The EC: A Hungarian View toward 1992

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I. INTRODUCTION

The integration of the Single European Market in 1992 is a serious challenge for Hungary, the pioneer of the Central and East European renewal process. This Article attempts to outline the major causes of concern, the expected impacts, and some strategic responses for Hungary as a Single European Market emerges.

II. REALITIES OF THE CHALLENGE

The establishment of a Single European Market is an historic milestone in the development of Western Europe and the system of international relations. The role of Western Europe in international relations was drastically weakened by the two World Wars. After a short reconstruction period, between 1950-1970, both Eastern and Western Europe have lagged behind North-America and Japan on the road of technology-intensive growth. From the European standpoint specialized sectors have been evolving in international economic relations. Comparative advantages in the production of material-intensive and energy-intensive products, in traditional light manufacturing and consumer durable goods are moving into the developing countries, especially the Far East countries. Meanwhile the output and export of technology-intensive products or future-oriented industries with significant financial flows are mainly concentrated in the United States and Japan.

The radical halt of Europe's economic loss of ground and the laying of the foundation of a European "risorgimento" opening up new horizons, are developments of world-wide dimensions. Undoubtedly, the pace of economic growth, structural transformation, and technical and scientific progress will be accelerated by the abolition of differing approaches to the system, the general harmonization of the social and economic environment and policies, and the large scale replacement of previous bureaucratic management techniques with the regional integration of market forces. These changes will effect the conditions of economic activity in approximately forty percent of the European Communities' ("EC") combined Gross Domestic Product ("GDP").


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Economists are well aware of the fact that the process of European integration is not exempt from contradictions and conflicts. There will obviously be disagreement among the Members States of the EC concerning the financing of costs stemming from the integration process, economic reallocation, and the sectoral and geographical reorientation of economic activities. In fact, it is possible that due to implementation problems resulting from conflicting interests, the establishment of the Single European Market will require more time and bear less favorable results than expected, in terms of growth, employment, and equilibrium.

The formation of a “European Europe” will also mobilize political interests and forces. These forces will be necessary to respond to the Asian challenge. Furthermore, they are needed to counter the weaknesses of a century-old Atlantic system of relations resulting from the dominant Pacific economic orientation of the United States and to cure, once and for all, the Euro-sclerosis of the 1970s.

The establishment of a unified internal economic environment in the EC will be a reality in the 1990s. This unification will result in a consumer population of 320 million, representing fifty percent of world trade in services, forty percent of world merchandise trade, and twenty-five percent of world production. This formation of a more pronounced market force, in the context of Western European integration, demands an immediate adjustment from all trade-sensitive foreign countries in the world.

III. THE EC CHALLENGE AND HUNGARY

The EC Challenge is a special part of the multiple “shock effects” influencing Hungary. In the last decade a structural equilibrium in the economic, social, and political crisis has emerged. This complex crisis was a multi-causal one. The driving forces encouraging rapid growth in the three decades after World War II have been exhausted. These forces included survival after the war and the life-energy releasing effect of “zero-time.”

In the 1950s and 1960s these forces included the resources redeployed into the productive sphere through expropriations, income-nivellation and the negligence of agricultural and infrastructural development; in the 1970s growing indebtedness. As far as the 1980s are concerned, a number of factors have already had a powerful and negative effect including missing the opportunity to adjust to the new type, technology-intensive world economic growth pattern and the new world economic value system, handling the consequences of indebtedness, and the “Eastern Challenge” resulting from the exhaustion of the driving forces in CMEA cooperation. For example, the share of CMEA countries in Hungary’s foreign trade decreased from seventy-one percent in 1960 to
forty-five percent in 1988 and it will probably be down to forty percent in 1990.¹ The model-functioning disorders, missing the world economic adjustment, structural obsolescence, and loss of market positions could be perceived prior to the 1992 challenge.

Prior to World War II the development level of Hungary was roughly similar to the Southern European countries. By 1985, per capita GDP based on purchasing power parity calculations was 11% higher in Italy, 48% higher in Spain, and 8% higher in Portugal.² The Hungarian share of world exports amounted to 0.65% in 1938 and 0.4% in 1988.³ The physical isolation of Hungary from the Western-European infrastructural developments is especially severe in road and communication networks. Thus, the difficulties resulting from the simultaneous economic and political hardships of external economic reorientation and improvement of performances, are multiplied by the challenge of 1992.

The external conditions of the social and economic progress in Central European countries are favorably influenced by the dynamic developments and accelerated modernization of neighboring Western Europe. Western Europe is a region which has played a decisive role in the historical development of Hungary in the last one thousand years. These developments are illustrated by the apparent curing of "Euro-sclerosis" in the 1970s, by the deregulation and liberalization of the economic environment and, finally, by the standardization of adjustment requirements. With the advent of the unification of the 1992 program, Hungary will be in a better position to modify its social and economic progress since the adjustment of traditionally weak Hungarian enterprises to the national markets of twelve countries is, by all considerations, a bigger task than having to adjust to a unified market.

At the same time, however, a new challenge will be introduced in Hungary involving a number of new shock effects in the form of increased sales competition in Western Europe, the extended scope of competition mechanisms, stronger trade-diverting and capital-draining effects, and the squeezing of non-competitive, outside countries and enterprises from Western European markets creating a more unified economic, technical, and administrative system. This danger is not hypothetical since it is reflected in the development of East-West relations in the second half of the 1980s. It is even more instructive to realize that so far the geographical enlargement and the "articulation of depth" of the EC has unfavorably influenced the industrial exports of less competitive CMEA countries at a higher rate. The 1988-89 Annual Report

¹ Statistical Yearbook of Hungary.
³ United Nations Yearbook for International Trade.
of ECE\textsuperscript{4} also highlights the fact that between 1980 and 1986 the supply of sources in industrial imports of EC countries shifted from Eastern Europe to South European countries. In a broader perspective, Central and Eastern European countries are unfavorably influenced by the geographical reorientation of Western European economic forces. If Western European economic dynamics are centered along the Hamburg-Sevilla axis instead of the Danube basin and the Alp-Adriatic zone, the external conditions of the development of Central European countries will further deteriorate.

The establishment of the unified internal market and a more solid foundation of the joint actions of Western European countries tends to increase the bargaining power of Western Europe in international relations. In a period of a decreasing trend, or low level of danger, arising from military conflicts, international power relations are primarily influenced by the size of international economic, and more precisely, financial, technical and foreign trading bargaining power. As a consequence of the more intensive interactions between the military, economic, and social aspects of security, the importance of the EC security policy in relying on greater bargaining power is indirectly increased even if the "European" character of assuming a military and security role is not developed until the mid-1990s.

The appearance of united Western European defense and political efforts could hinder the improvement of relations with outside countries and, parallel with the unification of the economic environment, draw a new line of demarcation between the countries separated from each other after Yalta. The risks stemming from the diverging priorities of a unified market and an all-European cooperation are far from being eliminated. It is also difficult, from the domestic politics viewpoint to prepare the individual Central European countries for strategic re-integration without the anxieties around "Fortress Europe" being clearly dismantled. Furthermore, the unfavorable possibility of Austria entering the EC and the deterioration of the special relationship between Austria and Hungary might pose a problem of primary importance to Hungary.

IV. Hungarian Options

Based on Hungary's history of development, continental situation, and present growth endowments, economic growth has been deeply embedded in the European division of labor. Only one-sixth of her foreign trade is with non-European countries. Therefore, the Hungarian external economic strategy is anxious to expand cooperation with overseas developed and outside developing countries. Nevertheless, these overseas

\textsuperscript{4} Economic Survey of Europe 64-82 (1989).
partners cannot counterbalance the consequences of deterioration of the European division of labor.

Hungarian policy makers, in line with the general attitudes in Eastern Europe, ignored the development challenges coming from Western Europe in the 1950s and 1960s. The power group interested in the preservation of the political and economic structures created after World War II strove to intensify cooperation among CMEA countries. The exhaustion of the earlier driving forces of CMEA cooperation and the widening sphere of the regional shortages made the futility of these attempts obvious by the eighties. The recent political collapse of the old system in the German Democratic Republic and Czechoslovakia made the realization of the idea of an “East European fortification” formed by chariot-countries hopeless.

A specific offshoot of regional protectionism is an all-European cooperation growing out of a CMEA-level response, that is, of the relations between the two regional organizations. These approaches lead into blind alleys, partly as a consequence of the dishevelled system of CMEA cooperation and partly due to the different interest relations and countervailing possibilities by countries vis-à-vis the European Communities. Therefore, the scope of regional cooperation is very limited at the outset. For example, the Hungarian economy has distanced itself in the last two decades from the Soviet-type Stalinist model and is advancing, on the basis of her national characteristics, on the road of development termed as “market economy Hungarian style.” A similar pattern will be followed in Poland and, with different timelags, in the various other Central and Eastern European countries.

The responses to the EC challenge and the character of relations between the EC and the individual CMEA countries will also reflect national characteristics and thus, be selective. Even the pace, depth, and complexity of the transformation taking place in the individual reform-countries shows considerable differences which makes either the modernization of economic cooperation between CMEA countries or the joint response hardly viable.

While the framework of traditional CMEA cooperation is not suitable for intensifying established relations with the EC, a new situation emerges because the transformation unfolding in Hungary and Poland is spreading over to East Germany and Czechoslovakia and because there is a possibility of postponement of Austria’s entry into the EC. Although the Central European CMEA countries following the road of transformation are trying to improve their positions in the “circles of Western Europe,” individually, their advancement toward the inner circles of the EC system of cooperation will take place in several stages, through a longer period of time. The concept for Pan-European Economic Integra-
tion seems to finding increasing acceptance. It has been contended that the Central-European reform countries, similar to the remainder of the EFTA, might cooperate more intensively with each other and the EC through interweaving markets without having to participate in the European political collaboration.

The transitional period can be improved by a Central European sub-regional system of cooperation which would link together, with differing intensities, the Central European countries involved the Western European circles of cooperation. At the moment the most rapidly assembled "core" of Central European cooperation could be an Austrian-Hungarian-Yugoslav subregional relation. These relations can be continuously expanded, depending on the success of the transformation process in other Member States. As far as Hungary is concerned, Central European cooperation is not an exclusive alternative vis-a-vis EC relations since the joint share of Austria and Yugoslavia in Hungary's foreign trade in 1988 represented ten percent, and the figure for East Germany, Czechoslovakia, and Poland amounted to fifteen percent. At the same time it could mitigate the external economic risks of transformation and strengthen Hungary's bridge-building role in East-West relations.

As a consequence of all these factors in external relations, the EC-connection is a matter of life and death from the point of view of Hungarian development. It is not a coincidence that among all the CMEA economies both the relative increase and the absolute share of the twelve EC countries was the highest in Hungary's trade in the two decades after the beginning of the Hungarian economic reform. Between 1970 and 1988 the EC share in Hungarian exports rose from 16% in both 1970 and 1985 to 24% in 1988. In Hungarian imports, the figure rose from 17% in 1970 to 21.8% in 1985 and 25.3% in 1988.

The EC countries import more than half of Hungary's timber and furniture exports and 31-43% of her food, raw material, leather, and clothing exports. The further development of Hungarian-EC relations is of decisive importance from the viewpoint of several production sectors. The Hungarian export product structure into the EC countries is more favorable than into the average of developed market economies as a whole.

Material intensity of Hungarian exports is focusing on the expansion of materials into neighboring countries, including those in the EC, because of transport cost efficiency. The opening of the Danube-Rhine-Main Waterway reduces the logistical disadvantages of Hungarian ex-

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ports and makes it possible to transport Hungarian goods to more distant regions of the EC.

The establishment of the Single European Market, the standardization of certain fields, and the simplification of the licensing and registration procedures can improve the market access possibilities of pharmaceuticals which represented 2.5% of all Hungarian exports to the EC, in 1987. In the high-tech fields, and in those with high technological development intensity, the standardization of technical norms influences all Hungarian imports. In 1987, the EC share was 40% of total Hungarian instrument imports, 27% in machines and equipment, within these 44% of metal producing machines, 37% of office machines, 32-33% of special industrial machines and electric machines and equipment.\(^7\)

The technical norms and standards of the Common Market will probably be adapted by a great number of "outside" countries depending on EC relations, therefore these norms and standards can be regarded as de facto Western European ones. As a result, the import dependence is more considerable in view of the relations with non-EC Western European countries. Although in 1987 the Common Market represented 7.5% in total Hungarian machine and equipment exports, export expansion to Western Europe presupposes the adaption of the new norms and standards. As a consequence of the narrowing markets of the Hungarian machine industry, specialized in CMEA markets, one of the requirements of the necessary market re-allocation is the adjustment in the field of standards.

In the case of heavy chemicals (which represented 10% of Hungarian exports to the EC in 1987, specified mostly by standardized parameters, containing homogenous semi-processed products) the norms and standards were established earlier, the chances for standardization are relatively modest, and their impact on the Hungarian economy will be small. Light industrial consumer articles such as cosmetics are expected to change less radically, due to the greater national resistance within the EC regarding unification.

The impact of coordinating and standardizing technical norms reaches beyond the EC to the whole of Western Europe. For dimensional reasons the outstanding role of the Common Market and the Western European region as a whole in the Hungarian reproduction process, makes it expedient and desirable that Hungary join the standards of the EC. The share of overseas OECD countries and that of the new industrial exporting countries tends to increase the external orientation of the Hungarian economy. Due to dimensional reasons the cooperation with the more dynamic new partners cannot countervail the shrinking

\(^7\) **Statistical Yearbook of Hungary.**
tendencies in CMEA cooperation. The relative importance of trade with the EC countries is almost twice as great as other average CMEA economies which indicates the high EC-sensitivity of the Hungarian economy and the interrelation of Hungarian economic reforms and the Europeanization of her national economy. The basic task of Hungarian external economic strategy is not to take a defensive attitude vis-à-vis the challenges of 1992 but, instead, to exploit the possibilities of the bigger internal market by an active, offensive strategy of renewal.

V. EXTERNAL CONDITIONS OF HUNGARIAN-EC RELATIONS

Prior to the rapid transitions in Central and Eastern Europe the receptiveness of the EC was not reassuring from the viewpoint of Hungarian cooperation efforts. These efforts are interpreted in the complexities of the European processes. There is an increasing international recognition that the failure of "perestroika" could lead to an open crisis in Central and Eastern Europe and the inability of present and future political forces to guarantee a peaceful transition and to protect a basic Soviet interest which might increase the danger of conflict situations and provoke a crack-down by the armed forces. A soft-landing of the transition in Central and Eastern Europe is a basic international and regional security interest. There is a strong correlation between diminishing confrontation dangers and military utilization of resources. If Eastern Europe succeeds in redeploying resources in the civilian sphere, the crisis situation, and confrontation danger, will simultaneously decrease. To launch and speed up this process with international resources seems to be an international interest and can lead to the transformation and erosion of the NATO and the Warsaw Pact.

European support of perestroika might generate new regional driving forces. Central and Eastern Europe has a bride-gift as well: the favorable endowment with cheap and relatively skilled labor. The countries, enterprises, and enterprise-coalitions will acquire a competitive edge from the input side if they rely on this human resource potential. The successful combination of Central European skilled labor, semifinished product and spare-part producing capabilities with Western technologies, management, and market organization can create alternative input-sources to the competition of the Asian countries. In addition, it might decrease the international financial and commercial imbalances. An extension of the united Europe toward the East might also improve the chances of Europe in the international competition.

The demarcation line between the two halves of Europe has changed frequently during its history. At present, a new milestone is represented by the efforts of Central Europe to reconsider the consequences of Yalta and reintegrate into the European and world economy. These endeavors,
as the events of 1956, 1968 and 1980 indicate, cannot be derived from Soviet perestroika. Nor can their success be exclusively linked to its future. There is no doubt that the success of perestroika is a fundamental national, regional, and international interest. It is not probable, however, that an inward-looking Soviet-Union emerging after an eventual failure of perestroika would strive to return to its previous presence and commitments if the Central European countries respect the geopolitical realities and did not endanger Soviet security and economic interests. The economic substance of a united Europe can first be extended to Central Europe and the pioneer countries of transition. This aspect makes the reconsideration of the previous motivations of the European policy and the creation of its Central European dimension more convenient.

On the basis of geographical boundaries and traditions of cooperation the European re-integration of the Hungarian economy cannot be indifferent for countries such as the Federal Republic of Germany and Italy. It is in the interest of Western Europe to take responsibility in the transformation of Hungary and Central Europe and facilitate a non-violent Central European transformation. This transformation would include an increase in the value of Central and Eastern European regions in the EC's geographical priority hierarchy by offering better market access possibilities, encouraging the flow of technologies and direct capital, by structural cooperation reaching beyond transportation and environmental protection, by opening the "gates" of organizations which Western European countries participate in such as the OECD, Council of Europe, and European Parliament, and by establishing European integration between enterprises, small communities, and different population groups.

The other, equally important external "pillar" of Hungarian Europe-policy is the new Soviet strategic and foreign political initiatives, the easing of tensions in the field of Soviet-American military confrontation, and the possibility of withdrawing foreign troops stationed in Europe. The new European policy of the Soviet Union, including the tolerant attitude toward Hungary's attempts to resolve the crisis create external conditions for the formation of new, more articulate ways of cooperation between Hungary and Western European countries. At the same time, a scientifically-based European policy in Hungary must not ignore the consequences of cyclical political processes and of a possible transitional Soviet restoration. Flowing from this, in the period of favorable external conditions, the more rapid pace of institutionalizing relations between Hungary and the EC is of key importance because this may offer contractual safeguards to the irreversibility of this process.

VI. HUNGARIAN STRATEGIC APPROACHES TO THE EC

Confronting external conditions and Hungarian endeavors also calls
attention to the necessity of implementation of these changes in stages. For the forces and interest groups in the center, and right from the center, of the Hungarian political sphere, obtaining the full EC membership for Hungary, the most intensive contractual and institutional participation in the Western European integration, is a strategic goal. From the viewpoint of reinforcing the European identity of Hungary and strengthening the process of democratization, setting this strategic goal is of decisive importance. However, the existing Hungarian external links hardly make it possible to take on the obligations stemming from the Single European Act approved in 1986, since they are not compatible with a possible later status of neutrality. The time requirements and unforeseeable developments of European re-organization and wide-scale constructive all-European cooperation and demilitarization following the normalization, necessitate the preparation of “stage type” intensification of relations and an openness to the new forms of cooperation resulting from these new developments.

In the present situation the accelerated implementation and further conceptual development of the Trade and Economic Agreement, signed in the autumn of 1988 between Hungary and EC, reflects an earlier stage of the political situation, justified by the accelerated transformation process and new political developments. It would be desirable to develop the trade agreement between Hungary and the EC into a more comprehensive cooperation in the fields of economic, technology, financial, and tariff policies. An asymmetrical free trade agreement between Hungary and the EC would ease the adaptation burdens of Hungary in the most critical period of transition and would make it possible for industrial and agricultural preferences given by the EC to be reciprocated after a certain period of grace.

The new Hungarian and Central European situation, unprecedented in the history of the external relations of the EC, and the more powerful expansion of the coalition government formed after the elections could make it worthwhile for the EC to accelerate the intensification of relations. This opening of relations could be made by offering a “special status” reaching beyond the scope of the free trade agreement. This special status in the “circles of Europe” is not incompatible with either the Callaghanite idea of a unified European economic cooperation zone or with that of Central European subregional cooperation.

The internal conditions of responding to the EC challenge do not significantly differ from the general requirements of the Hungarian renewal process. The requirements of adjustment to the Western Europe of the 1990s should become manifest in all segments of the new Hungarian development strategy. These segments range from external economic strategy to structural and educational policies, legislation,
standardization, environmental protection, and the modernization of the institutional structure.

On the governmental level, adjustment is expected from the implementation of a comprehensive integration package. External relationship building will focus on the blending of the European dimension of the new Hungarian foreign policy, security policy, trade policy — facilitating market access of Hungarian agricultural products, — decreasing the tariff burdens of Hungarian industrial goods, obtaining the full-scale treatment of most favored nation status, a complex cooperation policy reaching beyond the trade agreement and, finally, the combined scientific, educational, and cultural policy must be a high priority.

Regarding structural policy, it is well-known in the scientific community that in the last fifteen to twenty years the material, energy, capital, and intensive production and supply structure of Hungary has not generated dynamics, income, or stability, in the domestic economy or in hard currency exports.

The creation of more up-to-date forms of cooperation and the acceleration of European re-integration requires a powerful redeployment of resources, incomes, and economic activities. For instance, the simplification of the registration procedures and licensing of pharmaceuticals, followed by better access to markets makes it both expedient and desirable to concentrate on the development of the Hungarian pharmaceutical industry and related sectors such as biotechnology, the production of pesticides and insecticides and veterinary medicine.

Furthermore, it is necessary to reallocate a growing proportion of resources into the sector having greater technical development intensity such as manufacturing sectors, production of electric engineering consumer articles, telecommunication, vacuum techniques, computer programming, and instrument industry, to be prepared for the requirement of the Single European Market. It would be expedient to focus the initial stages of commodity and capital import liberalization on those sectors which bring the fastest results.

Beyond the transitional protection of the scope of activities, which will reach a competitive level only after a certain transitional period, the future of lastingly non-viable sectors and activities, and those not relying on specialization advantages, must be identified to countervail import competition. The further structural development and new-type export-orientation of Hungarian agriculture and food industry, having, by European standards, exceptionally favorable growth endowments, could be linked to a significant increase of the share of some import products from the EC including fodder, butter, milk powder, and Mediterranean fruits. In order to prevent greater social, political, sectoral, and regional tensions, the future of those Hungarian sectors and activities, which will be phased out as an aftermath of cooperation with the EC, must be deter-
mined in the framework of comprehensive cutback and restructuring plans.

The main field of Hungarian economic re-integration into Europe is the sphere of enterprise activities. A fundamental task of government activities is to establish an economic environment and management technique which compels and makes Hungarian enterprises interested in performing successfully in Western European markets. In addition, it must create the preconditions of enterprise-level competitiveness by abolishing the barriers of capital, manpower, and technology and revise the present overtaxation practice, offering attractive conditions to foreign investors and other partners by adjustment to the Western European measures of deregulation and standardization. In this context Hungary intends, after a preparatory period, to move in the "European House" as one among equal tenants and not as a night-lodger in the basement. Flowing from this, European inter-enterprise relations will be a popular growth area based on the Hungarian human resource potential, expertise, and technical developments mobilized through the European forms of cooperation and the establishment of a network of Hungarian banks, financial institutions and production and service enterprises.

VII. Conclusion

The creation of New Europe demands, parallel with preservation of national identities and cultures, the integration at levels of European population, the reinforcement of Europe-consciousness, and the establishment of behavioral cultures in harmony with the historically well-proven values of Europeanism. This process can be accelerated by easing the mobility of the Hungarian population around Europe in tourism, education, and jobs, and, in the framework of an all-European cooperation, by the creation and rapid development of a network of Hungarian institutions affiliated and integrated into various European Academies, European Institutes and the whole European teaching and educational system. Of course, Hungary's re-integration into Europe cannot be realized without a larger-scale adjustment to the historically well-proven Western European values of democracy, parliamentarianism, human rights, private ownership, and a moral value system. It is of great importance to reflect on the European-level party political lines of force in the Hungarian domestic political development and to make use of inter-party relations in the new political field of force in the integration process.

The new European policy of Hungary and the accelerated adjustment to the challenge of 1992 involves a number of breaking points regarding the institutional frameworks and power structures which have come about in the last decades. Overcoming the various kinds of resistance and moments of inertia resulting from these factors requires very
circumspect, creative solutions bearing in mind the room for change in the country and the possibility, with upcoming elections, of a newly-formed, government capable of officially representing the national interests.