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SUSTAINABLE AGRICULTURAL DEVELOPMENT: THE ROLE OF INTERNATIONAL COOPERATION

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Transition to Market Economies in Eastern Europe: The Case of Hungary

INTRODUCTION

A new political system began in Hungary with the free elections of March 1990. Associated economic changes involve a major transition from a 'command' economy to one based on the operation of market forces, which are also expected to affect the agriculture and food economy and to be based on a mixed ownership structure with a dominance of private property. Hungary was the Central European centrally planned economy (CMEA) with the earliest record of undertaking economic reform as well as being a leader in the more recent democratic political changes. As such her experience is that of a model case in the region.

LESSONS AND CRITICAL CONSEQUENCES OF THE PAST

For almost half a century Hungary has experienced far-reaching structural changes, some of which have resulted in failure. The unsuccessful experiments generally were those which related to the planning and control of agriculture at the macro level with the lack of the advantageous effects of market mechanisms. However, the first impact of change was in land holding with the land reform of 1945. Under the impact of wartime damage and a weakened economy, and with the further complication of political dependence, this did no more than transform ownership relationships in landed property, replacing a system which had been semi-feudal. It did not allow modernization to proceed, since it created very small-scale farms (minifundia) with weak command over means of production.

The period was also short-lived. By 1948, a communist regime was established which switched the pattern towards large-scale farming in many ways similar to the *kolkhozes* of the Soviet Union. This became dominant by 1961 and in many cases, probably as much as one-third, there was little change until very recently. They lacked capital and equipment, since the modernization of agriculture was not given a high priority by a regime which was more concerned with one-sided industrialization. Furthermore, they lacked strong proprietary motivation and suffered from the effects of unfavourable internal terms of trade. Following the death of Stalin in 1953, some efforts were made

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to encourage homestead farming by cooperative members through subsidization. It also became possible for small-scale farming to be carried on by those who were not principally engaged in cooperatives (industrial workers or pensioners, for example). Though neither of these initiatives was strengthened following the attempted revolution in 1956, there was a persisting shift in patterns of production with labour-intensive work tending to become concentrated in small-scale enterprises.

Throughout the 1960s and 1970s, the growth rate of food demand exceeded that of supply in Hungary. Furthermore, the main strategy involved attempts to increase the quantity rather than the quality of food produced, and in a general situation of scarcity there was minimal incentive for quality improvement. It should be emphasized, however, that agricultural performance, in the 1970s in particular, had some satisfactory features. For some years Hungary was one of the few countries in which incomes derived from farming for those people whose principal occupation was on the land approached parity with those of other sectors, even though their hours and working conditions were possibly less advantageous. Farming as a secondary activity was also profitable. This general position was maintained through the decade, since the price explosions on energy markets did not adversely affect the costs of farm inputs until the decade was drawing to its close.

By then, however, there were also other difficulties, in particular the decline of international demand consequent upon the effects of agricultural growth in the European Community and the greater internal integration of its food trade. By the middle of the 1980s, Hungarian agriculture, and much of the remainder of the economy, was drifting into a critical state. Indeed the centrally emphasized task of 'maintaining the living standard' could be achieved only with the restriction of agriculture to limit its resource use. There was little incentive to increase the technical efficiency of production or to provide stimulus to the labour force. Some growth did occur in the so-called 'second' and 'third' economies, but the mainstream was lagging.

In this critical situation, transition to a market economy and transformation of the structure of agricultural production to one involving a greater variety of type and scale become issues of key importance. It is complicated by the need to work within the context of international changes and by more general internal problems. Hungary has a general shortage of capital and major problems in effectively allocating what it has, following the principle of opportunity costs. The overall problem is severe. Though technologically outdated, many production processes are excessively capital-intensive and need renewal undertaken within a more effective allocation process.

APPROACHING A NEW OWNERSHIP SYSTEM IN AGRICULTURE

To create better prospects for an agricultural sector which faces external constraint and internal difficulties, the key requirement appears to be that of reforming landownership relationships which can be harmonized with a market mechanism. New legislation on landownership is urgently required as soon as possible and this needs to be coupled with revised regulations con-

cerning ownership of non-land capital assets used in farming. Cooperative law also needs attention.

Reforming ownership structures

Approximately 70 per cent of the country (9.3 million hectares) is cultivated, of which 12 per cent belongs to state farms and state combines, while 85 per cent is within the cooperative sector (including the amount farmed as household plots of members). Within the latter, two separate cases have to be considered. A large portion, of approximately 60 per cent, is both owned and used by cooperatives; of the remainder ownership of land rests with members or with individuals who are not themselves members. In considering reform of ownership there are two complicating factors:

- (1) The status of ownership in 1949 could be taken as the basis for reprivatization or compensation, with those who owned land at that time, or their descendants, having a prior claim.
- (2) While this appears to have merit it would obviously not necessarily completely reflect the current situation and the position of those who are at present engaged in farm work on particular tracts of land. A historical basis would not necessarily represent the facts of the contemporary operating pattern. Nor would either necessarily coincide with the need to ensure that future operation would be placed in the hands of those most suited to efficient farming, either on a private or a cooperative basis.

The Compensation Law passed by parliament does not imply that direct reprivatization must occur; indeed it has elements of compromise between the rights of prior ownership and those who make up the current farming peasantry.

Privatization processes in agriculture

Privatization is not only a way of handling issues of ownership; it is potentially an important tool in increasing agricultural efficiency. The need for change is widely recognized in Hungary for both reasons, though more conflicts are generated by the question of how to manage the process.

As far as the privatization of state farms is concerned, they can be placed into three groups. The first consists of those dealing with breeding of high-quality livestock of all types, or producing hybrid seeds, which act as suppliers to other enterprises. These so-called 'national farms' are not to be privatized; they will remain in the state sector into the indefinite future. A second group consists of state farms whose activity is profitable at the present time. These will eventually be passed into private ownership, but the process is not being given a high priority. That is reserved for the third group, of loss makers, which may be privatized as soon as possible. Government agencies will handle the process.

The privatization of cooperatives will be managed by the organizations themselves. The government wishes to help the process rather than intervening in it, hence decisions will largely be left to cooperative members. Where farming is efficiently conducted and where members are satisfied with their incomes, it is anticipated that no major land reorganization will be requested. However, it can be noted that in many cases the relationship between membership and management has often been more akin to an employee–employer form instead of reflecting a situation in which members were co-owners with an influence on managerial decisions. This internal issue must be addressed and discussions are taking place about new cooperative law to tackle the problem. It is a complicated issue since it involves questions both of ownership and of motivation.

In other cases, particularly where there is less efficient management, members may insist on the return of their land in order to engage in private farming. Even here, however, there is debate about the extent to which some cooperative activity should be retained and managed in order to handle the joint supply of inputs and the group marketing of products. It would be the basic activity of farm operation which would move onto a private, family, basis. A consequential problem would be that of establishing ownership in land and fixed assets.

STRUCTURAL CHANGES AS A SOURCE OF INCREASED EFFICIENCY

The policy environment

Unless real production costs can be reduced and quality improved, Hungarian agriculture cannot become competitive in world markets. In the past relatively high output prices and an increasing demand for products allowed managers to operate profitably despite basic weaknesses in farm performance. The record is not consistently poor; the annual growth rate of 3–4 per cent through the 1970s was a notable achievement. Nevertheless, substantial and increasing subsidization has been needed to bridge the gap between high input costs and the relatively low world market prices of agricultural products. At the same time, strong pressure was placed on farming to export more in order to win badly-needed foreign exchange. As competitiveness weakened, the state budget could only provide a decreasing amount of food export subsidies. Further, the burden of foreign debt, and the interest payments involved, has limited the resources available for general modernization. It is a great challenge to increase efficiency in such a situation.

Inner restructuring of large farms

It has already been suggested that a key element in improving efficiency will be a change in the way in which farming is managed, and aspects of the

process have been discussed. A number of points require elaboration. In the case of those state farms which remain as such it is not expected that management practices will remain static. Large organizations can be maintained to provide a broad framework, but operation can be divided into smaller decision-making units which are more sensitive to market conditions as well as being more able to supervise day-to-day farming operations. If privatization is desired, different kinds of economic decision-making units can be set up within the former large farm. These could include either cooperatives or companies as well as, possibly, family enterprises. The government agencies handling this process need to be able, within a defined legal framework, to cope with the problems of land and asset redistribution which will be involved.

Whenever cooperatives are involved, an atmosphere must be developed in which members have the right to make their own decisions. This will involve allowing them to modify the organizational structure of existing cooperatives or to break them up and found new enterprises. That might include reversion to private farming. The key element is that of allowing flexibility of choice, taking account of the need to create units of efficient scale appropriate to particular types of farming conditions. That is likely to require experiment in order for a more varied pattern to emerge, and for managerial capacity to be used which is appropriate to the scale and nature of enterprises.

Promoting viable family farms

People who believe in the comparative advantage of small farms often say 'I would do better, if it was mine.' There may be much truth in this view but other conditions, apart from ownership, are needed for successful small-scale operation. Apart from land and labour, substantial investments are required to sustain profitable businesses. Most of the people insisting on setting up on their own account tend to be aged 60 to 70, rather than 30 to 40. Apart from lacking access to finance, their knowledge of modern equipment and chemicals is limited. They may have some important skills, particularly in horticulture or animal husbandry, but this needs to be used effectively. In this context, Hungary has experience in allowing linkages to develop between small- and large-scale farming, which could be fostered. Potential does exist, in particular, for marketing the output of small-scale producers through cooperatives which would overcome the difficulty of lack of market information which is most acute among the former. This should be recognized and allowed.

FRAMEWORK AND GOALS OF A NEW AGRICULTURAL POLICY

Formulation of a new agricultural policy is approaching its final stage. The major issues have already received much discussion. Though new laws have yet to pass through parliament, the basic principles and goals which are emerging can already be outlined.

Liberalizing prices

Hungary has already had experience in applying market prices for agricultural products since a process of liberalization has been proceeding since the early 1980s. Step-by-step development occurred until the radical change early in 1990, when, except for bread-making wheat and some milk, the selling prices received by farmers became market prices, which also acted as the base for retail prices. This led to a significant increase in consumer prices in 1990, resulting in a decline in consumption. At the same time, rapid general inflation, affecting inputs to the whole food sector, has offset the increase in selling prices, creating a difficult situation. This has been prevalent for some time.

As in any open economy, Hungary periodically has had to adjust the internal price system to world market prices. There has been a specific relationship between consumer prices and producer prices because of government wage control policies. As a result of increasing input prices, there has been a gradual increase in farm producer prices. Together with a substantial reduction in government subsidies, the higher level of agricultural and food prices has become one of the major causes of the recent relatively rapid inflation. The unfavourable changes in the terms of trade have also given rise to inflationary forces.

Cutting subsidization of agricultural production

Subsidies to agriculture were significant in the 1960s and 1970s, though the level was tending to decrease. This was offset by a gradual increase in the prices of food products. In the 1980s, there were more substantial reductions in subsidies and the growth in output prices could only partially cover inflation-affected input costs. By the middle of the 1980s, the farming sector was already paying more to the budget in taxation than it received in subsidies.

Setting up the system of Agricultural Market Regulation (AMR)

Effective operation of liberalized markets requires a defined legal framework, appropriate institutions and suitable economic conditions. All of this involves different elements of policy, and it will take time and much discussion of the economic and political background to frame suitable agricultural market regulations. The basic concepts underlying current government thinking is that AMR should be a tool for intervening in demand, supply and price interlinkages when direct action is needed to reach a desired market equilibrium. It should provide stability within the market to avoid major damage through unexpected short-term adverse movements in producer prices and, against that background, allow the farm sector to increase its efficiency. This is regarded as important domestically, in order to ensure an adequate food supply, and externally to promote a satisfactory export performance. The latter is particularly important since agriculture has achieved an annual export surplus of 1–1.2 billion dollars

and the foreign exchange is vital as a source of finance for debt service and reduction, and for obtaining imports needed in other sectors.

There are three major tasks for the government to undertake. First, an organizational structure, involving a Committee of Regulation and a Grain Committee, has to be established. Following from that, the second issue centres on finance for establishing and operating an intervention fund. Thirdly, some thought is being given to the issue of production control, through quotas, which may be needed to guard against potential over-supply.

SUMMARY AND CONCLUSIONS

- (1) Hungary now has 130 per cent self-sufficiency in food production. This is unique in Eastern Europe.
- (2) Substantial development was achieved in food production during the 1960s and 1970s, one of the results of that being a growing ability to supply export markets. In the late 1970s and 1980s, the increase in production costs began to exceed that of selling prices of agricultural products.
- (3) From the beginning of the past decade export achievement has been a vital element in assisting the balance of payments situation, though fewer resources have been available to farmers to help them sustain their level of performance.
- (4) Transition to a multi-party political system has already taken place following the recent election of a new parliament. Nevertheless, it will take some years to make decisive changes in the economic structure of the country.
- (5) The ultimate economic policy goal is to allow market forces to play a dominant role in the whole national economy, as well as in the food sector. Very important decisions have already been taken concerning price setting, price liberalization and agricultural subsidy reduction. The government has yet to take decisions about Agricultural Market Regulation to prevent major instability appearing during the process of moving towards a market economy. This involves very complex questions relating to appropriate ways of matching progress towards liberalization with market stabilization. It is against that background that reform of the structure of Hungarian agriculture will have to occur.

DISCUSSION OPENING – TADEUSZ HUNEK*

Fekete and Forgacs have provided a very solid background for understanding the process of agricultural reform in post-socialist countries of Central and East Europe. There is nothing which I wish to add to it directly and I will simply congratulate them for their skill in providing an overview of experience in their country at very short notice in order to overcome difficulties with

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the conference schedule. Notice that they did emphasize the importance of agriculture as an export sector in Hungary, thus providing me with the opportunity to add a little detail relating to the main topic of our session – the possibilities for increasing the agricultural trade of the European region.

The following four factors will affect the agricultural trade situation of Eastern Europe:

- (1) The food sector in that region is still one of the most important parts of national economies, with 25–35 per cent of the labour force being engaged in food production, providing some 30–35 per cent of material product. The transition to a more market-oriented economy has decreased food demand by as much as 15–25 per cent in some cases, hence the export of food surplus is a key factor in preserving agriculture.
- (2) Many agricultural and food products are competitive in world agricultural markets, mainly owing to the low cost of labour in agriculture and food processing.
- (3) There is a general expectation, strongly shared by World Bank missions, that the food sector could provide a driving force in economic recovery through rationalization of its economic performance. As much as 25–30 per cent of output might be expected to enter trade.
- (4) Foreign trade liberalization, as a part of economic reform, can also be expected to have an impact on food imports. In the case of Poland, the share of imported food in total consumption rose from 2 per cent in 1989 to 10 per cent in 1990 and there is every indication that growth will continue.

The outlook for the future is obviously still very obscure, since so many changes are taking place, or are about to take place, and events are moving with great rapidity. All that we can be certain of is that there will be strong pressure from within all of the countries concerned to increase the agricultural trade of Eastern Europe, both on the export and the import side, and that this will have important implications affecting both the wider European market and the world in general.