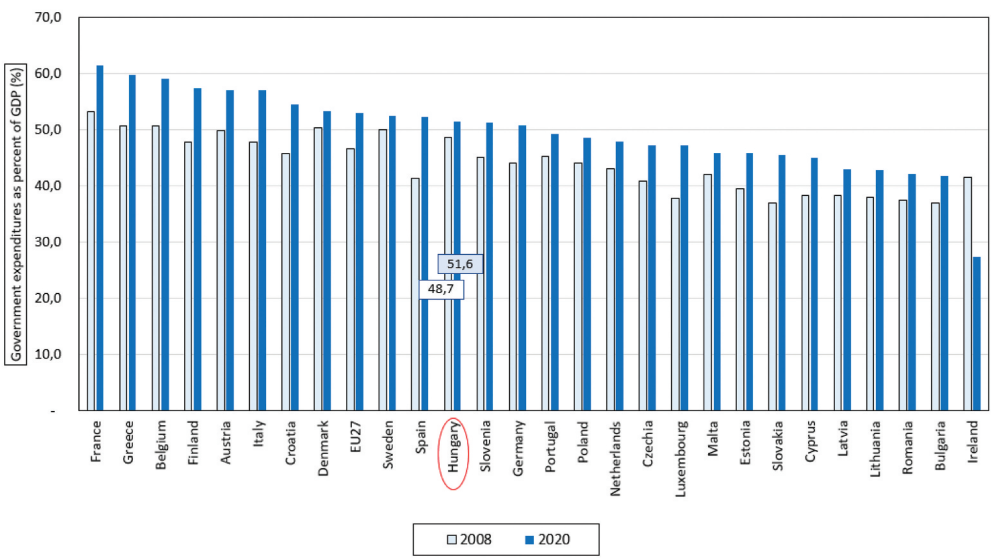

Figure 1. Government expenditure, percent of GDP.
Data source: Eurostat, gov_10a_main.

Still, the place of Hungary among EU member states is noteworthy. A *redistribution rate* around 50% of GDP may not be excessive by advanced West and North European welfare state standards but it is well ahead of other Visegrad member states, the customary comparators for Hungary.

The nature of the Orbán regime will be better documented by looking at a breakdown by functions of public spending (COFOG) (Figure 2).[8]

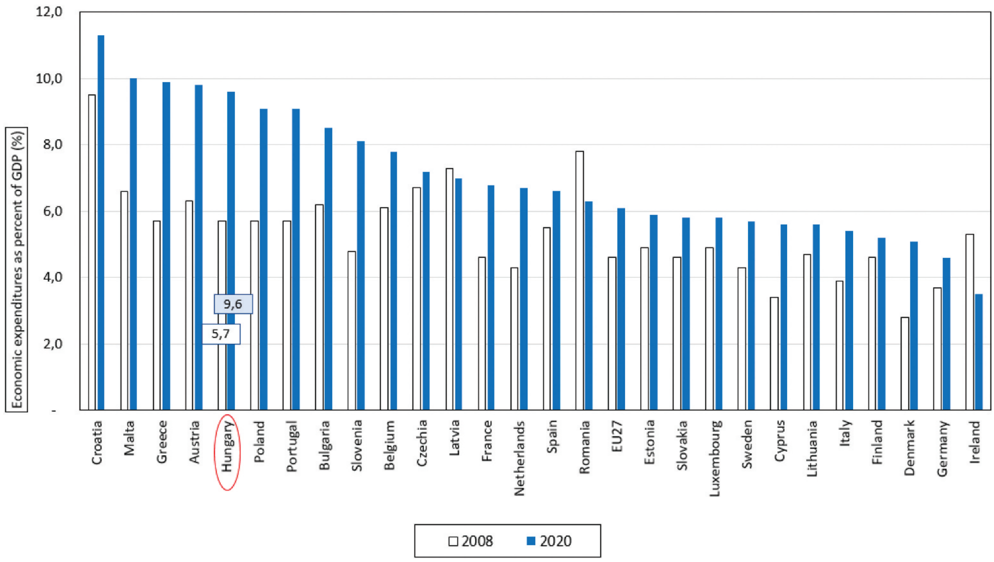

Figure 2. Expenditures of economic affairs (percent of GDP).
Data source: Eurostat, gov_10a_main.

The share of expenditures classified as serving *economic functions* reveals that the Hungarian government became much more active during the Orbán years: figures for the year 2020 were well above the EU average after a significant increase. But, again, the overall figure (close to 10% of GDP) will not say much about the nature of the regime's economic policy without specifying whether public funds go to subsidising existing state-owned firms, or to domestic small firms, or to national flagships as fiscal support, or funds are spent to incentivise foreign big businesses to settle in the country.

Such detailed analysis is beyond our duty here but mention has to be made of one key aspect of the Orbán government: it initiated a *re-industrialisation* drive after 2010, while it placed a heavy tax burden on the banks. Important to note is that no government bailout or capital injection in the Hungarian banking sector took place during and after the 2008 financial crisis: most banks were at that time in foreign ownership, and recapitalisation, if needed, was the owner's duty. Thus business subsidies went instead to loss-making public firms (e.g. railways) or were doled out as incentives to automotive and electronic giants, later to tyre factories and battery producers. Also, in the years following the GFC, the Orbán cabinet spent huge sums to enlarge the share of public ownership in banking as part of the declared goal of taking financial intermediation in national hands (Piroska, 2021).

The following COFOG-class (8) may seem to be marginal to our topic here, as the one on *recreation, culture and religion* is not generally regarded as a strategic aspect of the state. Yet, the Hungarian figures have stood out lately, and not just marginally (Figure 3).

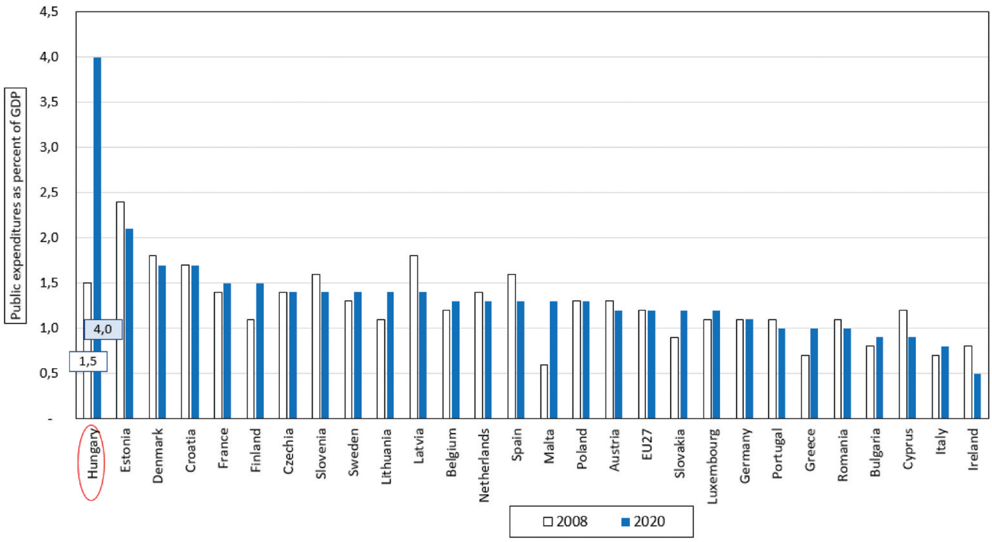

Figure 3. Public spending in Hungary on recreation (sports), culture and religion, percent of GDP. Data source: Eurostat, gov_10a_main.

The change between the pre-Orbán and the post-2010 era is striking. The Orbán regime spent on these particular COFOG titles three times as much as the EU average. This surprising spending increase is aimed at *identity and ideology issues*: pouring public funds to *soccer* identified as an instrument of national belongingness, and generous subsidies were paid to a selected circle of *churches*, public funding of pro-government *entertainers*, and massive financial funding went into government-controlled *public media*.

In most other expenditure areas, the Hungarian budget ratios are similar to or somewhat smaller than the EU-average (defence, environmental protection, health, education). There is, however, one more important area where the profile of the Orbán government differs greatly from the average: *social protection*. The massive and systematic reduction of its ratio sends a strong message about the nature of the Orbán regime: unemployment expenditures, old age pensions, disability and sickness benefits are not prioritised (Figure 4).

Fiscal policy is a key aspect of a particular policy path, and significant and lasting changes in the structure of government incomes and revenues (taxes) characterise the nature and the evolution of a political regime. *The declining share of pensions and other social protection items, and the high share of direct economic activity, as well as the outstandingly large amounts of public monies spent on influencing media, entertainment and supporting churches all fit into a particular socio-political pattern* (Figure 5).

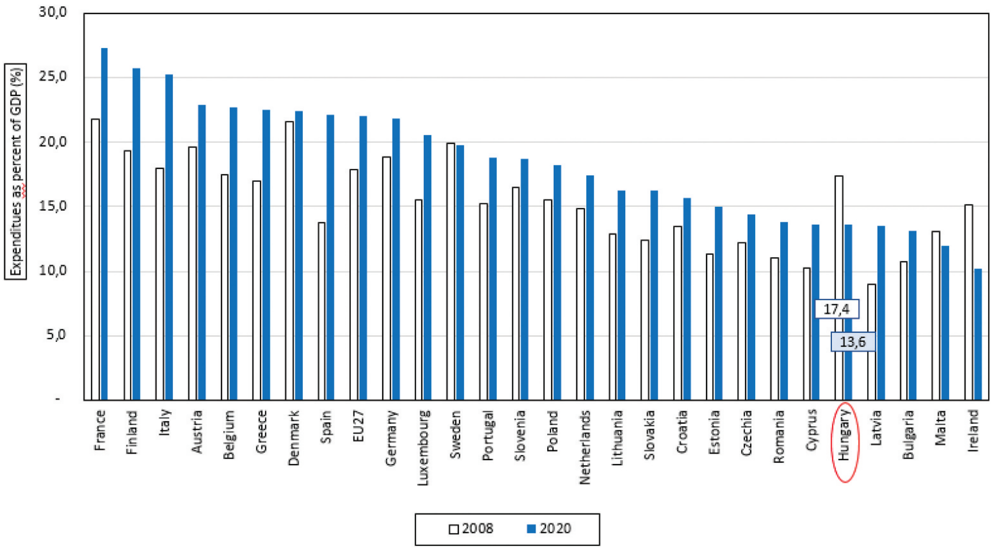

Figure 4. Expenditure on social protection, percent of GDP.
Data source: Eurostat, gov_10a_main.

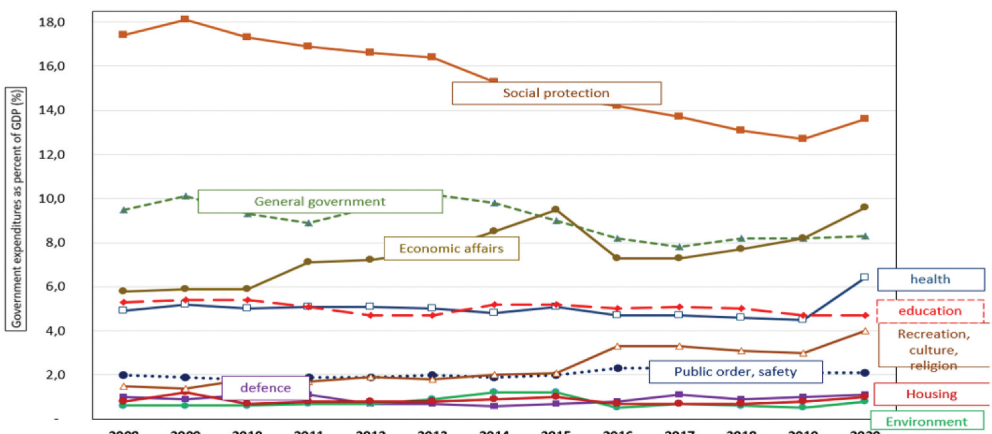

Figure 5. Evolution of classes of state functions in Hungary.
Data source: Eurostat, gov_10a_main.

These are telling data on the evolution path of the country even at a high level of data aggregation. A more detailed analysis of annual budget processes would make the picture sharper. Yet, fiscal trends underline what political science research has identified about the specific nature of 'Orbanism'. Is it populist? Well, the regime favours its 'own' people against 'others' whether foreigners or blameable locals, and is hostile towards independent organisations and professional bodies as 'elitist' (Benczes, 2021; Cianetti et al., 2018; Scheiring et al., 2019).

But there is a growing body of knowledge about Hungary becoming a fully-fledged *crony regime*.[9] This is the conclusion of the anti-graft global NGO Transparency International (TI, 2023), in its reports of corruption (Figure 6).

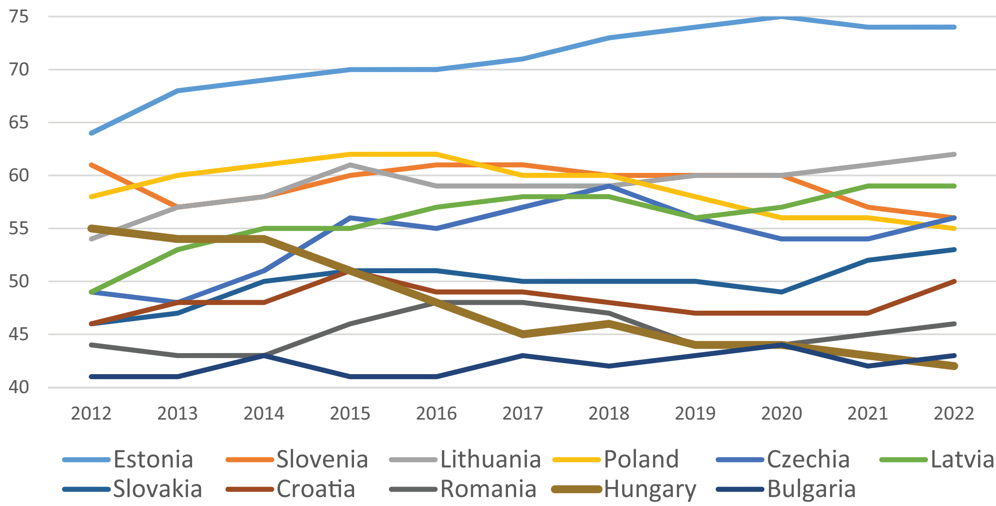

Figure 6. Corruption Perception Index in new member states, 2012–2022.

The evolution of the Corruption Perception Index is telling: it is hard to imagine that general ethics might change in a country within a decade or so by itself. The steep decline of norms (what domestic and foreign observers regard as favouritism, corruption and nepotism is referred to in Hungarian public media and official explanations as 'support for the national entrepreneurs' under a 'patriotic economic policy'. Moral decline is a strange result of a determined policy of weakening checks and balances, taking political control of the public media, turning public opinion away from living standard aspects towards identity and ideology issues.

Conclusions

More than three decades after the historically fast regime change in the eastern periphery of Europe, development paths have shown a wide variety. Group or cluster classifications in the academic literature are based mostly on legal-political measures and institutional characteristics of the countries concerned, but group cohesion, as in the case of the Visegrad 4, may quickly weaken due to policy differences (Bod, 2021). The case of Hungary, the country in our focus, is puzzling as legacy conditions, earlier institutional characteristics and structural indicators would have destined this country to lead, among a few, the convergence list. Instead, the Orbán regime has emerged as a structurally new variant.

The puzzling question raised in academia and beyond is why a relatively successful transition country should start slipping and, more recently, why the regime has become so entrenched. This second aspect, the longevity of the Orbánian rule, has led to the hypothesis of this research: the regime must deliver something that is appreciated by a large enough voting bloc. One might assume protection from transition frictions and risks, reduction of uncertainties; in that case the winning formula is good enough state capacity and adequate social transfers offered.

But this is not the case. The analysis of the size and structure of the fiscal policy revealed, instead, that the successive Orbán governments have economised on welfare spending, and state capacity has not been high enough to efficiently deliver public goods, nor to put the country onto a high growth path as a 'development state'. The winning strategy seems to be, as supported by the present analysis of the functional breakdown of the budget, to channel funds (domestic and EU-transfers, as long as they are available) for politically loyal entrepreneurs–rentiers who reciprocate the favour by supporting the ruling party and financing pro-government media; while a less well-off voting segment is incentivised to vote 'properly' by being taken care of in identity areas: national pride, sport as a cementing factor, religion, ethnicity. Additionally, bending the election law, party financing rules, as well as gerrymandering and other misuses of parliamentary power will make sure that even a slight majority in popular support for the opposition parties and movements could not be technically translated into an election victory.

A secondary research issue concerns the reasons for the ease of the social acceptance of Orbán's illiberal agenda. Again, the Orbánian agenda sounded appealing to a large enough segment of society as it offered clear answers to problems that had accumulated during the first decade of transition and later in the great financial crisis. Analysis of the pre-2010 period has led to a three-factor explanatory frame for the particular development path that Orbán devised: (i) correction of policies of the Socialist/progressive Liberals who took a 'best-pupil-of-the-class' attitude within the EU while being fiscally irresponsible in the run-up to the 2008 financial crisis; (ii) state-activist developmental policies in attempting to find answers for the middle-income trap; and (iii) consolidation of crony capitalist tendencies that have always been around in the region.

These overlapping tendencies are hard to discern. Yet, the above analysis of the size and composition of the national budget as well as indicators of state capacity, governance indicators and transparency indexes (not elaborated here) substantiate the claim that the Orbán system is different from being simply populist. Below is the tentative conclusions.

First, Orbán's regime accomplished a correction of the previously oversized external exposure of the economy and the premature withdrawal of the state. The process could be justified under rational socio-economic policy considerations, even if the methods and execution style could be duly criticised. But it is important to see that Orbán got the job in 2010, just after the end of a deep recession, and external business conditions in consequent years were rather good on the whole. When confronted with Covid in 2020 and inflationary shock in 2021, the Fidesz government nearly replicated the policy mistakes of the pre-2010 Left.

Concerning the second point: Orbán did offer a simple and reassuring reaction to the revealed and assumed weaknesses of the financial capitalist order as exposed during the GFC. The core of his policies is to concentrate financial resources into the central government, and to reshape the country through a re-industrialisation structural policy, applying protectionist measures. Such a policy regime may have helped correct the pre-GFC macroeconomic imbalances, but it has deep flaws (Bluhm & Varga, 2020). The Hungarian economy is too small and heavily integrated into global (mostly European) value chains to allow a successful turn to the development state mode. Also, such attempts set Hungary as a member state on a collision course with EU norms and institutions because of its protectionist and interventionist tendencies.

Here is the third, and most critical, aspect of the regime. The removal of checks and balances and the erection of a quasi one-party state seems to have been designed for redirecting domestic public revenues and EU transfers into the pockets of political entrepreneurs. Misuse of public funds and blurring the line between the state, the ruling party, clans and oligarchs is a complex problem for Hungarian society. Some voters have been accustomed to favouritism; others are not aware of the size of malpractice due to limited access to reliable media; and the political opposition lacks resources and political weight to successfully confront the ruling party.

What is new in 2022 and after, compared to the first decade and half of Hungarian membership, is the change in European sensitivity to cronyism. Because of that change, sizeable EU funds are at stake for Hungary, its government and, eventually, its society for legal non-compliance. Shortcomings in the rule of law and lack of transparency have provoked a challenge from EU institutions that have belatedly realised that heavy-handed and arbitrary government power in certain member states is incompatible with the common norms, and eventually with EU membership.

The main policy conclusion here is that if Hungary wants to remain inside, it must put an end to further solidifying of a crony state. It is compulsory to restore checks and balances under commonly accepted European guidelines for Hungary to remain a member state with full rights. Consequently, it is imperative to redefine government priorities by moving away from low-to-medium value added industrialisation towards an economic structure better integrated in global value chains.

In order to achieve that, a thorough budgetary and structural policy reform must be accomplished, as well as a timely accession to the eurozone in order to reduce the handicaps deriving from inflationary and volatile national currency. As for the middle-income challenge, admittedly, there is no universal policy formula to copy, nor a single avenue to a higher level of competitiveness. The member state government legitimately aspires to attain elbow room to act according to particular domestic conditions and challenges. But that argument must not be distorted into voluntarism, and domestic policy specificities shall not endanger systemic fit into commonly accepted European legal and institutional order.

Notes

1. Lane (2005) identifies the countries covered here as belonging to a sort of continental type of market capitalism, but more state led. He placed Slovenia, Czech Republic, Poland, Hungary, Slovakia, as well as Estonia, into this category while the two other Baltic countries were assigned to the second subgroup together with Croatia, Romania and Bulgaria based on their early 2000s data. Beáta Farkas argued that Hungary, Slovakia, Czech Republic, Estonia, Latvia and Lithuania seem to be similar, in terms of high economic openness, low level of state control (!) and moderate level of administrative burden, leaving Poland aside for being less open at that time (Farkas, 2011). Note that those classifications reflected the first 15–20 transition years – when countries mostly differed in terms of transformation *speed* rather than of its *destination*.

2. Under the historical conditions of Soviet-Russia and its European satellites during established Communist rule with its strict vertical control by centralised bureaucracy and limitations on *any* autonomy, the term *'state intervention'* is not really applicable. The very term assumes the existence of *two distinct agents*: one that intervenes and the other (the economy, business) that is exposed to intervention. But in an omnipresent bureaucratic party-state such separation does not exist; the term 'state intervention' is not relevant in the period before regime change.
3. PM Orbán, returning to power after 8 years in opposition, took a series of non-conventional legal and economic decisions, starting with a bank tax in 2010. Not that this measure is particularly Hungarian: Sweden had it before Hungary, and Austria, the United Kingdom, Belgium, France, Germany, Slovakia, etc. introduced some sort of financial sector levy. Still, the Hungarian measure stands out for its size, but also its declared goal of side-lining foreign-owned banks. True, banks in Hungary had enjoyed a pretty high return-on-equity for a long time before the crisis, and had been lightly taxed, therefore the incoming government felt justified to mete out a serious levy on cash-rich businesses (Bod, 2012).
4. The Hungarian chapter of Transparency International, an international NGO investigating corruption issues, was among the first to ring the bells about the potential consequences of a new Hungarian constitution in 2011 and a set of laws designed by Fidesz to use the state apparatus for party political ends, amounting to state capture (TI, 2012). Leading Hungarian economist János Kornai determined that the Hungarian governance evolved rather early into what he called an *autocratic hybrid regime* (Kornai, 2015). For policy analysts, PM Orbán's public speech in 2014 about aiming at turning Hungary into an *illiberal democracy*, and the new policy line of "Opening to the East" (meaning closer links to China and Putin's Russia) indicated a break with the former path to Western-type democratic system (Haines, 2014).
5. Rigid systems do not respond well. Of the sizeable body of literature on the collapse of the Soviet order, Solnick is particularly relevant to our arguments as he does not ascribe the disintegration of the USSR to economic or security imperatives but to a loss of confidence of the state apparatus in the ability of the Soviet leaders to retain control over government and society (Solnick, 1998). He concludes '. . . the Soviet system did not fall victim to stalemate at the top or a revolution from below (though elements of both were present) but rather to *opportunism from within*' (Solnick, 1998, p. 3, emphasis added). Bureaucrats deserted the system: 'In effect, Soviet institutions were victimized by the organizational equivalent of a colossal "bank run", in which local officials rushed to claim their assets before the bureaucratic doors shut for good' (p. 4).
6. John A. Cloud served as the economic desk officer for Poland, Hungary, and Czechoslovakia in the State Department's European Bureau of US in 1989. I, myself, advisor to MDF, emerging opposition party, also experienced caution from Western diplomats and visitors concerning the speed of changing the status quo.
7. The researchers cited assumed that all societies concerned, however different they were at that time, would develop to the same direction, see a chapter in *Different Path but Same Destination* (Rose & Mishler, 1994, p. 21).
8. COFOG is the classification system of government expenditure by types of function as published by Eurostat, the statistical service of the EU. I express here my gratitude to my colleague Zoltán Pitti (Corvinus University of Budapest) for preparing the charts.
9. Szanyi regards it a *patronage system* rather than *economic patriotism*. Centralised power reduces the role of independent public institutions such as the competition office and the courts. Political patronage, business capture and political rent-seeking are also identified (Szanyi, 2019). This particular form of state capture entails open and systemic corruption. The practice is visible to many, yet the public is influenced to regard cronyism as an instrument needed to establish a 'new national bourgeoisie and middle class' (Martin, 2017). See also Győrffy and Martin, 2022).

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