

Legitimation Crisis and the Reforms in the Non-Socialist  
Sector

of the Hungarian Economy in the 1980's

by

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(ABSTRACT)

Hungary has garnered much international attention throughout this decade due to the program of economic reforms undertaken by the Kadar regime. In particular, the introduction of new regulations which have for the first time permitted the development of small-scale private enterprise in the official economy, the tolerance shown towards some activities in the unofficial economy, and also the success of small-scale private agriculture have prompted a discussion concerning the increasing role of private initiative in socialist Hungary. Attention has also been focused on the impact of these reforms upon the stature of the Kadar regime, and whether or not they have provided a measure of popular legitimation for it. The amazing transformation of Kadar from traitor of the revolution to the popular reformist of Eastern Europe has been unique among the socialist states. Equally fascinating was his quick fall from grace in 1988. The recent reforms in the non-socialist sector in the Hungarian economy will be examined in terms of the model of bureaucratic centralism, as put forward by Andrew Arato, and the crisis of legitimacy it posits.

## Acknowledgements

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Of course the author would like to express his deep appreciation to his committee, a kind and merciful lot in all. Tim Luke, the Chairman of the committee is to be thanked for providing valuable direction in the difficult theoretical aspects of the thesis, and especially for not drenching the author's rough draft chapters in a sea of red ink. For that the author is particularly grateful. Rhys Payne and Lynette Rummel have not only been patient committee members, enjoyable teachers, and the best faculty members an unorganized Graduate Assistant could ever work for, they have also been accessible, helpful and friendly people. The author would have enjoyed himself much less here if not for them.

Despite the author's reputation as somebody slightly to the right of Attila the Hun with his fellow students, he would nevertheless like to thank them for some rather interesting times and his

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Finally, the author would like to thank some old friends who, although they have never stepped foot in Blacksburg and do not feel the slightest bit of remorse about it, have nevertheless provided things indescribable for which he would be much the worse without. To \_\_\_\_\_, who has always been there. To \_\_\_\_\_, mi'z ujs, hazifiu! Magyarország will never be the same for us having been there. And finally to those who caused it all... I have been accused of having a weird preoccupation with Hungary, this may be true. To those close friends I made in Szeged: edes Anita, kedves Judit, es draga kis Era, my love of Hungary is due mostly to you. Isten ald meg a Magyarot!

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## 1.0 Introduction

"From Stettin in the Baltic to Trieste in the Adriatic an iron curtain has descended across the Continent." These words spoken by Winston Churchill in Fulton, Missouri on March 5, 1946, have defined America's perception of the division of Europe for the last forty years. Certainly the famous descriptive phrase coined by Churchill in his speech, in so far as it still conveys powerful images to us in the West, remains a meaningful term in our political vocabulary. Nevertheless this decade has been a time of prominent change behind the Iron Curtain and new terms have entered our political vocabulary such as *glasnost* and *perestroika*, the twin foundations of CPSU General Secretary Mikhail Gorbachev's reform program. But before *perestroika* there was Goulash Communism, a term inspired by Hungary's experimentation with economic mechanisms and incentives generally regarded as capitalistic. Hungary has been the pioneer of economic reform in Eastern Europe in its search for better economic efficiency and performance than that provided by the traditional Soviet-style centrally planned economy (CPE), of which Stalin was the chief theoretician and champion.

The discussion in contemporary Hungary centers upon how to successfully build a socialist market economy, in which markets would be used as a tool to make socialist planning of the economy more rational and efficient.<sup>1</sup> This puts Hungary at the leading edge of what amounts to

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<sup>1</sup> see: Rezso Nyers, "National Economic Objectives and the Reform Process in the Eighties", in: *Acta*

a radical break from the Stalinist CPE. My particular interest in the recent Hungarian economic reforms is in that area which seems most antithetical to the Stalinist vision--the non-socialist sector of the economy. The focus of my inquiry will not be economic in nature; that is, it is not my goal to answer the question of how this sector works, though I will do that in part. Rather, my interest is political in nature; I wish to answer the question of who benefits. In particular I wish to explore the question of what impact the reforms in this sector of the economy have upon the legitimacy claims made by the ruling elites of the Hungarian Socialist Workers Party (HSWP).

I shall divide my study into five sections. In the first chapter I will put my investigation into perspective, both in terms of theoretical issues and historical background. For the former I will examine some of the recent literature on the nature of the Eastern European states, with a special view towards the nature of the legitimacy claims of these states and the issue of a "crisis of legitimacy". Particular focus will be given to the model of bureaucratic centralism put forward by Andrew Arato. For the latter, drawing upon the theoretical perspectives given by the model of bureaucratic centralism, I will narrow the field of vision to Hungary in particular, and discuss its recent history in terms of the crisis of legitimacy. Special attention will be given to the development of the Hungarian reforms as it relates to this crisis.

The second, third and fourth chapters will concentrate on the various substantive areas of my examination. Chapter two will be devoted to agriculture. I do this because of the proclaimed successes of Hungarian agriculture, and the fact that many of the reforms introduced in the Hungarian economy in the 1980's have their roots in experiments previously tried in the agricultural sector. For example, as Nigel Swain observes, "agriculture acted, not for the first time, as the torch-bearer for more general economic reform."<sup>2</sup>

The third chapter will deal with the industrial and service sectors of the economy. This is a general classification that contains within it a plethora of forms. I will concentrate on the more

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*Oeconomica*, Vol 35 (1-2), 1985, or: Laszlo Antal, Lajos Bokros, Istvan Csillag, Laszlo Lengyel and Gyorgy Matolcsey, "Turning Point and Reform", in: *Eastern European Economics*, Vol XXVI, No 4, Summer 1988, or: Janos Kornai, "The Hungarian Reform Process", in: *Journal of Economic Literature*, Vol VXXIV, December 1986.

<sup>2</sup> Nigel Swain, "Hungarian Agriculture in the Early 1980's: Retrenchment Followed by Reform", in: *Soviet Studies*, Vol XXXIX, No 1, January 1987, p. 25.



important forms of "small enterprise" created in 1982, and the difficulties they have had in fulfilling the expectations of the political elite to promote a new spirit of entrepreneurship in Hungary.

In the fourth chapter I will tackle the most bewildering sector, certainly the most diverse and amorphous one, the "unregistered economy". Of all the CMEA countries, Hungary is reputed to have one of the larger and most influential unregistered economies. The term "second economy" is often used for this sector alone, a mark of its significance.

My concluding chapter will review my arguments concerning the crisis of legitimation in light of the substantive chapters, and then develop this theme further in terms of the concept of "socialist democracy" These themes will finally be reviewed against the background of the surprising turn of events in 1988. Special attention will be given to the removal of Janos Kadar, the grand old man of Hungarian politics, from his position as General Secretary of the HSWP after more than thirty years tenure. The discussion will close on the debate concerning the possible introduction of a multiparty democracy in Hungary, and whether radical reforms hold out the potential of a resolution to the crisis of legitimacy. This discussion will also note the relationship between the ongoing reforms in Hungary to Gorbachev's *perestroika*. In many ways, the ability of the Hungarians to continue pursuing their own path depends still on developments in the Soviet Union, and thus the success or failure of Gorbachev's reforms will influence Hungary's direction as well. How permanent is reform in Hungary, and what does this say about the crisis of legitimation?

## 2.0 Theoretical and Historical Perspectives

### 2.1 *Theoretical Perspectives*

My starting point is a formulation of Max Weber, which holds that "a social order is legitimated if at least one part of the population acknowledges it as exemplary and binding while the other part does not confront the existing social order with the image of an alternative one seen as equally binding."<sup>3</sup> In this formulation mass dissatisfaction in itself does not constitute a loss of legitimation, it must be coupled with an alternative image of a valid form of domination.

The first question that arises, quite logically, is what is the legitimation doctrine and form of domination that the ruling elites of the East European countries hold as valid?

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<sup>3</sup> Max Weber, *Wirtschaft und Gesellschaft*, Tuebingen, 1972, pp. 16-17, authors translation cited from: Agnes Heller, "Phases of Legitimation in Soviet-type Societies", in: *Political Legitimation in Communist States*, eds. T.H. Rigby and Ferenc Feher, New York: St. Martin's Press, 1982, p. 45.

The legitimation doctrine of these states is Marxism-Leninism, which, in the view of David Lane, was

developed in the USSR under Stalin, [and] should not be equated with the writings of Marx and Lenin. It is qualitatively something different. Marxism-Leninism, then, is not merely an ideology which condones the domination of a ruling clique, but a value system which both guides and legitimates the activity of the ruling groups.<sup>4</sup>

Lane would see in Marxism-Leninism not only a value system which legitimates this particular form of domination, but also a doctrine which provides a teleological orientation for the ruling elites and all of society, a doctrine which not only establishes parameters of action and behavioral expectations, but also the ultimate rationale and goal for them. Lane further states that the legitimacy of the system, in the view of the ruling elites, is

based on the theoretical analysis of society carried out by Marx and Lenin as interpreted by the ideological and political elites of a given society. This means that the doctrine of Marxism-Leninism is assumed to be the only true science of society. As the writings of Marx and Lenin are open to more than one interpretation, a second important assumption is that the only true account of their theories can be made by the Communist Party.<sup>5</sup>

The telos of Marxism-Leninism is communist society, which is a classless society. This can only be achieved through the leadership of the Communist Party, because Leninist theory has

no confidence in the spontaneity of the working class to perceive its own class interests, and therefore the Party has to channel the workers' activity into the revolutionary cause. Even with the maturation of socialism, the Party is necessary to articulate and to aggregate the interest of the working class.<sup>6</sup>

As the working class is the most revolutionary class, so the Party contains the vanguard of that class and of the intellectuals that have linked themselves organically to the proletariat. Marxism-Leninism justifies the form of domination it has spawned--Party rule--by a claim to a superior rationality and advanced consciousness.

Lane calls these societies "state socialist", and places his work in the tradition of a "transitional economy of a workers' state" first formulated by Trotsky and further developed by Mandel.<sup>7</sup> While Lane admits that these societies are by no means ideal, he does believe that the "Soviet model is a positive example of planned economic advance to societies which are about to undergo rapid in-

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<sup>4</sup> David Lane, *The Socialist Industrial State*, London: George Allen & Unwin Ltd., 1976, p. 19.

<sup>5</sup> *Ibid.*, p. 20.

<sup>6</sup> *Ibid.*, p. 22.

<sup>7</sup> *Ibid.*, pp. 36-37.

dustrialization.”<sup>8</sup> In his view these societies are only partially socialist, drawing upon Mandel’s distinction between the socialist form of production and the bourgeois form of distribution to point out the contradictions in Soviet society.<sup>9</sup> Though recognizing some of the shortcomings of bureaucratic control, Lane defends the role of the bureaucracy in state socialism as necessary for the process of industrialization and social change, adding that their ideological commitment to developing the necessary conditions for communist society “condition” their activity.<sup>10</sup> He looks toward cultural factors as possible explanations of the underdevelopment of socialism in these societies. In the final analysis, these contradictions are, in his view, hurdles that must be overcome by a workers’ society in transition to socialism.

In his ideological presuppositions, Lane associates himself closely with what could be called orthodox Marxist positions, most notably in his use of a definition of class that is still determined by relations to the means of production. Criticisms of this view and use of class in these societies will be offered by Andrew Arato later, for now it should be noted that he finds the use of class inapplicable to state socialist societies, but rather views a critical stratification theory more useful. Along with his uncritical perception of the motivations underlying Marxist-Leninist ideology and his overestimation of the constraints provided by it and its attendant values, due to what Arato will later criticize as an untenable dichotimization of industrial societies into either capitalist or socialist/communist, as well as his orthodox use of class, Lane ends up with a view that, despite his attempts to the contrary, minimizes conflict in state socialist societies because of the lack of a critical and dynamic stratification and interest conflict theory. Lane thus fails to find a truly antagonistic relationship between the ruling elites and the population, and seemingly finds the ideology of Marxism-Leninism as self-legitimizing. It will later be argued that such an antagonistic relationship does exist and further that there exists a legitimation crisis in these societies.

A less generous view of these societies is presented by Konrad and Szelenyi in their *samizdat* study *The Intellectuals on the Road to Class Power*, in which, as Szelenyi describes it, they “came

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<sup>8</sup> Ibid., p.42.

<sup>9</sup> Ibid., p. 43.

<sup>10</sup> Ibid., p. 42.

to realize that the dictatorship of the proletariat is a myth, an ideology which legitimizes the power of an oppressive new social force."<sup>11</sup> They view their work as a roughly sketched out reinterpretation of the "New Class" theories of such left-wing critics of state socialism as Trotsky and Djilas. Konrad and Szelenyi differ from Lane, who also draws upon the tradition of Trotsky, in that they don't view these societies as transitional workers' states on the way to socialism. Unlike Lane, but similar to Trotsky, they do believe that an oppressive new class form of domination exists in these societies. It is a Marxist critique of Soviet Marxism in that it employs a class analysis approach to the problem of oppression in these states, yet their definition of class employs Weberian elements in order to redress problems caused by what they view as Marx's overly economic definition of class. This redefinition is necessary for the elaboration of their own version of the "New Class" theory.

Their starting point is the ongoing formation of an autonomous intellectual class with immanent interests in Eastern Europe in the context of a rational-redistributive economic system arising out of the Asiatic mode of production. Production in this region has been organized around the telos of catching up to the more advanced West. In the rational-redistributive economy

authority to redistribute the surplus product from a central point is not granted according to inherited status, much less by tradition or charisma, but by a purposive rationality--an ideology which has grown into a common consensus that the organs of central planning and redistribution are capable of redistributing the surplus product in the most rational manner.<sup>12</sup>

Thus disposition over surplus product by the ruling elites is legitimized by their claim to purposive rationality, moreover, with the telos of development, surplus can be extracted by extra-economic, that is, political means. The ideology that justifies this authority over the distribution of surplus product is Bolshevism.

It is Konrad and Szelenyi's contention, however, that Bolshevism served a dual purpose. It also legitimized a new form of class rule, a disguised rule by the ascending intellectual class. They write:

Bolshevism enabled the intellectuals to rid themselves of the ideological ballast which they had been obliged to carry as representatives of the working class. For in treating the proletarian state as the

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<sup>11</sup> George Konrad and Ivan Szelenyi, *The Intellectuals on the Road to Class Power*, translated by Andrew Arato and Richard E. Allen, Brighton, Sussex, England: Harvester Press, 1979, p. xiii.

<sup>12</sup> *Ibid.*, p. 51.

*sine qua non* of socialism the Bolsheviks made an end of socialism as a political, economic, and social problem, simplifying it to a mere matter of organizing state and economy. The Bolshevik intellectuals did not ask in what sort of institutional order the associated producers would find maximum political and economic freedom, but only: How can state and economy be organized so that every decision-making position will be monopolized by the party's trained cadres, and in such a way that those power positions cannot be limited in scope by other kinds of legitimations (be it tradition, capital ownership, or political representation)?<sup>13</sup>

Bolshevism, through Lenin's thesis on the vanguard role of the Party, succeeded in mystifying class relations such that it freed the intellectuals from their dependent position so that Party rule, equated with the dictatorship of the proletariat, in actuality became the class rule of the intellectuals. With the class rule of the intellectuals, the telos of development was substituted for the achievement of socialism. The ideology of scientific socialism became a tool for the protection of the position of the ruling elites, the top strata of the still evolving intellectual class.<sup>14</sup> I would agree with some of the criticisms put forward by Feher, Heller and Markus about conceptual and practical problems with rule by an intellectual class; they characterize this version of "New Class" theory as the "Eastern European variants of that frustrated masochism of radical intellectuals which is certainly not unfamiliar in the West either."<sup>15</sup> The emphasis of their critique lies not with the theoretical difficulties of coming up with a suitable definition of the intellectual class that encompasses the breadth of the ruling elites, but moreover on the practical results of such class theories which seek to use "the explosive critical potential of Marxist theory," in the words of Konrad and Szelenyi, to further the cause of emancipation.<sup>16</sup> It is in the intended emancipatory effect of these class theories that Feher, Heller, and Markus feel they fall short. In their view,

To the apologetic idea of a homogenous society disseminated by the official ideology they counterpose its inverse: the critical idea of a society whose members are homogeneously united (as to their basic interests) against a relatively small ruling class. This view forgets that the unity of all those ruled ... is merely a negative one.<sup>17</sup>

By glossing over the atomization that has occurred in "real" socialism, which divides the subordinated strata of society against each other even as it sets these strata against the ruling elites, class

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<sup>13</sup> Ibid., p. 141.

<sup>14</sup> Ibid., p. 183.

<sup>15</sup> Ferenc Feher, Agnes Heller and Gyorgy Markus, *Dictatorship over Needs*, New York: St. Martin's Press, 1983, p. 121.

<sup>16</sup> Konrad and Szelenyi, op. cit., p. xvi.

<sup>17</sup> Feher, Heller and Markus, op. cit., p. 132.

theories "seem to bring with them the danger of a new substitutionism," that is, exchanging one type of oppression for another. Certainly Konrad and Szelenyi do not argue for an all-decisive clash between two diametrically opposed classes, indeed they do not even predict the demise of the domination of the intellectual class, but only of the hegemony of the ruling elites vis a vis the technocracy. But in arguing for the mediating role of the marginal intellectuals between the the intellectual class, especially the ascendant technocratic strata, on the one hand, and the workers on the other hand, they too open themselves to the charge of substitutionism.

A relatively recent model attempting to understand these states is that of bureaucratic centralism, put forward by Andrew Arato and drawing upon the work of Juergen Habermas. Of course Habermas is concerned with a model of state-organized late capitalism, and does not deal with the state socialist systems. Arato, though his views differ in some important respects from Habermas', finds the Starnberg model of system reproduction (incorporating his own revisions) the most suitable basis in which to undertake a new critique of the actually existing socialist countries. He desires to use this new model as his basis because he believes that classical Marxist theory is entirely incapable of such a task due to serious shortcomings within the tradition. In particular Arato faults its theory of the state, of history, and of class and revolution.

According to Arato, the dichotomization of industrial societies into either capitalist or socialist/communist must be abandoned in favor of restoring Marx's theory of discontinuous social formations to account for bureaucratic centralism. He also views the traditional theory of the state as tragically flawed, hiding the state behind superstructure, when in his estimation the state is "the guiding center and identity of most modern systems," particularly of bureaucratic centralism.<sup>18</sup> Arato also rejects classical and "New Class" theories of class as useful in bureaucratic centralism, because "these theorists do not consistently acknowledge the fusion of superstructure and base, and the primacy of the state, that of the political, over the economy."<sup>19</sup> In his opinion, while "there is no critical sociology without a dynamic theory of stratification and interest conflict, in state-

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<sup>18</sup> Andrew Arato, "Understanding Bureaucratic Centralism", in: *Telos* 35, Spring 1978, p. 74.

<sup>19</sup> *Ibid.*, p. 75.

organized societies this theory cannot be a class theory."<sup>20</sup> It is not Arato's intention to abandon the self-critique of Marxian theory, but to "reconstruct" it, while maintaining certain features of it "regulative" for his project, such as the concept of the critique of ideology, the theory of discontinuous social formations, the necessity of a critical stratification theory and of conceptualizing models of social reproduction for modern industrial societies.<sup>21</sup>

However, Arato does differ from Habermas on several points, which, in addition to the different nature of the systems he wishes to analyze, also accounts for the adjustments he makes to the model. Arato rejects Habermas' *Evolutionstheorie* as he rejected traditional Marxist historical determinism, his imposition of class on all post-primitive societies, and what he views as Habermas' "unjustifiably small number of possible social formations on a single developmental plane."<sup>22</sup> Given Arato's desire to revive Marx's theory of discontinuous social formations, he views such a high level of abstraction as an oversimplification which does not pay due consideration to historical particularities and culture in general (in this regard, he also finds Habermas' ideas on culture problematical), and the role of the state as the primary carrier of historical identity in the modern era in particular.<sup>23</sup> According to Arato,

While systems of reproduction in general have crisis *tendencies* based on immanent contradictions, the objective and subjective emergence of system-transcending ruptures depends on a specific inter-relation of system and history, of the state as agent of reproduction and of culture as a medium of self-expression. National tradition is the terrain of this confrontation of statist pressure and cultural submission or resistance. Since their formation, modern nation-states have been the hidden or open battlegrounds between the desire of administrative centers of power to legitimate their rationalization, control and unification of social-cultural spheres, and the quest of underlying populations, nationalities, cultures, subcultures, strata and religions for autonomy and self-affirmation. The memories, traditions, symbols of these confrontations do not seem to die--though they are often buried.<sup>24</sup>

In this vein he later writes that

Marxist-Leninist statism could not engulf the whole of society except on a specifically Russian basis, utilizing Russian institutions and national ideologies. But in the process, both Marxism-Leninism and Russia were altered almost beyond recognition.<sup>25</sup>

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<sup>20</sup> Ibid.

<sup>21</sup> Ibid., p. 76.

<sup>22</sup> Ibid., p. 78.

<sup>23</sup> Ibid., pp. 77-78.

<sup>24</sup> Ibid.

<sup>25</sup> Ibid., p. 84.



It is Arato's intent to utilize the Starnberg model as his basis, but "to open it up from the inside toward national-cultural histories."<sup>26</sup>

As stated earlier, Arato's model is that of bureaucratic centralism, which he divides into two distinct yet related stages--Stalinism and neo-Stalinism. It is an entirely different solution to the problem of modernization than that of the West, due to historical divergences in the systems of integration developed--for "the principle of integration throughout Russian history ... is the autocratic and bureaucratic state."<sup>27</sup> Bureaucratic centralism as an organizational principle emerged during the 1920s with the monopolization of power (and not capital) by the party-state, in which, in contradistinction to the development of capitalism, "Stalinism is *both* the formative process *and* the first stage of bureaucratic centralism."<sup>28</sup> This organizing principle lies, specifically, in the "antagonistic relationship of the pyramidically organized and unified party-state bureaucracies to the wage laborers and consumers."<sup>29</sup> The process entailed the organization and self-homogenization of the Party into the hierarchically institutionalized bureaucracies while at the same time the population was subjugated to the plan. Moreover, this antagonistic relationship became "socially anonymous" because both the primary mission of the state (the implementation of the central plan), and the monopolization of power by the party are "presented as the representation and fulfillment of collective interests on the basis of scientific knowledge of history in general and economy in particular."<sup>30</sup> The ideology of Marxism-Leninism, developed by Stalin, based its legitimacy claim upon its purported superior rationality. The central plan, administered by the party-state, bound the legitimacy claim of the party-state to the steering function of the system.

This politicization of the steering function of the system and of redistribution brings with it certain problems to the party-state. As Arato notes, "In Habermas' terminology, therefore, we might say that there is a permanent need here to legitimate the political order, which, however, ...

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<sup>26</sup> Ibid., p. 78.

<sup>27</sup> Ibid., p. 79.

<sup>28</sup> Ibid., p. 79.

<sup>29</sup> Ibid., p. 80.

<sup>30</sup> Ibid., p. 81.

combines functions of social integration and system integration."<sup>31</sup> From this Arato raises two questions. First, is the claim to rational knowledge made by the party-state sufficient to legitimate the political order it has established? And secondly, what happens to the claim of rational knowledge in the context of crises of planning rationality?

To the first question, Arato seems to suggest that it was accepted by and large only by those who actively sought to empower this claim, mostly alienated intellectuals and radicalized workers who supplied the leadership and organized cadres of the leftist factions. He notes that the great bulk of the population, the peasantry, has never had cause to view the political order as rational and more than likely has not. Putting the problem in Gramscian terms, he holds that domination replaced hegemony for the bulk of the population. Domination was secured by the terror, which broke all points of resistance and atomized the population. However, brute force can subdue, but it does not motivate. To this end other forms of legitimation were employed which appealed to traditionalistic and nationalistic motifs, the culmination of which was the cult of personality, which provided the "basis of unity for all nationalistic legitimations."<sup>32</sup>

The second question implies a breakdown of the acceptance of the first by those who had helped to construct the political order, that is, a crisis of legitimation among the ruling elites. Referring back to Weber's definition of when a legitimate social order is constituted, we may note that when a legitimation crisis threatens both pillars of the social order, its position becomes untenable.<sup>33</sup> Here again the terror and the cult of personality served to consolidate not only Stalin's position within Lenin's party, but also that of the party-state. Arato states that during the 1930s the terror "had to shift its objectives not only because of the potential formation of new strata but also because the rationality crises were becoming more visible to the upper echelons of party and military leadership."<sup>34</sup> The terror and the cult of personality, the hallmarks of Stalinism, were

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<sup>31</sup> Ibid.

<sup>32</sup> Ibid., p. 82.

<sup>33</sup> see for example: Bill Lomax, "Hungary--The Quest for Legitimacy", in: *Eastern Europe: Political Crisis and Legitimation*, Paul G. Lewis, Ed., London: Croom Helm, 1984, pp. 70-78.

<sup>34</sup> Arato, op. cit.

necessary for the consolidation of bureaucratic centralism, yet taken too far, this formative process would serve not to consolidate the system, but to render it incapable of system steering. There was then, a "clash of two organizational principles, one based upon the party, and the other on the cult of personality--neither one possible without the other."<sup>35</sup> The system, Arato believes, is based upon the consolidation of the organizational principle of the party--it required a Stalin, but it also required that he die, both propitiously and without a like successor.

The consolidation of bureaucratic centralism has resulted in a modestly

self-reproducing model of a system whose key contradiction lies on the level of planning rationality ... The rational claims of the plan are contradicted by the fact that global plans cannot be rational in detail; the political needs of the plan are specifically incompatible with goal-rationality in many instances.<sup>36</sup>

This leads to a legitimation problem, because, as Arato again notes Habermas' contention, a system "in which social and system integration are the tasks of the same institutional order, steering problems are at the same time problems of legitimation."<sup>37</sup> The party-state must respond to this problem, but the question is how?

Habermas provides some answers to the problem he has posed. Drawing upon the work of Offe, he makes the observation that while

the state compensates for the weaknesses of a self-blocking economic system and takes over tasks complementary to the market, it is forced by the logic of its means of control to admit more and more foreign elements into the system.<sup>38</sup>

While this was written with the late capitalist systems in mind, definite parallels can be found in bureaucratic centralism, such as the attempts to simulate the market to increase the rationality of planning and to allow a measure of small- scale private entrepreneurship to fill in the gaps left by the large- scale socialist economy.<sup>39</sup>

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<sup>35</sup> Ibid., pp. 82-83.

<sup>36</sup> Ibid., p. 83.

<sup>37</sup> Ibid., p. 83.

<sup>38</sup> Juergen Habermas, *Legitimation Crisis*, translated by Thomas McCarthy, Boston: Beacon Press, 1975, p. 47, from: Claus Offe, "Tauschverhaeltnis und Politische Steuerung", in: *Strukturprobleme des kapitalistischen Staates*, (Frankfurt, 1972), p. 27ff.

<sup>39</sup> see: Rezso Nyers, "National Economic Objectives and the Reform Process in Hungary in the Eighties", in: *Acta Oeconomica*, Vol 35 (1-2), 1985, or; "Efficiency and Socialist Democracy", in: *Acta Oeconomica*, Vol 37 (1-2), 1986.

Habermas also notes that the pressure placed upon the administrative system can be removed "by transposing the integration of inner nature *in toto* to another mode of socialization, that is, by uncoupling it from norms that need justification."<sup>40</sup> This again raises the issue of appealing to other forms of legitimation to make up for the deficit caused by the inability to meet the expectations set by the supposed superior rationality of the global plan. For as Habermas states, if

governmental crisis management fails, it lags behind programmatic demands *that it has placed upon itself*. The penalty for this failure is withdrawal of legitimation.<sup>41</sup>

This speaks to the need to utilize other forms of legitimation, as Arato already pointed out in his discussion of charismatic legitimation, certainly a form of legitimation divorced from norms that need justification, which he found necessary for the formative stage of bureaucratic centralism.

In a similar vein Agnes Heller identifies two phases of legitimation in the Soviet Union to make up for the deficit caused by what she has called substantive rationality.<sup>42</sup> Substantive rationality, a Weberian type along with goal rationality and instrumental rationality, is the formal legitimation claim of Marxism-Leninism rooted in its purported superior rationality to achieve that which is in the interest of the proletariat, but which Heller believes must eventually either be rooted in formal rationality and pluralism or become ideologized myth supplanted in practice by charismatic or traditional legitimation. Stalin chose charismatic legitimation. This was the first phase, which, upon Stalin's death, because of the concomitant abuses of the terror which accompanied it, was abandoned. After a period of hesitation, in which Khrushchev again experimented with substantive rationality (hence his famous statement to the West, "We will bury you"), the Soviet elites settled into traditional legitimation. This traditional legitimation was rooted in both the Russian national tradition and also the tradition of Soviet rule, lest an overreliance on the former inflame ethnic passions, and also because Soviet rule had seen the most spectacular military triumphs since the invasion of Bonaparte and the emergence of the Soviet Union as a superpower.<sup>43</sup>

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<sup>40</sup> Habermas, *op. cit.*, p. 94.

<sup>41</sup> *Ibid.*, p. 69.

<sup>42</sup> Heller, *op. cit.*, p. 51.

<sup>43</sup> *Ibid.*, p. 58.

Such also implied a return of conservatism, which her colleague Feher has expanded upon in his discussion of paternalism as a mode of legitimation.<sup>44</sup>

These views roughly accord with Arato's own. He writes:

The "planning elite" can ultimately be protected in two directions: by a generalized move toward a pseudo-market that would *seem* to remove a significant portion of economic rewards and punishments from the sphere of responsibility of the plan, or by a drastic shift of the cultural milieu of legitimation from the party-state to the nation-state.<sup>45</sup>

This shift in legitimation corresponds to Heller's notion of traditional legitimation, and also accords with Habermas' idea of a form of legitimation divorced from norms that need justification. The pseudo-market would compare with Nyer's discussion of the reforms that have been occurring in Hungary this decade. In Arato's view, the first direction cannot succeed in solving the underlying contradictions of planning and rationality because a global plan is impossible. This will constrain the Soviet Union more towards the latter course, yet it is not one that most of the states in its orbit can pursue, given Soviet hegemony.

Arato's model is the most satisfactory attempt to explain the nature of these states. For example, his preference for stratification theory over class theory, which allies him with Feher and Heller against Habermas, provides him with a flexible yet insightful critical tool of analysis of the form of domination and the conflicts it generates. In discussing the ruling elites he states that the

technocracy and bureaucracy are neither a single class nor two classes. These institutional structures, forms of hierarchy are basically opposed, yet their relation to all others is one of domination. They are torn by fundamentally different rationalities, but against the population as a whole they represent the legitimating principle of rational knowledge.<sup>46</sup>

In this regard, Konrad and Szelenyi, although they view these two groups as part of an intellectual class, provide an insightful explanation of this conflict. They note that the technocracy cannot by itself "see when efforts to maximize redistributive authority and make it more efficient come into conflict with the ethos of rational redistribution."<sup>47</sup> For this reason the political bureaucracy checks the efforts of the technocracy to the extent that their attempts to increase the rationality of system

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<sup>44</sup> Ferenc Feher, "Paternalism as a Mode of Legitimation", in: *Political Legitimation in Communist States*, Ferenc Feher and T.H. Rigby, Eds., New York: St. Martin's Press, 1982, pp. 64-81.

<sup>45</sup> Arato, op. cit., p. 84.

<sup>46</sup> Ibid., p. 87.

<sup>47</sup> Konrad and Szelenyi, op. cit., p. 161.

steerage conflicts with the ideologically mandated social integration. This model does not demand an economic interpretation, but rather one that realizes the primacy of the political over the economic. In this way it can recognize that "without the constant unifying activity of the Communist Party itself, technocracy and bureaucracy disintegrate into particularistic and competing technocracies and bureaucracies."<sup>48</sup> It may be a contradiction of much of today's social sciences, but the usefulness of this model is that it attempts to be explanatory without trying to be necessarily predictive. By understanding the endemic crises of a system in a systems theoretic way, while at the same time opening itself up to historical-cultural particularities, it provides the flexibility needed to understand the crises in the context in which they occur, as well as the responses, and yet provides a way to relate the particular system under examination to other like systems.

For this project, the idea of an endemic crisis of legitimacy, the introduction of foreign elements into the economic system to attempt to overcome these crises, and the interrelation of system and history along with the idea of the state as a battleground are regulative.

To return to Weber's formulation, the crisis of legitimation persists in Hungary because not only is the introduction of foreign elements into its economic system unable to resolve the underlying contradictions of the global plan, but also because the other option of appealing to a form of legitimation that is divorced from norms that require justification has until the present not been developed in Hungary such that the alienation on the part of the population towards the system has been overcome. There furthermore does exist an equally exemplary and binding conception of a social order in the mind of the population.

Instead, what does exist in Hungary is, in the terms of Feher and Heller, a bribe extended by the ruling elites towards the population.<sup>49</sup> At this point I will deal specifically with the Hungarian system and its historical-cultural peculiarities.

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<sup>48</sup> Arato, *op. cit.*, pp. 86-87. see also: Konrad and Szelenyi, *op. cit.*, p. 162.

<sup>49</sup> Ferenc Feher and Agnes Heller, *Hungary 1956 Revisited*, London: George Allen & Unwin Ltd., 1983, p. 147.

## 2.2 *Historical Perspectives*

In order to understand the assertion of a crisis of legitimacy in Hungary and how the state has sought to overcome it, one must examine the formative experiences of Hungary under the system of bureaucratic centralism. To that end I will briefly describe Hungary during the Rakosi period and the events that led up to the 1956 Revolution, as well as some aspects of the repression of the revolution, before I discuss the Kadarist "compromise" and the program of reform. For if the interrelation of history and system is important, as Arato argues, then certainly in Hungary's case the revolution is the chief juncture of that interrelation.

### 2.2.1 The Rakosi Era: A Stalinist Period of Abnormality

Matyas Rakosi was once described by Beria as the Jewish king of Hungary.<sup>50</sup> A more accurate description, however, would characterize him as one of the mini-Stalins the Father of the Nations installed in the Eastern European nations following the conclusion of the Second World War. It is important to note that under Rakosi, Hungary experienced a similar formative stage of bureaucratic centralism, though under different conditions than those that existed in the Soviet Union. Such was only inevitable, perhaps, because Stalin was convinced it was necessary. Thus, in the estimation of Feher and Heller, the "Rakosi period was totally *outside* Hungarian national development ... it was a period of *direct Russian rule*."<sup>51</sup>

From a contemporary Hungarian point of view, Rezso Nyers, the chief architect of the New Economic Mechanism (NEM) reforms of 1968, provides an interesting periodization of the devel-

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<sup>50</sup> Feher and Heller, *Ibid.*, p. 143.

<sup>51</sup> *Ibid.*, p. 148.

opment of socialist democracy in Hungary. The years between 1945-48 were a brief period of "pristine democracy", characterized by a "search for ways, revolving around the alternative of "bourgeois or people's democracy" and with wide opportunities to have a say in public matters."<sup>52</sup> Initiatives came from both below and above, but it was not known in which way democracy would develop. The period between mid-1948 to mid-1949 brought sudden and somewhat unexpected developments, with the cessation of almost every earlier existing institution and organization and the restructuring of economic and political life. As Nyers describes it,

The main form of asserting democracy was then nationalization, the "conquering" of economic positions by workers. The Hungarian Worker's Party, coming about through the union of the communist and social democratic parties got not only a hegemonious role, but an absolute one.<sup>53</sup>

It was during this period that Rakosi consolidated his position, shocking public opinion, according to Nyers, by declaring that "we are already under the dictatorship of the proletariat."<sup>54</sup> From 1949 to 1956, an "overcentralized" political and economic system modelled on Stalin's was constructed, which Nyers states represented a break with the communist ideology of 1945-47, that of the "people's democratic trend."<sup>55</sup> According to Nyers,

The system institutionalized in this period started as a worker's democracy, in which the peasantry and the intellectuals were formally given the role of allied partners--yet not even the worker's democracy could evolve. The Party leadership wished to represent the worker class alone, and thus it came more and more antagonistic against even the concrete interests of the real working population. Eventually, dictatorial instruments were applied against the peasantry and the intellectuals.<sup>56</sup>

Thus in Nyers' view, a socialist democracy began to develop only from 1957 onwards. Whether one agrees with the details of Nyers' analysis or not, the important point here is that the Rakosi period is seen as an abnormality by most all observers, in which the cult of personality attempted by Rakosi under Stalin's sponsorship (whether admitted or not), and the attendant concentration of power in his hands, is seen as responsible for the numerous misdeeds and grave mistakes made during this period.

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<sup>52</sup> Rezso Nyers, "Efficiency and Socialist Democracy", p. 7.

<sup>53</sup> Ibid.

<sup>54</sup> Ibid.

<sup>55</sup> Ibid.

<sup>56</sup> Ibid.



Another contemporary Hungarian view on the Rakosi period, one that focuses on the economic aspects of his rule, is provided by Ivan Berend and Gyorgy Ranki. As Rakosi consolidated his rule, his mimicry of Stalin went beyond the political, a new economic strategy was implemented as well: "Gradualism was changed in favor of an immediate and complete adoption of a Soviet-type economy."<sup>57</sup> The characteristics of the centrally planned command economy are no doubt familiar: near complete nationalization of all industry, banking and trade; forced collectivization of agriculture with compulsory deliveries; and forced, one-sided industrialization focusing on heavy industry to the neglect of the consumer goods industries. Berend and Ranki summarize:

Soviet industrialization, even if it was formed by the special historical circumstances of an isolated, frightened, backward rural Russia, became an unquestionable general theoretical model of socialism. The often awkward, oversimplified but rather categorical statements of the aging, "infallible" Stalin, whose cult became more and more bizarre, determined the details of economic policy adopted. Rakosi was, nevertheless, not only an obedient follower of Stalin, but was proudly advertised officially and permanently as "his best pupil".<sup>58</sup>

As Berend and Ranki describe it, Rakosi and his clique took their mimicry of Stalin to the point of trying to surpass the Soviets in implementing Stalin's model. Their proud buzzword during those times was "*overfulfillment*"--thus "Rakosi and his closest clique wanted to "overfulfill" not only their ambitious plan directives but also the orthodoxy and extremism of Stalin's course in general."<sup>59</sup> Rakosi's emulation of Stalin went even beyond religiously applying his theory of socialist industrialization, though certainly it was accepted presuppositionally as valid; Rakosi pursued a policy of forced industrialization and striving for economic autarky because he further internalized Stalin's paranoia and motivations--at Stalin's urging, planning revolved around the "belief in an unavoidable third world war."<sup>60</sup> Berend and Ranki state that

The system of central planning, worked out in the late 1940's and early 1950's, was adequate for a maximal rate of development, one strongly concentrated on primary production, because it was from the very beginning essentially a strategy of war economy.<sup>61</sup>

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<sup>57</sup> Ivan Berend and Gyorgy Ranki, *The Hungarian Economy in the Twentieth Century*, New York: St. Martin's Press, 1985, p. 199.

<sup>58</sup> *Ibid.*, p. 204.

<sup>59</sup> *Ibid.*

<sup>60</sup> *Ibid.*, p. 205.

<sup>61</sup> *Ibid.*, p. 214.

With such motivations, the process of industrialization became not only frantic, but also increasingly chaotic and irrational. In an interview Berend had with Erno Gero, the chief economic architect of the Rakosi period, in 1960, Gero admitted that "We had the information, that we had to count on a forthcoming war in three to four years."<sup>62</sup> Certainly Berend and Ranki would agree that this period was an abnormal one in the course of Hungarian development, that the policies followed were not rooted even primarily on the basis of any calculable economic rationality.

Naturally, such policies created major contradictions in economic development, which led to severe economic and social strains in Hungarian society. Berend and Ranki give us a veritable catalogue of problems and the effect they had upon the society:

The decline in the standard of living, the intolerable tension in the countryside, the decay of agriculture, the overall shortages and the increasing impossibility of fulfilling the overambitious industrialization targets (not to mention the political disaster), and the atmosphere of terror, generated a crisis situation even before the end of the first 5 year plan period.<sup>63</sup>

As an example of the irrationality of the situation, especially of the economic program, they estimate that between 1949 and 1953 that "uncompleted investments and accumulating stocks absorbed about one-fifth of the growth of national income."<sup>64</sup> It cannot be denied that development did occur, but the program of development pursued was not an economically viable one in the long-term, and even before then generated such contradictions that the cost of development was becoming too high, in all aspects.

The death of Stalin in the spring of 1953 unleashed the suppressed desires for reform in many quarters of Eastern Europe, and in Hungary this desire was given added impetus by the intervention of the leading political figures in the Soviet Union, who viewed with alarm Hungary's disintegrating crisis situation. In June of 1953, the Central Committee of the Hungarian Workers Party, in a closed session, strongly criticized previous economic policy and decided to change course. Rakosi was constrained to exercise what amounted to vastly inadequate self-criticism and, while maintaining his position as the powerful Party Secretary, was forced to give up his role as Prime Minister

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<sup>62</sup> Ibid., p. 205.

<sup>63</sup> Ibid., p. 220.

<sup>64</sup> Ibid.

to the popular champion of agricultural reform (in this respect it is of interest to note that he had once shared a close working relation with Bukharin), Imre Nagy. Nagy announced the programme of the "New Course" on July 4, 1953, which criticized the errors of the old economic policy, blaming the program of forced, one-sided industrialization. Policy and structural changes were announced which featured more moderate growth, greater emphasis on consumer goods, and agricultural reforms which even allowed a process of decollectivization, such that the number of members and the area of collective farms dropped by forty percent.<sup>65</sup> Berend and Ranki make the interesting observation, however, that radical change was not possible because the leading figures of the Party did not understand the fundamental causes of the economic difficulties. They state:

Even the government programme of I. Nagy in July 1953 revealed this. While it was very critical of former economic policy, it had nothing to say about the system of planning. The latter was still identified with socialism itself. All that they thought could be done was to use the given planning system more rationally.<sup>66</sup>

This is no doubt an accurate criticism, but the unfortunate Nagy programme was never given the chance to find this out. It is a statement on how dependent Hungarian politics were on the volatile situation in the Soviet Union at that time that when Malenkov, Nagy's protector, was ousted in early 1955 from the premiership, Rakosi, who had been obstructing the New Course all along, was able to remove the isolated Nagy from his position for being a revisionist.<sup>67</sup> The old course was once again resumed, though not with increasing opposition and discontent from below. Imre Nagy prophetically warned "that the masses, having lost their faith, will reject both the June way and the Communist Party."<sup>68</sup> The Soviets, once again alarmed by the deteriorating situation in Hungary, intervened yet again, but this time, perhaps indicative of their own troubles, they acted cautiously and with some indecision "as to just whom they would like to see replace Rakosi."<sup>69</sup> In mid-1956, after entertaining several possibilities, they finally did replace Rakosi, but with Erno Gero, who, while acceptable to the Party elites, turned out to be a less than felicitous choice with the masses.

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<sup>65</sup> Ibid., p. 221.

<sup>66</sup> Ibid., p. 222.

<sup>67</sup> Lomax, op. cit., p. 73.

<sup>68</sup> Ibid., p. 74.

<sup>69</sup> Ibid.

Whether or not another choice could have prevented or ameliorated the subsequent events is a matter of speculation that cannot be definitively resolved one way or the other, certainly arguments exist for both positions. What is important is that on October 23, when members of the hated Hungarian secret police fired on a large unarmed crowd assembled outside the State Radio Building, the revolution had begun.

### 2.2.2 The Suppression of the Revolution: Kadar's Forgotten Legacy?

A description of the events of October 23 to November 4, 1956, is beyond the scope of this study. In broad terms, an accurate description of the revolution would portray it as popular and national in character, meaning that it had great support from many segments of Hungarian society and was directed against a system perceived as an oppressive form of foreign domination. One can to this day walk past the City Park close to the Heroes' Square and see the large empty platform from which the bronze statue of Stalin was pulled down and beheaded.

Bill Lomax has argued that Kadar at first wished to create a compromise in which as many of the goals of the revolution as possible could be incorporated into his government, and in an effort to win the support or acquiescence of the populace he appealed

to the legitimacy of the revolution itself, and by aligning himself both with the original demands of 23 October and with the programme of the Government of Imre Nagy established on 28 October 1956.<sup>70</sup>

Kadar was subsequently at pains to differentiate between the true popular revolution of October 23-28 and the counter-revolution to which the Nagy government was too weak to resist from October 29 to its suppression by Soviet troops on November 4, claiming that he in essence was the one to remain true to the former's principles.<sup>71</sup> In the immediate aftermath of November 4, Kadar

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<sup>70</sup> Ibid., p. 78.

<sup>71</sup> Ibid.

sought desperately to reach a compromise with Imre Nagy and his supporters who had taken refuge in the Yugoslav Embassy, as well as to win the cooperation of leading figures from the non-Communist political parties, and to gain the confidence and support of the workers' representatives in the workers' councils.<sup>72</sup>

Kadar's attempt to effect a reconciliation with the people such that his government could consolidate its position through persuasion rather than repression failed, not for lack of effort, but because Kadar's own position was tenuous, and he was accordingly powerless to force two sides to come together who did not want to do so. Lomax writes that Kadar failed because

he had met not only with the resistance of the Soviet leaders and of the Stalinists within his own entourage, but also with the unwillingness of the Hungarian workers, writers and non-Communist politicians to cooperate with him. Their minimum demands, for a withdrawal of Soviet forces and for the return of Imre Nagy [who, having Kadar's promise that he and his entourage could safely return to their homes, was nevertheless abducted by Soviet troops upon leaving the Yugoslav embassy and taken to Romania with the others], were ones which it did not lie within his power to meet.<sup>73</sup>

In order to retain the confidence of the Soviets and thus his position, Kadar was constrained to follow a line of severe repression of the workers, peasants, and dissident intellectuals (and at that time any well-known intellectual worthy of the appellation was a dissident one). Government propaganda became more violent and announced that its task was to defeat the counter-revolution, all autonomous or insubordinate organizations were broken up, and mass arrests and numerous executions followed. The process of repression and consolidation lasted until 1961, when the last of three collectivization drives (in which it is reported that the first and third used the carrot, while the second relied more on the stick), brought 90% of the arable land into the socialist sector.<sup>74</sup> Once the consolidation of his regime was secured, Kadar then began to work out his "compromise" with Hungarian society.

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<sup>72</sup> Ibid.

<sup>73</sup> Ibid., pp. 80-81.

<sup>74</sup> Ibid., p. 84.

### 2.2.3 Kadarism and the Program of Reform

In his pioneering study on the early Hungarian reforms, William F. Robinson begins with the contention that

In a sense the Kadar era in Hungary began not with the suppression of the revolution of 1956 but with the Soviet installation of Imre Nagy as Hungarian premier in June 1953 and the subsequent beginning of the New Course.<sup>75</sup>

Certainly it cannot be denied that Kadar's reforms lie within the tradition of the New Course and that he has looked towards it for some inspiration, precedence, and justification of his own program. However, the acceptability of reform, and hence a truer point of origin, stems from the shock of the revolution. Comisso and Marer state that

Politically, the acceptability of reform in Hungary is a result of its unique national trauma, the 1956 revolt, combined with the general changes in economic priorities and party-state relations that hit all CMEA states in the mid-1950's.<sup>76</sup>

While situational and economic causes have influenced the reform imperative, such as Hungary's position as a small resource-poor country dependent upon trade and the need to switch from extensive to intensive development, the early and relatively progressive will for reform stems from the trauma of 1956 and the legitimation crisis it so starkly revealed. The Kadar regime was one always trying to overcome its early legacy, searching to extract from the populace a measure of legitimacy or at least support.

Of course the economic expression of these reforms is the famous New Economic Mechanism (NEM) introduced in 1968. The NEM did not abandon the CPE, but reduced it in scope. This was accomplished by abandoning the compulsory character of the CPE in favor of indirect controls. By focusing on macro-economic issues and utilizing indirect mechanisms like the rate of investment, price reforms, and shifting priorities concerning allocation, it was the intent of the reformers to generate profit-oriented enterprise self-interest to enhance productivity and economic rationality. Referring back to the model of bureaucratic centralism, it is clear that these reforms fall within the

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<sup>75</sup> William F. Robinson, *The Pattern of Reform in Hungary: A Political, Economic and Cultural Analysis*, New York: Praeger Publishers, 1973, p. 3.

<sup>76</sup> Ellen Comisso and Paul Marer, "The Economics and Politics of Reform in Hungary", in: *International Organization* 40.2, Spring 1986, p. 422.

concept of introducing foreign elements into the economic system to increase its rationality. However, these reforms operate within the basic integrating principle of the planned economy. As Comisso and Marer note, the "Hungarian advocates of reform sought not to weaken the Party but to use it to pursue their particular economic goals."<sup>77</sup> The principles of Party hegemony and the global plan were never at stake, the only issue was one of increased economic rationality.

What is less well known is the previous beginnings of political liberalization once Kadar had consolidated his regime's position. This liberalization is embodied in his "Alliance Policy", which he forcefully declared in his speech to the National Council of the Patriotic Peoples' Front (PPF) in 1961:

Western political commentators say ... [that] this Kadar group is very cunning: they want to fool everybody. [Why?] Because Rakosi used to say, a long time ago, "Whoever is not with us is against us." Kadar now says, "Whoever is not against us is with us." ... We can safely acknowledge this. Indeed, we do believe that whoever is not against the Hungarian people is with them ... whoever is not against the Hungarian Communist Party is with it. Of course, some of those who share our opinions are more conscientious, and also share our long-range aims; another group is with us in the simple everyday things. For example, there are many hundreds of thousands who are not Marxists but who respect our Party and our government for having created a legal order and normal atmosphere in the country. They are with us, and we must further develop our policy in this spirit.<sup>78</sup>

Certainly Kadar's claim that the Party and government had earned the respect of much of the population at that early time represents an unrealized desire rather than a statement of fact. It was a bold proclamation of a change in course and an attempt to reduce the alienation between the people and the Party. Up to then, the policy of "socialist legality" had by and large consisted of the systematic repression and punishment of "counter-revolutionary" elements, culminating in the internationally well-publicized trial and execution of Imre Nagy.<sup>79</sup> Yet despite the obvious unpopularity of such repression, its systematic nature was a stark contrast to the random violence and senseless show-trials of the Rakosi period (such as the Laszlo Rajk show-trial and execution), and the lesson was clear: those who do not disobey or take stands against the system will not be both-

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<sup>77</sup> Ibid.

<sup>78</sup> Robinson, op. cit., p. 70; as quoted in: *Magyar Nemzet*, December 10, 1961; translation taken from: Dr. William Juhasz, ed., *Hungarian Social Science Reader 1945-1963*, New York-Munich: Aurora Editions, 1965, p. 278.

<sup>79</sup> Lomax argues that the international attention given to the trial indicates that it was one desired more by the Soviets, not to intimidate an already beleaguered Hungarian population, but to serve notice to all potential rebels in the Communist world that they would not tolerate any questioning of their hegemony over Eastern Europe. see: Lomax, op. cit., p. 83.

ered, but those who do will be punished. By openly announcing this change in policy, Kadar served notice to the population that the period of repression was over and that there did exist an incentive for obedience. Kadar also served notice to those of Stalinist bent in the governmental apparatus that the random abuse and brutality of the Rakosi period would not be tolerated, and this was perhaps more important in his attempt to reduce the alienation between the people and the state. During the period of consolidation, Kadar had had to rely on the Stalinists in the Party to carry out the program of repression and consolidation, but now that this had been accomplished, he could purge the most compromised of the Stalinists and warn the others against a return to the old ways, as a guarantee *to the people* that an incentive for acquiescence did in fact exist.<sup>80</sup> Thus, as Feher and Heller note, the emphasis on socialist legality cannot be equated with legitimacy, but rather it is "the best organized, least irrational--moreover, instrumentally rational--and therefore *to some extent* tolerable system of oppression."<sup>81</sup> It is, in short, a relative good, relative to the excesses and irrationalities under Rakosi.

I have previously mentioned Feher and Heller's idea of a bribe extended to the population, which, in their view, seems to refer to the phenomenon of "consumer socialism".<sup>82</sup> They hold, however, that Kadarism has gone beyond the bribe offered; it has further "*redirected Hungary back to the traditional national course of her distorted development.*"<sup>83</sup> This view has also been endorsed by George Schoepflin in his examination of contemporary Hungarian political culture. He writes:

On the one hand, the official Marxist-Leninist set of values is overtly--or at least ostensibly--committed to producing a revolutionary transformation of society along highly egalitarian lines, whilst on the other the existing government has succeeded in creating a relatively stable, rather cautious system that bears an uncanny resemblance to the pre-war, neo-k.u.k. order. The paradox may be explained by the failure of the Communists to effect fundamental changes in the dominant political culture of Hungary...<sup>84</sup>

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<sup>80</sup> see: Lomax, *Ibid.*, pp. 85-87; Robinson, *op. cit.*, pp. 72-73.

<sup>81</sup> Feher and Heller, *op. cit.*, p. 151.

<sup>82</sup> Lomax, *op. cit.*, p. 89.

<sup>83</sup> Feher and Heller, *op. cit.*, p. 148.

<sup>84</sup> George Schoepflin, "Hungary: An Uneasy Stability", in: eds., *Political Culture and Political Change in Communist States*, Archie Brown and Jack Gray, Eds., London: The Macmillan Press Ltd., 1977, p. 153.



Such a failure to transform the political culture cuts right to the core of the legitimation crisis, and the failure of what Schoepflin called the overt values of the legitimating doctrine of Marxism-Leninism. In order to understand more fully the concept of a legitimation crisis in Hungary it is necessary to differentiate between hegemony, legitimacy, and support.

The concept of hegemony has come into prominence through the work of Antonio Gramsci.

He writes:

What we can do, for the moment, is to fix two major superstructural "levels": the one that can be called "civil society", that is the ensemble of organisms commonly called "private", and that of "political society" or "the State". These two levels correspond on the one hand to the function of "hegemony" which the dominant group exercises throughout society and on the other hand to that of "direct domination" or command exercised through the State and "juridical government."<sup>85</sup>

According to Carnoy, Gramsci's innovation is to place civil society in the superstructure rather than the base, as was the case with Marx through Trotsky, with the result that

it was the *State itself* that was involved in reproducing the relations of production. In other words, the State was much more than the coercive apparatus of the bourgeoisie; the State included the hegemony of the bourgeoisie in the superstructure.<sup>86</sup>

State was no longer hidden in the superstructure, it rather came to the fore of Gramsci's thought. It is, in his view, "the entire complex of practical and theoretical activities with which the ruling class not only justifies and maintains its dominance, but manages to win the active consent of those over whom it rules..."<sup>87</sup> Gramsci called Marxism the "Philosophy of Praxis", and it is clear that his writings were written very much in the context of the political struggles in which he took part; that is, much of what Gramsci wrote was an attempt to explain the failure of the workers to not only effect a socialist revolution in Italy of the post-World War One period, but also why so many of them allied themselves with the Fascists. In order to explain the failure of the Communists to transform political culture, that is, to establish hegemony in the Gramscian sense, we must note the differences between Gramsci's Italy and these states.

In her discussion of overt and covert modes of legitimation in the Eastern European states, Maria Markus speaks to the issue of this failure. She begins with the idea of a breakdown in the

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<sup>85</sup> Antonio Gramsci, *Selections from the Prison Notebooks of Antonio Gramsci*, edited and translated by Quinton Hoare and Geoffrey Nowell Smith, London: Lawrence and Wishart, 1971, p. 12.

<sup>86</sup> Martin Carnoy, *The State and Political Theory*, Princeton: Princeton University Press, 1984, p. 66.

<sup>87</sup> Gramsci, *op. cit.*, p. 244.

process of verification of political institutions and their consistency with socially constitutive values that is supposed to legitimate the political order:

In cases where there exists a more or less autonomous civil society, the latter's institutions provide the forums for both the elaboration of values and for their confrontation with the functioning of the political institutions. In Eastern Europe both these processes are placed under the direct control of the state and therefore, in this respect, there is an identification of the *subject* and *object* of legitimation--a situation rather paradoxical from the point of view of modern legitimation. But, at the same time, as it is well known virtually to everyone and even admitted in official documents, sociological surveys etc., despite the monopolization of the means of socialization and public communication, the regimes of these countries have succeeded neither in their attempts to transform "popular mentality" (Gramsci's "commonsense" understood as a "historically produced conception of the world of the masses") in the desired direction, nor in the unambiguous assimilation of the "high culture".<sup>88</sup>

Leaving aside the issue of high culture as not pertinent to the immediate topic, Markus gives two reasons for the failure to transform the popular mentality of the masses.

To begin with, Markus notes the inability of the official ideology to "deal in an open and non-contradictory way with the traditional cultural and value patterns of the societies in question."<sup>89</sup> Civil society is politicized by the doctrine of Marxism-Leninism, yet it is not able to deal with the contradictions created by this politicization and the traditional cultural and value patterns of the societies they claim to be transforming. In this regard it is instructive to refer back to Arato's remarks concerning national tradition as the terrain of confrontation between statist pressure and cultural submission or resistance. The state, as we remember, becomes a battlefield in this confrontation between rationalization and control and socio-cultural autonomy.

The second reason the ideology has failed in this program of transformation, according to Markus, is

the fact that this ideology is both incapable of withstanding the test of verification with social reality (while proclaiming its testability), and devoid now of any real pragmatic orientative value within this reality as well.<sup>90</sup>

In a Habermasian sense, the ideology has failed to implement programmatic demands that it has placed upon itself, because of its inability to deal successfully with national tradition and culture, and has thus lost any orientative value and subsequently its ability to legitimate the political order.

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<sup>88</sup> Maria Markus, "Overt and Covert Modes of Legitimation", in: *Political Legitimation in Communist States*, Ferenc Feher and T.H. Rigby, Eds., New York: St. Martin's Press, 1982, p. 87.

<sup>89</sup> Ibid.

<sup>90</sup> Ibid.

We might also note the connection between the politicization of civil society, the contradictions of this politicization with national tradition and culture, and also the crisis of planning rationality in this legitimation crisis.

In the Soviet Union this crisis is overcome by forms of legitimation divorced from norms that require justification--that is, tradition. Thus the Soviet Union has in place at least a partial hegemony, given that hegemony for Gramsci is tied up in notions of class domination, something that is not applicable in bureaucratic centralist societies; we might argue, according to the model of bureaucratic centralism, that Soviet hegemony has legitimated a form of domination that is not in fact class domination. But if hegemony requires the active consent of those dominated, it is surely only partial in the Soviet Union and non-existent in Hungary. Hungary has no recourse to traditional legitimation as does the Soviet Union. Bill Lomax has described the traditional order in Hungary as one "combining the paternalism of an authoritarian regime with the cynical compliance of a demoralized people."<sup>91</sup> Cynical compliance is by no means active consent, the standard for hegemony. In this respect, as Lomax further notes,

The Kadar regime's dependency on Moscow is, and always has been, its weakest point, its Achilles' heel, for having been installed in 1956 by Soviet force, it has remained in power ever since only because Hungary has remained under Soviet control.<sup>92</sup>

As for charismatic legitimation, the disastrous experience under Rakosi, that pale emanation of Stalin, has precluded another such experiment. Only Romania suffers currently from such an attempt. If cynical compliance is not hegemony, neither is it legitimacy--traditional or otherwise. Rather, as Feher and Heller conclude, the fact that

they have reverted to a *national pattern of oppression*, has helped them to find, even though remaining in the position of masters, a language that is to extent in common with their people. All this adds up to the consolidation of *government*, not the legitimation of a *system*; and the latter, *as it stands*, having never been accepted by this nation, is illegitimate precisely in this sense.<sup>93</sup>

This should certainly demonstrate that hegemony is non-existent in Hungary, however, it does not conclude our discussion of legitimacy.

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<sup>91</sup> Lomax, *op. cit.*, p. 96.

<sup>92</sup> *Ibid.*, p. 101.

<sup>93</sup> Feher and Heller, *op. cit.*, p. 153.

It is because of the failure of these alternative forms of legitimation that Feher, Heller and Markus argue that the "gap could be bridged only by extensive pure pragmatism."<sup>94</sup> Of the "in-sincere" justifications given, they mention the division of the world as a fact, the necessity of the Soviet presence, and the need for order (identified with their own), such that "rationalization through interests ... are part and parcel of increased pragmatism."<sup>95</sup> This pragmatism is supplemented by a return to substantive rationality, which, as earlier noted, in Hungary has taken the form of economic reforms that have introduced foreign elements into the economic system. But from the viewpoint of Feher, Heller and Markus, as well as Arato (though for different reasons), such efforts cannot succeed. The former would point out the insufficiency of substantive rationality for self-legitimation, while Arato would point out that such efforts do not solve the crisis of planning rationality.

Add to this, returning to the second pillar of Weber's dictum, Feher, Heller and Markus' assertion that in Hungary "the overwhelming majority of the population does have an image of an alternative political order--that of the Western European or North American liberal-legal state--which is acknowledged by them as exemplary," and we have come the full circle of the legitimation crisis.<sup>96</sup> They summarize the failure of substantive rationality to alter the crisis as follows:

It eventually rationalizes the pragmatism of the government, a rationalization which occasionally has to be combined with the bare and brutal display of non-legitimate power, once again in a pragmatic way.<sup>97</sup>

In terms of the model of bureaucratic centralism, the legitimation crisis persists in Hungary because the crisis of planning rationality cannot be overcome by the introduction of foreign elements into the economic system, which seeks to increase economic rationality, nor can alternative forms of legitimation divorced from norms that require justification (charismatic or traditional legitimation) be used. Feher and Heller have characterized the former as substantive rationality, which if it is not to become myth, must transcend its inability to legitimate itself by allowing a measure of formal

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<sup>94</sup> Feher, Heller and Markus, *op. cit.*, p. 155.

<sup>95</sup> *Ibid.*

<sup>96</sup> *Ibid.*, p. 138.

<sup>97</sup> *Ibid.*, p. 155.

rationality and pluralism. In this regard we might note the similarities between their concept of myth and the concept of steering problems becoming a problem of legitimation in bureaucratic centralism, and in this sense, the introduction of formal rationality would conceivably transform the form of domination into one that, in Habermasian terms, would separate system integration and social integration, in which case steering problems would no longer be a problem of legitimation. An important factor would be whether or not such a disjunction would, if possible, still organize the economic system around the principle of the plan, though without the principle of the guiding role of the party.

As for the ability of the ruling elites to appeal to forms of legitimation divorced from norms that require justification, Feher and Heller, Lomax, and Arato all note that appealing to traditional legitimation in a country that is subordinated to a foreign power is ineffectual, and that charismatic legitimation ultimately endangers the whole system.

Thus alternative forms of legitimation cannot resolve the legitimation crisis in Hungary. Moreover, the fact that much of Hungarian society does have an image of an equally binding and exemplary social order, completes the argument for an ongoing legitimation crisis. Thus, the introduction of foreign elements into the economic system, which in Hungary has taken the form of the development of consumer socialism and the ongoing program of reform, coupled with the return to the traditional national form of oppression, which provides a common language between the Party and the population and has spurred the development of consumer socialism and the re-emergence of a social order that is reminiscent of the neo-k.u.k. pre-war one, all serve to bribe the population into supporting the regime, not legitimating it or its system.

The concept of support also warrants some discussion, because often observers of contemporary Hungary have viewed support as a compromise between the Party and the population, or a legitimation of the regime, though not the system. In the latter sense Schoepflin speaks of the achievement of a "partial legitimacy" by the Kadar leadership, which is certainly an ambiguous term.<sup>98</sup> Support is, however, neither partial legitimation nor regime legitimation. An unpopular

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<sup>98</sup> Schoepflin, *op. cit.*, p. 154.

regime may be considered legitimate, either because it attained power in a legally prescribed manner, or because of tradition, and conceivably even through the power of charisma. However, in the case of Hungary, support is entirely performance-related, it is dependent upon the regime reproducing an acceptable level, and even steady increment, in the quality of life--primarily measured in economic terms. To equate support with regime legitimation would therefore turn legitimacy into a mere popularity contest, robbing the term of any content. Turning to the idea of a compromise, a cursory examination of the current situation in Hungary would indeed suggest a compromise between the government and the population. Maria Markus, for example, takes such a position.<sup>99</sup> However, strong arguments against this view can be made. Feher and Heller take the position that indeed no compromise is possible in Hungary because the two necessary preconditions are missing. First, there are no autonomous social forces with some measure of social power. Moreover, and somewhat paradoxically, there are none because one of the two sides is not ready to come to terms within the limits of mutually acceptable prescribed rules--namely, the government.<sup>100</sup> In short, a compromise from above is not a compromise. As such, those policies which elicit support from the population remain bribes, not compromises extracted.

Lomax provides some useful insights into the success of the Alliance Policy and the social and economic programs pursued under it. He writes:

"The secret of Kadarism", the dissident writer Miklos Haraszti has observed, "was that it really did believe in the integrating capabilities of the state-run system." Its leaders felt sufficient confidence that by granting measured degrees of independence and autonomy to society they could actually win not just the passivity, but the complicity if not quite the loyalty of major sections of the population.<sup>101</sup>

It should be noted that concessions granted are not compromises agreed upon. Through this process the regime "sought to incorporate into the system the different social interests and pressures of civil society in a way which turns the pursuit of self-interest from potential opposition into tacit

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<sup>99</sup> Markus, *op. cit.*, p. 91.

<sup>100</sup> Feher and Heller, *op. cit.*, p. 151.

<sup>101</sup> Lomax, *op. cit.*, p. 96.

collaboration."<sup>102</sup> Feher and Heller are naturally quite critical of this process: "The leaders persist in the policy of group and individual corruption."<sup>103</sup>

Returning to the idea of the traditional national course of distorted Hungarian development, Lomax observes that these policies have recreated a dependent middle class similar to that of the pre-war Horthy period.<sup>104</sup> He further states that the working class has been "bought off", because

the means by which its members have attained improved well-being and higher living standards--the uninhibited pursuit of private interest and self-achievement--have sapped the very collective spirit through which social solidarity might emerge and take on an organized form.<sup>105</sup>

The net result of the Alliance Policy and many of the NEM reforms has been to perpetuate through a system of incentives the stratification and atomization of society into a series of often mutually contradictory dependent relationships upon the state. In this regard socialist pluralism does not breed autonomy but dependence. Such points out the need, as Arato argued, for a critical stratification theory.

The Alliance Policy, as it has developed in relation to economic reform, is an attempt to integrate group and individual interests into economic decision-making. The HSWP claims it strengthens democracy and pluralism in the economic arena. In relation to the previous command economy, this is undoubtedly true. However, such claims must be critically examined, because the competition and incorporation of interests in the economic arena is still institutionally set in a highly inegalitarian way, as the discussion of industry in chapter three will demonstrate. Suffice it to say that the private forms of small enterprise have no institutionalized voice in economic decision-making at the national level. A representative summation of the interplay between political and economic reform from the viewpoint of the HSWP comes from Rezso Nyers:

No political reform will take place in Hungary which would basically change the political objectives, or the conceptual set-up of the political system, nor is such a change a condition of the consistent and successful implementation of the economic reform process. But the development of the system of political institutions, in order to conform to practical needs, is and remains on the agenda. Similarly,

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<sup>102</sup> Ibid.

<sup>103</sup> Feher and Heller, *op. cit.*, p. 154.

<sup>104</sup> Lomax, *op. cit.*, p. 98.

<sup>105</sup> Ibid., p. 98.

changes in the style of policy-making are on the agenda and will continue. The general trend is to work out a national consensus under the aegis of a strengthening and growing democracy. This demands that particular social interests be integrated from time to time, and in this integration process the main role will continue to be played by the Hungarian Socialist Workers' Party; but an important role will be given to the Patriotic People's Front, the Trade Unions, the Cooperative Movement and the representative local bodies.<sup>106</sup>

As can be gleaned from this declaration, the integrating principles of the leading role of the party and the global plan remain valid. As economic reform has left intact the global plan, so political reform will leave intact the leading role of the HSWP. Rather, Nyers anticipates a need for the rationalization of political institutions to parallel the rationalization of the economic system--those interests which have been integrated into the economic arena must eventually be integrated into the political arena. Indeed, to this end there has been a trend towards the "debureaucratization" of the state to allow for a greater interplay of interests; this process is certainly one of rationalizing political institutions. But as Comisso and Marer note, "Debureaucratizing the state is a far cry from diminishing Party hegemony. It merely allows a measure of simulated pluralism to accompany the simulated market."<sup>107</sup> The paradox of the situation is that as the HSWP grants more autonomy to various interest groups, and integrates them into this system of competing dependent interests, it is in fact attempting to have far greater control over society than was previously possible.

The facade of this seeming-compromise should by now be penetrated. To summarize the arguments against the idea of a compromise, I quote from Lomax:

The fraudulent nature of the Kadarist "social compromise" arises from the fact that its terms were never freely agreed to but dictated in advance, that the rules of the game were laid down from above, and the referee was from the start in the pay of the authorities. The master strategy of Kadarism has been to provide inducements to all sectors of the population, not only the middle and professional classes, but skilled and unskilled workers too, to collaborate in maintaining this myth of social compromise. But the attainments, whether cultural, social or economic, of this collaboration have never been more than concessions granted by the regime that could be withdrawn at any moment, at the stroke of a pen.<sup>108</sup>

What we have then is a more elaborate charade. Many participate for a variety of reasons, though self-interest predominates. But if it is more elaborate, it is also more fragile. Liberalization and reform can be viewed as a compromise, as building socialist democracy, or as a necessary raising of the stakes to buttress a fragile myth. Given the monopoly of power by the HSWP, and its basis

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<sup>106</sup> Nyers, "National Economic Objectives and the Reform Process in Hungary in the Eighties", p. 14.

<sup>107</sup> Comisso and Marer, *op. cit.*, p. 453.

<sup>108</sup> Lomax, *op. cit.*, p. 99.



in Soviet hegemony, it appears most likely to be the latter. If the myth is effective, the Party has more efficacious control over the people and more room to maneuver, because it need not rely primarily on coercion to govern.

However, the danger lies in Habermas' observation that the freedom of action in such societies contracts in crisis situations when it is needed most. If the myth should falter or fail, the concessions granted would be withdrawn and coercion would be stepped up. It is a seeming compromise in that the system could be more intolerable, but it is in the interest of the regime to make it tolerable. As for the people, they get the regime and the Soviets off their backs in return for good behavior. It is a series of concessions for support. Support is performance-related, should the government not come through those goods upon which support is contingent, or if these goods generate socially undesirable phenomena, resulting in unrest, measures towards recentralization and a consolidation of the Party's position will occur. Too much unrest, and repression will be stepped up, reform may be discredited, and support forsaken for maintaining power without it.

If pluralism can be said to exist in Hungary, it is within the HSWP itself. A closer examination of the HSWP is in order, because it is the primary actor in political and economic life. In the view of Comisso and Marer, the HSWP has put an emphasis on three areas to avoid the excesses of the Rakosi era: on socialist legality to subordinate the state apparatus, especially the security apparatus, to Party control; on strengthening the mass organizations in order to do the same with the populace; and on collective leadership within the HSWP so that the Party would not come under any one person's absolute control.<sup>109</sup> We shall examine the latter idea.

Comisso and Marer list three principles of collective leadership: the "socialization" of political power, tolerance of diversity, and restrictions on political resources.

The "socialization" of power refers to the diffusion of power within the HSWP. All decisions are made in collective bodies, hierarchically arranged according to geographical boundaries or along functional lines, with power flowing from top to bottom. An individual's power rests upon that of the collective body, and lower ranking members are dependent upon the center for power. An

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<sup>109</sup> Comisso and Marer, *op. cit.*, pp. 433-34.

individual is not admitted to a decision-making body unless he or she is committed to abide by the decisions of the collective body. Political resources (such as responsibility for an organization) are granted by the collective body, and do not become the fiefdom of the individual, they are not an independent power base. Rather they are treated as responsibilities, and can be withdrawn if managed incompetently, or become unmanageable. Power is the ability to influence collective decisions, thus it is in the interest of the individual to strengthen their political resource, but not to make it autonomous of the Party. Political power thus is often a "collective good."<sup>110</sup>

Tolerance of diversity flows from this socialization of power. Because political resources and the power to act are regulated by the collective bodies, a diversity of views within the collective bodies are encouraged. For the same reason, controlling each other's actions outside the collective body to discourage unilateral decisions is common, because insofar as power is taken away from the collective body, power is taken away from the individuals who comprise it. Because of the centralized nature of the Party apparatus, disagreements over policy arise at the highest levels, where they are decided in the collective bodies and handed out for implementation. While there is a tendency towards a reformist and conservative wing of the Party, factionalism is harshly discouraged as in other fraternal Parties. The further loyalty to the Party rather than to concrete social or organizational interests also gravitates against factions. Therefore there is much flip-flopping on individual issues, and consequently liberal or conservative tendencies are never eliminated, but reappear at each debate.<sup>111</sup>

Restrictions on political resources insures that no mobilization of an autonomous constituency is undertaken by an individual member to unduly influence collective decision-making. In this sense it "gives leaders an incentive to *reduce* the relevant public; in effect, the very conditions that preserve limited pluralism in the Party work to prevent the emergence of real pluralism in society."<sup>112</sup>

The effects of all this is a tendency towards centralization, coalition-building, fits and starts in the reform process with many minor reversals, and a resistance to decentralization and increasing

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<sup>110</sup> Ibid., p. 440.

<sup>111</sup> Ibid., p. 441.

<sup>112</sup> Ibid., pp. 441-42.

the private sector by the regional elites who depend upon such political resources as they have (such as economic organizations) to influence the center.<sup>113</sup>

The biggest push for strong collective action by the center on behalf of reform is impending economic disaster. Such was the case in the early 1980's following the "age of illusions" from 1972 to 1979.<sup>114</sup> The tremendous debt-load from foolish borrowing during this time led to Hungary's need to join the IMF and World Bank along with austerity measures to avoid rescheduling, and further economic reforms towards a regulated socialist market economy were implemented. These entailed a reversal of the recentralization of the previous decade that went even beyond the original NEM reforms and the creation of new forms of private enterprise with greater freedom to act.

Such measures led to favorable reviews by the Western press of "Goulash Capitalism" and growing privatization. Hungary received almost rapturous praise at times, in part because it was such a stark contrast from the other more moribund members of the CMEA, and in part because was perceived as a vindication of the superiority of capitalism. The Western observer often had the tendency to view these developments in Western terms: the rise of capitalism in Hungary, or a capitalist sphere in Hungary. These views are far from the Hungarians self-understanding of what they are doing. While Rezso Nyers writes that as the reform lies on an "objective situation and objective interests. As such, it is essentially an irreversible process in Hungary," this hardly entails a conversion to capitalism, as argued earlier.<sup>115</sup> In fact, a rather different goal is envisioned:

The basic principle is invariably to organically link central planning with the market mechanism in a single uniform system. That is, it is out of the question that the economy be divided into two spheres with their own laws, that planned control would prevail in the one, while the other would be ruled by the self-regulation of the market ... The substance of the present further development is to improve economic regulation, to improve its "market conformity", as well as to find a more rational solution for the "feedback" of market effects.<sup>116</sup>

Again, the connections between this statement and the Habermasian idea of introducing foreign elements into the system to increase economic rationality is apparent. Not only does it denote the Party's desire for increased economic rationality, it moreover underlines their desire for more ra-

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<sup>113</sup> Ibid., pp. 444-447.

<sup>114</sup> Ibid., p. 442.

<sup>115</sup> Nyers, op. cit., p. 10.

<sup>116</sup> Nyers, Ibid., p. 7.

tional control over the economy as well, that is, they wish to take the semi-legal and illegal second economy out of the shadows and integrate them into the economic system *under their control*. And in this sense economic reform represents not only an attempt to resolve the legitimation crisis, or at least to win the support of the population, it also represents an attempt to gain control over the whole of society through the integration of dependent interests into an economic system it controls.

## 3.0 The Vanguard of Reform: Hungarian Agriculture

No area of the Hungarian economy has performed as well and provided more impetus for reform than has agriculture. Speaking of the events leading to the introduction of the NEM, Comisso and Marer write

Agriculture thus became the vanguard of Hungary's reform movement. Increased agricultural yields and output have contributed significantly to improved economic performance and allowed the sector to serve as a model and rationale for the introduction of economy-wide reforms in 1968.<sup>117</sup>

Speaking of an "agricultural model" of reform inside Hungary is commonplace, and increasing curiosity about a "Hungarian model" of agriculture outside the country testify to the importance of its achievements.<sup>118</sup> More importantly for my discussion, much of the credit given for its successes are attributed to private production within agriculture. Is this accurate? What is the structural configuration of Hungarian agriculture, and what role does private production play? What is the position of the HSWP on these matters?

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<sup>117</sup> Comisso and Marer, *op. cit.*, p. 424.

<sup>118</sup> see: T. Laky, "Enterprise Business Work Partnership and Enterprise Interest", in: *Acta Oeconomica*, Vol 34 (1-2), 1985, p. 32; Kathleen Hartford, "Hungarian Agriculture: A Model for the Socialist World?", in: *World Development*, Vol 13, No 1, 1985, p. 123.

Hungary has a long tradition as an agricultural nation, and yet the post-war period has seen more upheaval in agriculture than at any other period. A brief description of its post-war development would be instructive.

The years from 1945 to 1956 saw wild swings in agriculture that mirrored the chaos of the times. The immediate post-war years saw the dissolution of the large feudal estates that had dominated Hungarian agriculture for so long in favor of peasant small-holdings. This structural readjustment performed well, and agriculture began to rebuild from the devastation of war.<sup>119</sup>

The years from 1949 to 1956 were ones of great hardship for Hungarian agriculture, as the brutal collectivization drives under Rakosi saw massive migrations out of agriculture and a drop in productivity. Marrese write,

the government moved to establish political and economic control throughout the country and to speed up the growth of industry, especially heavy industry, at the expense of agriculture and social infrastructure.<sup>120</sup>

The only brief respite in this process was from mid-1953 to early 1955 when, as Prime Minister, Imre Nagy attempted to implement his New Course, which allowed a process of decollectivization. Rakosi returned to the course after toppling Nagy, but, as the country plunged into revolution in late 1956, the collectivization process was sharply reversed once again by the brief Nagy government.<sup>121</sup>

The years from 1957 to 1965 saw a more orderly and rational development of agriculture among socialist lines, though important reforms marked the process. Political and ideological concerns still remained important factors though. Berend and Ranki provide a most provocative description of the early Kadarist approach to agriculture, which both provided the foundation for subsequent developments, and set a precedent for the pragmatic approach Kadarist agricultural policy has demonstrated. They write

To consolidate regained power demanded the allegiance of the previously alienated peasantry. It was not enough to stop harassment and forced collectivization. It had to stop using the much hated

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<sup>119</sup> Csaba Csaki, "Economic Management and Organization of Hungarian Agriculture", in: *Journal of Comparative Economics* 7 (1983), p. 319.

<sup>120</sup> Michael Marrese, "Agricultural Policy and Performance in Hungary", in: *Journal of Comparative Economics* 7 (1983), p. 333.

<sup>121</sup> *Ibid.*, p. 334; Berend and Ranki, *op. cit.*, p. 230.

method of compulsory delivery as well. It became politically necessary so much the more because the Nagy government had already declared the abolition of the system. A return to the despised old method in the given situation would have been a political disaster. Consequently, one of the first measures of the Kadar government was the abolition of the compulsory agricultural delivery system, and also the centrally determined compulsory sowing-plans. In this way the basic pillars of the command economy in agriculture were destroyed ... nothing remained but market connection.<sup>122</sup>

In their view, this was "a pioneering step towards a new economic model."<sup>123</sup> However, the goal of a predominantly socialist agricultural sector, one dominated by cooperatives and state farms rather than peasant small-holdings, was still openly expressed as valid.

To this end the government developed a new plan to transform Hungarian agriculture, very different from traditional plans. According to Berend and Ranki,

The essence of the new policy was the so-called "dual target", that is, to achieve a dynamic agricultural development accompanied by a gradual-deliberate collectivization. According to this philosophy, agriculture was no longer a basis of accumulation for industrialization.<sup>124</sup>

The new slogan was "balanced growth", in which the previous "price scissors" of low investment and low agricultural prices, which provided the basis of accumulation for industry in the Stalinist model, was to be eliminated. Rather there was a gradual rise in both.<sup>125</sup> Collectivization was to be achieved through a gradual "pull effect", in which the government would help cooperatives achieve full mechanization and a much higher level of production, thus raising their incomes above those in private agriculture, to provide an incentive to form cooperatives. Another incentive was the acceptance of "transitory" or "lower" forms of cooperatives, instead of rigidly sticking to the Soviet "kolkhoz" model, that is, "the possibility of maintaining independent peasant farms and establishing joint marketing or to combine private animal husbandry with collective tillage, etc."<sup>126</sup> What was further unique about this plan was that "instead of a forced collectivization in one 5 year plan period, this long run plan calculated 15-20 years as a transition toward collectivized agriculture."<sup>127</sup> This long run plan was soon dropped in favor of an accelerated program of

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<sup>122</sup> Berend and Ranki, *op. cit.*, p. 230.

<sup>123</sup> *Ibid.*

<sup>124</sup> *Ibid.*, p. 231.

<sup>125</sup> *Ibid.*

<sup>126</sup> *Ibid.*

<sup>127</sup> *Ibid.*, pp. 231-32.

collectivization beginning in 1959, however, as we have earlier mentioned. In this revised plan, "instead of the financial-material basis of collectivization, the political factor was given the main emphasis."<sup>128</sup> This did not mean a return to the kolkoz model of collectivized agriculture however, and as previously mentioned, physical coercion was significant in only the second of the three drives, though psychological pressure was a part of the entire process. Thus the main elements of Kadarist policy can be detected in the development of socialist agriculture--incentives are provided to integrate individuals, in this case peasants, into the government regulated system, supplemented by the willingness to resort to some measure of coercion to overcome any resistance.

While the reforms mentioned above are fundamental to the development of the oft discussed Hungarian model of agriculture, the particular reform that is of most interest to this study, the reform that was the vanguard of later reforms in other sectors of the economy, and, because of its unparalleled success, that has provided the strongest justification for the reform movement, came in 1965. This most important development is what Marrese has characterized as a "change in attitude" towards private plot production. He writes:

The government realized that private plot production increased the standard of living of the rural population, contributed toward greater agricultural supplies for the urban population, industry and exports, and added to the state's tax base. Moreover, to the extent that private-plot farmers acquired land, credit, fodder, seeds, tools, fertilizers, marketing facilities, and transportation from the collective, the interdependence between the private sector and the collective sector was strengthened.<sup>129</sup>

This change in attitude then served to strengthen the HSWP in regards to both power and support. By increasing the standard of living among the rural population and providing more agricultural goods for the urban consumers the regime could only enhance its support among the general public, which in turn made its position more secure. At the same time, in so far as it began to integrate private plot production production into the cooperative system, it rationalized agricultural production while achieving greater control over the countryside, and also provided the government with much needed tax revenues and hard currency income from exports for its budget. There were certain dangers of course, such as the development of too great an income differentiation between the rural and urban populations, which upsets the workers and some of the intellectuals. Such

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<sup>128</sup> Ibid., p. 232.

<sup>129</sup> Marrese, *op. cit.*, p. 336.



developments have led to complaints about the other danger, that of fostering bourgeois individualist attitudes among the peasantry that run counter to socialist values. I will have the opportunity to discuss these problems later. Finally, we may note that reform began in agriculture three years prior to the introduction of the NEM. The HSWP was able to monitor the results of its experiments in agriculture, and apply the experience and knowledge gained towards the formulation of more general reforms.

This provides a good point of departure for examining Hungarian agriculture during the 1980's, with particular attention to the role of private small-scale agriculture.

An obvious question concerning Hungarian agriculture is what is its basis, what are the foundations and role of agriculture in the view of the HSWP, and how does this effect private production?

Csaba Csaki listed some "fundamental principles" of present Hungarian agricultural policy that are instructive:

(i) It is a fundamental goal of Hungarian agricultural policy that the agriculture and food industry should totally satisfy domestic demand with respect to all products that can be produced in the country and should produce as much of a surplus for export as possible, mainly in convertible currency sales... (iv) Small-scale production forms an integral part of Hungarian agriculture ... The household plots of cooperative members are regarded as an integral part of the large-scale enterprise and the interrelations between the collective and the household farms in the area of production and sale are an extension of the large-scale farms...<sup>130</sup>

These principles are corroborated by Marrese, who listed some of the achievements of Hungarian agriculture for which the government was quite pleased:

(1) abundant self-sufficiency in agricultural goods, (2) the prominence of agricultural exports, (3) an extensive large-scale socialist agricultural sector that interacts effectively with Hungary's numerous small-scale producers...<sup>131</sup>

The themes of economic rationalization and efficiency, integration of private interests into the state-led system, and increased support through increased consumer goods run throughout these views.

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<sup>130</sup> Csaki, *op. cit.*, pp. 323-25.

<sup>131</sup> Marrese, *op. cit.*, p. 329.

That Hungarian agriculture must produce enough food in a sufficient variety to satisfy domestic consumption demands is a corner-stone of Kadarist social policy, according to Nigel Swain.

He reports that

By feeding its people well, Hungarian agriculture continues to achieve its most important objective, namely, to "strengthen social and political stability", as the Minister of Agriculture expressed it in his New Year message of 1984, and, in a similar vein, 1985...<sup>132</sup>

The loss of good will from the population, the regime's most important political capital, so to speak, that would result from an inability of Hungarian agriculture to meet the demand of the population not due to natural disaster is unacceptably high.

The continued ability of Hungarian agriculture to earn hard currency from exports as well is another top priority of the HSWP. Hartford reports that in 1981, agricultural and food products accounted for 25.2% of total exports and, more importantly, 33% of the non-rouble, hard currency exchange; in 1982 the figures were 25% and 37% respectively. She concludes that

For a country that depends on foreign trade for nearly half its national income, and that requires substantial imports of Western technology, this means that agriculture has become very important indeed.<sup>133</sup>

Seen in this light, it is imperative for the HSWP to keep agricultural productivity and exports up. The hard currency that agriculture brings to the economy is needed to fund development, which is necessary if the Kadarist social policy of a regularly rising standard of living, or at least in these tough times of austerity due to their heavy debt load, one that does not sink too greatly, is to be maintained.

Now to how this effects private production. Both Csaki and Marrese have brought up the fact that small-scale private agriculture, meaning primarily the household plot, has been integrated into the large-scale socialist cooperatives, rationalizing production. In fact, Marrese concludes that one of the reasons for the success of Hungarian agriculture is the "symbiotic conditions between socialist agriculture and private agriculture."<sup>134</sup> What does this mean in practice, how did it develop, and why?

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<sup>132</sup> Swain, *op. cit.*, p. 27.

<sup>133</sup> Hartford, *op. cit.*, p. 127.

<sup>134</sup> Marrese, *op. cit.*, p. 343.

First let me describe what forms fall within small-scale agricultural production. There are three types of units: approximately 800,000 household plots, nearly one million small auxiliary farms, and a small number of private farms. Combined there are 1.8 million families involved in this sector, which translates into almost half the population.<sup>135</sup>

Household plots are those parcels of land assigned to cooperative members who have worked a sufficient number of days for the cooperative to meet the eligibility requirements for such a plot. The requirements vary from cooperative to cooperative, for men and women, and retired cooperative members need not meet the work requirement to receive one. The size of the plot is limited to 0.6ha for crop land, and 0.23ha of vineyard or orchard per member. Consequently the plots increase in size depending upon the number of family members who have met the requirements of the cooperative.<sup>136</sup>

Auxiliary farms subsumes several forms. They include small plots of land given as part of the remuneration of the state farm and other state workers, home and courtyard gardens, or land still worked by former agricultural workers. Almost all are under one hectare.<sup>137</sup>

Perhaps the easiest question to answer concerning the development of small-scale agriculture in Hungary is why it has been encouraged. Some figures may illustrate the answer rather well. In 1981 the 7.6% of the arable land given over to small-scale production accounted for 31.4% of gross agricultural production, and although this is a percentage drop from 54.8% in 1960 (due to the amazing rises in productivity in economies of scale agriculture through the use of TOPS--technically operated production systems), nevertheless, the absolute value of output has been increasing.<sup>138</sup>

Small-scale production is particularly strong in certain areas, while leaving other areas to TOPS. Small-scale production accounts for 22.7% of crop production and 40.2% of livestock.

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<sup>135</sup> Hartford, *op. cit.*, p. 138.

<sup>136</sup> *Ibid.*

<sup>137</sup> *Ibid.*

<sup>138</sup> *Ibid.*, pp. 138-39.

Within these categories small-scale agriculture produces 57.1% of potatoes, 59.3% of vegetables, 47.8% of fruit, 38.8% of wine grapes, 51.6% of pigs, and 40.7% of poultry.<sup>139</sup>

Surveys of the time allocated to small-scale agricultural production found that only 20.1% of the work done in this sector was performed by active agricultural workers, while the rest was performed by pensioners (24.9%), family dependents (33.2%, mostly by housewives), and the remaining 21.9% by non-agricultural employees, intellectuals, and students. All told, 2.3 billion work hours were spent in this sector that otherwise would have remained mostly unproductive, which is more than the amount of labor spent in large-scale production.<sup>140</sup> Add to this the use of household funds that are invested in this sector, and the state has saved a substantial sum of money. Hartford quotes a 1976 estimate that states that the government would need to invest 100 to 110 billion forints to replace the animal quarters and plantings of small-scale production with that suitable for large-scale production, plus a further 45 to 50 billion forints of working capital.<sup>141</sup>

To further elaborate on the continued support given to small-scale agriculture by the regime, it would be instructive to examine an account from Swain of the events that transpired the last time the HSWP vacillated on its policy towards small-scale agriculture.<sup>142</sup> A confluence of events occurred to shake the confidence of small-scale producers with disastrous effects.

During 1974 the government had to suspend contracts for pigs from private plots due to EEC import restrictions. This was not enough to cause concern, but the Eleventh Party Congress in early 1975 was. It must be remembered that this period was one of conservative backlash against the NEM reforms, in which the reform process was even reversed. It was an inhospitable political atmosphere for private initiative, both legal and illegal. At the Congress not only was small-scale agriculture not supported, it was hinted that a harder line was coming. Attacks were made on profiteering and speculation, generally unfavorable signs for the private sector, and neither Kadar

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<sup>139</sup> *Ibid.*, p. 139.

<sup>140</sup> *Ibid.*, p. 138.

<sup>141</sup> *Ibid.*, pp. 138-39.

<sup>142</sup> Nigel Swain, "The Evolution of Hungary's Agricultural System since 1967", in: *Hungary: A Decade of Reform*, eds. P.G.Hare, H.K. Radice, and Nigel Swain, London: George Allen & Unwin Ltd., 1981, pp. 244-47.

nor Nemeth, the second most powerful political figure at that time, mentioned the household plot in their speeches. Swain puts the blame for much of what followed upon the Party Congress and the poor decisions made there. In particular he criticizes the political elites for allowing political considerations to outweigh economic ones, and also the further connivance of sections within agriculture and cooperative farm management to take advantage of the political environment unfavorable to small-scale agriculture because they viewed it as a nuisance or a threat to the cooperative work, which was the only work the managers had incentives to support.<sup>143</sup>

Subsequent to the Congress a propaganda campaign in the press commenced decrying excessive peasant incomes, and it was suggested that a progressive income tax be instituted to rectify this danger to the socialist principle of income egalitarianism. At the same time structural factors in the cycle of pig production caused a slight decline in the price for pigs promised before the Congress was announced.

The economic factors and the inhospitable political climate of threats and negative press campaigns combined with dramatic and catastrophic results, producing a political fiasco of the first order. Various reports were put forward in which one stated that the country's whole stock of sows in the private sector were killed in one week of panic, while another claimed that 100,000 pigs were slaughtered in ten days. Figures suggest that in a one year period over 1,000,000 pigs were killed, a 20% drop in the national stock! Vegetable and fruit production was down as well, such that in early 1976 both meat and vegetables actually had to be imported.<sup>144</sup>

The government reaction to this threat to its social policy was swift. The Minister of Agriculture and Food Supply was promptly sacked. This was followed by an increase in the purchasing price of pork, as well as improving the position of these small-scale producers with the state vis a vis the large-scale producers. Moreover, the new uniform tax code for small-scale agriculture effectively raised small-scale producer incomes, and investment aid and an increase in the area under small-scale production were introduced to stimulate production in this sector. Finally, the government pledged its continued support to small-scale agriculture, with Kadar himself speaking fa-

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<sup>143</sup> Ibid., pp. 244-45.

<sup>144</sup> Ibid., p. 246.

vorably of the household plot at the 1976 Congress of Agricultural Co-operatives.<sup>145</sup> Having miscalculated the sensitivity of small-scale producers to the environment around them, the government was determined to win back their confidence and to prevent a repeat performance by further integrating small-scale agriculture into the large-scale sector.

As small-scale agriculture has developed in Hungary, the emphasis has been shifted from self-sufficient production to commodity production. Thus one can speak of a division of labor in Hungarian agriculture in which large-scale farming is devoted to capital-intensive farming involving economies of scale, whereas small-scale production concentrates on labor-intensive agriculture or where the risks of investment are best undertaken by those doing the work.<sup>146</sup> This is what is meant by a symbiosis between large- and small-scale agriculture.

In practice, this integration has been furthered by state policy which requires that assistance be given by the cooperatives to the household plots, and increasingly to auxiliary farms as well.<sup>147</sup> Such assistance ranges from buying inputs on behalf of the small-scale producers to helping to organize pig production, in which all the inputs are provided (including the piglet), and then picking up the fattened pig for slaughter. Moreover, 90% of these contracts are long-term, which provides incentives for the small-scale producer to invest in better facilities.<sup>148</sup>

On the other side, incentives had to be offered to the managers of cooperatives to insure their willing cooperation with the small-scale producers. The reasons were clearly demonstrated in our discussion of the crisis of small-scale agriculture in 1975. To briefly restate the problem, cooperative farm managers traditionally considered the household plots as an annoying inconvenience or even a danger that detracted from work done on the cooperative.<sup>149</sup> To correct this disincentive, new

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<sup>145</sup> *Ibid.*, pp. 246-47.

<sup>146</sup> Hartford, *op. cit.*, p. 140.

<sup>147</sup> *Ibid.*

<sup>148</sup> *Ibid.*

<sup>149</sup> Swain, *op. cit.*, pp. 244-45.

measures were introduced in 1977 in which stimulating improved production became a criterion for a 20% bonus for management.<sup>150</sup>

One of the failures of Hungarian agriculture had been with capital-intensive investments in large-scale animal husbandry, which had reportedly been pursued because county-level administration pushed for it over decentralized small-scale production.<sup>151</sup> This of course reflected their interests, because their responsibility over such a large investment meant added influence in Budapest.

In 1982, with the introduction of the "economic work partnerships", the practice of subcontracting out livestock to be fattened by small-scale producers increased dramatically. By 1983 state farms had contracts with 20,000 state farm employees, 23,000 industrial workers, and 20,000 cooperative farm members to fatten 18,000 calves, 190,000 pigs, 17,000 sheep and 500,000 chickens.<sup>152</sup>

Here is a case of conflict between regional and central elites. The regional elites were able to get their investment at first, because the small-scale producers could not lobby for their interests. But when the investment failed, wasting precious capital, the central elites chose an economically more rational decision. Indeed Swain writes,

There was good reason for this continued government support for small-scale agriculture. First, production on the household plot of pigs and vegetables remained cheaper than on the large-scale farm ... Second, it was only thanks to the successful integration of the small-scale sector that overall production levels remained high.<sup>153</sup>

Wasted capital in times of austerity threatens economic recovery, which threatens the Kadarist bribe, which has an adverse impact on support for the regime and its room to maneuver. Hence continued support for small-scale production.

It is very important to note that the increasing support of small-scale production has integrated them more and more into socialist agriculture, such that "it is impossible any longer to establish a clear dividing line between collective and private production."<sup>154</sup> Planning has not been replaced,

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<sup>150</sup> Ibid., p. 247.

<sup>151</sup> Marrese, *op. cit.*, p. 331.

<sup>152</sup> Swain, "Hungarian Agriculture in the Early 1980's: Retrenchment Followed by Reform", p. 31.

<sup>153</sup> Ibid.

<sup>154</sup> Hartford, *op. cit.*, p. 141.

but rather the market has been harnessed for planning. Hartford remarks that the lesson of the symbiosis between large- and small-scale production is "not the bankruptcy of socialist approaches, but the lesson [is] that it is possible to put new wine into the old bottles."<sup>155</sup> The HSWP not only managed to support its weak economy through this symbiosis, which in turn buttresses its consumerist bribe, but, paradoxically,

The household producers of today are much more closely tied into the network of state-dominated commodity exchange and co-operative organization of production than their predecessors a generation ago. State plans probably come closer to meeting their objectives than they did before the NEM reforms.<sup>156</sup>

It should be apparent that the symbiosis discussed can be viewed as an introduction of foreign elements into the economic system to rationalize it and increase its efficiency. This serves the dual purpose of garnering the support of both the peasantry and urban consumers, while at the same time integrating the peasantry into the state-controlled large-scale socialist agricultural sector through incentives that make private commodity production dependent upon the state.

Moreover, as Hartford writes,

Over the long run, the very developments in the domestic economy which might help solve agriculture's present problems will decrease its importance relative to industry in national economics and in economic policy. Such a transformation might indeed make it less costly for the Hungarian leaders to discard the "Hungarian model" in favor of one which more emphasizes increasing scale, state ownership, and centralized control.<sup>157</sup>

Implicit in this statement is that the HSWP remains in firm control ultimately over the fate of Hungarian agriculture. It is using unorthodox methods to be sure, but all is integrated under their control. It has harnessed the market for its own purposes in agriculture, subordinating it to the plan, while integrating the interests and private commodity production of the peasantry into the state-controlled socialist agricultural sector. If the peasantry are winners in this deal, it is only by the good graces of the regime, which remains the biggest winner of all.

How long then will small-scale agriculture continue to play a role in Hungary? Nigel Swain reports that

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<sup>155</sup> Ibid.

<sup>156</sup> Ibid.

<sup>157</sup> Ibid., p. 144.



In 1984, and again in 1985, the Minister of Agriculture pledged support for small-scale agriculture; an article in *Magyar Mezogazdagsag* in 1984 noted that it figured in Hungary's long-term agricultural plan until the end of the century...<sup>158</sup>

Small-scale production thus remains a part of Hungarian agriculture's indefinite future, in other words, as long as it serves the purposes of the HSWP.

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<sup>158</sup> Swain, op. cit., p. 31.

## **4.0 Reform in the Industrial and Service Sectors: The Small Enterprises**

### ***4.1 The 1982 Reforms: Bold Moves and Unmet Expectations***

In 1982 a number of new forms of economic organization were created through government regulations which were grouped under the classification of "small enterprise". Previous to these reforms individual private enterprise did exist in Hungary, most notably there were skilled and unskilled artisans and individuals involved in retail shopkeeping. Before the reforms introduced in 1982, the required licenses to practice as a skilled artisan or a retail shopkeeper were granted upon the discretion of the official bodies, but the reforms have since made it a right of citizens to obtain

such licenses if they meet the required qualifications.<sup>159</sup> The small enterprises created, however, were private partnerships or cooperatives, and were expected to fulfill a variety of needed functions. Primarily, "the economic policy considered the small and flexible units capable of prompt response to any demand primarily as a means of improving the standard of living."<sup>160</sup> This would occur through several ways:

It was assumed that the said units would be capable and ready to significantly increase the range of choice of consumer goods, satisfy many sorts of demand for services, as well as to organize such activities in the spheres of both production and consumption which the traditional organizations are unable to carry out.<sup>161</sup>

This view stresses the ways in which small enterprises were to support Kadarist social policy in a time of, in the words of Rezso Nyers, a "socialist recession period."<sup>162</sup>

Another view, which stresses the economic objectives, also listed the desire to reduce bottlenecks in services and subcontracting, which was stressed above, but further stated:

The legalization of the second economy was expected to include the accumulated savings of the population into the "blood circulation" of the economy, thus somewhat mitigating the disadvantages deriving from the lasting decline in investment. The small ventures were expected to revive competition and to mitigate price rises, at least in some areas. There also was an idea that in consequence of the decelerating economic growth, enterprises would make efforts to get rid of superfluous labor, and, understandably, of unskilled labor or that of people with low qualification, and that these would be absorbed by the developing small ventures.<sup>163</sup>

This view lists expectations that have a direct bearing on social policy as well, in that the small ventures were expected to mitigate inflation and structural un- or underemployment. By unleashing suppressed and latent private initiative, the government hoped to soften the negative costs of austerity without committing its own scarce resources, and in fact, by bringing out much of this activity from the shadows of the semi-legal and illegal economic sector, it would even increase its revenues

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<sup>159</sup> G.J. Kovacs, "Job-creating Capacity of the Private Sector in Hungary between 1981-1985", in: *Acta Oeconomica*, Vol 37 (3-4), 1986, pp. 346-49.

<sup>160</sup> T. Laky, "Small Enterprises in Hungary - Myth and Reality", in: *Acta Oeconomica*, Vol 32 (1-2), 1984, p. 41.

<sup>161</sup> Ibid.

<sup>162</sup> Rezso Nyers, "National Economic Objectives and the Reform Process in Hungary in the Eighties", p. 4.

<sup>163</sup> Gyorgy Varga, "The Role of Small Ventures in the Hungarian Economy", in: *The Hungarian Economy in the 1980's: Reforming the System and Adjusting to External Shocks*, Josef C. Brada and Istvan Dobozi, Eds., Greenwich, Connecticut: JAI Press Inc., 1988, p. 89.

while extending its control over previously unregulated areas. Thus the main themes of economic rationalization and interest integration reappear in the 1982 reforms.

These forms were part of a series of reforms in the broader economic context designed to stimulate "socialist entrepreneurship". While this did not by any means implicate a change from the system of central planning, there was

a clear shift of emphasis from that of stimulating "enterprise self-interest" to that of stimulating individual and small-group self-interests ... Such tendencies should, however, find expression as part of a "fusion" of private and public interests (utilizing for this purpose "self-regulating" markets to the extent possible), keeping within fundamental ideological constraints in a non-rigid fashion.<sup>164</sup>

In order for this fusion of public and private interests to take place, a "basic restructuring of environmental conditions" was required.<sup>165</sup> The reforms instituted, including those creating the small enterprises, were to reflect this restructuring.

There is however, little agreement on the meaning of socialist entrepreneurship, nor is it universally regarded as desirable.<sup>166</sup> This disagreement extends to the reforms as well. The elites of large-scale industry generally do not favor reforms in enterprise management, nor in small enterprise, as their self-interests do not lie in decentralization or risk-taking.<sup>167</sup> Conservatives and lower level cadres within the HSWP also do not have a high regard for decentralization, the former because it disturbs their ideological sensibilities, and the latter because it takes resources out of their control. The trade unions (TU) also line up against reforms concerning small enterprises because it takes workers from out of their control.<sup>168</sup>

These reforms have certainly not been undertaken in an ideological void, and, as can be gathered from my remarks above, a degree of turmoil and struggle within the HSWP has proceeded along with the implementation of these reforms. As Jan Adam reports, a chronic problem is "disagreement in the leading circles of the party and government about important economic policy

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<sup>164</sup> Jacob Naor and Peter Bod, "Socialist Entrepreneurship in Hungary: Reconciling the "Irreconcilables"", in: *Columbia Journal of World Business*, Summer 1986, p. 56.

<sup>165</sup> *Ibid.*, p. 58.

<sup>166</sup> *Ibid.*, p. 57.

<sup>167</sup> *Ibid.*; Laky, "Enterprise Business Work Partnership and Enterprise Interest", p. 32.

<sup>168</sup> Stephen Noti, "The Shifting Position of Hungarian Trade Unions Amidst Social and Economic Reforms", in: *Soviet Studies*, Vol XXXIX, No 1, January 1987, p. 73.

problems ... and about the need for the reform and its extent."<sup>169</sup> Economic necessity, however, given Kadarist social policy, has generally tended to give those favoring reform the upper hand.<sup>170</sup> But progress has been partial and slow, tending to go in spurts, as noted before. These developments, then, have been

sanctioned on ideological grounds by the adoption of an evolutionary stance on ideological matters. "Secondary" forms of ownership are thus beginning to emerge as well as the delegation of "strategic" ownership functions to bodies, other than ministries, which are more entrepreneurial and more flexibly attuned to market conditions than were bureaucratic ministries.<sup>171</sup>

This stance and willingness to experiment has been extended to small enterprise to some extent as well, though they are generally more sensitive to ideological constraints, which limit the scope of such experimentation, especially in regards to forms of ownership and their financial basis.<sup>172</sup> Again, the willingness to implement reforms does not mean at all that they will be administered smoothly, consistently, or without set-backs. Reform becomes vulnerable when its performance is less than satisfactory or, especially, when it generates what is considered to be excessive socially undesirable phenomena, such as unjustifiably large income differentiation or too much autonomy.<sup>173</sup>

Nevertheless, the need for reform has become so pressing, that many have argued for a greater tolerance of "the unfavorable effects of a market economy," such as "putting up with a decline in job security, rising inflation, and a greater differentiation of incomes."<sup>174</sup> Such flexibility is needed

because it is the only means to avoid a crisis due to the internal and external tensions of management. Moreover, only such a sacrifice can, in the long run, lead toward everybody's cherished dream of a harmoniously developing economy. If this policy does not produce a breakthrough, or if the transitional difficulties are used as an excuse to restrain new efforts, then a significant drop in the standard of living and other adverse social consequences will be inevitable.<sup>175</sup>

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<sup>169</sup> Jan Adam, "The Hungarian Economic Reform of the 1980's", in: *Soviet Studies*, Vol XXXIX, No 4, October 1987, p. 624.

<sup>170</sup> *Ibid.*, pp. 625-26; Comisso and Marer, *op. cit.*, p. 449.

<sup>171</sup> Naor and Bod, *op. cit.*, p. 66.

<sup>172</sup> see for example: K. Falus-Szikra, "Small Enterprises in Private Ownership in Hungary", in: *Acta Oeconomica*, Vol 34 (1-2), 1985, pp. 13-26.

<sup>173</sup> Naor and Bod, *op. cit.*, p. 67.

<sup>174</sup> Marton Tardos, "The Increasing Role and Ambivalent Reception of Small Enterprises in Hungary", in: *Journal of Comparative Economics* 7 (1983), p. 287.

<sup>175</sup> *Ibid.*

It is in light of such considerations that the reformists have been able to muster up enough of a political consensus to push ahead with reform, though it is debatable that it has been able to do so effectively, given the political constraints.

Because of these constraints, the reforms concerning small enterprise have enjoyed only mild success, while encountering at times significant opposition. For example, Laky reports that the 1983 figures indicate that

the number of members working in the more than ten thousand small units represents less than 2 percent of employees in the national economy, that is, 98 percent of those employed do not participate in small ventures. Also the majority of those belonging to the two percent have kept their jobs with the original employers so that they spend their leisure time in the small enterprise.<sup>176</sup>

This has expanded since then, but not such that they have fulfilled the expectations set for them.

What are these unmet expectations? Varga provides a useful list:

1. A part of the small ventures have not become autonomous market actors, but a considerable part of them have become built into the large-enterprise order, thus strengthening their autarkic nature ...
2. Most of the new organizations do not mitigate shortages of consumer goods and services or in the sub-contracting sphere, but they do help in exploiting the capacities of large firms ...
3. It seems to have been a naive idea that the new organizations would absorb the surplus labor released by the enterprises. As a matter of fact, in three years merely 30,000 people have left the socialist sector to become independent small entrepreneurs. Against expectations, primarily qualified employees have joined the small ventures and the consequence is that the less qualified labor becomes more valuable to large enterprises.
4. The fact that the majority of association are internal ventures allows enterprise managers to handle employees in a differentiated manner so as to make venturing possible for some workers and employees groups and to exclude others from this opportunity ...
5. The hopes attached to the mobilization of savings by the population have only been partially realized ... The consequence is a preservation of the handicraft character of small-scale production and wasteful consumption...<sup>177</sup>

To summarize the gist of these shortcomings, the small enterprises have not been able to change Hungarian economic structure and performance to any great extent, but rather have been forced to mold themselves to the needs of large-scale enterprise and subordinate themselves to the economic system these large-scale enterprises dominate.

There are many opinions for the failure of small ventures to perform as expected, and it will be useful to review some of them here. Varga argues that the limited success of the small ventures is due to lack of a well-planned and forthright introduction of the reform:

Experience shows that society and the institutional system have not been prepared adequately for the development of small ventures. This is indicated by the sometimes passionate debates about them. It is a fact that the introduction of ventures into the social fabric caused certain ideological disturbances

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<sup>176</sup> Laky, "Small Enterprises in Hungary - Myth and Reality", p. 42.

<sup>177</sup> Varga, op. cit., p. 91.

... Ideological clarification is not promoted by the fact that the system of economic control and management gives the feeling sometimes of loosening, sometimes of tightening rules on small venture behavior.<sup>178</sup>

The ideological disturbances mentioned refer to an unsettling of the status quo that people are accustomed to, or have interests in. Varga mentions the modification of usual career paths, a weakening of egalitarianism and the consequent emergence of inordinate income differentiation, and a greater mobility of labor and organizations that appears unstable or anarchic; the result of the reforms is to render previously immutable socialist values "anachronistic", which causes confusion and dismay among some quarters.<sup>179</sup> The battles over these reforms lead to vacillations in government policy, which renders the market unstable, and works against entrepreneurialism.

The reasons for the modest success of the small ventures, in Laky's viewpoint, are two-fold.<sup>180</sup> First, the social and economic environment has provided little incentive for the efficacious functioning of existing small enterprises, nor for the creation of new ones. On the other hand, and in part following from the former reason, the new small enterprises are cautious and distrustful, which curtails entrepreneurial activity. This view then would concur with Varga's observations, though she stresses the distrust on the part of the would-be entrepreneurs a bit more. Another similar view is provided by Gabor Revesz, in his discussion of what he calls the "direct market sector", which encompasses all economic activity which is market oriented. He lists four limits and impediments to this sector. First, the "limits of their functioning are set from several sides by *statutory*, formal bounds."<sup>181</sup> In particular he mentions the limits on the number of employees and the system of progressive taxation as limiting factors.

Secondly, the "*authorities* often hinder the setting up, functioning and survival of small-scale activities (small enterprises) by *informal* measures."<sup>182</sup> Revesz mentions here the unfair use of taxation by officials to stop any unwanted private activity.

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<sup>178</sup> Ibid., p. 92.

<sup>179</sup> Ibid.

<sup>180</sup> Laky, *op. cit.*, p. 59.

<sup>181</sup> Gabor Revesz, "On the Expansion and Functioning of the Direct Market Sector of the Hungarian Economy", in: *Acta Oeconomica*, Vol 36 (1-2), 1986, p. 114.

<sup>182</sup> Ibid.

A third and rather important factor is that it

is a characteristic impediment to the functioning of small-scale activities and enterprises as well as to asserting their efficiency ... that they cannot get properly *integrated into the system of the division of labor as a whole*. It is often hopeless for them to acquire up-to-date *means of production* (machines, materials, parts, etc.).<sup>183</sup>

An excellent example he gives is that the most basic of instruments for any business, a telephone, is almost impossible to come by for a small enterprise.

The fourth and final reason Revesz gives is that

Under the given conditions the business conduct of small producers/small entrepreneurs is typically mistrustful. People have been taught to be careful because of historical experience, frequent and incalculable changes in the conditions of their activities and business, for reasons sometimes motivated by political/ideological considerations, for reasons they cannot understand or accept. They prepare themselves for a new "squeezing" cycle of the policy and economic policy, for a worsening of statutory conditions of business or--on the other side--for losing the benevolence of those big organizations (their representatives) on which (of whom) their chances greatly depend. Therefore, even irrespectively of the said limitations, small producers and small entrepreneurs arrange themselves provisionally, trying to secure the way of withdrawal.<sup>184</sup>

This is a clearer elaboration of the distrust felt by the would-be entrepreneurs, which is exacerbated by the lack of ideological clarification and hesitant implementation of reform by the government, the interference and resistance by lower level governmental and party cadres, and the concomitant fluctuation of policies and signals emanating from the state concerning small enterprise. These entrepreneurs are sensitive to such things, as were the small-scale agricultural producers, and remain distrustful because the seeming commitment of the government to small enterprise has not been supported by consistently implemented policies to back up that verbal promise.

Rezso Nyers himself has admitted to such problems. He writes:

In spite of the extraordinary liveliness of small ventures, much hesitation is still felt here also on the part of entrepreneurs. Many people still feel that things will not last, a feeling unjustified "in general and in principle" since even the Party Congress declared itself in favour of the maintenance and even development of this sector, yet "in concrete terms and in practice" it is still justified. There is a certain temporariness also about Hungarian market relations. In the case of several products and services it cannot be predicted whether or not the socialist firms will nevertheless be able of doing the job, or whether there will not be a powerful import competition on the market. But the problem is more substantial because of the uncertainties of material supply and taxation, as well as because the government has no established trade cycle policy yet in connection with this sector.<sup>185</sup>

Lack of a consistent commitment to, and worked out institutionalization of, market relations and the small ventures has hampered the latter from developing fully and introducing needed competi-

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<sup>183</sup> Ibid., p. 115.

<sup>184</sup> Ibid., p. 116.

<sup>185</sup> Nyers, op. cit., p. 13.



tion in the economic system. Despite the verbal commitments made, the new values embodied in socialist entrepreneurialism have not been firmly implanted in the state or the mass population, but rather the system of dependencies inculcated by the state and inconsistent implementation of the new reforms have not brought most of the semi-legal or illegal second economy activities out into the legal private economy, and those that have joined have been integrated into the large-scale socialist enterprises in such a way that they are dependent upon them, reinforcing their autarkic nature rather than introducing real competition. This lack of competition reinforces traditional problems, such as high monopoly-like incomes for the small entrepreneurs, which in turn leads to regulations like progressive taxation to control market incomes, which then drives the legal small private entrepreneurs underground, starting the whole cycle again.<sup>186</sup> The return to traditional solutions to solve problems caused by the half-hearted implementation of reform, perpetuating the problem, poses serious difficulties for the small enterprises, and the reforms in general. These difficulties will become more apparent as we examine in detail the new small enterprises.

While several forms of new economic organizations were introduced in 1982, the overwhelming majority are of two particular types, the Business Partnership (GMK) and the Enterprise Business Partnership (VGMK), and so I will limit the discussion to these two types.<sup>187</sup>

## 4.2 *The GMK*

The GMK is a private association of 2 to 30 people, in which each member must contribute capital to a collective fund or possess a professional skill required by the GMK, and in which each

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<sup>186</sup> see for example: K. Falus-Szikra, "Wage and Income Disparities between the First and Second Economies in Hungary", in: *Acta Oeconomica*, Vol 36 (1-2), 1986, pp. 101-02.

<sup>187</sup> If one surveys the English language literature on the small enterprises, one will find that no agreement has been reached on the best translation of these two terms; therefore I, along with others, find it practical to use the Hungarian abbreviations.

member must participate in the work of the GMK. The GMK may hire employees. It is interesting to note that of all the forms of small enterprise introduced, Laky has argued that, with the exception of the Civil Law Partnership (PJT), the GMK stands alone in possessing the essential classical qualities of an enterprise.<sup>188</sup> These qualities are: 1) an autonomy of organization - freedom of direct control from another organization/institution in which the choice between business acts depending on profit, and entailing risks made in its pursuit, is that of the organization; 2) freedom of decision on the profit - whether to reinvest or not; and 3) freedom of decision on the whole enterprise - whether to keep it running or close it down. Within the GMK one can find three functional categories of roughly equal size: those providing intellectual services, those providing miscellaneous, often personal, services, and those performing industrial activities.<sup>189</sup>

Of these three, it was those engaged in industrial activities that the reformers were most interested in and had great expectations for, because it was hoped they would perform two needed functions: 1) that they would create the desperately needed "background industry" to fill in the gaps in the economy left by the larger more inflexible socialist industries, and 2) that they would invest money into production instead of leaving it for savings or consumption.<sup>190</sup> Of these two, the GMK's have modestly fulfilled the latter function, but have by and large failed to perform the former. The reasons generally are those detailed previously, which I will now flesh out more as it pertains to the GMK's.

First, I shall discuss the social and economic environmental factors that inhibit the development of the GMK's into their full potential.

Socially, the GMK's have been facing a hostile attitude on the part of the general public, from administrative cadres, and from those in industry. These are the results of traditional prejudices against privateering, in which it was assumed wealth was quickly and unscrupulously gained. This adversely affects those GMK's in industrial activity because it often leads to administrative inter-

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<sup>188</sup> Laky, *op. cit.*, p. 44.

<sup>189</sup> *Ibid.*, p. 46.

<sup>190</sup> *Ibid.*

ference and the refusal of some in industry to deal with "privates" because they "fear from the appearance of corruption."<sup>191</sup> Laky states that

Very little has been done to settle the *social status* of participants in enterprise, for changing value judgements following from a given dogmatic approach which has become obsolete from the point of view of social and economic development, and for the elimination of opinions of inherent inconsistency which accept moonlighting and refuse the licensed activity.<sup>192</sup>

This accords with the previous discussion of the ideological disturbances caused by the introduction of new socialist values which seem to contradict with the older values, such as egalitarianism and anti-individualism.

This inhospitable environment goes beyond the question of social status, it is further grounded in large-scale socialist industry protecting their interests in the face of competition from small enterprise, and insufficient profit motivation to overcome their antipathy towards small enterprise. Varga speaks of the "duality" of the economy, and the lack of sufficient resources, as the source of the "ideological and economic conflicts" between the large-scale socialist sector and the small private enterprises.<sup>193</sup> He writes:

While the large firm is dependent ... on the products and services of the small firms, it often also is at war with them, first of all for the factors of production, especially labor. The large company justly feels that in wage policy, a socially sensitive field, it is at a disadvantage relative to the small ventures, while the small ventures justly protest that they are in a de facto disadvantageous situation in respect of material supply and credit conditions. It follows that in the contemporary Hungarian economy we can witness a curious competition mainly between the large firms and small ventures, partly on the market for commodities and services, but first of all on that for resources.<sup>194</sup>

Decentralization and greater scope for private initiative through the small ventures threaten them in the market, in the competition for labor and other resources, and detract from their relative importance and ability to influence central decisions. As long as this inhospitable environment and uphill struggle against socialist industry persists, entrepreneurs will not trust the long-term stability of the economic environment, which will adversely effect the development of entrepreneurial activity.

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<sup>191</sup> Ibid., p. 59.

<sup>192</sup> Ibid., p. 56.

<sup>193</sup> Varga, op. cit., p. 93.

<sup>194</sup> Ibid., pp. 93-94.

A word more on economic disincentives is necessary. Most immediate is the problem of acquiring sufficient amounts of capital, because of the restrictions placed on the sources of capital, mostly for ideological reasons. As Falus-Szikra notes, it "is a well-known theorem of Marxian political economy that personal incomes should serve in socialism a single purpose--personal consumption and the individual-family investment required for this."<sup>195</sup> Informal data suggests

that though capital required for starting had been collected, it was far less than would have been required for "the assets that are expected by the given activity" and either money or confidence or both were not sufficient to acquire the necessary assets.<sup>196</sup>

The competition for capital has left the small enterprises at a disadvantage, given the limited sources of capital allowed, and the limited resources from these sources in Hungary. Uncertainty has also left entrepreneurs unwilling to risk too much of their own resources. Some regulations have been produced to deal with this problem, but until there is a more free flow in the capital markets, this will remain a problem.<sup>197</sup>

In addition to the problem of sufficient capital, there still remains the problem of an insufficient supply of capital goods and other inputs. Often times, new capital goods are too expensive, if available at all, while the ability to buy used equipment is severely hampered by the practice of the large socialist firms to cling to theirs until it has been written off until zero value.<sup>198</sup>

Finally, there is the problem of disincentives from taxes designed to prevent too much income differentiation, which impedes productivity and actually encourages illegal activities.<sup>199</sup> Moreover, as Varga notes about a tax package introduced in 1985 which also charged a 10% surtax on enterprises which engaged the services of small ventures:

Many managers consider the introduction of the surtax as a kind of signal and exhibit a cautious behavior towards small ventures. The impact of the criticisms levelled at the high incomes and of the "income adjustment" attainable through the higher taxes might be that small ventures submerge into the illegal sphere and the monopoly position of the remaining legal ones will be strengthened.<sup>200</sup>

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<sup>195</sup> Falus-Szikra, "Small Enterprises in Private Ownership in Hungary", p. 17.

<sup>196</sup> Laky, *op. cit.*, p. 46.

<sup>197</sup> see for example: Falus-Szikra, *op. cit.*, pp. 22-25.

<sup>198</sup> Laky, *op. cit.*, p. 58.

<sup>199</sup> *Ibid.*; Falus-Szikra, "Wage and Income Disparities between the First and Second Economies in Hungary", p. 101.

<sup>200</sup> Varga, *op. cit.*, p. 92.

The effect of these attempts to regulate small venture incomes through taxation, rather than to introduce needed reforms to encourage more competition, is to reinforce the negative spiral mentioned previously. This reliance on ineffective attempts to regulate small enterprise income is also responsible for the caution and distrust of the small-scale entrepreneurs, as well as their fear of a reversal of the regime's commitment to them, remembering well the old expropriations. As a result there is a tendency to to maximize short-term profits while the opportunity remains, rather than reinvesting for long-term profitability, which further reinforces the downward spiral.<sup>201</sup>

These factors manifest themselves, moreover, in another detrimental phenomenon, which is the overwhelming tendency of GMK members to keep their original job in the socialist sector, thus reducing their efforts in the GMK to leisure time work. This can be explained by both the desire for security and to develop business contacts. Still, restricting their GMK activities to part-time work decreases productivity and, most likely, profits. Nevertheless,

The majority of private enterprises apparently do not want more than that at the moment: they want to become neither really "private" nor really "enterprise" which includes both the freedom and the hazard of self-employment. Especially as long as the socio-economic consequences are so uncertain.<sup>202</sup>

What happens as a result is not the development of an entrepreneurial attitude, but merely the extension of an employee attitude.<sup>203</sup> This extension of the employee attitude, of a person bred to be ostensibly dependent on the state, is an interesting paradox. The center of the HSWP wants to encourage this entrepreneurial spirit to add new life to the economy (and to drain life from the unregistered economy), and yet it cannot easily restructure the dependent relations it has created to another form to reflect greater economic rationality. It is caught in a trap of its own making. The legacy of old socialist values, and the difficulty in introducing new values, is especially troubling, as mentioned before. Laky makes a very pointed observation concerning the troubling ironies involved:

It follows that all who formed a PJT or a GMK represent at the same time the group willing to observe law and order, as against all others who have continued to keep out of the bounds of legality offered to them and have continued to do moonlighting work and make untaxed income. Still, those

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<sup>201</sup> Laky, *op. cit.*, p. 56.

<sup>202</sup> *Ibid.*, p. 48.

<sup>203</sup> *Ibid.*, p. 52.

persons who were willing to work legally (I could quote numerous conversations showing their strong preference for legitimate ways) and who strengthen authority relations in society with their declared voluntary obedience, were frequently exposed to rebuff they had never met in "privateering".<sup>204</sup>

It is a strange irony indeed when privateers are treated with more respect than legal private entrepreneurs. This ambivalence and confusion is a result of the inadequate preparation by the political elites for the introduction of small enterprise, both ideologically and structurally. This ambivalent preparation and reception has resulted in the ambivalent performance the small enterprises have achieved. The attempt to draw out private interests from the underground and reintegrate them in an open, more economically rational, and controlled fashion with the large-scale socialist sector has so far fallen prey to the contradictions of the half-hearted attempt.

### 4.3 *The VGMK*

The VGMK is a partnership of no more than 30 people recruited from the employees and pensioners of a particular organization, contingent upon the previous approval of the enterprise manager. It was expected that the VGMK would occur in those industries where dormant capacities and underutilized workers were.<sup>205</sup> This would spur productivity and reward workers who desired to be more productive, in effect introducing wage differentiation.

Even greater hopes were attached to the VGMK though by the reformers. With the penetration of these forms into large-scale industry, a new cooperation between workers and managers would emerge that would replace the previous wage-labor relationship with one founded upon partnership - which would naturally have great repercussions:

This also means a different attitude to *work*: it was hoped that with the employees directly interested in the profit, manipulation with work performance would be put an end to, and better forms of work organization based on individual capabilities and endowments would be created. The performance

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<sup>204</sup> Ibid., p. 55.

<sup>205</sup> Ibid., p. 49.

reserves thus disclosed would also react upon the usual activities of the enterprise and gradually transform the internal work organization. All this might give a new content to socialist ownership: the employees would become really interested in the protection of the means of production.<sup>206</sup>

What was envisioned was a radical transformation of socialist enterprise, which would truly integrate the workers into the socialist means of production. Furthermore, it would provide a great service for the regime in that such cooperation would render much of the unregistered economy moot. Such positive worker integration into the socialist system of production could possibly even begin to give some content to the party's claim to represent workers' interests. Unfortunately, the VGМК did not quite live up to the reformers' hopes. In fact, the VGМК experienced quite a bit of opposition from many quarters.

First some figures. Industry was quite reluctant to use the VGМК at first, not surprisingly, most were opposed to them for quite a while. By May of 1983, when the VGМК had become the most common form of small enterprise, they nevertheless existed in only 18% of the economic units of socialist industry. By the end of the year this had increased to 34%, and it wasn't until 1984, when it reached 65%, that a majority of socialist industry made use of the form--and then only sparingly.<sup>207</sup>

Why did the managers of socialist industry oppose the VGМК at first, and why do they continue to show reluctance to use them fully? There are several key reasons.

To begin with, many important economic incentives are lacking.<sup>208</sup> First, the enterprises are not responsive to the modest profit they realize from VGМК activities. Secondly, contrary to expectations, the enterprises are not interested in eliminating shortages, indeed, they sometimes have an interest in maintaining them in order to protect their sales position. Hence they do not avail themselves of the opportunity to utilize the productive capacities of the VGМК to meet the demand.

Most importantly, the managers have a definite interest in maintaining the centralized hierarchy of socialized industry:

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<sup>206</sup> Laky, "Enterprise Business Work Partnership and Enterprise Interest", p. 29.

<sup>207</sup> *Ibid.*, p. 30.

<sup>208</sup> *Ibid.*, p. 34.

This is because an autonomous choice from among the activities, such as, for example the decision on the use of the venture as an economic unit no longer presupposes the employer-employee relationship, but the common decision-making of equal partners, taking risks and responsibilities jointly. This would mean at the same time in the big-enterprise organization, set up in compliance with the strict rules of hierarchy, a whole system of small organizations, independent of these rules, having the right to make decisions of their own and restructuring the income hierarchy, would be brought about.<sup>209</sup>

Protection of the organization hierarchy and the ability to control what goes on in the enterprise are the primary concerns of enterprise managers. It far outweighs the profit motive at this time. There are several reasons for this.

First, it is in the natural interests of the manager that he or she be able to manage, to control, and not just to guide. This includes what gets produced, how much, and how much gets paid to produce it. It is the prevailing management style in socialist industry, managers find the notion of entrepreneurialism rather foreign.<sup>210</sup>

Second, because of the many regulation restraints placed upon enterprises, especially the very strict wage constraints, which are tied to manager bonuses, there is an economic incentive to control the enterprise in a centralized hierarchy.<sup>211</sup> It is interesting to note that many managers perceived the VGMK as merely a substitute for overtime work.<sup>212</sup> Managers would much prefer a change in wage regulation to give them more flexibility to set wages. However, the government has consistently denied that request.

This is because of invariable conflicts in this area. Managers, for a variety of reasons, do not have a strong incentive to hold wages down. Workers are ideologically steeped in income egalitarianism, and generally oppose income differentiation to promote productivity. The state who, through subsidies and other outlays, must ultimately pay the bills and ensure a developing economy, is interested in seeing that wages and investment do not outstrip productivity and profit, while at the same time holding to its ideological commitment to relatively low wage differentiation.

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<sup>209</sup> Ibid.

<sup>210</sup> Naor and Bod, *op. cit.*, p. 57.

<sup>211</sup> Laky, *op. cit.*, pp. 39-41.

<sup>212</sup> Ibid., p. 30.



Thus all seem to be at cross purposes with one another, and the state views wage regulation as a Pandora's box that should be opened only with great care, or dire need.

Finally, it is in the interest of enterprise managers to maintain a centralized hierarchy so that they can, as the person responsible for the enterprise, influence central decisions on matters of interest to them. In as much as the VGМК's might decentralize the enterprise, it would decrease their influence.

As a result of these interests, enterprise managers have shown little interest in changing their method of operation, and thus of allowing enterprise pluralism to develop through the VGМК's. Therefore:

The VGМК's have, in fact, become work brigades because the enterprises have remained interested not in establishing work partnerships but in the results that can be attained with the accustomed endowments and operations within the prevailing dependency relations and the narrow limits set to enterprise autonomy.<sup>213</sup>

It has been possible to constrain the VGМК's into the centrally hierarchized socialist enterprise because, although it contained the possibility of becoming an enterprise in its own right, it is nevertheless completely dependent upon the enterprise manager, whose permission it needs to exist. As Laky noted, "In the 'market' it is faced with one single 'buyer', its own enterprise."<sup>214</sup> Thus there is very little the VGМК can bargain over with the manager, and ultimately the latter's interests will prevail. Therefore the VGМК performs the functions which are in the interests of the enterprise manager. For example, in many enterprises with few VGМК's, those that do exist are often not engaged in productive activities, but are often the more highly skilled, but normally less well paid, maintenance workers, who are allowed to form a VGМК so that they can supplement their incomes. This allows the enterprise to hold on to these highly valued and scarce workers.<sup>215</sup>

This leads well into the conflict between the VGМК and the TU. Here the conflict is more readily identifiable. Quite simply, the VGМК "fundamentally undermined the very *raison d'être* of the organized labor movement: its power of collective bargaining."<sup>216</sup> In so far as the TU had

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<sup>213</sup> Ibid., p. 35.

<sup>214</sup> Ibid., p. 34.

<sup>215</sup> Ibid., p. 39.

<sup>216</sup> Noti, op. cit., p. 73.

no control over the VGMK, which employed their workers in socialist enterprise, they could not represent fully their constituency. The clash was magnified in that the VGMK came into direct conflict with the Socialist Brigade Movement (SBM) and the Socialist Work Competition (SMV), a part of Hungary's revolutionary heritage from the late 1950's, and considered by the TU to be an "important shop floor power base."<sup>217</sup> Because of the revolutionary and socialist traditions of the SBM/SMV, its conflict with the VGMK contained an ideological component as well. The struggle had an even wider context though:

Union resistance was all the more determined because the issue was part and parcel of the question of economic and social reforms, including the reorganization of the union movement, and the unions rightly believe that the outcome of this particular struggle would be crucial in determining the future direction of Hungarian trade union reforms.<sup>218</sup>

In the movement of a seeming pluralization of economic life, with the emphasis on interest incorporation, the TU's were gradually moving away from their traditional transmission-belt role, transmitting government policy from above downwards, towards a more representative role, expressing worker interests from below upwards. The battle over the VGMK became a test of the power they would yield as an institution.

Most importantly, the clash was not simply one between the TU and the VGMK's-

Although for institutional reasons union attacks were directed against the government, which was technically responsible for the introduction of the VGMK, the battle was, in reality, joined well and truly by political reformists and conservatives as well and since the issue at stake was the expansion of private enterprise--of which the VGMK were but one although a prominent form--it is hardly surprising that the debates were heated.<sup>219</sup>

This account accords with Varga's discussion of the ideological disturbances created by the introduction of the small ventures, as well as some other accounts. Had not Kadar firmly sided with the reformists, the VGMK would have fallen without doubt.

A recount of the long battle, with all its complexities, would not be appropriate here. Rather, it is more instructive to look at the results as they now stand and analyze them.

The reformists wanted to let the SBM/SMV die a slow death or abolish them outright. This was primarily because they were a relic of a time in which quantitative, rather than capital-intensive

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<sup>217</sup> Ibid., pp. 72-73.

<sup>218</sup> Ibid., p. 73.

<sup>219</sup> Ibid.

qualitative production was emphasized.<sup>220</sup> They were committed naturally to the introduction of small-scale private enterprise as an integral part of their reform package.

The conservatives wanted to halt the expansion of private enterprise, primarily because they feared its consequences, which is understandable given their commitment to Marxist-Leninist orthodoxy. They believed the best way to deal with the present problems were to revitalize and work through the present forms, and thus were very committed to preserving the SBM/SMV.<sup>221</sup>

What then were the results of this struggle. In typical Hungarian fashion, the battle ended in stalemate and compromise. The VGMK was preserved without modification, while the SBM/SMV were revitalized. Yet the survival of the latter could not have occurred without strong conservative support within the HSWP, it is not a sign of TU parity with the HSWP. In fact, the TU leadership was strongly rebuked for taking TU autonomy too literally.<sup>222</sup>

This of course still leaves the problem that the VGMK's are in reality work brigades rather than small enterprises that were to transform socialist industry internally. Laky's comment on this problem is instructive:

I am fully aware of the reluctance of the Hungarian protagonists of the VGMK's to bring about changes because even the smallest changes may trigger off the avalanche that has been threatening the VGMK's with destruction from the very beginning. Nor do they wish to recognize the work brigades for fear that if they were to get out of the safety belt of economic policy still protecting small ventures, the VGMK's would immediately be hamstrung by wage regulation or simply by a final prohibitive decision ... But realities require, sooner or later, a solution.<sup>223</sup>

Obviously, reform will not come easy. The reformists may have preserved the VGMK, but they are preserving an imperfect reflection of their ideal, and it will take awhile before circumstances may be such that they can generate the political consensus to carry the reform through the further necessary steps.

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<sup>220</sup> Ibid., p. 72.

<sup>221</sup> Ibid., p. 72.

<sup>222</sup> Ibid., p. 81.

<sup>223</sup> Laky, op. cit., p. 43.

## 4.4 *Whither Small Enterprise?*

The reforms creating these new forms of small enterprise have not met the expectations of the reformers, and in this regard they can be viewed as less than successful. Unlike agriculture where there has been a long experiment with alternative forms of ownership and production, meaning cooperative farms and household plots, in the traditionally over-centralized industrial sector the introduction of, and experiments with, reform have been more abrupt and less coherent. The Scylla and Charybdis of creating the necessary environment (in all its aspects, that is, both economically and socially), and incentives for reform utilizing private enterprise on the one hand, while staying within the boundaries of acceptable negative externalities resulting from reform, all within the context of building a sufficient consensus within the HSWP to move forward, on the other hand, is indeed a peril fraught journey. What steps should be taken to overcome the shortcomings of the present situation?

Revesz suggests several needed steps. To begin with:

It is necessary to achieve that people have trust in the steady existence of small-scale production and small enterprising sector and in the relative stability of the terms of its functioning. It must be made unambiguous formally and in codified ways that socialist commodity production is a multisector economy where small-scale activities and small enterprises are not only provisional complementary and auxiliary parts but integral elements. By *creating stable conditions* for their activities and by *setting up their representations* which authorities consider real partners and in which *statutory rights* are vested, desirable contributions can be made to creating their business and existential security.<sup>224</sup>

In order to coax entrepreneurs into the legal private sector the HSWP must win their confidence. This requires a clear commitment to this sector and the translation of this commitment into formal actions. For the former this sector must be clearly endorsed ideologically as a legitimate part of a socialist economy, not just provisionally, but as an ongoing integral part of it. Then this commitment must be translated into political and economic reality, where the economic environment is conducive to their functioning, and in the political arena, where they must have a recognized voice in interest mediation. Of special importance is that the market be free of arbitrary interference from the state, which has proven rather destructive of the market.

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<sup>224</sup> Revesz, op. cit., pp. 118-19.

Revesz notes that this ideological commitment also has a social aspect to it. Touching upon the biggest ideological stumbling block to the acceptance of private enterprise in society, Revesz states that "it must be made generally known and introduced in the ideology that the multisector commodity producing socialism is a dynamic economic formation to which there belongs a differentiation (somewhat milder than in capitalism) in the incomes and wealth of individuals and families."<sup>225</sup> In other words, the social status of small enterprise must be settled as well.

Finally, Revesz notes that action must be taken to rationalize the large-scale socialist sector, though he does not discuss this aspect.<sup>226</sup> Varga, however, puts his emphasis on this aspect. In his view, in order to overcome the duality of the Hungarian economy, and all the ideological and economic problems this duality causes, the dominant large-scale socialist industrial sector must be reformed. He writes:

The key to a lasting solution may be found in a consistently implemented reform of the large-enterprise sphere, as a result of which the profit-motivated or self-governing socialist firm, operating as a venture sensitive to the market and costs, would become the basic unit of the economy, and shortage phenomena would cease. This is a basic condition for the consolidation of the existence of small ventures, for transferring the intrafirm ventures in large enterprises to the regular hours of work, and for establishing smooth cooperation between large companies and small-scale businesses.<sup>227</sup>

In this view, the firm implantation of the values of socialist entrepreneurialism, and the restructuring of incentives for its development in large-scale socialist industry are necessary preconditions if the dominant socialist sector will ever allow small enterprise to develop to its potential. Varga notes that this will end the shortage economy, which would not only encourage small enterprise, it would do so at the expense of the unregistered economy, one of the reasons for the introduction of small enterprises in the first place. Only if this occurs will the HSWP have successfully integrated private interests into the economic system it leads.

According to Berend and Ranki,

The increased role of the legalized second economy reflects the determination of the government to control, regulate and tax, but not directly run the national economy as a whole. This is becoming an important element of the Hungarian model.<sup>228</sup>

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<sup>225</sup> Ibid., p. 119.

<sup>226</sup> Ibid.

<sup>227</sup> Varga, *op. cit.*, p. 94.

<sup>228</sup> Berend and Ranki, *op. cit.*, p. 249.

It seems that the price of incorporating private and small group interests into the national economy, especially those interests that currently find their expression in the unregistered economy, in a like symbiosis as that occurring in agriculture, is to extend the above mentioned principle to the large-scale socialist economy as well--in short, for the HSWP to resign itself to controlling and regulating the national economy, rather than trying to run it. Only this may expand the integrative abilities of the HSWP-led system. Whether this is too high a price for the HSWP remains to be seen. As Varga notes, "the negative features of the present situation are natural concomitants of a huge social experiment pointing to a progressive direction."<sup>229</sup> Perhaps the appropriate question then is not if the price of reform is too high, but rather is the price of ineffective reform too high? The great unknown is if there exists a logical dynamic within the course Hungary has begun down that compels them towards greater reform, with reversal coming only at great cost. And moreover, which costs will be seen as greater, that is, will reform that is economically rational require transcending the system of bureaucratic centralism?

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<sup>229</sup> Varga, *op. cit.*, p. 94.

## 5.0 The Unregistered Economy

In the last chapter, it was noted that one of the primary purposes of the introduction of the small enterprises was to bring much of the unregulated private economic activities under government control, to provide a legal outlet for activities that hitherto had been illegal. In this chapter, the discussion shall focus on the challenge this sector poses to the regime, and why it is important for the regime to try and bring these activities under its control.

The most common term used to refer to this sector is the "second economy", but this often includes those private activities that are permitted by the state. As more of the activities in this sector continue to be legalized, the term can breed some confusion about whether one has in mind all market-oriented activities, or just those that have not been legalized. Therefore it is useful to adopt the term proffered by Istvan Kemeny, the "unregistered economy", to refer to those market-oriented activities that have not been formally legalized.<sup>230</sup> The activities in this sector range from the off-white to the pitch-black, that is, some activities are tolerated or even encouraged, while others are strictly forbidden and heavily punished.

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<sup>230</sup> Istvan Kemeny, "The Unregistered Economy in Hungary", in: *Soviet Studies*, Vol XXXIV, No 3, July 1982, p. 349.

What is the basis of the unregistered economy? Part of the answer has already been hinted at in referring to the unregistered economy as market-oriented. According to Kemeny:

the functioning of socialist economies should be understood as being conditioned not primarily by centralized economic planning and then to some extent modified by the market, but rather by both central economic planning and the market working in concert or in contradiction. The market is therefore not a side-issue but one of the pillars of the economy.<sup>231</sup>

The second economy, and primarily the unregistered economy within it, is then based upon the market, and is one of the key pillars of socialist economies.

This view is shared by others. Maria Los argues that the "second economy in its entirety is not, however, based on any idealized informal community exchange economy, but rather on the capitalist principles of the free market, competition, and profit-seeking."<sup>232</sup> This would accord with Varga's conception of a dual economy in Hungary, and, as noted, many of the problems of the small ventures stem from the difficulties of integrating these two sectors based upon different principles.

However, as expressed above, this dual economy does not signify two separate economies that do not interact. How could it be so when the overwhelming majority of workers are employed in the socialist sector? As Kemeny explains:

To be correct, it should be reformulated to state that almost everyone lives *partly*, or--even more exactly--to a *very small extent* from his formal wage or salary. To a far greater extent they live from other activities, from those activities associated with the secondary, parallel, hidden, or, more simply, market economy.<sup>233</sup>

It is assumed that nearly every Hungarian is involved with the unregistered economy to some degree, and both Kemeny and Los believe that Hungary's unregistered economy is the most extensive among the CMEA countries.<sup>234</sup> Kemeny goes so far as to argue that

in Hungary it is the real market, i.e. economic activity which increases GNP, that is predominant ... the growing influence of the market and the positive development of its character have ensured not only the functioning of the economy but also its development.<sup>235</sup>

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<sup>231</sup> Ibid., p. 349.

<sup>232</sup> Maria Los, "The Double Economic Structure of Communist Societies", in: *Contemporary Crises*, Vol 11, No 1, 1987, p. 46.

<sup>233</sup> Kemeny, op. cit., p. 357.

<sup>234</sup> Ibid., p. 361; Los, op. cit., p. 47.

<sup>235</sup> Kemeny, op. cit., p. 361.



Whether or not such an assertion is perhaps generous in its estimation of the character and extent of the unregistered economy is difficult to determine. Los will present a somewhat different perspective on the character of this sector, which will be discussed shortly.

Nevertheless, Los also observes that

In Hungary, where market mechanism have long been given some official recognition, an extremely wealthy second economy elite has emerged and gradually acquired a significant measure of economic autonomy. The bureaucratized, heavy-industry-oriented official economy has grown to depend on the second economy for the satisfaction of consumer needs.<sup>236</sup>

Certainly the household plot of Hungarian agriculture has provided for the satisfaction of consumer demands, but in such a manner that it was integrated into the socialist large-scale agricultural sector. But as also noted in the discussion of the foundations and development of Hungarian agriculture, it can fairly be said that it has the greatest market-conformity of all the sectors of the Hungarian economy. Perhaps this has accounted for the successful integration of individual private interests into the socialist sector of agriculture, while the utter lack of market-conformity in socialist industry has precipitated the rise of a powerful unregistered market economy to compensate for the irrationality of the planned economy. Moreover, it would appear this lack of market-conformity has stifled the development of the legal small ventures which have not been able to integrate themselves successfully with socialist industry, being caught as they are between the distrust of the managers of socialist industry and governmental regulations on the one hand, and the unfettered competition of the privateers on the other hand. This accounts for the adoption of an employee attitude rather than entrepreneurial attitude by the legal small-scale entrepreneurs.

What is more, as hinted at above, Los argues that

despite the radically different economic and ideological principles governing the first and second economies the social structure they produce overlap to a great extent. The class privilege seems to carry over from the first to the second economy. Clearly, the second economy is not a reversal of the prevailing class structure whereby the officially underprivileged class would be able to compensate for its subordinate status through the means of the alternative economy that systematically favours members of that class.<sup>237</sup>

The use of the concept of class is overreaching according to the model of bureaucratic centralism, rather we should speak in terms of strata. Any attempt to argue for the formation of a bourgeois

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<sup>236</sup> Los, *op. cit.*, p. 43.

<sup>237</sup> *Ibid.*, p. 45.

class in Hungary would encounter the same difficulties as positing the development of an oppressive bureaucratic class. We must remember the atomization that occurs in these societies due to the primacy of the political over the economic aspects of the society. Nevertheless, we can posit two oppressive strata that overlap despite their antagonistic relationship to each other.

Why is it an antagonistic relationship? To begin with,

the overall importance of the second economy is highly political. Its continuing existence negates the self-sufficiency of the communist state economy; it frees large areas of economic activity from direct state control ... it may be argued that the second economy represents a "pre-political" counter-ideological sphere which both contributes to and expresses the skepticism about the legitimacy of the dominant economic order.<sup>238</sup>

The unregistered market economy and its relatively autonomous participants represent an ideological challenge to the state in so far as its integrating principle of the market directly challenges the Marxist-Leninist integrating principle of the CPE.

The ideological challenge is embodied in the existential challenge of the unregistered market economy. Los argues that

It is clear that when the importance of the state economy shrinks so does the real base of the Communist Party's monopoly. This process appears to be most advanced in Hungary, where the new financial elite has been able, by means of corruption and the sheer intimidating power of its capital, to secure considerable political influence. In short, the absolute monopoly of the party elite has been weakened by the new competition between private capital and the party's political dominance. Since any crack in the totalitarian (one-party) monopoly over both the political and economic spheres is bound to produce new areas of relative freedom and some leeway for individual initiative and expression, the Hungarian-style second economy must be viewed as a significant test of the limits of ideological change within the Soviet bloc.<sup>239</sup>

The ideological challenge is intertwined with the political and economic challenge to the HSWP's control over Hungarian society. The monopoly over the apparatus of coercion remains with the state, and is used to check the power of the unregistered economy and its participants, though more often than not that power is utilized against the atomized more vulnerable actors in the unregistered economy. However, the coercive apparatus can only check the power of the market and its participants, it cannot control it nor eliminate it--it makes participation in it more risky. But in so far as steering problems in bureaucratic centralist societies like Hungary become legitimation problems, and the HSWP is constrained to rely upon the unregistered market economy to meet consumer

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<sup>238</sup> Ibid., p. 46.

<sup>239</sup> Ibid., p. 47.

demands and rationalize the CPE, it detracts from the political and economic control of the party over Hungarian society, perpetuating the legitimation crisis. So while the HSWP must rely on the unregistered economy and its elites, it is nevertheless a marriage made in hell, an uneasy mutually interdependent relationship.

However, the antagonistic yet compensatory relationship of the unregistered economy to the planned economy generates serious contradictions:

This reality suggests that in the long run the second economy is bound to create its own elite and to add to the exploitation of the already oppressed and powerless population. In sum, the second economy appears to contribute to the continuation of the dominant economic relationships while at the same time eroding the ability of the bureaucratic party-state to effectively control and manage the society. This contradiction characterizes well the essence of the second economy's role within the studied societies and explains the ambivalent nature of the policies adopted by the authorities.<sup>240</sup>

The dual economy has engendered a dual stratification, in which the elites of the two find themselves enmeshed in a perverse parasitic mutual dependency. Existential concerns such as an insufficient official income motivate the majority of minor participants in the unregistered economy, but they and those who do not have the opportunity to participate in the unregistered economy find themselves exploited further by the two elites. Hence the complaints of exploitative get-rich-quick privateers is coupled with a continuing alienation from the party-state who cannot meet their existential needs, and further have an ambiguous relationship with the privateers. While the unregistered economy meets these existential needs, it does so at an increasing cost, generating further contradictions as the majority of the population slides below the poverty line, unless the individual can finally earn in twelve hours of official/unofficial work what he should be able to make in a normal workday.

Kemeny makes an insightful comment on how the rationalizing effect of the unregistered market economy nevertheless generates contradictions in economic policy because of the state's inability to control the national economy, which renders the plan irrational:

The greatest problem of Hungarian economic policy is that it is seeking the path of salvation blindfolded. Its efforts are tragi-comical because their starting point is unreal: the authorities have little idea of the actual size of the GNP, of the sources from which it is derived or the way it is used, nor of the amount and the distribution of the population's income, the quantity and productivity of work or the places where it is carried out.<sup>241</sup>

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<sup>240</sup> Ibid.

<sup>241</sup> Kemeny, *op. cit.*, p. 365.

While the unregistered economy compensates for the inability of the planned economy to meet the existential needs of the population, the uncontrollable and incalculable nature of this sector make planning increasingly irrational, perpetuating a vicious circle. This also accounts for the periodic crackdowns on the unregistered economy, as the state attempts to restore some rationality to economic planning by striving to control the unregistered economy.

Los does recognize the unusual nature of Kadarist social policy, which is more tolerant of the individual to meet his existential needs through the unregistered economy, which constitutes the bribe offered:

Sometimes, however, a trade-off may be possible and a temporary balance established. In Hungary, for example, the population has been offered a freer second economy in an implicit exchange for a ban on any independent political expression. Thus, out of the fear of losing both, the society may be pushed to accept the party's concession in one area at the cost of another area.<sup>242</sup>

This is a concise summation of the Kadarist "bribe" offered for support, as the regime attempts economic rationalization through reform to integrate individual and group interests into the state-run system.

The most successful expression of this, as noted, has been the household plots in agriculture. This success, as well as the increasing contradictions in socialist industry, for all the previously discussed reasons, has stimulated further efforts to translate this success to other sectors. Janos Kornai, a prominent Hungarian economist, has summarized concisely the tolerance of Kadarist policy towards the unregistered economy and the attempt to translate agricultural successes to other sectors:

There is a deliberate effort to legalize formerly illegal activities, or to be tolerant of ambiguous cases, provided that these activities are regarded as socially useful or at least not harmful. This tolerance awakened tremendous energy in a large part of the population. It is certainly not a very satisfactory organization of human activity; it is full of conflicts and unfair actions, but still, without the tolerance, this energy would remain dormant.<sup>243</sup>

Kornai recognizes both the usefulness and the contradictions of this tolerance and attempt to integrate private interests into the state-led system to bring some rationality into the economic system while attempting to gain greater control over it. While these efforts may temporarily relieve tensions

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<sup>242</sup> Los, *op. cit.*, p. 52.

<sup>243</sup> Janos Kornai, "The Hungarian Reform Process", p. 1708.

in the system and the society, it does not provide a long-term solution for the contradictions still apparent in the inadequate efforts to mesh two different principles of integration.

The question becomes then how does the party-state overcome the impasse of the dual economy and the negative externalities it creates? Los sees two alternatives:

A growing detachment of the society from its ruling apparatus may lead eventually to a situation where the power elite is really pretending that it is ruling but in fact it is simply living off the mis-managed state economy and exercising a ritualistic control over the state. On the other hand, however, it may lead to the elite's attempts to revise the very principal of the total party monopoly in order to save at least a partial one. This may involve a recognition of the market consumer economy as fully compatible with the dominant ideology and a legitimation of a mixed economy model.<sup>244</sup>

Hungary has hesitantly opted for the latter course, believing that it can integrate individual and group interests into a socialist market economy in which the market is organically joined with the plan, and in which the HSWP plays the role of supreme arbiter in interest mediation. In so far as this would be successful, it would also subvert the unregistered economy by driving it *aboveground* as it were.

This was the intention of the HSWP with the small ventures, and in that sense they comprise an important part of their battle strategy against the unregistered economy--to bring the unorganized participants of the unregistered economy, in the very least, into the legal (and therefore regulated) economy, and thus hopefully to undercut other elements by the resulting rationalization of the economy. Rezsó Nyers states as much in his discussion of the small ventures:

On the other hand it provides a legal form for such activities which earlier had found their place in the illegal or semi-legal "second economy". The process evolving under the slogan "with small ventures against the second economy" has been unambiguously successful--despite the accompanying concerns and problems--but time is needed for their completely smooth fitting into society and the market relations need further development for a complete suppression of the second economy.<sup>245</sup>

The problems of this integration have already been discussed, those being the failure to implant the new values of socialist entrepreneurialism most everywhere, and the failure to further develop market relations, as Nyers says, in the large-scale socialist industrial sector such that this sector would be profit- and cost-sensitive. Whether or not this will be possible, or whether the political costs will be too high remain to be seen. These issues will be addressed in the concluding chapter.

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<sup>244</sup> Los, op. cit., p. 53.

<sup>245</sup> Nyers, op. cit., p. 11.



## 6.0 Whither Hungary?

The reforms discussed in this study have attempted to increase economic rationalization and efficiency in order to stimulate intensive development and improve the standard of living while at the same time integrating private interests into the state-led economic system. The paradox of the process is that by allowing an alternative to working for the state, that of small-scale private entrepreneurship, in the legal economy, these private producers would be under governmental control to a much greater extent through their integration into the legal economy than they were in the unregistered economy.

This process has been most successful in the agricultural sector with the household plots and subcontracting out the raising of livestock. It has been suggested that the market-conformity of socialist agriculture and incentives offered to state and cooperative farm managers to stimulate small-scale production have been responsible for the successful symbiosis of large-scale socialist agriculture and small-scale private agricultural production.

It is exactly these factors that have been lacking in socialist industry, which accounts for the modest successes of the small ventures and the continued importance of the unregistered economy. Furthermore, the new values of "socialist entrepreneurialism" have been incompletely implanted in all the strata participating in socialist industry and in Hungarian society in general. This is due

to the unresolved ideological debates surrounding these values and to the persistence of a dual economy, in which socialist industry remains overly centralized and hierarchical in internal structure, more interested in preserving its monopoly position than in becoming market and cost sensitive. In short, these multiple ideological and structural failures redound upon each other in a negative manner.

While the regime has long been tolerant of the second economy, the increased importance and internal stratification of the unregistered economy has posed several challenges to it. A pragmatic approach to the ideological and economic challenge of the unregistered economy has been followed by the HSWP in return for an undisputed monopoly over the political life of the nation. Los has suggested that the financial power of the leading privateers has had a corrupting and corrosive effect on the leadership provided by the HSWP, in which its political and economic monopoly has been challenged, and its ability to manage the economy and control society has been impeded. Kemeny has argued that the importance of the unregistered economy has made central planning increasingly irrational, which poses a threat to the regime.

The result of the affluent lifestyle of the elite privateers, the stratification of society between the political and privateer elites on the one hand, and the rest of the population (in which much of the population, especially those in dual subjection to the two elites, continue to slide below the poverty line), on the other hand, has been to exact an increasing ideological and political cost to a regime which is sensitive to the goodwill of the people.<sup>246</sup> This dilemma is furthered by the inability of the regime to manage the economy, due in part to the importance and incalculable effects of the unregistered economy.

This impasse between the dominant and largely inefficient socialist industrial sector and the irrational effects upon economic planning of what Kemeny calls the "rationally and strategically ordered free market" (and also of the ongoing integration of Hungary's economy with that of the

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<sup>246</sup> Los, *op. cit.*, p. 47; on the concept of dual subjection, see: T. Kolosi, "Structural Groups and Reform", in: *Acta Oeconomica*, Vol 37 (1-2), 1986, p. 19.



Western international capitalist economy), has pushed Hungary towards the discussed reforms, and will continue to push it further along this road.<sup>247</sup> As Rezso Nyers stated:

Both the present situation and the forecasts about the future argue for the reform, thus the reform process relies on an objective situation and on objective interests. As such, it is essentially an irreversible process in Hungary.<sup>248</sup>

The question then becomes what measures become necessary to render reform successful.

As stated earlier, Hungary is progressing towards a socialist market economy, in which the market is organically linked to the plan, while integrating group interests into the national economy through both integrating principles. In order to attain market conditions the monopolistic position of much of the overly-centralized socialist enterprises must be broken, and their hierarchically organized bureaucratic management style must be dropped in favor of more open and entrepreneurial methods to increase profit and cost sensitivity. This desired new style of management is embodied in socialist entrepreneurialism. Also, administrative interference into enterprise management and the market must be sharply curtailed, while a restructuring of incentives must be shaped to encourage risk-taking. Nyers outlined several measures introduced and the agenda for the second half of the eighties to accomplish these goals.<sup>249</sup> As noted earlier, these changes are necessary to unleash the competitive capabilities of the small ventures, which is also necessary for a socialist market economy. As Nyers observes,

It would be a mistake and an error to reduce the problem to the confrontation of "large-scale factory or small establishment", because none of them can squeeze out the other. In this respect the socialist countries were on a false track for a long time and, therefore, the small economic organizations offered more to the consumers under capitalist conditions.<sup>250</sup>

The integration of small ventures into the socialist market economy will therefore also undermine the unregistered economy, and the negative externalities it causes. Control over the unregistered economy is not the only goal of economic reform, however, for as Nyers also states:

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<sup>247</sup> Kemeny, *op. cit.*, p. 358.

<sup>248</sup> Nyers, *op. cit.*, p. 10.

<sup>249</sup> *Ibid.*, p. 9.

<sup>250</sup> Nyers, "Efficiency and Socialist Democracy", p. 6.

It is of fundamental importance for the implementation of societal policy that the central control over macroeconomic processes should not diminish, it ought to increase rather in the context of the economic reform process.<sup>251</sup>

The cumulative effect of the reforms should be to make economic planning more rational to render social policy, which aims at social management, more efficacious.

The desired goal is to legitimate the system by improving its performance while integrating individual and group interests into it. As Nyers notes about the goal of reform:

An economic democracy based on a satisfactory balance of interests ought to lead, eventually, to a higher level of "economic tolerance" towards each other, and to a more conscious and more organized order in the social cooperation among groups, enterprises, sectors and occupations.<sup>252</sup>

This is strange talk when one considers that the effect of what Arato referred to as the fusion of base and superstructure and the domination of the state over the economy has been the atomization of the politicized society, which has served for the most part to prevent the joint articulation of interests of various strata vis a vis the state. Kadarist policy in particular has sought to neutralize political opposition through the piecemeal integration of different interests into dependent relationships upon the state. Yet economic democracy, which Nyers seems to equate with socialist democracy (as shall later be argued), suggests that various interests can be integrated into the socialist market economy such that conflicts of interest will not develop into full-scale contradictions amongst various strata or between certain allied strata and the state.

A subject of increasing importance as these reforms have unfolded and failed to meet expectations is that of socialist democracy, and the need to modernize the state in order to make it compatible with the economic reforms. Some reforms have already been touched upon in discussing the measures required to develop the socialist market economy. Nyers cut to the core of the debate surrounding the interrelationship of political to economic reform when he notes how

widespread the opinion is that human action striving after efficiency either does not tolerate democracy or accepts it to a limited extent only; and, according to this concept, democracy also works against people undertaking sacrifices for the future in any given case. Accordingly, democracy can only assert itself in the case of plenty and richness, while efficiency can only be based on authoritarian decision and discipline ... Whether efforts at economic efficiency can be coupled *in metrio* with the developing socialist democracy is a fundamental problem of the future development of the East European socialist countries, Hungary being among them. If our present assumptions are verified, the two efforts will help each other; if, however, it turned out later that democracy had still to be constrained in the interest of an "efficiency breakthrough"--and the latter is no doubt a harder

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<sup>251</sup> Nyers, op. cit., p. 15.

<sup>252</sup> Nyers, op. cit., p. 11.

requirement--then intensive economic growth and the cause of democracy would get separated from each other. The former would develop *better than the latter*.<sup>253</sup>

It is the view of the reformers within the HSWP that it is dangerous to develop the former without the latter because the danger exists that "what is won on the swing is lost on the roundabout."<sup>254</sup>

An interesting expression of this sentiment is provided by the Hungarian economist Zsuzsa Ferge:

Ultimately, the economic reform in Hungary is meant to improve living and working conditions and to contribute to the legitimation of the system. However, the economy cannot solve all the problems by itself. Genuine legitimation presupposes genuine participation, and this implies a change not only in the economic, but also in the social and political arenas. If old and new tensions can be legally resolved in revitalized political institutions, then the process of legitimation may be successful. That is why the economic reform has to be combined with political and social policy reforms.<sup>255</sup>

The political institutions need to be revitalized so that more interests can be integrated into the political arena, participating in the competition for political goods. If this can be accomplished, then it is believed that socialist democracy can be legitimated.

However, we must be careful about what is meant about democracy, for as Nyers warns us, socialist democracy is not the same as "bourgeois democracy". He presents the interesting analogy of a competition between the two that is not zero sum, likable to warfare, but "may rather be compared to collating performances, with the difference that the competing systems also cooperate during the competition."<sup>256</sup> Interdependence and coexistence are pragmatic and humanitarian conditions of the competition. It is to be used as a "propelling force", although Nyers does not argue for convergence, rather "the socialism of the future demands that we surpass bourgeois democracy."<sup>257</sup>

Nyers defines the difference and historical divergency of the two concepts of democracy as follows:

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<sup>253</sup> *Ibid.*, p. 1.

<sup>254</sup> *Ibid.*, pp. 1-2.

<sup>255</sup> Zsuzsa Ferge, "The Crisis and the "Welfare State" in Eastern Europe with a Focus on Hungary", in: *European Economic Review* 31 (1987), p. 219.

<sup>256</sup> *Ibid.*, p. 3.

<sup>257</sup> *Ibid.*, p. 2.

the notion of democracy obtained different interpretations in the social fights of the last century: the bourgeois notion of democracy is related to governing the *state*, while the socialist notion of democracy *expands into social democracy*, where *economy and culture* get a central place.<sup>258</sup>

This explains why socialist democracy and economic democracy are more or less interchangeable terms. The focus of socialist democracy is not on opening up the state as an arena for the competition of interests, that is, upon formal political rights and privileges, but upon using the state to regulate economic rights, to integrate economic interests into the economic system through the planned economy, in which the party plays the role of mediator.

This can be seen in Nyers' discussion of the use of power in the public interest in socialist democracy:

It can be verified that the activity of the economy as a whole is indeed directed at improving the economic and social situation of wider groups of the population than that of systems of capitalist types. This becomes possible because the state power of a socialist type disposes of the resources of the economy across a wider range, and because the socialist political systems are capable of integrating a greater range of different economic group interests in fact almost totally, through the socialist planned economy.<sup>259</sup>

This is still the dominance of the state over the economy. Democracy is economic interest mediation in the context of a planned economy rather than the bourgeois focus on formal political rights and the state.

Given this emphasis, Nyers' definition of the main requirements of democracy should come as no surprise. He writes that

democracy can only operate well and purposively in the whole of the economic process; that is, only if it permeates *the whole* of economic life, for a *partial* democracy can only have a limited impact. Thus, the main requirements of democracy are: the participation in decision-making of representatives of every interest; an understanding and acceptance of the majority decision by the minority; open and democratic checking of the economic processes; and an effective feedback system in economic control activities in the interest of making corrections already underway.<sup>260</sup>

Naturally certain interests are prohibited from developing, namely large-scale bourgeois capital. This also raises questions concerning the increasing role of foreign economic interests, and how they will be represented. While small enterprises will have an institutionalized voice in this system, given the regimes commitment to a multisectoral economy, this will not endanger "the dominating role of the state and cooperative sectors in the economy," which seemingly will perpetuate their disad-

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<sup>258</sup> Ibid., p. 3.

<sup>259</sup> Ibid., pp. 3-4.

<sup>260</sup> Ibid., p. 8.

vantage vis a vis the larger sectors.<sup>261</sup> In fact, this version of democracy rather appears like a new version of corporatism, in which the party-state reconciles various economic interests in the context of a planned economy, albeit one that attempts to harness the market to increase economic rationality and efficiency in planning. As Nyers states, "In a multisectoral socialist economy, governmental economic control has still to be developed for some time in the interest of a harmonious cooperation between sectors and their good fitting with each other."<sup>262</sup> Given that the government desires firm control over macroeconomic processes for the implementation of socialist objectives in social policy, governmental control to insure harmonious cooperation between sectors may well become a regular feature of the system.

With this in view, we may turn to Nyers' summarization of the agenda for the development of socialist democracy in the eighties. He writes:

We may call it a task on the agenda of the eighties that the worker-peasant democracy has to be expanded, on an even wider social basis, into a true people's democracy. Also, it must bring about and simultaneously operate its political, economic and cultural systems of institutions. In this process every group has to join institutionally, relying on its own interests, yet on the basis of a strong alliance of interests between manual workers and intellectuals. The Party, playing the leading role, no longer represents merely a class interest, but integrates the social and political forces. It does not merely declare social interests, but forms and expresses the social consensus in the major problems.<sup>263</sup>

This is an ambitious corporatist project indeed, integrating all the legally institutionalized interests into the planned economy, though socialist ideology requires a formal emphasis be given to the interests of workers. Yet it must be emphasized that the integrating principle remains to be the leading role of the party, working through the centrally planned economy.

The substance of democratization and the devolution of power thus comes at the level of planning, which attempts to integrate more interests, and the granting of more autonomy to the state and cooperative enterprises while developing a multisectoral economy, in order to create a competitive socialist market economy. The HSWP, while remaining the mediator of interests, will no longer attempt to simulate the activities of the market through administrative measures, but desires to give substantive autonomy to the socialist enterprises. Democratization thus most pow-

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<sup>261</sup> Ibid., p. 10.

<sup>262</sup> Ibid.

<sup>263</sup> Ibid., p. 8.

erfully should occur at the enterprise level, dropping bureaucratic management methods in favor of more democratic management methods.<sup>264</sup> The primary example of this should, when the economic environment has progressed sufficiently, be the dropping of administratively controlled wage policy in favor of a "wage bargain" between the TU's and the enterprises, though even then this shall be "carried on within the framework of the national economic plan and with government coordination."<sup>265</sup> The reason presumably being the desire of the government to be able to control macroeconomic processes. This will also presumably be matched with continued administrative oversight of the small ventures so that large-scale industry might not be at too much of a disadvantage against the more flexible small ventures.

Socialist democracy does not seem to be too far removed from what the respected Hungarian economist Janos Kornai has termed the "medium state", one between the "minimal" or "night-watchman" state (limited to protection of the citizen against violence and theft, plus the enforcement of voluntary contracts), and the "maximal" state, to which the Stalinist model approached.<sup>266</sup>

He describes the medium state as follows:

One cannot associate with this concept any notions of "optimality". Let us start with some normative ideas. In discussions of the role of the state among political scientists, economists and philosophers, three functions are mentioned: (1) Active governmental macro-policy is needed for stabilization, full employment and balanced economic relations with the outside world. (2) Governmental activities are required to combat adverse externalities and ensure the appropriate supply of public goods. (3) Governmental redistribution of income is called for on the grounds of social justice and in order to support the poor and weak. Let us use the term "*justifiable medium state*" for a state in which governmental activities are restricted to those which serve at least one of these three functions to a substantial extent.<sup>267</sup>

It should be noted that Kornai's focus is upon the individual's economic freedoms, that is, "the right of the individual to dispose freely of wealth, of income, of time and of effort," as opposed to political or intellectual freedoms, which he views as other matters.<sup>268</sup> The medium state therefore offers more opportunities to exercise these freedoms, though they are restricted in the interest of

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<sup>264</sup> Ibid., pp. 11-12.

<sup>265</sup> Ibid., p. 12.

<sup>266</sup> Janos Kornai, "Individual Freedom and Reform of the Socialist Economy", in: *European Economic Review* 32 (1988), pp. 239-41.

<sup>267</sup> Ibid., pp. 262-63.

<sup>268</sup> Ibid., p. 235.

any of the above mentioned functions of the state, though primarily in the interest of social justice and welfare. Thus the extension of freedoms in the medium state he is discussing does not entail traditional bourgeois political freedoms. In fact, socialist democracy, as described, did not include the extension of these freedoms.

Kornai views recent Hungarian developments as moving towards this medium state, although he makes a realistic assessment of this process:

one should not expect the end result of the reform process in socialist countries to be a "justifiable medium state" or the realization of any well thought-out blueprint embodying the three reasonable functions mentioned earlier. It will certainly not be an embodiment of a rigorous normative theory but will be an arbitrary, ad hoc medium state, arising out of improvisations, myopic political struggles, pressures and counter-pressures, innovation and inertia, and compromises between a yearning for the expansion of liberty and a temptation for its restriction. On the one hand such a state will retain governmental activities not needed for the performance of the three justifiable functions. On the other, some of the three functions may remain partly or completely unperformed, just as they have been up to now.<sup>269</sup>

This has characterized the Hungarian process, as they have reacted to economic crises. The discussion of the small ventures pointed to this.

As has also occurred in Hungary, Kornai sees in this process a heterogeneous coalition of groups that push forward the reform process, one that is united more out of necessity than like-mindedness. He notes that

The cement holding the "coalition" together is precisely the ever acute danger of reversal; the fear that things may take a turn for the worse. Ultimately, this cohesion may contribute to a stabilization of a "medium" state in which the opposing political and social forces, the ideologies and the systems of ethical values are delicately balanced.<sup>270</sup>

The economic crises have so far this decade held together the coalition of reform in Hungary, as they have sought to press the logic of their reforms forward, in the hope that this will turn the economic crisis around. In a similar vein, T. Kolosi has attempted to examine the structural groups that have pro- or anti-reform interests, and argues that those strata that should be pro-reform seem to be in the ascendency, and he envisions a model in which the old hierarchical redistribution model, and two reform oriented models, a market reproduction model and a corporate-reconciliation-of-interests model, will evolve into a system of relations "in which the mutually-correcting influences of all three reproduction models (of equal rank) can institutionally assert

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<sup>269</sup> Ibid., p. 263.

<sup>270</sup> Ibid., p. 265.

themselves in all spheres of the reproduction of social conditions."<sup>271</sup> It has been previously argued that elements of all three models appear to be present in the presentation of socialist democracy by Nyers.

How should we interpret these views of the direction of Hungarian reforms in terms of the model of bureaucratic centralism and the crisis of legitimacy? Arato described the bureaucratic centralist societies as ones in which the base and superstructure were fused together, society is politicized, and the state ensures the dominance of the political over the economic. The principle of integration is the party-state, and the instrument is the economic plan. Although there is an antagonistic relationship between the party-state elites and the population, it is made socially anonymous by the plan. In the elaboration of socialist democracy, the fusion and the politicization of society persists, and socialist democracy, as economic democracy, maintains the dominance of the state over the economy. The party and plan as principles of integration also remain regulative, and the social anonymity of the antagonistic relationship is well disguised under a planned economy that promises it can integrate all legitimate economic interests into itself. However, Arato noted that the move towards a pseudo-market, one of two options the party-state elites could choose to try and resolve the crisis of legitimacy, ultimately cannot solve the contradictions between the political requirements of the plan and economic rationality, a global plan remains an impossibility. This suggests that Hungary's move towards a socialist market economy (which nevertheless contains corporatist elements), cannot resolve the contradictions of the plan, though it may succeed in making these contradictions more socially anonymous as well. Given that the Achille's heel of Soviet domination prevents a move towards the nation-state, as opposed to party-state, as the other option to resolve the crisis of legitimacy (that is, an appeal to nationalism as a mode of legitimation that is divorced from norms that require justification), it would seem that in the long run these measures, if they progressed as expected, would still fail to resolve the crisis of legitimacy.

However, things have not progressed as expected, and, indeed, the last several months (from the Fall of 1987 to the present time), has seen a remarkable turn of events. November of 1988 has

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<sup>271</sup> T. Kolosi, "Structural Groups and Reform", in: *Acta Oeconomica*, Vol 37 (1-2), 1986, p. 25.



seen some of the most surprising speculations in Eastern Europe since the Prague Spring of 1968. Certainly no final assessments or predictions can be made, but it would be instructive to examine the recent events in light of the previous examination, the model of bureaucratic centralism, and the crisis of legitimacy.

If there were any doubts by the middle of 1987 that the economic crisis was becoming critical indeed, the publication of "Turning Point and Reform" under the auspices of the rejuvenated and daringly liberal People's Patriotic Front put those doubts to rest. It began with the assertion that "The experience of the 1980's, and especially from 1985 on, indicates that Hungary's economy is in very dire straits."<sup>272</sup> After describing the history and nature of the problems, it declared that the "time is ripe for comprehensive, radical, democratizing and decentralizing market reforms."<sup>273</sup> An extensive number of proposals were made, entailing both economic and political reforms. The most radical, from the point of view of the integrating principles of bureaucratic centralism is that the leading role of the party, while still theoretically valid, in practice would appear to be rather diluted in favor of a more powerful National Assembly. They suggest that it be made possible for "deputies who promote their own independent platforms during the campaign freely to form their own blocs in the National Assembly," and that the "role of lawmaking, as well as the personal and contextual determination of government policies, should be concentrated in the hands of the National Assembly."<sup>274</sup> From the nature of the proposals made, it would seem theoretically possible that the HSWP could find itself in a position in which it would have to share power.

In the response by the Working Group on the National Economy, a group under party auspices, there was much agreement on a variety of topics. However, there was a great parting of paths concerning the formation of blocs in the National Assembly and in the role of the party in general. In their view,

While maintaining and strengthening its leadership role within society, the party must take on new tasks required to advance the reform process, and it must exercise political leadership over the same

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<sup>272</sup> Antal et al., p. 5.

<sup>273</sup> Ibid., p. 23.

<sup>274</sup> Ibid., p. 39.

process. Substantive and comprehensive programs that are absolutely necessary--including the inevitable unpopular measures--cannot be executed without the party.<sup>275</sup>

The economic disagreements, though substantial at points, were a matter of different emphases. The former stressed monetary policy in reform, while the latter stressed structural reforms. However, it was in the issue of the role of the party that the part in ways had implications concerning the core components of bureaucratic centralism. The HSWP was not willing to share power.

However, all was not well within the HSWP. As the economic situation continued to deteriorate, it became apparent that the Kadarist "bribe" was becoming unglued, as unofficial political groups began to organize spontaneously, challenging the HSWP's monopoly over the political life of the nation.<sup>276</sup> Kadar seemed more and more out of touch with reality in the economy, in society, and within his own party. As one observer of Hungary put it:

As the Kadar regime tried to muddle through the second half of the 1980's, the clouds darkened over its head, public morale declined, and since the summer of 1987 an outright crisis became evident. The paternalistic relationship between Kadar and the people steadily declined as age and fatigue took their toll on him. The once vital leader was increasingly unable to provide real leadership and carry out the comprehensive and radical reforms urgently needed to pull Hungary out of its quagmire. He had increasingly come to look like a conservative who was afraid to take risks and clung to old habits and practices.<sup>277</sup>

On the last day of a special three day HSWP Special Party Congress, May 22, 1988, after 32 years in power, Janos Kadar was replaced as the party leader by Prime Minister Karoly Grosz. Kadar was given the honorary position of party Chairman, a new position which does not have defined responsibilities. He lost his position on the Politiburo, but not on the Central Committee.

Kadar's legacy is a people who were bought off, but never won over. Kadar cautiously, yet pragmatically cultivated a system of incentives which integrated the important groups of a stratified and demoralized society into a series of often mutually contradictory dependent relationships upon the state. The goal was always to monopolize political activities, extend control over economic life, and consummate the process by reconciling the people to the system on the system's terms, such that the system would be held legitimate by a people it controlled. The reform process would begin

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<sup>275</sup> Working Group on the National Economy, "Statement of the Working Group on the National Economy", in: *Eastern European Economics*, Vol XXVI, No 4, Summer 1988, p. 57.

<sup>276</sup> see: *Christian Science Monitor*, November 28, 1988, p. 10; *Washington Post*, December 5, 1988, p. A19.

<sup>277</sup> Alfred Reisch, "An Assessment of the Kadar Era", in: *Radio Free Europe Research*, Vol 13, No 22, Part 3, p. 24.

by ensuring the support of the people, and would end by integrating them into the system. In the end, the people held out longer than Kadar. As he lost the energy and fortitude to see his project through, he lost the hush money of an acceptable standard of living, and the bribe began to fall apart. He lost not only the support of the people, but also of the party he had run for over three decades. He was overtaken by the momentum of a system he had created. A new generation will raise the ante even higher in an attempt to preserve as much of Kadarism as is possible. It is ironic that Kadar was removed so that Kadarism might be salvaged, that the "bribe" might be reestablished.

Speculation over Kadar's future in the party grew rampant in the spring of 1988 as it became clear that Karoly Grosz was making a play for Kadar's position. His position was helped by growing dissatisfaction not only within society, but also within the party, most markedly among the middle cadres. These cadres were caught between the Scylla and Charybdis of rising popular discontent and the deteriorating central leadership which could provide neither the direction nor assistance the middle cadres desired. In addition, intellectuals within and outside the party became increasingly critical of the failings past and present of the party, and openly debated "the need to reconsider its leading role, and for more institutionalized pluralism and economic liberalism."<sup>278</sup> A crisis of confidence in the old guard around Kadar grew:

This crisis of authority and legitimacy had a deeply demoralizing effect on the party itself and on its dependent organizations. According to official sources, some 45,000 members have left the party in the last year, although by now the number is probably twice as high. Most basic units have simply ceased to function. The Communist Youth League's largely inactive membership has fallen from 900,000 in 1986 to 720,000; and its leadership in desperation jumped on the bandwagon of radical reform. Growing numbers of workers have been deserting the official trade unions. Attempts have been made to create a trade union of scientific and academic workers and a youth organization outside the official structures. The center was not holding.<sup>279</sup>

Kadar made some last minute attempts to restore party discipline, but by and large his efforts only "aggravated the party's malaise, and the delegates to the conference, most of them middle-level cadres, were out for blood."<sup>280</sup> When the dust settled at the conference, a victory for the radical reformers emerged that was unparalleled in party history.

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<sup>278</sup> A. Nicholas, "Kadarism without Kadar?", in: *Radio Free Europe Research*, Vol 13, No 22, Part 3, p. 25.

<sup>279</sup> *Ibid.*, pp. 25-26.

<sup>280</sup> *Ibid.*, p. 26.

Kadar and seven other veterans of the Politburo, most closely associated with the grand old man, lost their positions, and all but three of the eight were not reelected to the Central Committee. All five of the recent appointees to the Politburo, three of whom were appointed in 1985 (including Grosz), the other two in 1987, retained their positions. Only six new members were named to the Politburo, however, bringing its size down to eleven from thirteen. The two most notable appointments to the Politburo were Rezso Nyers, father of the NEM, whose political career had stalled with the reversal of the reform program in the mid-seventies, and Imre Pozsgay, the darling of Hungarian intellectuals for his outspoken support of political reform, and the only other member of the political elite besides Kadar to enjoy any amount of popular support. The appointment of Pozsgay can also be viewed as a political comeback. In 1982 he was sacked as the Minister of Culture at the instigation of one of Kadar's old cronies, due to his liberal views. He was appointed to head up the moribund People's Patriotic Front, which he transformed into a vibrant forum for the discussion of a variety of topics and views. It is somewhat symbolic that as he was elevated to the Politburo, the Kadar crony who had him demoted was dropped from it. Two other strong voices for reform were added to the Politburo, Miklos Nemeth, a well respected economist, and Ilona Tatai, the second woman appointed to the Politburo, and the director of the Taurus Rubber and Tire Company, one of the most progressive firms in Hungary. As for Grosz, there is much speculation whether his transformation from a dogmatist to a Hungarian version of Gorbachev is genuine or self-serving. Nevertheless, the energetic and determined manner with which he sought to turn around Hungary's economic crisis when, in a surprise move in 1987, he was appointed Prime Minister have earned him a measure of respect within the party. More importantly perhaps, in "regard to reforms, his thinking and actions clearly resemble those of Soviet party leader Mikhail Gorbachev; and Grosz has obviously won his sympathy and support," although it was reported that for the first time the Soviets did not play a direct role in the election of a new Hungarian party leader.<sup>281</sup>

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<sup>281</sup> see: Alfred Reisch, "Grosz Replaces Kadar as Party Leader", in: *Radio Free Europe Research*, Vol 13, No 22, Part 3, pp. 3-7; Economic Intelligence Unit, *Hungary: Country Report*, No 3, 1988, pp. 7-8.

Since the reorganization of the upper echelons of the HSWP, events have, by East European standards, moved fast and furious. According to Ivan Lipovecz, editor of the respected economic weekly HVG, "This is the year of pluralism in Hungary. After the leadership changes in May, everybody suddenly changed, and people felt a new-found strength."<sup>282</sup> Over the last several months a number of groups have sprung up, concentrated mostly in Budapest, and united only in their desire to present an alternative to the official party-sponsored groups. In fact, the groups have divided upon lines similar to the pre-Stalinist period of 1944-47.<sup>283</sup> On the right are the nationalists/populists in the tradition of the Smallholder's Party, the most powerful party of that period. Not surprisingly, its seeming successor, the Democratic Forum, is the most popular of the new groups. In the middle of the spectrum, the Circle of Young Democrats are Western-style Democrats who are the heirs of the old Liberal Party. They are also called the "urbanists" because many of them are Jewish intellectuals who were the isolated dissident elite in Budapest's intellectual ghetto. They have close ties with the ecological movement in Hungary and with the alternative youth organization, the League of Young Democrats. On the left would be the radical reformists of the HSWP, such as Nyers and Pozsgay, who are in their outlook like the old Social Democrats.

While the emergence of these groups is noteworthy phenomena, even more important is that Hungary is moving towards a new Law of Association that will provide a legal framework for such groups, and may eventually culminate in the development of a multiparty democracy in Hungary. The HSWP is preparing what has been called a "democracy package" that over the next 18 months will establish personal and political liberties such as the freedom of association, freedom of the press, freedom of religion, free labor unions, and the right to form independent political groups.<sup>284</sup> Within two years a new constitution should be completed that most party leaders expect will provide for a return to a multiparty system in which other independent parties may compete with the HSWP for seats, though they will not be able to assume control of the government.<sup>285</sup> In an inter-

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<sup>282</sup> *Christian Science Monitor*, November 28, 1988, p. 10.

<sup>283</sup> *Ibid.*

<sup>284</sup> *Washington Post*, December 5, 1988, p. A1.

<sup>285</sup> *Ibid.*

view with the *Christian Science Monitor*, Imre Pozsgay stated "I think the multiparty system is unavoidable. It should be realized within two years."<sup>286</sup> While Pozsgay might be expected to push for such political reforms, even Grosz is reported to have stated to the Central Committee around the same time that he had accepted "the position that we should advance toward a multiparty system."<sup>287</sup> However, there is disagreement over the nature this multiparty system should have, if it is implemented. In the view of Justice Minister Kalman Kulcsar any leading rival political party would have to work in coalition with the HSWP in parliament or otherwise recognize the leading role of the HSWP and its ultimate control of the government.<sup>288</sup> While such a view is likely to prevail, as important a figure as Pozsgay presents another view. Recognizing political realities (though in stark terminology), he stated that "We must guard stability as we move toward freedom from dictatorship. Bridges must be built to get us from one phase to another," nevertheless, as regards the final goal, he further observed that "When I think of a multiparty system, it's not like Poland. It's more like Austria."<sup>289</sup> As for resistance from conservatives, he stated "We are confronting the critics, meeting them head on, and moving ahead fast."<sup>290</sup>

So far the process of radical political reform has been helped by a few factors. The reform process has come from above as much as from below. While Pozsgay may make other party leaders nervous, the anticipation of reform from above allows the leadership to operate from a position of strength, in so far as political reforms are not perceived as concessions from a weak regime but rather progressive measures from a government that desires to have its people participate more in the governmental process. On the other side of the coin, the population seems to have kept the lesson of 1956 well in mind. As the *Washington Post* reported, "most of the dozens of opposition groups that have sprouted here in the last year have stuck to remarkably moderate platforms and

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<sup>286</sup> *Christian Science Monitor*, November 28, 1988, p. 11.

<sup>287</sup> *Washington Post*, December 5, 1988, p. A19.

<sup>288</sup> *Ibid.*

<sup>289</sup> *Christian Science Monitor*, November 28, 1988, p. 11.

<sup>290</sup> *Ibid.*

conciliatory stances toward the authorities."<sup>291</sup> Moreover, Grosz has so far proven himself an adept understudy of Kadar, in that his "leadership is carefully balanced - some say divided - among liberals, moderates and conservatives."<sup>292</sup>

All these factors contribute to another reason for the advancement of reform. The pragmatic approach to reform from both sides has so far satisfied the Soviets that the HSWP is in control of the situation. Given the unrest in many parts of the socialist world, the relative calm that prevails in Budapest has given the HSWP implicit permission from Moscow to continue with their reform process.<sup>293</sup> However, the lenient attitude from Moscow is contingent not only upon the ability of the HSWP to control the reform process, but also upon Gorbachev's own reform movement in the Soviet Union. Kadar was successful in pushing through limited reforms despite Brezhnev's distrust of such things, a great accomplishment. However, Hungary has been able to develop more radical reforms because of the change in Soviet leadership towards a reform-oriented one. Politically speaking, the climate is more conducive to radical reform than at any previous time in Eastern Europe. Should Gorbachev's efforts fail or become mired down through conservative resistance within the party-state, this would have a chilling effect on reform in Hungary as well. Not for the first time would there be a reversal in the reform process.

The recent developments raise the issue of whether such political reforms are an extension of the two directions the elites can move towards in order to overcome the crisis of legitimacy, or is it possible that a bureaucratic centralist state can transcend itself, mutating into some other form of social integration. This question must be applied to the historical specificity of Hungary.

Much depends not on the political will of the party leadership in Budapest, but in Moscow. Hungary is de facto not a fully sovereign nation, much of her sovereignty lies with the Soviet Union. Hungary cannot significantly alter its form of social integration without the approval of the Soviet Union. If the Soviet Union insists that Hungary maintain as regulative the integrating principle of the party and its tool, the planned economy, then we must conclude that these reforms, if effective

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<sup>291</sup> *Washington Post*, December 5, 1988, p. A19.

<sup>292</sup> *Ibid.*

<sup>293</sup> *Ibid.*

(and that is not certain), will assuredly increase the support for the regime, given that it will become the most tolerable of the bureaucratic centralist societies, but will not resolve the legitimation crisis. The crisis of planning rationality will still exist, although the market may make it more socially anonymous, and Hungary will still be prevented from moving from party-state to nation-state as an alternative mode of legitimation. Socialist democracy will have taken on a much more radical meaning than at first imagined, but the essence of the project will remain intact, as will the attendant problems.

If however Hungary would be given back a good deal of her sovereignty, to undergo some form of Finlandization, she would then be given the gift of an alternate mode of legitimation, namely, that of the nation-state. This would be powerful indeed, given Hungary's long, sad history as a fiercely proud nation nevertheless dominated by greater powers. Popular pressure may of course cause the system of bureaucratic centralism to transcend itself into something else, one that, in the words of Agnes Heller, would introduce a measure of formal rationality into the system. It is conceivable that the system of bureaucratic centralism may nevertheless remain, but in this case the elites could still appeal to the alternate mode of legitimation, the nation-state, to overcome the crisis of legitimation. It remains to be seen how resilient the system of bureaucratic centralism will be as the latest wave of reform attempts to resolve its contradictions.



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