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Welcome by the Chief in Editorial Board

The English special issues of the journal of social sciences Polgári Szemle endeavour to provide scholarly assessments of economic and social developments in Hungary and of the country's history, and to explore its relationship to the rest of the world, with special focus on European identity and our relations with the European Union. For this reason the editorial board has rightly placed a study penned by academician Gábor Hamza about Robert Schuman's intellectual oeuvre and relations with Hungary first in this 3rd English special issue in Volume 15.

Gábor Hamza

The Political and Intellectual Legacy of Robert Schuman, the "Father" of European Integration – with an Outlook on His Relations with Hungary

Summary
The essay gives a brief outline of the milestones in Robert Schuman's life and eventful political career. The purpose of Robert Schuman's activity was the restoration and reinforcement of peace between peoples and nations. Some of his views remains relevant today. The study shows his intellectual oeuvre and relations with Hungary.

Keywords: Robert Schuman, Europe, Hungary, European Community, Schumann Plan, Schuman Declaration, Jean Monnet, integration

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Schuman's life and activity

Robert Schuman, who had a prominent part in forging the European integration, was born on 29 June 1886 in Clausen, Luxembourg. It is worthy of mention that although Schuman was born in Luxembourg, he was a German citizen. This is because his father, Jean-Pierre Schuman, who was born in Évrange, Lorraine, obtained German citizenship in 1871, after the cession of Alsace-Lorraine to Germany (and the change of its name to Reichsland Elsass-Lothringen). Robert Schuman became a French citizen in 1919, after World War I and subsequently to the conclusion of the Treaty of Versailles.

The prominent participant of French political life over several decades, Robert Schuman, who delivered his historic declaration inspired and elaborated by Jean Monnet, on the re-commencement of Europe (*Déclaration du 9 mai 1950,* also called the "Schuman Plan") in the famous *Salon de l'Horloge* at the Quai d'Orsay at the French Ministry of Foreign Affairs on 9 May 1950, had close ties with Hungary in the period between the two World Wars. In the first part of this essay, a brief outline is given of the milestones in Robert Schuman's life and eventful political career ("cursus honorum").

Robert Schuman started the secondary grammar school at the *Athénée* of the Grand Duchy of Luxembourg, and continued his studies at the Imperial Secondary Grammar School (*Reichsgymnasium*) of Metz, where he graduated in 1904. During the next few years he studies law, economic policy, theology, national and global economics and finances at various universities in Bonn, Munich, Berlin and finally in Strasbourg. In 1910 he served as an intern in Metz and in the same year his doctorate was also awarded *summa cum laude.* It is also important to note that his mother died in an accident in 1911.

The young Schuman seriously entertained the idea of becoming a priest, but an old family friend advised him against. After his second in 1912, he attended a meeting in the Benedictine monastery of Beuron. At that time, Willibrord Benzler (1853–1921), the Bishop of Metz established a group of young intellectuals with the aim to renew the liturgy. In addition to Robert Schuman, this group included Heinrich Brüning (1885–1970), subsequent imperial Chancellor, and the well-known and highly respected theologian Franz Xaver Münch (1883–1940).

Until his death Robert Schuman remained a member of the Görres Society (*Görres-Gesellschaft*), which was established in January 1876 with the aim to eliminate the subordination or marginalisation of German Catholics in academic fields. In 1913, Bishop Benzler requested Schuman to undertake the role of president for Catholic youth associations. Joined by two hundred volunteers, in that year he organised a meeting of German Catholics in Metz.

During World War I, between 1914 and 1918, Schuman provided civil service in the administration of the Boulay district headquarters. His duty was primarily to oversee formerly French-owned goods expropriated by Germans. In 1918, after the retreat of German troops, he became member of the Metz city council, which clearly shows

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that after the re-annexation of the region and the change of imperial rule, he had the confidence of the French authorities.

In 1919 he was elected member of House of Representatives the for the Lorrain Republican Union. In the interwar period, in 1944 Robert Schuman was a member of the *Parti Démocrate Populaire* (PDP), the predecessor of the Christian democratic party subsequently re-established as the *Mouvement Républicain Populaire* (Popular Republican Movement). He could fulfil his mandate as a representative up to August 1940. The *Parti Démocrate Populaire* published its theoretical journal *Politique* once in three months, in a relatively low number of copies, but well-known and highly regarded by intellectuals, and Robert Schuman was among its committed, proactive staff members. However, this undoubtedly highly important activity of his still needs to be explored and analysed for assessment.

In May 1940, after the outbreak of World War II, he served as State Secretary for Refugees jointly with Charles de Gaulle. When France capitulated, in June 1940, he refused the ministerial post offered by Prime Minister and Marshal Philippe Pétain. In August 1940 Robert Schuman was arrested by the Gestapo in Paris, as his cooperation with the National Socialist Germany could not be won. He was the very first Member of Parliament imprisoned by the Gestapo.

His arrest was to a great extent also due to the fact that he had maintained good relations with Kurt von Schuschnig (1897–1977), the Chancellor of the Republic of Austria before the Anschluss, who was also compelled to spend several years in the concentration camps of the National Socialist Germany (NS-Staat), under circumstances that were difficult and humiliating, but still considerably privileged.

After his detention, Robert Schuman was first expelled from Lorraine, and then deported to Neustadt on the Rhine, where he was kept in "special detention". In 1942 he managed to escape from this place. He found refuge first in St Martin's Benedictine monastery near Ligugé, then in a Trappist monastery, and finally in a Catholic orphanage. It is worth mentioning that the most important thing he had carried on him everywhere was his missal.

In 1945, the French Resistance accused Robert Schuman, wrongly and in the absence of evidence, of "unworthiness of the nation". However, the Lorraine electorate, and more specifically, the Thionwille District, elected him to the national assembly by a clear majority of the votes, and he presided the financial committee of substantial powers. He undertook to serve as a minister on several occasions in frequently changed governments of the 4th French Republic (*Quatrième République*). Between 1946 and 1947 he was a Finance Minister, and on 23 November 1947 he became the Prime Minister.

His position of high responsibility as head of government ended in 1948. He was compelled to resign as a result of the grave, nearly irresolvable economic and political problems. As a Prime Minister, he exhibited exemplary perseverance in protecting France from both rightist and leftist extremities to prevent disintegration and to contribute to improving and cementing citizens' confidence in democracy. Between 1948 and 1952, he acted as foreign minister for eight short-term governments. During this

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period he secured continuity in France's foreign policy, consciously steering the state toward a new path (*nouveau chemin*) of a "European profile".

When the European Coal and Steel Community was established by the Treaty of Paris, aimed primarily at eliminating hostility between France and Germany was signed (on 18 April 1951), Robert Schuman served as foreign minister. The Treaty of Paris provides a highly centralised and detailed regulation of coal and steel production in the six member states. In legal terms, this treaty was a *traité-loi,* or law-making treaty, known in French law.

In his capacity as foreign minister, on 26 May 1952 Schuman signed the *Deutschlandvertrag* in Bonn, which settled relationships between France and the Federal Republic of Germany, on the one hand, and France and the United Kingdom (represented by Robert Anthony Eden [1897–1977] as Foreign Secretary) and the United States of America (represented by Secretary of State Dean Gooderham Achison [1893–1971]), on the other. In 1955 and 1956, Robert Schuman had another prominent position in French political life as minister of justice (*garde des sceaux*).

During the conclusion of the treaties signed in Rome on 25 March 1957 to establish the European Economic Community and the European Atomic Energy Community (EURATOM), he no longer had a position in government. On behalf of France, these treaties were signed by Christian Pineau (1904–1995) and Maurice Faure (1922–2014), both members of Guy Mollet's government.

It is well-known that the Schuman Plan, meant to implement the (partial) integration of Europe, had been masterminded by Jean Monnet, whose concept had a decisive impact on Robert Schuman. However, it is less known that the term "community" comes from Carl Friedrich Ophüls (1895–1970), who was later on the very first ambassador of the Federal Republic of Germany in Brussels. Note that Ophüls was a disciple of economist and philosopher Ferdinand Tönnies (1855–1936), who was influenced by the views of Max Weber (1864–1920). The first president of the Commission, Walter Hallstein (1901–1982) had studied from Carl Friedrich Ophüls.

At that time, the French public did not yet unanimously support Robert Schuman's ideas about the European Community (or Communities). This explains why the majority of the members in the French national assembly received the various drafts about a "European defence community" and a "European political community" drafted with Schuman's substantial contribution. In 1952 he had to give up his position as foreign minister. Nevertheless, Robert Schuman's political vision of a new Europe became increasingly known and accepted, and gradually made its way towards implementation.

Between 1953 and 1958, Robert Schuman truly exerted himself in establishing the European integration. He tirelessly popularised his ideas about the continent in a specific form at numerous lectures delivered in the countries of Western Europe. In 1958 Schuman was elected president of the Common Assembly of 78 members, an advisory body to the European Coal and Steel Community, which was seated in Strasbourg and may be considered as the predecessor of the European Parliament. He held this office up to 1960. Once his presidential mandate expired, he remained a member of the Common Assembly up to February 1963. By a unanimous vote, the

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assembly assured Robert Schuman of its recognition of his outstanding achievements made as "father of Europe".

In 1958, Schuman was awarded the Karlspreis, handed over to him in Aachen. In 1959, jointly with Karl Jaspers (1893–1969), he was awarded the Erasmus Prize representing high international recognition.

Robert Schuman died on 4 September 1963, at the age of 77, in Scy-Chazelles near Metz.

The purpose of Robert Schuman's activity was the restoration and reinforcement of peace between peoples and nations. "People should make friends with you and this friendship will unite our countries" – wrote Federal Chancellor Konrad Adenauer (1876–1967) to him in 1962. The "European Community" is a work of peace born in his soul, which renders war impossible between two nations that had been enemies for centuries. This peace is also an example for the other regions of the world. "A united Europe is the harbinger of future universal solidarity," wrote Schuman in 1960. A world re-organised this way considerably facilitates peace and solidarity between rich and poor countries and peoples, overall disarmament and the protection and preservation of the economic achievements.

In his famous speech delivered on 9 May 1950, he considered it important to highlight that "Europe cannot be built in a day, neither as part of a plan based on some absolute priority; Europe will be realised through practical results, one step of which lies in setting a common goal." However, this common goal is not linked to the world of ideas. This is proven by the fact that two of the three treaties establishing the European Communities cover specific areas, namely, coal and steel production and nuclear energy generation. The speech known as the Schuman Declaration has not lost of its significance and timelines during the decades since it was voiced. In 1985, the commission presided by Jacques Delors rightly set 9 May, the date of delivering the Schuman Declaration, as Europe's Day.

Schuman's relationship with Hungary

Robert Schuman's interest and political activity was not confined to Western Europe. One of the highly significant evidences for this is that he visited Hungary three times, and this can be considered as his special attention to and obvious interest in Hungary. He made his first visit to Budapest in August 1930. In 1934 and 1935 he paid a several-day visit in the company of pro-Hungarian members of the French National Assembly and journalists. During his 1934 stay in Budapest, the Pál Almássy, Speaker of the House of Representatives entertained the French MP's for lunch. In the Budapest headquarters of the National Radical Party, the French representatives and journalists also visited journalist and politician Endre Bajcsy-Zsilinszky, subsequently an important voice against German expansion. A detailed report is given of this meeting in the 27 May 1934 issue of the paper *Szabadság* ("Freedom").

During the visit, Pierre Baudouin-Bugnet, Chairman of the French National Assembly's Committee for Central Europe and a member the visiting group that also in-

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cluded a senator, emphasised the need for cooperation. The visit also received highly favourable publicity in the contemporary French media. André Nicolas, a journalist who also participated in the group, stressed the significance of mutual understanding between Hungarians and the French in the prestigious journal *Frontières.* In September 1935, Robert Schuman and his fellow MP's by invitation of the Confederation of Hungarian Industrialists, the Hungarian National Economic Association and the daily *Pesti Hírlap.* The delegation also included Ernest Pezet, author of the high-profile book entitled "La Yougoslavie en péril" ("Yugoslavia in Peril"), published in 1933, who visited Hungary on no less than five occasions, and wrote about it with exceptional sympathy in his books and articles published in various widely read papers.

In addition to Hungary, Robert Schuman was also deeply interested in Austria, which was highly resented for political and ideological reasons by national socialists, especially after the *Anschluss* that took place in March 1938. This was the primary reason for the above-mentioned fact that after the German occupation of the northern part of France, in August 1940 the Gestapo arrested Schuman and kept him in detention for several months.

Special mention needs to be made of the profound influence a 1938 work entitled "Lutte pour la civilisation et philosophie de la Paix" (Fight for civilisation and for the philosophy of peace) by Maurice Blondel had on Robert Schuman, as it warned of the threat from the national socialist Germany (NS-Staat) to the Central European region and triggered quite a strong response at that time.

Robert Schuman's relationship with Hungary and the activity of the pro-Hungarian group in the French National Assembly between the two World Wars are still waiting for exploration and research. The study of this matter is by no means indifferent in our days, when Hungary is a full member of the European Union. Although indirectly, Robert Schuman had an outstanding role in the preparation for accession, as he considered the countries of Central Europe, including Hungary, as part of integrating Europe. It was not his fault that accession only took place with a more than fifty years' delay, on 1 May 2004.

Schuman's views

Robert Schuman considered the community of European states as a natural commercial community. Similarly in many respects to Francisco de Vitoria (1483/93–1546), the author of *Relecciones Teológicas,* who was active in the first half of the 16th century and is considered as one of the founders of modern international law, he considered this community based on commercial and economic relations as the natural expression of *communicatio* and *societas.* As his baseline, Schuman also presumes a kind of *societas prefecta,* which provides for the availability of all the means suitable for achieving the common goal, and in this particular case, for increasing European citizens' rights, prosperity (*bonum commune*) and intellectual riches. Quoting Francisco de Vitoria again, the community of European law and states is a kind of *"totus orbis … qui aliquo modo est una respublica".* The *bonum commune* justifies, and moreover, requires the

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transfer of certain elements in the sovereignty of the individual states to the supranational European community. The coexistence of the various European nations is thus traced back to the moral rules built on and rooted in natural law, never forgetting that the community of European states is not merely based on economic factors.

In our opinion, Schuman's definition of democracy remains valid to this very date: "It (i.e. 'democracy' – *the author*) is at the service of people and works in agreement with it." Robert Schuman linked the concept of democracy to Christianity. In his view: "Democracy owes its existence to Christianity." However, he also recognises that democracy is easy to distort and may deform. He raises politicians' responsibility in his following warning: "Nothing is easier for political counterfeiters to exploit good principles for an illusion, and nothing is more disastrous than good principles that are badly applied." Unfortunately, this view of his remains relevant. The same applies to the election of the European Parliament, to be established on the basis of direct elections for the representation of the Member States' interests. In relation to this, he writes: "People (the European peoples) should be able to monitor and facilitate developments in the institutions of the European Community/Communities through their representatives specifically elected for this purpose (the members of the European Parliament). Thus, the members of the community's parliament need to be elected based on *direct universal suffrage.*"

Robert Schuman was familiar with the works of Felicité Lamennais (1782–1854), one of the most significant persons in French Catholic liberalism. In his debates with the collectivist ("communist") ideologists of his age, Lamennais drafted the fundamental principles of Christian liberalism: "What is democracy? It is the full liberation of the individual, securing the totality of human rights, and full personal autonomy." Felicité Lamennais also included the freedom of speech and the freedom of the press in the totality of human rights. As he put it: "Only the freedom of speech provides a guarantee against dangerous words. Free debate is the only remedy to all spiritual aberrations."

As known, Christian liberalists built their ideas of freedoms on the belief that every human being is a sovereign entity and every human personality is from God the creator. With a view to this, they denied the extreme conflict that has evolved between the individual and the society and between individualism and collectivism in modern times (in the 19th, 20th and 21st centuries).

The personalist philosophers and thinkers who gathered around the journal *Esprit,* established by Emmanuel Mounier (1905–1950), endeavoured to find a way out of the trap of individualism and collectivism. Personalist thinking focussed on the dignity and freedom of the human personality ordered by God, thus they lent a transcendental perspective to liberalist teachings, and moreover, in an age when the ideas and utopias of collectivism were aggressively enforced. "Every person is created in the image of God, every person is called to the formation of one immense Body, mystical and physical, in the charity of Christ" – taught Emmanuel Mounier.

In addition to the freedom and dignity of the human personality, personalist philosophers also attached high significance to human solidarity and the gospel principle

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of love: in their opinion, the basis of social coexistence is not some kind of a violent collectivism, but solidarity and love. Schuman intended to create European unity on the basis of Emmanuel Mounier's above described complex teachings.

Robert Schuman emphasised on several occasions that Europe should be given a spirit (*esprit*). He puts it as follows: "This togetherness (of peoples) cannot and should not remain an economic and technical undertaking. It must be given a soul. Europe will not live and will not be saved except to the degree in which it has awareness of itself and of its responsibilities, when it returns to the Christian principles of solidarity and fraternity."

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György Matolcsy

Successful Crisis Management in the Light of the Twelve Economic Turnarounds

Summary

In 2019, now more than a decade after the global economic crisis of 2008–2009, it is appropriate to look back on the events of the period, which was one with a major bearing on economic history. The complex challenges emerging in the aftermath of the global economic crisis and the answers given to them remain fundamental determinants of our daily lives to this day. Moreover, as on a number of occasions in the course of history, the economic crisis also challenged the dominant trends in connection with the development of economics as a science. The very first and perhaps the most important reference point in the debates was the way in which to manage the crisis. According to neoliberalism, the former predominant school of economic thought, short-term salvation could be found by supply-side reforms causing demand to decline, a view which was increasingly challenged over time by economists seeking a broad distribution of Keynesian economic stimulus and the burdens of reform. Hungary is a country where this debate and its consequences have been quite spectacular.

Due to the flawed economic policy pursued before the crisis, the global storm of 2008–2009 hit an extremely weakened Hungary. As a result of that and the flawed crisis management based on neoliberal foundations that predominated the period, Hungary suffered one of the worst crises seen in Europe up to 2010. In the aftermath of the severe damage, the civic government entering office in 2010 announced a new approach to crisis management. Building on coordination between branches of economic policy, the strategy adopting a combination of innovative, conventional and unconventional measures successfully stabilised Hungary, setting the country on

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a new path of convergence. This paper provides an overview of the most important steps and achievements of that crisis management.

Journal of Economic Literature (JEL) codes: G01, E60, O47, E52
Keywords: economic crisis, economic policy, economic convergence, monetary policy

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Hungary in the years before the crisis

The global financial crisis of 2008 hit an extremely weakened Hungary. Well before the crisis, serious funding and structural problems had emerged. As a result of the fundamentally flawed economic policy pursued after 2002, which built on external indebtedness, imbalances developed in a wide range of areas across the economy. These imbalances contributed to Hungary's deteriorating competitiveness, a halt in convergence, and increased vulnerability. The potential growth rate of the Hungarian economy increasingly fell behind rates in the EU Member States and the Visegrád Countries (Czech Republic, Poland, Slovakia), exacerbated by a low level of employment, slowing productivity growth, and an inadequate level of investments. Well before the crisis, starting from 2005, the investment rate had declined, showing substantial divergence from regional developments. Hungary's activity and employment rates were among the lowest in the European Union. Before the crisis, excessively high taxes on labour and an overly generous system of social benefits had acted as barriers to the development of the labour market on both the demand and the supply sides, hindering economic growth.

In addition to soaring public deficits, a major current account deficit had also accumulated. In the absence of adequate internal savings, the Hungarian economy embarked on the perilous path of external indebtedness, with all economic agents accumulating significant volumes of debt, to a large extent denominated in foreign currency. The general government financed the deficit primarily from external funds, which gave rise to high levels of rollover and exchange rate risks, while also increasing external debt. The situation was exacerbated by the fact that – in the absence of adequate available internal savings – the domestic banking sector increasingly provided credit in foreign currency, primarily in Swiss franc (Matolcsy, 2008).

Apart from the course of fiscal policy, matters were made even worse by monetary policy decisions. Responding to the flawed economic policy measures that had led to high external debt and thus weakened the forint, in 2003 the central bank raised the base rate to 12.5 per cent, a particularly high level by historical standards. While this prevented the HUF exchange rate from depreciating further, the resulting double-digit lending rates gave rise to return requirements that manufacturing companies found difficult to meet. Moreover, the artificial strength of the exchange rate boosted foreign currency lending, driving economic agents to replace the now expensive forint funds with foreign currency loans on an increasing scale. By the time of the crisis,

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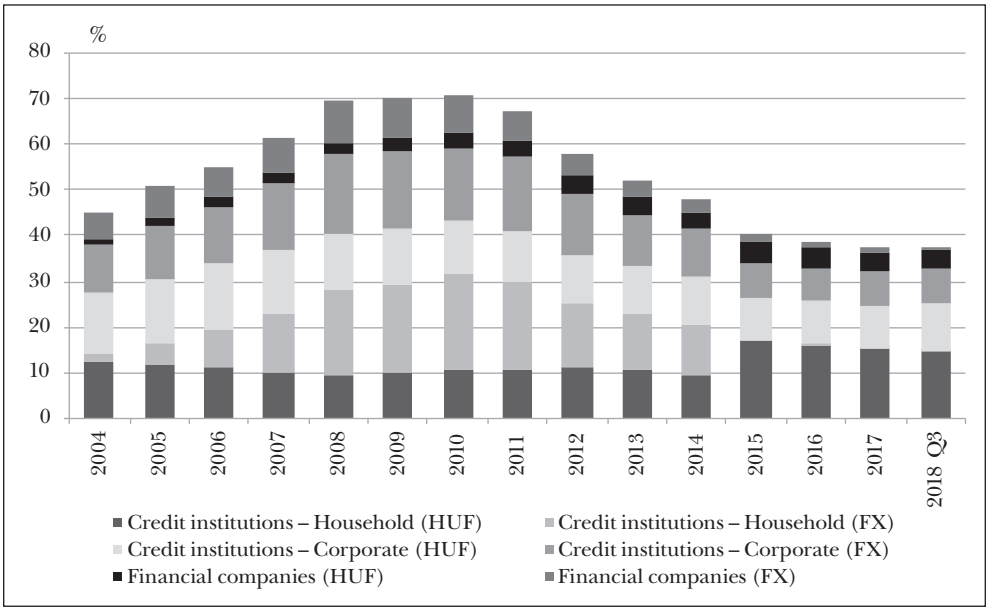
the volume of credit as a percentage of GDP exceeded 70 per cent, in which the share of foreign currency loans was steadily rising, exposing the private sector to elevated exchange rate risk (Matolcsy, 2007).

Figure 1: Credit-to-GDP ratio in Hungary



Source: MNB

First responses – conventional formula, failed crisis management

In the risk-averse market sentiment prevailing after the crisis, in the space of less than one year the forint depreciated by close to 40 per cent from the level of EUR/HUF 230. As a result of the high foreign exchange exposure, households were hit particularly hard by the depreciation of the domestic currency. Due to the rising exchange rate, households were faced with a drastic increase in their payment-to-income ratios, while the options for public debt financing narrowed. All of this was accompanied by the excessive deficit procedure (EDP) that had been in place against Hungary since 2004, adding to the difficulties in managing the crisis.

Clearly, budgetary consolidation was needed, but a flawed assessment of the problems impeded crisis management. The measures focused exclusively on the supply side of the economy, putting an additional squeeze on the already sluggish demand through austerity. However, measures focused on the supply side could not be successful, because policy-makers applying fiscal austerity significantly underestimated the size of the fiscal multiplier (the growth effect of a unit of government action) and its devastating force in an environment of recession (Matolcsy, 2018). Despite the gov-

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ernment's cutbacks on fiscal expenditures, fiscal consolidation was undermined by lower tax revenues due to the accompanying contraction in internal demand, which was even accelerated by the measures. Instead of the desired restoration of equilibrium, the results were a deeper recession, rising unemployment and steadily increasing debt ratios. Conventional crisis management based on austerity measures only paved the way for additional adjustments.

Amounting to 4 to 5 per cent of GDP, the fiscal austerity measures adopted in 2009 based on the IMF–European Commission rescue package of autumn 2008 cost households the dearest. The increase in the general VAT rate, the freeze on wages in the public sector, the withdrawal of 13th-month incomes and 13th-month pensions, the changes to pension indexation, the increased retirement age, the freeze on the family allowance, and the more rigorous rules of eligibility for childcare aid and childcare allowance, all hit households, which were simultaneously faced with increased instalments on their foreign currency loans. On the other side of the scale, there was only a moderate reduction in contributions payable on labour, and a slight increase in the minimum wage. Owing to the spillover effects, rather than driving economic developments towards equilibrium, the measures implemented resulted in major real-economy sacrifices and persistently high inflation (Matolcsy, 2015).

The austerity measures and the gradual decrease in the wage ratio led to a substantial contraction in household consumption and consequently in Hungarian output, resulting in even poorer debt indicators for the country. Additionally, despite the availability of EU funds, investments saw an even greater fall than consumption overall, further reducing Hungary's potential growth. On the whole, due to the high fiscal multiplier resulting from the crisis environment, the role of fiscal policy in the post-crisis decline proved to be decisive (Matolcsy, 2018).

The failure to implement comprehensive tax reforms was accompanied by unfortunate timing, given that the whole of Europe was functioning in crisis management, as a result of which external demand could not contribute to counterbalancing the losses incurred on the expenditure side of the budget. Indeed, conventional crisis management based on austerity measures brought new problems to the surface. The electoral mandate of the governing party was severely damaged, which led to political instability and a government crisis. Financing and growth problems evolved into a political crisis, as a result of which, over time, economic policy lost its social support for the introduction of reforms of any kind. Consequently, a turnaround towards equilibrium could only be made by means of an economic policy that went beyond the conventional formula of austerity measures, the opportunity for which was created by the 2010 change in government.

Historic turnarounds in post-2010 Hungarian economic policy

In and of themselves, recessions do not only involve a fall in aggregate demand, but also provide an opportunity to renew economic thinking. New types of ideas chal-

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lenging the former mainstream may also gain prominence, potentially offering new ways to reflect on the way a crisis is managed. In 2010, economic policy faced multiple problems as a result of the earlier flawed crisis management. Its task was to create financial stability and implement structural reforms at the same time. The government coming into office made a radical break with the previous crisis management practices. In order to stabilise the economy, it implemented growth-friendly measures using innovative and targeted means, while also improving the fiscal balance (Matolcsy and Palotai, 2014). The following sections address the most important turnarounds achieved in Hungarian economic history since 2010.

Turnarounds in fiscal matters

The change in Hungarian fiscal policy was brought about by the inauguration of the new civic government in 2010, which is now serving its third term. The task did not look easy: financing processes had to be stabilised while creating opportunities for economic growth through structural reforms.

Turnaround in the tax regime

The tax regime was reformed with a view to supporting economic growth while maintaining budgetary equilibrium. In order to achieve this dual objective, it was necessary to boost employment and investments, which could be achieved most effectively by reducing taxes on capital and labour. The tax reform launched in 2010 was underpinned by a new philosophy. The most prominent change was the government's shift in focus from taxes on labour and capital to indirect consumption and sales taxes. The reduction of tax and contribution burdens on labour, along with the offer of targeted benefits (Job Protection Action Plan), has had a positive effect on economic operators' labour market decisions, increasing incentives to work (Baksay and Palotai, 2017).

In addition to the taxes on labour, the levies on capital also significantly distort investment decisions by economic operators, and there is broad consensus that they are among the most harmful tax burdens. As early as the second half of 2010, the tax burden on capital decreased significantly as a result of raising the threshold for the higher corporate tax rate from HUF 50 million to HUF 500 million, which expanded the range of small and medium-sized companies subject to the lower tax rate. In 2017 a flat corporate tax rate was introduced, and the rate was lowered to 9 per cent. The Hungarian SME sector enjoys substantial support from the new forms of small taxpayer company forms established in 2013 (KATA, KIVA), which has been used on dynamically increasing scale due to the favourable tax conditions. The measures reduced the tax burden on domestic companies, with tax cuts amounting to up to 2 per cent of GDP by 2018 (Baksay and Palotai, 2017).

Apart from tax cuts to stimulate growth, ensuring the balance of the general government also required measures that provided additional resources for the imple mentation of the tax reform. Budgetary resources could not be provided through

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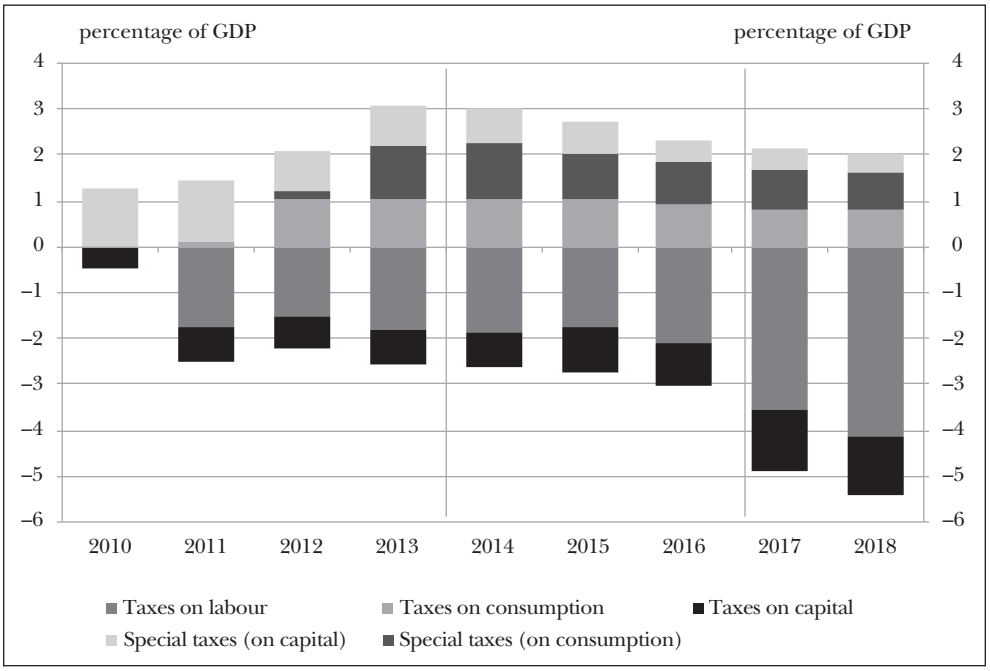
Figure 2: Cumulative static fiscal impact of tax adjustments implemented since 2010



Source: Palotai, 2017

conventional austerity measures, as they would have in fact undermined the positive effects of tax reform on economic growth. The government thus shifted its focus towards burden sharing. The imposition of consumption and sales taxes is less detrimental to real economic growth as these taxes do not significantly divert capital allocation and labour market decisions. In addition, sector-specific taxes can help to maintain the budgetary equilibrium while leading to a fairer and more equal distribution of public burdens.

The main thrust of the tax reforms was raising the upper VAT rate from 25 per cent to 27 per cent, raising excise duty rates in several steps and reforming sector-specific taxes. Apart from rate increases, the significant growth in consumption and sales tax revenues was also driven by the gradual widening of the tax bases through a variety of innovative steps for the formalisation of the economy. In the process, a prominent role was played by the introduction of online cash registers, the Electronic Trade and Transport Control System (EKÁER), and online invoicing, along with the implementation of reverse VAT in some areas. As with taxes on labour, economic policy also pressed for the application of targeted allowances in the field of consumption taxes, reducing the VAT rates on certain widely uses services (Internet and restaurants) and on basic foodstuffs (milk, eggs, poultry, fish and pork) (Palotai, 2017).

The increase in the share of consumption and sales taxes was partly due to the imposition of various special taxes. A shift in the tax regime as a whole also took place

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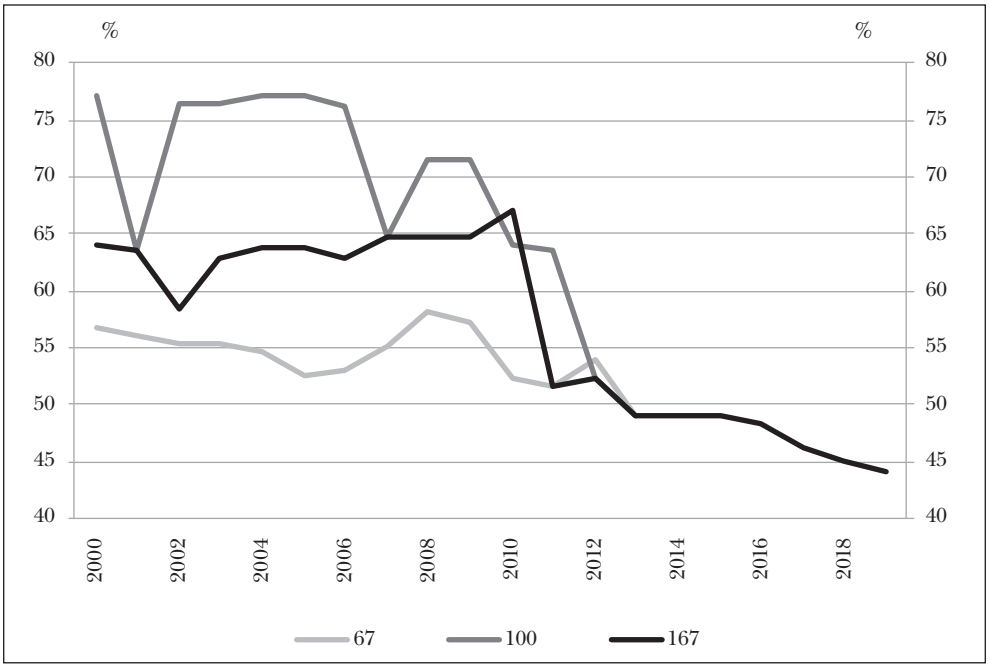
in sector-specific crisis taxes through the conversion of the special taxes levied on specific sectors into consumption and sales taxes after 2013 (e.g. transaction levy, insurance tax, telecommunications tax, public health product tax). Service sectors with the ability to bear a greater share of the public burdens and subject to lower effective tax rates (retail, finance, insurance, energy, telecommunications) have seen their share of the public burdens gradually decrease in recent years, while the need to maintain the budgetary equilibrium has remained a priority.

Turnaround in motivation

In cutting taxes on labour, one of the biggest changes was the introduction of the flat-rate personal income tax. The flat rate, first reduced to 16 per cent in 2011 and to 15 per cent in a subsequent move in 2016, was lower than both of the previous tax rates, and the abandonment of progressive taxation supported additional performance, higher labour intensity, and the accumulation of knowledge capital. The marginal tax wedge fell below its previous levels in most wage categories after the reforms in 2013 and has since decreased further as a result of subsequent cuts in taxes and contributions, and due to the substantial targeted benefits available (target groups of the Job Protection Action Plan, family tax allowance) (Matolcsy and Palotai, 2016).

Figure 3: Marginal tax wedge in Hungary 67%, 100% and 167% of average earnings



Source: OECD, MNB

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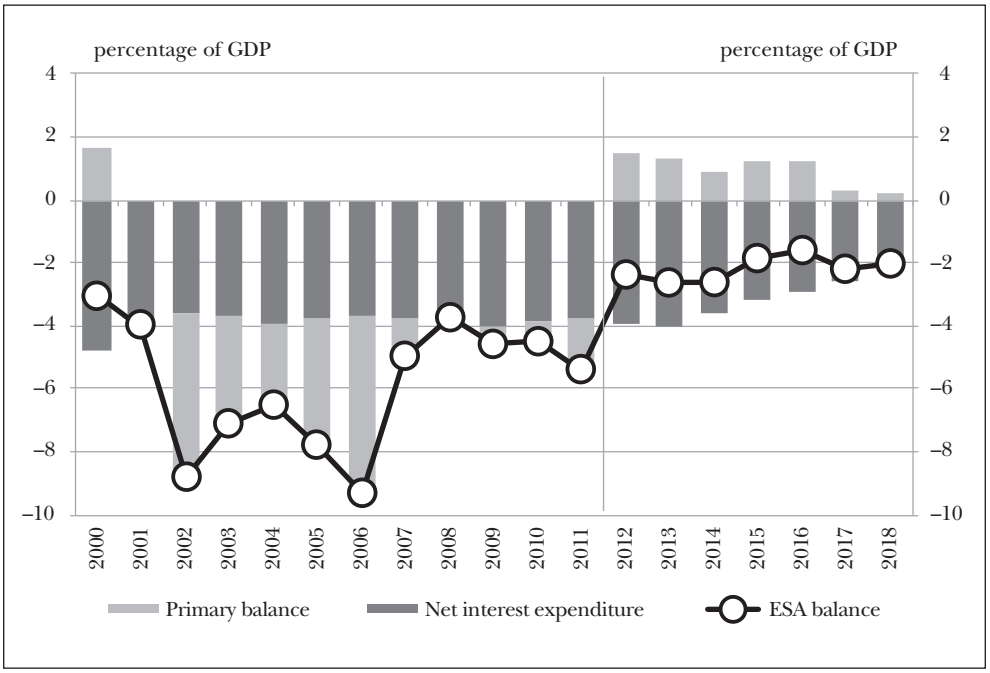
Turnaround in general government

As a result of the successful fiscal turnaround, since 2012 the deficit has remained stable below the Maastricht criterion of 3 per cent. In order to assess this achievement in Hungary's economic history, it is worth recalling that after the regime change, Hungarian economic policy was never able to bring the deficit below 3 per cent, and doing so ultimately led to the closure of the excessive deficit procedure (EDP) that had been in place against Hungary since its accession to the EU in 2004. Thanks to the fiscal turnaround, the deficit was reduced and economic growth resumed at the same time (Matolcsy and Palotai, 2016).

Figure 4: Changes in general government balance indicators



Note: The data do not contain the imputed interest expenditures incurred since 2012 on account of the pension system reform. The data for 2018 show the forecast in the MNB Inflation Report of December 2018.
Source: HCSO, MNB

As part of the Széll Kálmán Plan, the social benefit system, which had previously been excessively lax and had in fact provided disincentives to work, was transformed in several stages. In addition to blocking certain fiscal expenditures, the government's new economic policy has also curbed the indebtedness of local governments.

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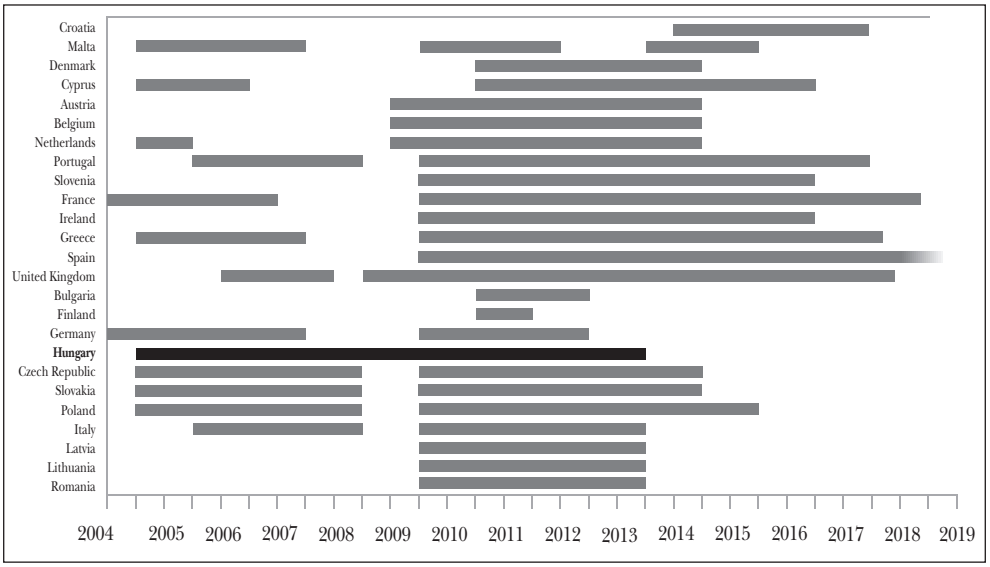
Closure of the excessive deficit procedure – turnaround in the EDP

Since the year of its accession to the EU, Hungary had continuously been subject to an excessive deficit procedure. Consolidation of the fiscal balance was justified not only by an extremely high level of indebtedness, but also by the need to comply with the requirements of the European Union. Continuous violation of the rule had already compromised access to EU cohesion funds assisting convergence. Improving the general government balance and achieving the EDP closure had thus become inevitable for the reduction of vulnerability factors.

Following the successful fiscal turnaround, after 9 years the excessive deficit procedure against Hungary was finally closed in 2013. The economic policy threat of the suspension of access to EU funds was eliminated, and the achievements of the successful new economic policy could no longer be questioned even internationally.

Figure 5: Excessive deficit procedures against individual countries



Source: European Commission

Turnaround in public debt

One of the objectives set for post-2010 economic policy was to break the rapidly rising trend of public debt and to set it on a downward path. The government enshrined this objective in the debt rule, elevating it to the constitutional level in the Fundamental Law adopted in 2011.

Through the sustainable consolidation of public deficit and by stimulating economic growth, the fiscal turnaround provided for the reduction of the debt

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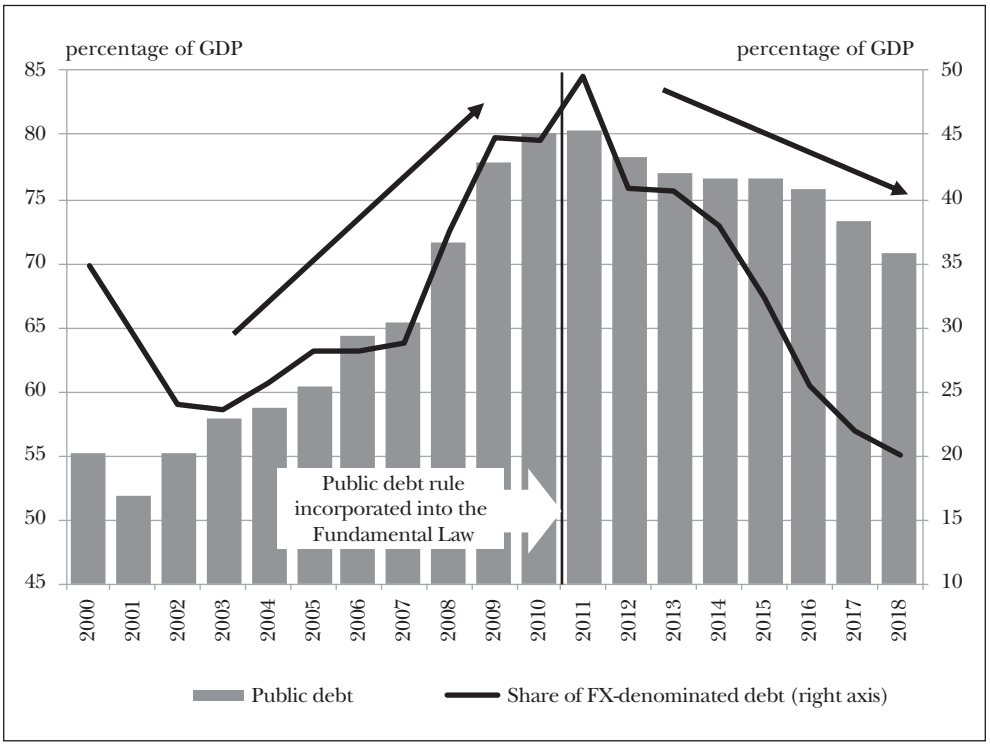
ratio, which was stabilised as a result of the measures taken by the government. From its historic peak of over 80% in 2011, the debt ratio was reduced by over 10 percentage points by late 2018, which makes Hungary the only economy in the European Union to have recorded a steady decrease in its gross government debt as a percentage of GDP every year since 2012. This has been accompanied by a steady decrease in the foreign currency ratio of public debt, significantly reducing Hungary's external vulnerability. Amounting to nearly one half of central government debt in 2011, the foreign currency ratio fell to around 20 per cent by 2018. This major reduction was partly due to full repayment of the country's EU and IMF loans. In addition to more moderate levels of risk premiums (CDS) and sovereign market yields, Hungary's improved standing has also been confirmed by the better ratings awarded by international credit rating agencies (Matolcsy and Palotai, 2016).

Recent years have also seen major improvements in the financing structure of public debt, partly supported, via the promotion of domestic financing, by the central bank's Self-financing Programme launched in the summer of 2014 (see below).

Figure 6: Developments in gross public debt as a percentage of GDP and the foreign currency ratio of debt since 2000



Source: MNB

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Turnaround in the labour market

Starting in 2008, the global crisis was accompanied by a sharp decline in corporate demand for labour, leading to a major fall in the number of persons employed. In the years following 2010, a number of government measures, mainly aimed at increasing the labour market participation rate, contributed to the recovery of the labour market from the crisis. The number of those becoming inactive was reduced by tightening the conditions of eligibility for disability pension and by gradually raising the retirement age. The reduction in the amount and duration of transfers related to the absence from employment, which may be seen as a measure to tighten the allowance system, discouraged early exit from the labour market. Facilitating the use of flexible forms of work, in particular part-time employment, supported labour market access for certain disadvantaged groups.

In parallel with the government measures to increase activity, the government also provided targeted assistance for the labour-market integration of (mostly disadvantaged) social groups of increasing activity. Employers employing disadvantaged workers (e.g. the unskilled, the long-term unemployed, and people over 55) have been granted significant allowances on their contributions under the Job Protection Action Plan, the primary focus of which is to boost demand for labour. The extension of public employment programmes in 2013 facilitated access to employment for groups that had sought to enter the labour market after inactivity, but had been met with low demand from the primary labour market, thereby providing a major part of those groups with an adequate transition for their subsequent entry into the primary labour market.

Mainly as a result of the introduction of targeted structural measures affecting the labour market, Hungary's activity rate has increased dynamically since 2010. The improvement in Hungary's relative position in terms of the activity rate is mainly attributable to social groups that are at a disadvantage in the labour market: the low-skilled, young people, people over 50, and women with young children. The activity rate of these groups has increased significantly over the past nearly one decade, and the gap with the EU average has also been substantially reduced in the case of these groups.

The increase in labour market participation has been accompanied by improvements in employment, with new active labour absorbed by the market. In 2013, employment started to rise rapidly, increasing the number of persons employed by more than 750,000 compared to 2010.

As employment increased, unemployment fell to a historic low. In Hungary, the unemployment rate fell from 11 per cent in 2012 to 3.7 per cent in 2018, which is currently one of the lowest rates in the European Union.

Turnarounds in monetary policy– achieving and maintaining price stability

Following the crisis of 2008–2009, successful crisis management was based on finding the right responses, as well as on coordination between key branches of economic

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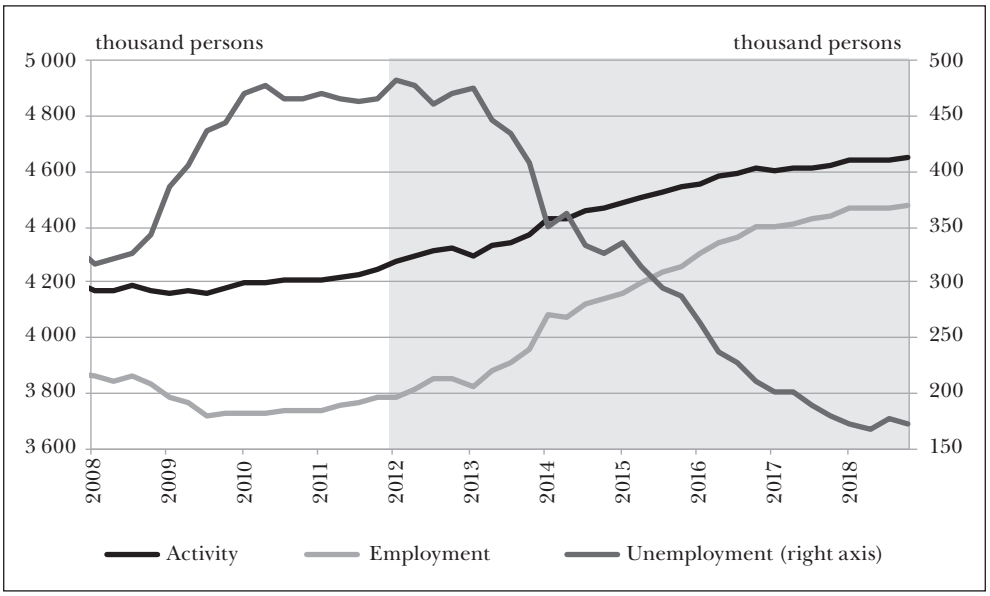
Figure 7: Changes in the number of active persons, persons employed and the unemployed



Source: HCSO

policy. While the world's major central banks helped their economies with monetary stimulus on an unprecedented scale almost immediately after the onset of the crisis, Hungarian crisis management continued against monetary headwinds up until summer 2012. Monetary policy made a full turnaround with the appointment of the new central bank management in 2013. The renewal of central bank policy was also largely determined by the effective transformation of the institutional system, i.e. the integration of the Financial Supervisory Authority at the end of 2013.

Cuts in the central bank base rate and their impact

Major central banks around the world responded to adverse macroeconomic developments with immediate monetary easing. The MNB launched its easing cycle in August 2012, cutting the policy rate from 7 per cent by 610 basis points to a historic low of 0.9 per cent in three steps over 4 years. Launching the easing cycle was supported by several factors. Due in part to the successful fiscal turnaround, Hungarian risk premiums showed a sustained improvement in investor sentiment, while a series of new easing measures by leading central banks also provided for looser monetary conditions. The central bank's easing measures were also supported by the fiscal turnaround beginning in 2010, improving fiscal discipline, the declining trend of public debt, the moderation of external vulnerability, and the structural reforms aimed at stimulating long-term growth (MNB, 2017).

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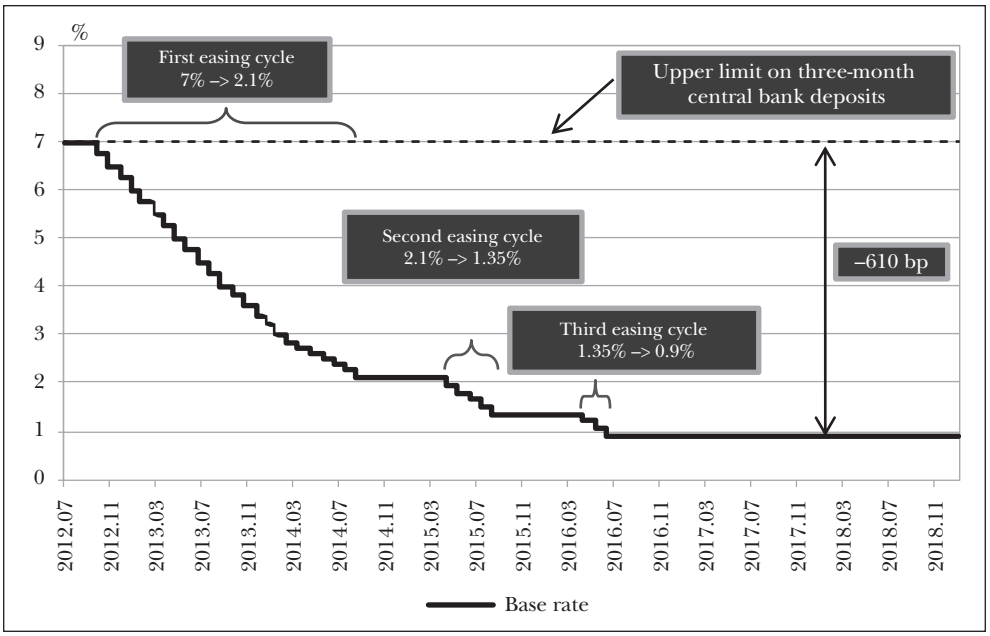
Figure 8: Changes in the Hungarian base rate



Source: MNB

The policy rate was cut in a series of steps until late 2015, when the historic low of 0.9 percentage point was reached. Since then, the base rate has remained unchanged at that level. Keeping the base rate on a sustained hold was underpinned by the idea that the central bank, while easing monetary conditions, would seek to establish interest rate levels that were consistent with the sustainable achievement of the inflation target even over the longer term.

The central bank's easing cycles have had significant growth effects. Substantial base rate cuts have reduced the chances of a deflationary environment emerging, and have contributed significantly to the rise in output. In addition to the positive macroeconomic effects of the easing cycle, the economy has remained balanced, and its external financing capacity has also been stable over time.

The easing of monetary conditions has also had an impact on financial markets. The looser interest rate conditions have greatly reduced the interest burden on the private sector, preventing further falls in the volume of lending, consumption and investments after the crisis. It was not only the private sector that benefited from monetary easing; yields on short-term and long-term government securities also decreased significantly. With sovereign market yields declining, the position of general government improved as a result of falling interest expenditures. While in 2013 general government interest expenditures exceeded 4 per cent of GDP, that ratio was almost halved by 2018 as a result of the gradual repricing of HUF debt.

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Transformation of the central bank toolbox, introduction of unconventional instruments

In summer and autumn 2016, the Magyar Nemzeti Bank introduced a new monetary policy toolkit in whereby it carried out unconventional monetary easing while keeping the base rate on a sustained hold, and taking inflation developments into consideration. The core element of the system was the transformation of the policy instrument by means of a quantitative restriction on the three-month deposit, through which the MNB supported lending and self-financing, and ensured a further decrease in relevant money market yields within the interest rate corridor. Implemented from 2016 Q4 onwards, the quantitative restriction was supported by the MNB cutting the O/N lending rate to the base rate, i.e. introducing a completely asymmetric interest rate corridor, and cutting the reserve ratio from 2% to 1%. In autumn 2016, the MNB introduced a fine-tuning foreign exchange swap (FX-swap) instrument, which provides HUF liquidity and enables the central bank to maintain a sufficient level of liquidity in the banking sector by means of weekly tenders.

As a result of introducing the quantitative restriction, the MNB's holdings of the 3-month deposit decreased from almost HUF 2,000 billion in late September 2016 to approximately HUF 900 billion in November 2016 and to HUF 75 billion in late 2017; the instrument was then discontinued in December 2018. The banking sector's surplus liquidity was channelled into O/N deposits, and the downward pressure on yields from crowded out liquidity was perceivable in all relevant markets. After the introduction of the quantitative restriction in summer 2016, yields hit the lower boundary of the interest rate corridor. The effective functioning of the system of quantitative restriction was supported by the fact that, at the initiative of the MNB, in May 2016 the submission system of the BUBOR (Budapest Interbank Offered Rate) was reformed, which, due to the imposition of submission requirements, brought about an increase in the volume of trading in the unsecured interbank market, along with a tangible improvement in the information content of BUBOR rates (MNB, 2017).

At its meeting in November 2017, the Monetary Council took the decision that the loose monetary conditions should have an effect on both the short and the long sections of the yield curve. To ensure this, the Council decided to introduce two unconventional instruments from January 2018, which would constitute an integral part of the Bank's set of monetary policy instruments. Monetary policy interest rate swaps (MIRS) were introduced as a general monetary policy instrument and the Mortgage Bond Purchase Programme (JVP) as a targeted programme, the declared purpose of which was to promote the wider use of fixed-rate mortgage loans and the development of the mortgage bond market.

Both MIRS and the Mortgage Bond Purchase Programme achieved their objectives. The instruments supported the extension of loose monetary conditions to long-term maturities, along with market stability, and contributed to the development of the mortgage bond market and to reducing banks' interest rate risk and, consequently, to the further spread of long-term, fixed-rate mortgage loans, where new lending increased from 61 per cent at the beginning of 2018 to about 90 per cent by the end

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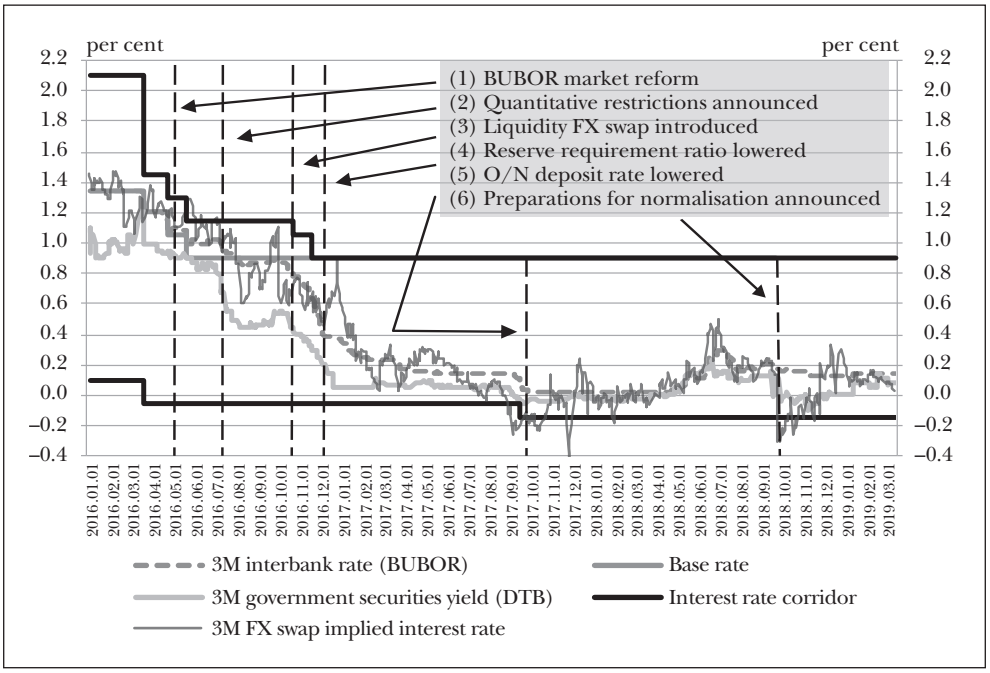
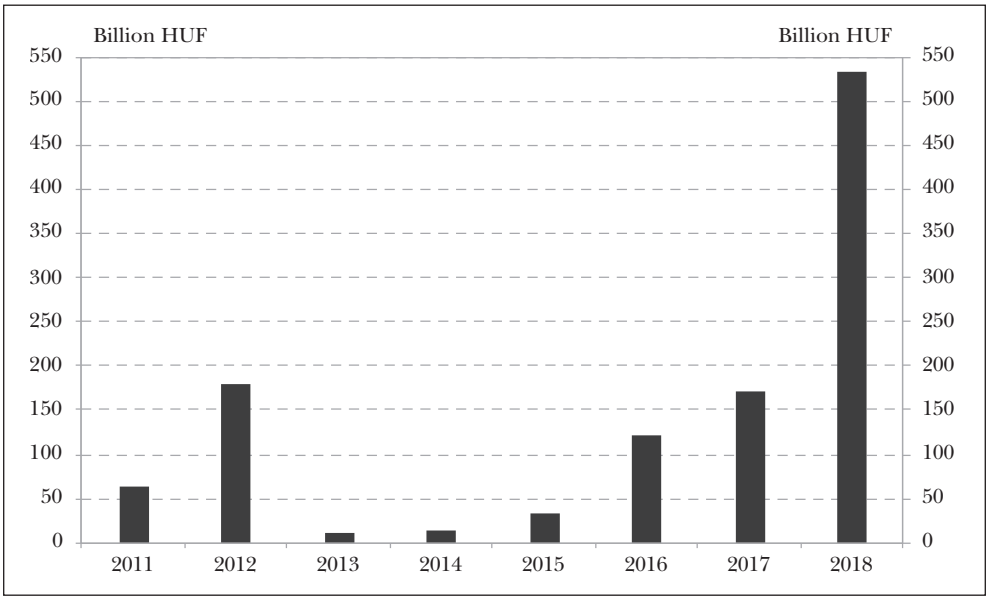
Figure 9: Changes in short-term yields (2016–2019)



Source: MNB

Figure 10: Gross annual market issue of fixed-rate mortgage bonds



Source: MNB

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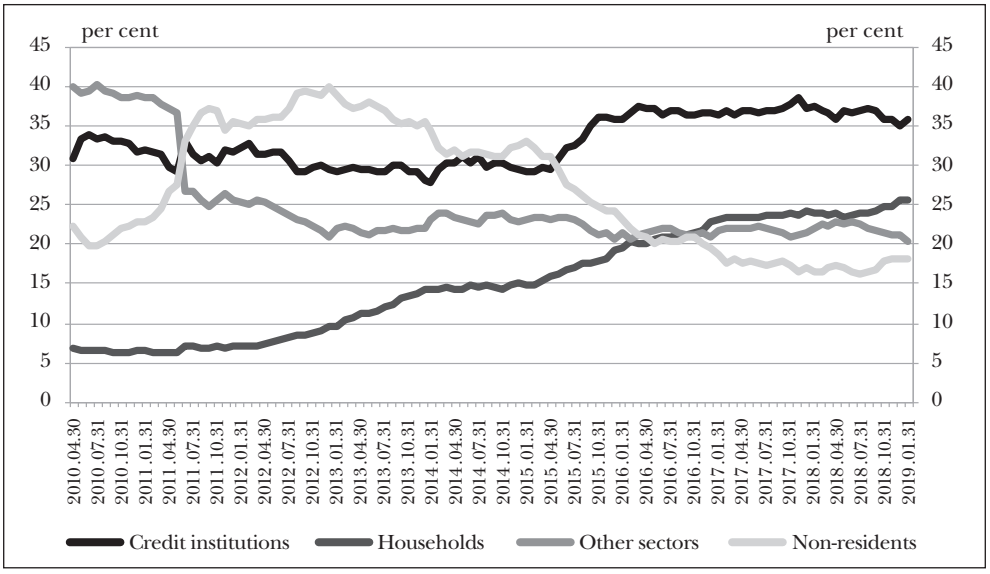
of the year. Compared to sovereign yields, the premium on mortgage bond yields had slipped into negative territory along the yield curve until the phase-out was announced, and low financing costs substantially supported new issuance. The gross issuance of fixed-rate mortgage bonds equalled the combined market volume of the previous 7 years, confirming that the programme supported the development of the mortgage bond market to a substantial extent.

Following discontinuation of the Mortgage Bond Purchase Programme, the MNB will continue to energise the mortgage bond market support banks' access to long-term HUF funding via the use of instruments outside its monetary policy toolkit, in particular by means of regulations on the mortgage financing adequacy ratio (MFAR).[1]

The Self-financing Programme – towards a more stable economy

The Self-financing Programme was announced in April 2014, and during its implementation the MNB transformed its monetary policy toolkit in order to channel banks' surplus liquidity from central bank deposits to holdings of liquid securities with longer-term securities. Due to the specificities of the Hungarian securities market, this primarily translated into stronger demand for government securities. In combination, the central bank's programme, the foreign currency repayments by the Hungarian Government Debt Management Agency, financed via HUF issues, and the cooperative attitude and adjustment of the banks allowed for a shift towards a healthier debt structure and a gradual decrease in external exposure (MNB, 2017).

Figure 11: Holders of Hungarian public debt



Note: Up to December 2012, the ratio of credit institutions also includes holdings of money market funds.
Source: MNB

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The central bank's Self-financing Programme significantly reduced Hungary's external vulnerability, strengthened its financial stability and improved its international standing. Between 2014 and 2016, the year marking the end of the programme's active phase, Hungary was able to repay nearly EUR 11 billion worth of foreign currency debt, so that sovereign market yields decreased in line with the inflation target. The foreign currency ratio of public debt shrank from 42 per cent in 2014 to 25 per cent at the end of 2016 and below 20 per cent at the end of 2018. The Self-financing Programme played a particularly important role in the realisation of finance based on domestic investors and the local currency, and its results laid the foundation for the strategic objective of bringing government debt fully under Hungarian control.

Turnaround in the central bank balance sheet – when less is more

Lower external vulnerability made possible a turnaround in the central bank balance sheet, which had a positive impact on both the MNB and the national economy. At the onset of the crisis, Hungary was forced to borrow from international institutions due to the unfavourable financing situation of the state, which led to an increase in the assets and liabilities of the central bank balance sheet. As a result of increased liquidity in the banking system, the bloated balance sheet generated significant interest costs for the MNB. The significant financing capacity created by the economic adjustment following the crisis, and the resulting decrease in external debt and external vulnerability, have made it possible to reduce the central bank balance through targeted programmes without compromising reserve adequacy. This is a noteworthy development even by international standards. Indeed, after the crisis, much of the world followed the emerging trend that central banks generally increased their balance sheet totals in pursuit of their monetary policy objectives. In its monetary policy easing cycle (2008–2014) that followed the crisis, the Fed's total assets-to-GDP ratio increased by 17 percentage points, the ECB balance sheet increased by 20 percentage points as a result of the asset purchases started after 2014, and that of the Czech central bank by 40 percentage points from 2013 onwards due to its bloated foreign exchange reserves. By contrast, since the start of Hungary's turnaround in monetary policy in 2013, the MNB's total assets-to-GDP ratio has fallen by 12 percentage points. Moreover, in parallel with the reduction of Hungary's central bank balance sheet, its structure has also become more efficient due to a substantial decrease in the ratio of interest-bearing liabilities. Despite the low-yield environment, the turnaround in the central bank balance sheet has left ample room for monetary policy actions, while also improving the efficiency of monetary transmission. It is important to emphasise that, in contrast to international developments, the MNB has managed to maintain loose monetary conditions even with a shrinking balance sheet (Erhart et al., 2015).

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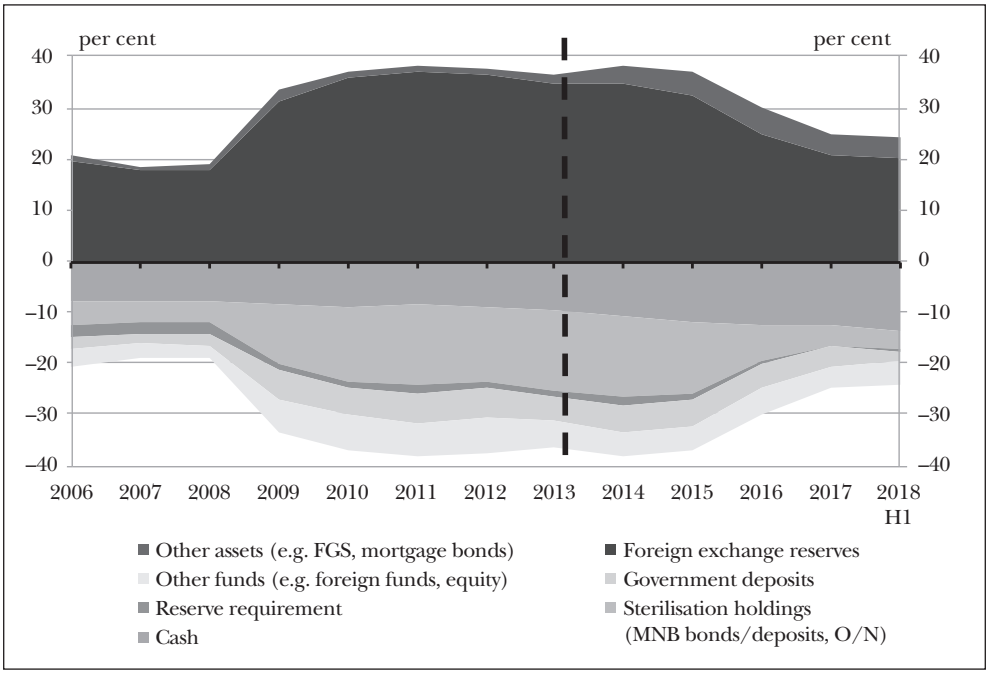
Figure 12: Changes in the main items of the MNB balance sheet as a percentage of GDP (annual averages)



Source: MNB

Turnaround in lending – the ice breaks in a frozen credit market

Corporate lending

Following the onset of the financial crisis of 2007–2008, the supply of credit in the domestic banking system dropped dramatically, with corporate lending suffering a credit crunch between 2009 and 2013 Q2 (Balog et al., 2014). In these years, as a combined result of disbursements and repayments, the volume of corporate lending contracted by an annual average of 4 to 5 per cent. Micro, small and medium-sized companies, which had only very limited access to other funding, were hardest hit by the shrinking credit volume: lending to these companies fell at an annual rate of around 4 to 8 per cent.

In SME lending, the Funding for Growth Scheme launched in 2013 broke the negative spiral and set developments on a stable growth path. With a slight lag, this trend was followed by the credit volume of the overall corporate sector; consequently, by the end of 2018 both the overall corporate credit volume and lending to the SME sector was growing at a rate above 10 per cent (MNB, 2019b).

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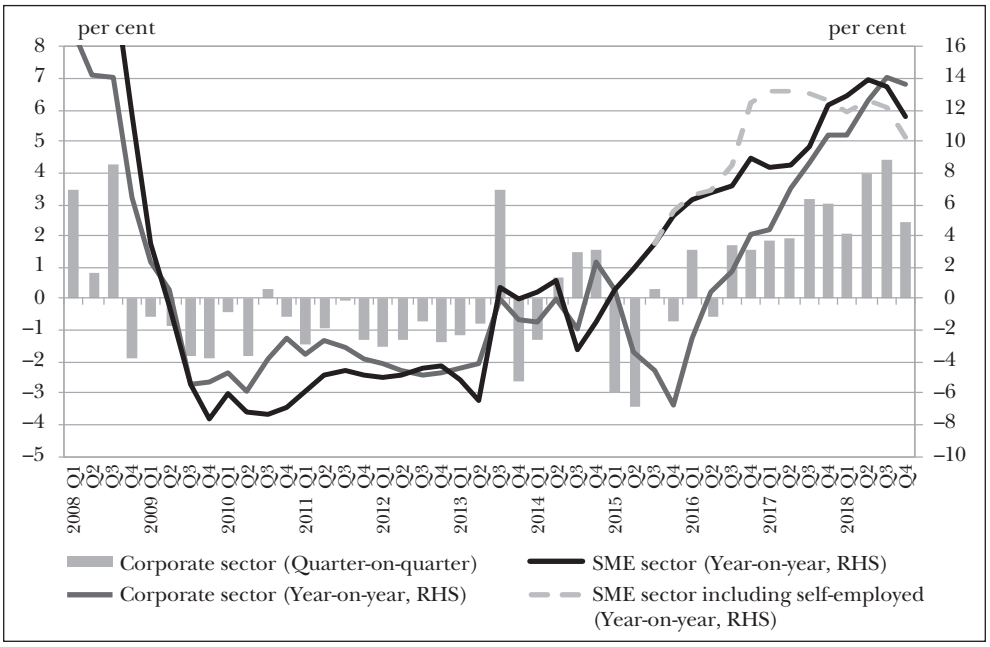
Figure 13: Growth rate of the credit volume in the overall corporate sector and in the SME sector



Note: Transaction based, prior to 2015Q4 data for SMEs are estimated based on banking system data.
Source: MNB

Introduction of the Funding for Growth Scheme

Short of bank financing, Hungarian-owned enterprises in the SME sector were hit particularly hard by banks' restrained willingness to lend and by rising risk premiums, which increased the risk of the credit market freezing.

In June 2013, the central bank launched the Funding for Growth Scheme (FGS) as a new targeted instrument in its monetary policy toolkit designed to mitigate the protracted disturbances in lending to SMEs, provide a stimulus to the economy and strengthen financial stability. Under the FGS, the central bank provided refinancing loans at a 0% interest rate to credit institutions, which could pass these loans on to SMEs with an interest margin capped at 2.5% and maturities of up to 10 years. This provided a very favourable and predictable financing option, without any exchange rate risk.

The FGS was launched in June 2013, and its first phase, spanning a mere three months, accomplished its short-term objectives, i.e. to ease credit market constraints and boost competition between banks. With a view to achieving a stronger growth effect, in the second phase of the scheme the focus shifted to new lending, and to investment loans in particular, with only limited room for loan redemptions. In autumn 2015, the MNB decided to phase out the FGS, since the objectives set at the start of the programme had been successfully achieved. In line with the intended phase-out, the third phase was even more targeted than the previous two. On the one hand, it

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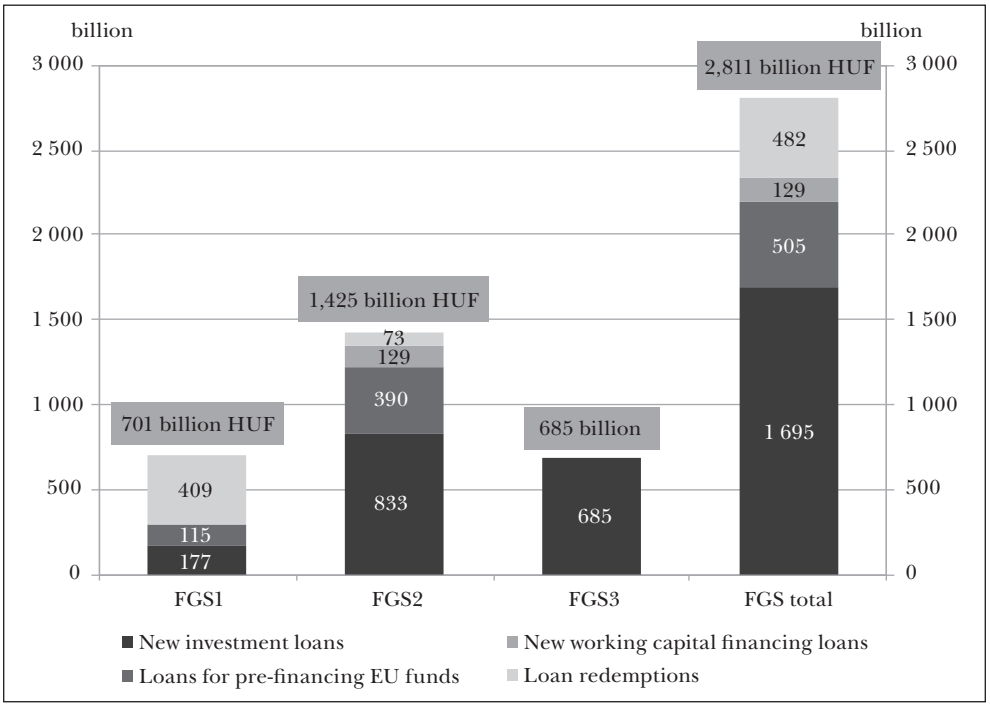
enabled HUF-based funding for investment purposes only, while SMEs secured by a natural foreign currency hedge also gained access to foreign currency funding, which had not been available in the previous phases.

Figure 14: Distribution of loan purposes in the different FGS phases



Note: the data for the second phase of the FGS include the loans extended under the FGS+ scheme, worth HUF 23 billion, which ran in parallel with the FGS.
Source: MNB

Over the approximately four years until March 2017 during which the FGS was operational, almost 40,000 domestic businesses gained access to more than HUF 2,800 billion worth of funding in the three phases of the scheme combined. Of this, nearly HUF 1,700 billion was used to finance investments. In addition to improving access to credit for SMEs, the programme has also had a significant indirect impact by restoring a previously malfunctioning credit market, which has provided a further lasting contribution to economic growth (MNB, 2018a).

Introduction of the Market-Based Lending Scheme

Against the backdrop of the gradual phase-out of the FGS, in parallel with its third phase, the Market-Based Lending Scheme (MLS) was launched at the beginning of 2016 to promote market-based lending without central bank refinancing.

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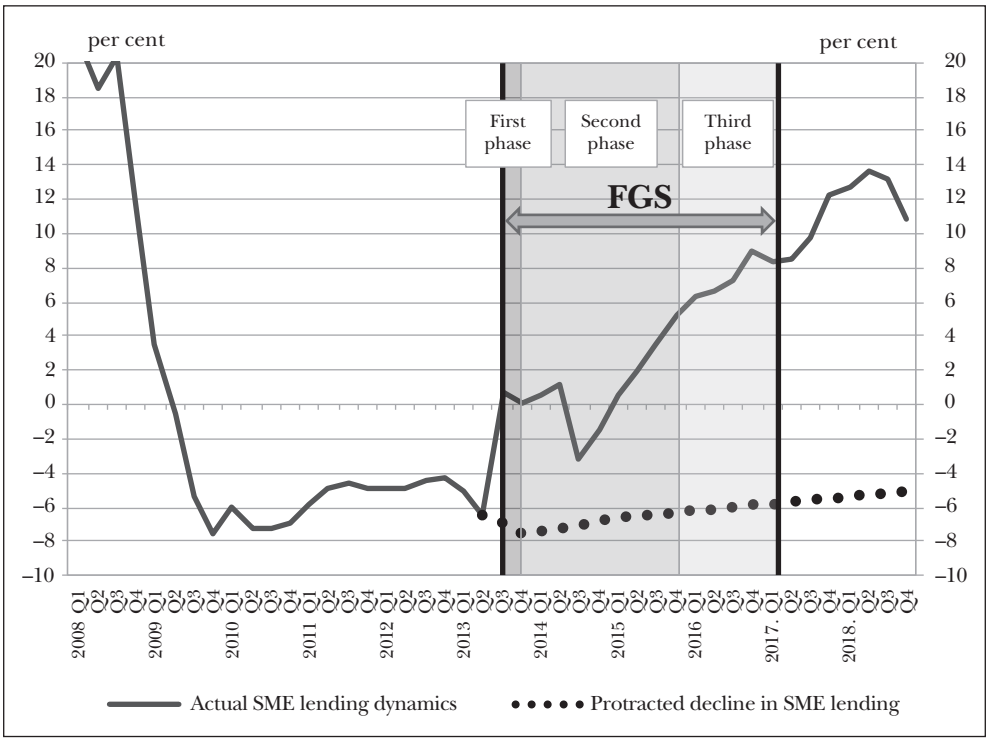
Figure 15: Growth rate of the credit volume in the SME sector



Source: MNB

To support lending activity, the MLS employed a combination of two central bank instruments. interest rate swaps conditional on lending (LIRS), and the preferential deposit facility. The LIRS provided banks with a means to hedge the interest rate risk on their long-term SME loans, whereas by accessing the instrument, banks undertook to step up their net lending to SMEs by at least a quarter of the transaction value during the term of the transactions, i.e. over a period of 3 years. Under the preferential deposit facility, the central bank offered credit institutions concluding LIRS contracts the option to earn interest on a larger part of their liquidity at the central bank base rate (MNB, 2015).

The SME lending increment undertaken in the first phase of the MLS in 2016 amounted to approximately HUF 200 billion, corresponding, at the level of the national economy, to a 5-per cent increase in the overall SME credit volume. Under the second phase of the MLS, launched in July 2017, banks continued to increase their SME lending commitments for 2017 (MNB, 2019b).

Introduction of FGS Fixed

Although by 2018 corporate lending had reached an adequate level in terms of dynamics, its structure was still not healthy enough. The distribution of maturities of

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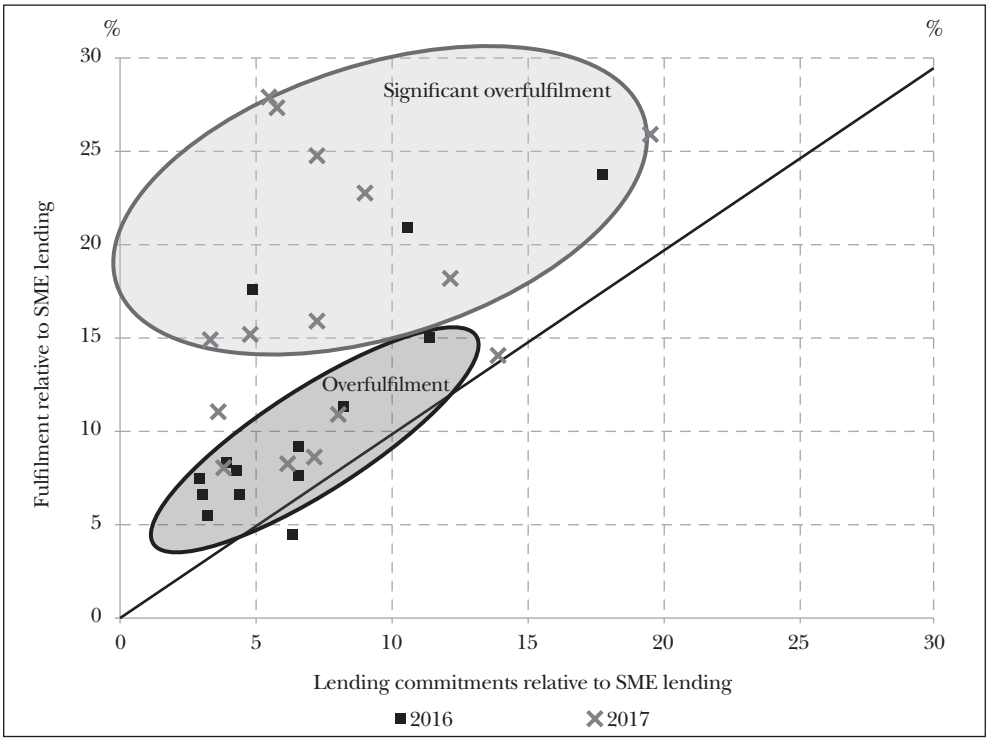
Figure 16: Fulfilment of the lending commitments made under the Market-based Lending Scheme



Source: MNB

SME loans shifted towards shorter terms, accompanied by another major fall in the ratio of fixed-rate loans.

For that reason, following its decision to reintroduce an instrument that had already achieved significant results and had a positive impact on the volume and structure of lending, in early 2019 the MNB launched a new version of the FGS with an allocated budget of HUF 1,000 billion. The new scheme, announced under the name of FGS Fixed, is identical with earlier phases of the FGS in terms of key parameters and the method of implementation, except that it is even more targeted. It is available for investment purposes only, for maturities of at least 3 years. As a new feature, the programme is liquidity neutral given that banks' surplus liquidity resulting from the credit volume disbursed under the FGS Fixed is sterilised through preferential deposits at the base rate (MNB, 2018a).

Household lending

Following the onset of the crisis, households' attitudes to borrowing were determined by the pursuit of prudence and debt reduction. Accordingly, credit institutions' household credit volume decreased steadily between 2010 and 2016, in which a major

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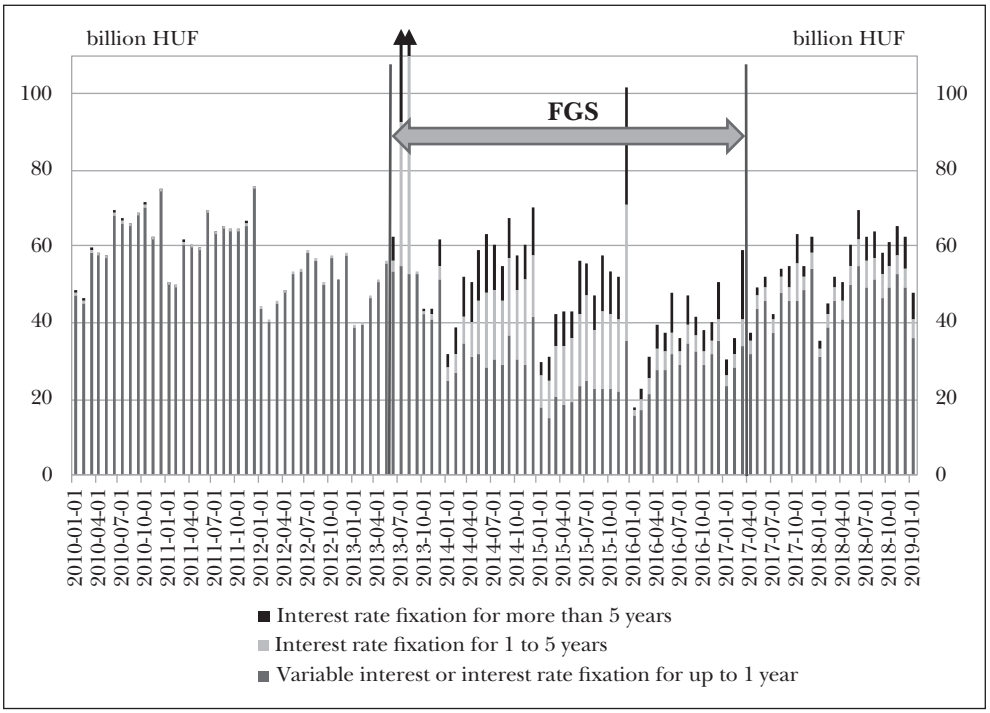
Figure 17: Breakdown of new HUF corporate loan contracts of up to EUR 1 million by interest rate fixation period



Source: MNB

role was occupied by government programmes (preferential full early repayment, and settlement of unilateral interest rate increases and exchange rate margins).

In terms of new contracts, lending reached its low point in 2012 and 2013. In these years, the annual volume of new retail lending was just over HUF 300 billion, representing a drastic drop compared to the HUF 2,000 billion contracted in 2008. However, from 2013 onwards, the retail credit market started to recover gradually as growth picked up in the real economy and incomes. In 2018, total new retail lending reached HUF 1,500 billion, with the overall household credit volume increasing by more than 7 per cent. In 2018, the housing loan market, which plays a particularly important role in retail lending, reached pre-crisis levels in nominal terms in terms of new contracts. In addition, current new lending is accompanied by a far greater volume of maturing loans; consequently, a similar contract volume amounts to a much lower rate of debt growth across the sector.

This becomes evident when looking at household debt as a percentage of GDP: while this indicator stood at 31 per cent after the onset of the crisis (exceeding the readings of several countries in the region), the ratio of household debt to GDP is currently below 15 per cent, which is one of the lowest in the European Union.

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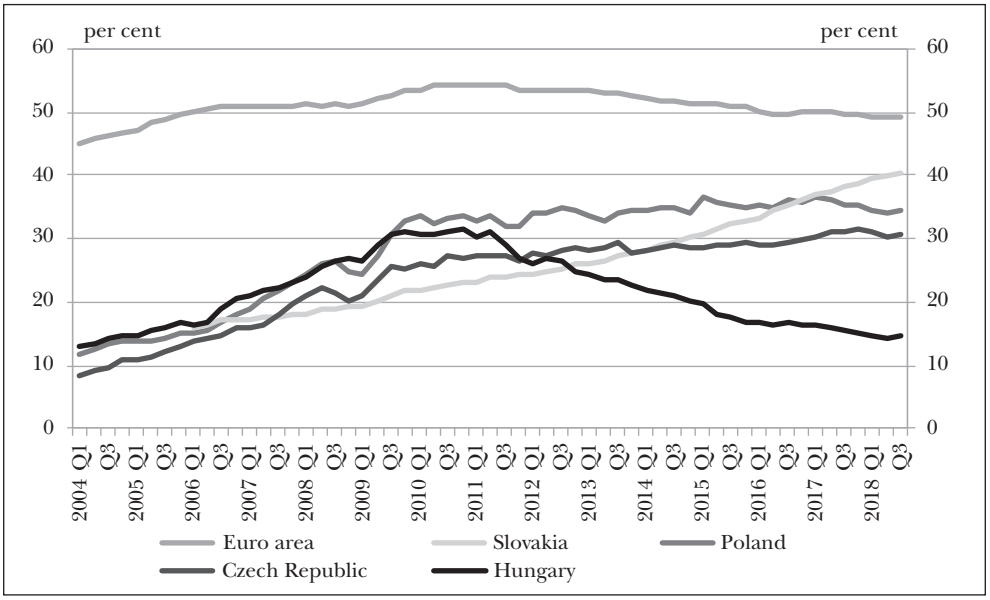
Figure 18: Household credit-to-GDP in an international comparison



Source: ECB, MNB

The healthy growth of household lending is ensured, among other things, by the debt brake rules applied as of 2015 to maximise payment to income and LTV ratios, and by the predominance of loans with rates fixed for longer periods in new lending (MNB, 2019a). In the latter process, an important role was occupied by the introduction of the Certified Consumer-Friendly Housing Loans, which provided consumers with calculable terms of borrowing, while increasing competition through the easier comparability of bank offers. By the end of 2018, the share of CCFHL products had risen to over 60 per cent within loans with interest rates fixed for over 5 years. These rules enable household debt to grow so that debt is spread over the balances of a higher number of households, which in turn makes it less vulnerable to unexpected changes in the economic environment.

Turnaround in foreign currency debt – against the trap of foreign currency loans

Foreign currency lending to households proved to be one of the most damaging and costly episodes in the history of Hungary's financial sector since the regime change. Foreign currency loans carried significant macro-financial risks, which substantially increased Hungary's vulnerability. The HUF conversion of foreign currency loans was therefore a key economic policy objective, which, however, could only be accomplished in 2014–2015. The reason was that the conditions for a conversion that was free of any financial tensions were only in place by that time. These were:

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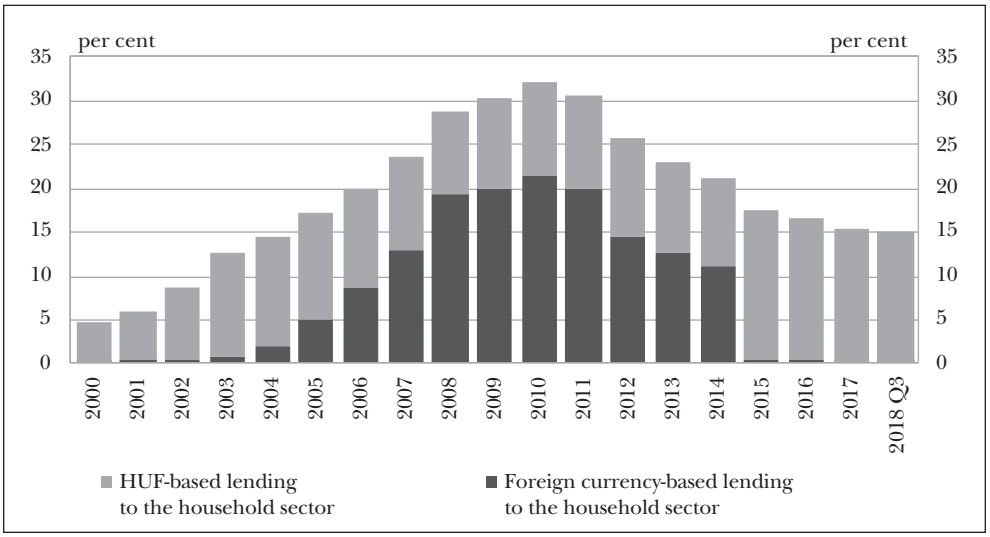
– a robust regulatory environment,
– low forint interest rates,
– a stable and consolidated macroeconomic environment,
– available foreign exchange reserves.

The approximately EUR 9 billion required for conversion was provided to banks by the Magyar Nemzeti Bank, so that the conversion was carried out without causing any tension in the foreign exchange market (Kolozsi et al., 2015). Additionally, the MNB also played a major role in the settlement of accounts taking place simultaneously with HUF conversion, both in the development of the methodology that was mandatory for all credit institutions, and in monitoring the implementation of the measure (MNB, 2016).

Figure 19: Volume of lending to households in the overall financial intermediary system as a percentage of GDP, by currency



Source: MNB

In the course of HUF conversion, the risk from foreign currency loans was virtually eliminated via economic policy cooperation between the Government, Parliament and the Magyar Nemzeti Bank. The timing of the programme was all the more appropriate in light of the fact that in a mere two months after the exchange rate fixation, the Swiss central bank removed its peg to the euro, which subsequently led to sharp appreciation of the Swiss franc. From the previous range of HUF 250 to 260, the CHF rate surged to HUF 320 in a matter of days; however, the impairment resulting from higher vulnerability could have been much more severe, up to 70 per cent (Fábián, 2015), without the preceding technical implementation of the HUF conversion. In addition to the exchange rate effect, the MNB's monetary policy moves also had a positive effect; namely, the 2.1-per cent BUBOR applicable at the time of conversion

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has fallen by nearly 200 basis points in recent years, which was also reflected immediately in the interest rate on newly converted HUF loans. Overall, in the four years since the conversion, thanks to the measure debtors have been relieved of significant extra burdens. In combination, the absence of a settlement with banks, continued exchange rate risk, and a persistently high level of external vulnerability could have increased households' expenditures by up to HUF 2,100 billion.

Turnaround in growth and convergence

The economic policy turnaround after 2010 affected both structural and financing conditions for growth. Major turnarounds were achieved in many key areas of the economy, which paved the way for the transition of the Hungarian economy to sustainable growth and the resumption of real economic convergence.

Driven by the protracted deleveraging pressure resulting from debt accumulated before the crisis, households' consumption reversed in 2013, following the trend reversal in the labour market. This was largely supported by the reduction of households' foreign currency debt from autumn 2011 onwards, and the introduction of the flat-rate personal income tax. As a combined result, households increasingly stepped up their consumption, creating the most important foundation for strong domestic demand, on which domestic economic growth is based.

Following the crisis, major changes have been observed in households' propensity to save. Since the crisis, the savings ratio has increased to over 9 per cent of disposable income. The financial net worth of households started to increase steadily after 2010 and has reached historically high levels in recent years, while household indebtedness fell below the levels seen in the years preceding the crisis. Between 2010 and 2018, the net financial position of families improved by more than HUF 25,000 billion, nearly one-third of which was due to the reduction of earlier debt, and two-thirds to financial investment from current income, and the revaluation of existing savings. Driven by a stable economic outlook, improving household confidence and favourable income trends have resulted in the persistence of higher savings rates compared to previous periods, providing a stable growth path and financing environment for the Hungarian economy.

Another key pillar of domestic growth comprises the improvement of investment fundamentals as a result of a boost in corporate lending. Thanks to the central bank's loan programmes, the Hungarian economy experienced an investment trend reversal as early as 2014, with the Hungarian investment rate rising from the earlier 16-17% to over 27% in 2018. Expanding investments also provide for an increase in Hungary's potential growth rate over the longer term.

Previously, Hungary had achieved rapid growth only by widening its current account deficit, building on external debt. However, on the new convergence path, the economy is predominantly financed from internal resources, without external indebtedness. Households' high propensity to save, the inflow of EU funds, and the foreign trade surplus accumulated as a result of the strong export sector have all contributed

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to an improved balance of payments. Overall, the balance of payments has shown a surplus for almost a decade now.

The sustainability of growth has also been supported by the restructuring and steady decline in external debt. Following a turnaround in external debt, the country's net external debt ratio fell below 10 per cent of GDP at the end of 2018 and is currently projected to reach 0 per cent around 2021, i.e. from the end of the decade domestic participants may have more foreign receivables than the foreign debt they are required to repay.

Summary of the aggregate effects of monetary policy and of the economic turnarounds since 2010

Overall, both conventional and unconventional central bank moves have provided substantial and comprehensive support for macroeconomic growth. Since 2013 the Hungarian economy has grown by 23.1 per cent in total, almost half of which, 12 per cent, was driven by monetary policy programmes. We estimate that interest rate cuts and central bank programmes directly contributed to GDP growth by more than 6 per cent in 2013–2018. Specifically, the credit flow generated by the FGS contributed 3.5 percentage points, the MLS program 0.9 percentage points, and interest rate cuts 1.7 percentage points. That said, the central bank programmes also have a number of indirect effects. In 2013, the economy was characterised by a credit crunch, where the lack of trust between banks and other participants in the economy was a major barrier to healthy lending. The central bank programme also played a substantial role in restoring confidence and revitalising the SME market. On the other hand, through the conversion of foreign currency loans, households were protected from significant losses, which was one of the drivers behind the turnaround in consumption and household investment. Also taking indirect channels into account, we calculate that the central bank boosted growth by nearly 12 per cent, i.e. more than one-half of the GDP growth of 23.1 per cent over the period.

Thanks to the MNB's easing cycle, its Self-financing Programme, and the transformation of the central bank's toolkit, yields fell significantly, resulting in significant savings for the budget, households and companies alike. Due to falling sovereign market yields, public savings on interest amounted to a total of HUF 2,400 billion between 2013 and 2018. Interest payments by corporates to credit institutions have fallen by a total of HUF 1,400 billion since 2012. Interest payments by households to credit institutions have fallen by a total of HUF 1,400 billion since 2012. Up to the end of 2018, more than HUF 2,800 billion worth of loans were disbursed under the FGS programmes. HUF conversion curbed the increase in households' debt burden by nearly HUF 2,100 billion. The MNB programmes introduced since 2013 have thus injected a total of some HUF 10,000 billion into the economy.

In 2013, real economic convergence resumed amid strong growth across the EU Member States, and the pattern of growth became balanced. In the six years since 2013, domestic GDP growth has averaged 3.5 per cent, approximating 5 per cent in

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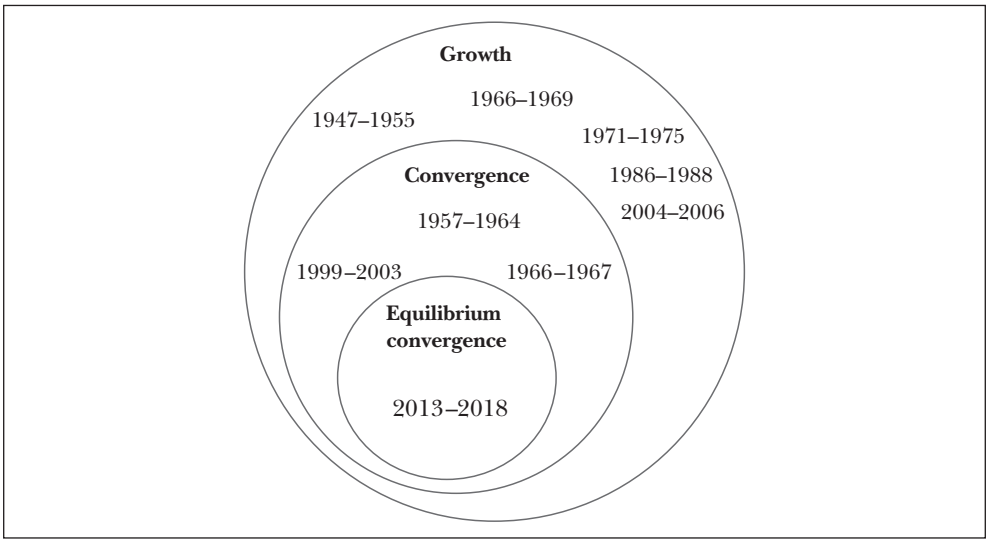
Table 1: Impact of MNB programmes in HUF billion

Impact of MNB programmes	**10,100**
Funding for Growth Scheme	2,800
Savings on interest by the public sector	2,400
Savings on interest by corporates	1,400
Savings on interest by households	1,400
HUF conversion	2,100

Source: MNB

2018. Moreover, that growth was achieved in a context of moderate economic activity in Europe, whereby Hungarian GDP growth exceeded the growth rates of advanced Western European economies by an average 2 percentage points during the period, and 3 percentage points at the end of the period. What makes the period of growth and convergence since 2013 unique in Hungarian history is that convergence is being achieved under sustainable macro-financial conditions.

Figure 20: Growth periods in Hungary



Note: A growth period is defined as any period during which real GDP growth of at least 1 per cent can be shown. Another important criterion is that growth should last for 3 consecutive years. For the purposes of this paper, convergence is defined as the approximation of Hungary's per capita level of development, measured in fixed terms in USD, to that of Austria. In that regard, periods have been taken into account in which convergence was achieved for at least 2 consecutive years. For the purposes of equilibrium convergence, years have been taken into account in which convergence was accompanied by a surplus in the balance of payments, and declining external debt.
Source: Maddison, UNCTADstat, MNB

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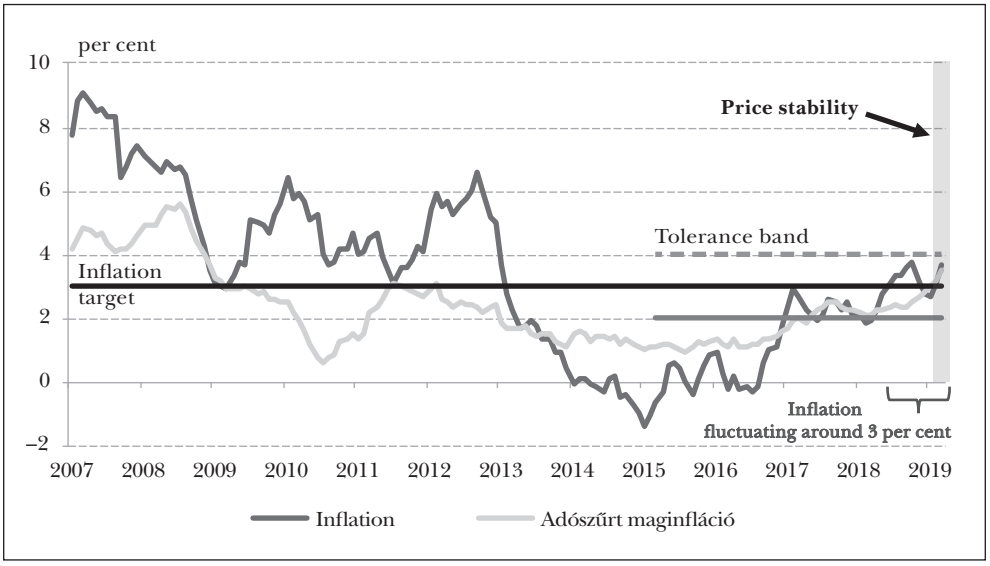
From a central bank perspective, given that the primary objective of the MNB is to achieve and maintain price stability, mention must also be made of price index developments. Domestic inflation remained high following the economic crisis, then fell steadily in 2013 and remained at around zero per cent until 2016 in a global environment of extremely low inflation. However, since the beginning of 2017, except for a few months, the price index has been moving within the central bank's tolerance band, fluctuating around the 3 per cent target since mid-2018. At the beginning of 2019, as tax-adjusted core inflation rises, Hungarian inflation is confirmed to be at a level that is consistent with price stability.

Figure 21: Changes in inflation and tax-adjusted core inflation



Source: HCSO, MNB

Challenges of the future

The international monetary policy and macroeconomic environment is currently changing: most of the advanced economies have reached a mature stage of economic growth, emerging market capital flows have become more volatile and uncertainty over the economic outlook has increased. Several analyses have already raised the possibility of the reoccurrence of an economic crisis. For a converging, small, open economy such as Hungary, this means that economic policy must continue its efforts to reduce the country's vulnerability, strengthen the lines of defence created and preserve financial stability.

In order to sustain recent years' rate of convergence over the long term, the positive trends that have emerged must be maintained, while further measures to improve competitiveness are also needed. The key challenge in the process is for Hungary to

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escape the middle income trap. The lessons learned from economic history clearly show that convergence will not happen automatically. In the case of faster growing economies, their additional economic growth compared to advanced regions usually peters out before they can catch up with the advanced economies.

The point in the turnaround in competitiveness that is required for successful convergence is to replace the former predominantly extensive growth model with a knowledge and capital intensive growth model that is based on quality criteria. There is no universal formula for successful convergence. That said, high productivity, the use of modern technologies, high levels of human capital and favourable demographic trends have generally contributed to the convergence of successful countries. Hungary must also take its own path in strengthening its competitiveness, while also taking into account international experience and domestic conditions.

The 330 proposals of the Competitiveness Programme published by the Magyar Nemzeti Bank in February 2019 seek to promote Hungary's achievement of a turnaround in competitiveness. Implementation of the programme may be sufficient means to ensure that, by 2030, Hungary's level of development is raised to 80 to 90 per cent of Austria's level, which provides the highest standard of living in the region. But those measures can only be assessed by studies to be prepared in more than a decade's time.

Notes

[1] To be calculated at consolidated level as the ratio of newly raised HUF funds secured by household mortgage loans (e.g. mortgage bonds, other mortgage-backed securities, mortgage bank refinancing loans) to the net volume of household HUF mortgage loans maturing in more than one year.

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László Domokos

How Does the State Audit Office Promote Good Governance in Public Finances?

Summary
The State Audit Office of Hungary (SAO) conducts audit of more than 800 organization, (which can be public institution, municipalities, state and/or municipality owned enterprises, foundations and non-state service providers) on the efficiency, effectiveness and the regulation of the usage of public funds in accordance with good governance. In addition, SAO has an important role for analyzing and assessing the budgetary risk and shortcomings, with this action it also supports the stability of Hungary. The SAO not only supports good governance by conducting audit and providing "guide", but also leading by example and functioning as a role model for institutions using public funds.

Journal of Economic Literature (JEL) kódok: E6, F33, H6, H83
Keywords: State Audit Office of Hungary, public finance, fiscal consolidation, transparency, Fundamental Law of Hungary, Fiscal Council

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Introduction

The best indicator of a supreme controlling organisation's efficiency is improvement in the lawfulness and efficacy of using public funds. In order to achieve greater social impact, the number of audits may need to be increased. More importantly, audits should result in the correction of errors and elimination of deficiencies by the audited organisations. However, this is only the direct outcome of the reviews performed by the audit office. The direct impact achieved by the disclosure or the supreme audit organisation's reports; focused communication and consultancy based on its audits may be more significant. In the past 10 years the management of the State Audit Office of Hungary has also endeavoured to increase the number of audits in order to eliminate any blots in the audit of public funds. It has also achieved that its audits do not remain without consequences, in other words, the audited organisations take the actions required on the basis of SAO's findings and proposals. As a result of SAO's utilitarian communication activity applying modern implements, public confidence in SAO has improved and the more important findings and conclusions made in the audit office's reports and analyses have become widely known and recognised.

The State Audit Office has two powers that are not characteristic of the other supreme supervisory institutions. The first one is SAO's authorisation, aside from auditing the final accounts of the government, to compile an opinion for Parliament on the merits of the draft budget act. SAO's other special authorisation relates to the *ex officio* membership of SAO's president in the Fiscal Council, i.e. Hungary's independent fiscal institution. In this context, SAO is required by law to contribute to the Fiscal Council's work by its analyses. In order to fulfil this obligation, SAO compiles 8 to 10 analyses about the current situation of the government budget and certain fiscal policy issues. Consequently, the efficiency of SAO's work can also be judged by the extent of its ability to contribute to the creation and retention of the fiscal balance. For this reason, in this article first the Audit Office's contribution to fiscal stabilisation is presented, and then the method of SAO's contribution to good governance in the entire field of public finances is described.

Successful fiscal consolidation after the global financial crisis

SAO's efforts made in the fiscal field can be considered successful, as since 2012 the budget balance has been restored and retained. The ratio of government debt to GDP has been on the constant decrease. In order to better understand successful consolidation, it is reasonable to familiarise yourself with the circumstances that required the consolidation.

In the 1990's, transition from a socialist to a market entailed a massive economy economic recession. Transition was rendered more difficult by the huge government debt accumulated by Hungary by the end of the 1980's. However, as by the end of the 1990's, the economy had set out on a growth trajectory, the equilibrium in public

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finances had also improved, and by 2002, the government debt hardly exceeded 50 per cent of GDP.

In 2003, however, balance in the Hungarian economy started to deteriorate again. The reason was that due to the favourable world economic situation and Hungary's 2004 accession to the European Union, access to external funds became easier and cheaper over the short term. The Hungarian government of the time endeavoured to boost the economy by using external funds, and as a result of various – mainly flawed – incentives, from 2006 the rest of the economic participants also chose indebtedness to external creditors in foreign exchange. Table 1 sums up the consequences.

Table 1: Deterioration in the external and internal balance, 2003–2011 (as a percentage of GDP)

Description	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**
Net financing requirement	–8.3	–9.6	–8.0	–6.7	–6.5	–5.7	0.9	2.1	3.3
Balance of the government sector	–7.1	–6.5	–7.8	–9.3	–5.0	–3.7	–4.5	–4.5	–5.4
Gross external debt	57.9	69.9	80.6	90.4	102.9	120.9	142.6	143.9	148.8
Gross government debt	63.1	58.7	60.5	64.5	65.5	71.6	77.8	80.2	80.5

Source: Edited by the author, on the basis of data by the Central Statistical Office

Clearly, the balance of local governments exceeded the 3 per cent allowed in the EU regulations by more than double, and in 2006, more than treble, and a slight improvement started only after 2007. With the exception of 2006, the net financing requirement, i.e. the extent of using external funds, was even higher. As a result, the gross external debt rocketed, and from 2004 it was further boosted by the gross government debt and its financing from external funds. By 2008 the gross external debt had grown to double the 2003 figure, and the gross government debt exceeded the 60 per cent limit set by the EU by more than 10 percentage points in 2008.

In the autumn of 2008 the global crisis hit Hungary in this situation. The Hungarian government needed the lifeline thrown by the European Union and the International Monetary Fund, i.e. a rapid credit facility to prevent Hungary from sinking into insolvency. As a result of additional external loans, Hungary's gross external indebtedness broke a record and approximated one-and-a-half times its GDP. Extremely painful austerity measures had to be taken to keep the government sector balance below 5 per cent, but the price paid for this was a drop in GDP by more than six per cent. Simultaneously, both businesses and the population curbed their spending, which in turn resulted in change of the net financing requirement from the negative to the positive.

Despite the help offered by international organisations, it was clear for the new Hungarian government set up in 2010 that Hungary had to consolidate its budget and stabilise and then boost its economy by its own efforts. As a result of a successful con-

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solidation, by 2012 the budget deficit had dropped and then remained permanently below 3 per cent of GDP (see Table 2). Thus, in 2013, Hungary was released from the European Union's strict fiscal supervision called Excessive Deficit Procedure.

Table 2: Improvement in the external and internal balance, 2011–2017 (as a percentage of GDP)

Description	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Net financing requirement	3.3	4.3	7.3	5.2	7.4	6.2	4.3
Balance of the government sector	–5.4	–2.4	–2.6	–2.6	–1.9	–1.6	–2.2
Gross external debt	148.8	129.2	117.8	117.1	108.7	97.0	84.9
Gross government debt	80.5	78.4	77.1	76.6	76.6	75.9	73.3

Source: Edited by the author, on the basis of data by the Central Statistical Office

The data of the table clearly show that in 2012 a steady decrease also began in the gross government debt. Decline in the gross external debt was even faster, as household savings represented an ever increasing ratio in government debt financing. Acceleration in economic growth, which began in 2013 and approximated five per cent in 2018, had a major role in the favourable change in indicators.

The State Audit Office's audits to facilitate the consolidation of public finances

In 2010 Hungary's public finances compared to a tank with water leaking through several large holes. In such a situation the most important task was to focus our audits to the most critical places, revealing the causes of deficit and making proposals for its elimination. Perhaps the most significant components of this activity included the following:

– Mandatory private pension funds;
– Indebtedness of local governments;
– Management of government debt;
– Business associations in public ownership;
– Our audits and analyses of the fiscal risks involved in the monetary policy.

Audit related to mandatory private pension funds

The most striking example was provided by mandatory private pension funds. The State Audit Office thoroughly explored the topic from all angles in 2010, when the operation of guarantee fund underlying private pension funds was audited. The original purpose of the guarantee fund was to guarantee pension disbursement for the beneficiaries of pension funds should they become insolvent. If the guarantee fund is emptied, the central budget was supposed to step in and perform the liabilities. We identified minor deficiencies in the Fund's management, but the most significant finding of the audit was that it shed light on the unsustainability of the entire regime.

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In 1996 Hungary set up a pension regime essentially based on the idea that the younger generations withdrew the majority of their individual pension contributions and transferred them into private pension funds, and the budget was expected to top up the shortfall in social security revenues by ever increasing amounts in order to pay the allowances of those who had already retired. The difference, the European Commission refused to recognise as an adjustment item, increased the government deficit and the government debt at a pace accelerating year by year. To give you just a few characteristic data: the central budget used HUF 28.1 billion to support the pension insurance fund in 1998 and HUF 599.1 billion in 2009, representing more than a twenty-fold increase, and exceeding 2 per cent of GDP in 2009. The central budget contributed to the financing of retirement benefits increasingly: while back in 1998 its contribution amounted to 3.6 per cent, in 2009 it was already 21.1 per cent.

As a result of the financial crisis that began in 2008, savings in pension funds dropped by more than 21 per cent, and thus we were clearly running the risk that yield on the savings deposited in private pension funds may remain below the inflation rate during the savings period. To address to this risk, in 2009 Parliament amended the relevant act to undertake a yield guarantee, in other words, it required that if the real yield of the saving remains negative up to the establishment of the pension, then the private pension must be determined as a multiple of the deposit and the inflation rate. This decision was adopted at a moment following eleven years of nearly 6 per cent average inflation rate, while the mean nominal yield of savings hardly exceeded 1 per cent. Undoubtedly, ultimately the payment of this guarantee also required coverage from the central budget. Nevertheless, not even estimates were made of how many thousand billion forints of additional expenditure this guarantee – or it would be more factual to call it a blank cheque – required of the taxpayers of the time. This financially unsustainable system had to be discontinued. This shut off the flow that tapped and drained pension contributions from the government-organised social security system. Subsequently, the budget of the Pension Insurance Fund was stabilised, and moreover, surplus was made for several years.

Audits revealing local government indebtedness and its causes

The other most critical area was the system of local governments. For this reason, aster 2011 the State Audit Office conducted comprehensive audits, first of the Local Government of Budapest, then of the cities with county rights, and then by representative sampling, it selected 62 city and town governments for audit. Finally, financial equilibrium was analysed at numerous minor local governments selected on the basis of a risk analysis. Chart 1 illustrates our comprehensive findings.

The figure shows that by the end of 2010, local governments' liability from bond issuance had increased to HUF 588 billion, nearly 25-fold, in comparison to the opening balance in 2007. By the end of 2010, their liabilities from borrowing had increased by HUF 192 billion, representing 41 per cent, on the 2007 opening balance.

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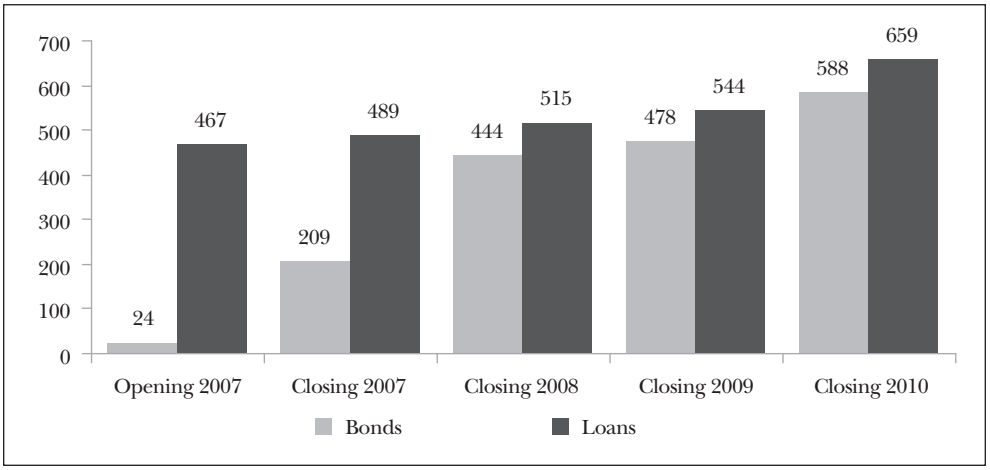
Chart 1: Local government bonds and loans, 2007–2010 (HUF billion)



Source: SAO Report no. 1282, p. 12

In November 2011, the State Audit Office compiled a summary report of the experiences gained during local government audits and made proposals for several government actions. These were aimed at solving the grave financial situation, on the one hand, and at the prevention of the local governments' repeated indebtedness on the other. It is recalled that the local governments' debt was consolidated, and any transactions giving rise to debt were made subject to government authorisation.

After debt consolidation, the State Audit Office still keeps the audit of a wide circle of local governments on the agenda, as it wishes to prevent the individual local governments from repeatedly running into debt. Thorough audit is required precisely because after the prevention of overt indebtedness, poorly managed local governments have been maintaining their solvency temporarily in implicit forms of indebtedness (e.g. the late payment of supplier claims or borrowing through their business associations.

The audit of government debt management

Government debt management was the third critical area we needed to urgently audit. Our report about the audit of the debts and long-term commitments of the central sub-system in public finances, published in August 2012, identified gross shortcomings. Chart 2 gives a good illustration of the situation that evolved.

In the audited period increase in foreign exchange debt from 28.0 per cent in 2006 to 44.7 per cent in 2009 was an essential risk factor. In 2010 the risk realised by a massive forint weakening, and increased government debt by HUF 1656.7 billion.

SAO's audit found that the cost and risk management model developed in 2004 for the purposes of debt management had not undergone either internal development, or an audit or a content review. This model did not manage the average remaining maturity of HUF and FX debts, the impact of change in the yield curve on debt man-

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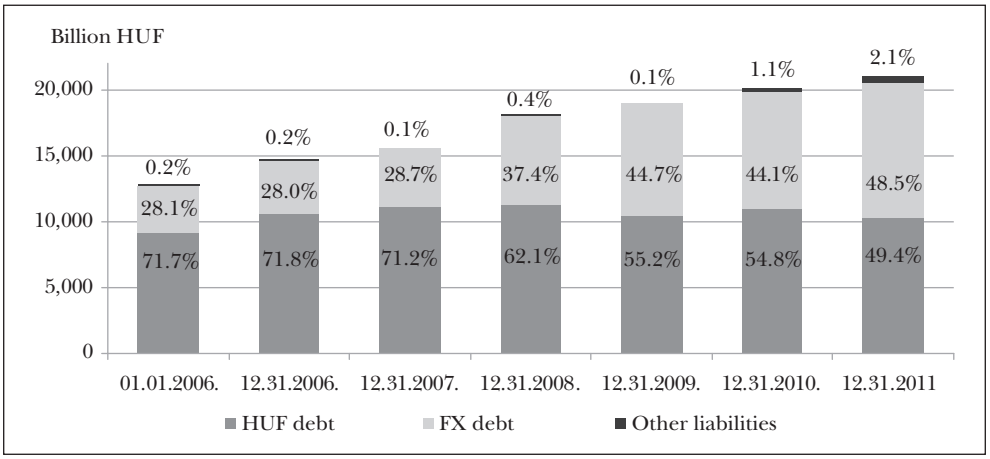
Chart 2: Composition of government debt, HUF/FX



Source: SAO Report no. 1294, p. 17

agement costs, the market stress situations and the risk involved in credit rating. Államadósság-kezelő Központ Zrt. (the government debt management centre) had failed to assess and evaluate the costs and effectiveness of the individual financial and financing operations. SAO recommended that the Minister for the National Economy should take action to review the developed cost and risk management model and to elaborate an evaluation system in support of the cost efficiency of the debt management activity in order to monitor and reduce debt financing costs.

We also identified heavy future burdens during the audit of long-term liabilities, as shown in Chart 3.

It is easy to read from the figure that as a result of motorway concessions and PPP projects, the Hungarian budget incurred liabilities in the amount of HUF 150 billion payable by 2027, and amount of these commitments will exceed HUF 100 billion even in 2030. For this reason, SAO analysed the implementation of projects in a PPP scheme in the framework of several audits. It was established that these projects were generally overpriced, and instead of the risk sharing expected of a PPP scheme, the government remained the only party to assume the related risks. SAO requested reviews of the PPP contracts and the establishment of liability.

SAO audited government debt management every year in the framework of its audit of the annual accounts, and then in 2015, it repeated the comprehensive audit. It can be established that in the past few years the exchange rate risk of the government debt has considerably decreased as by the end of 2016 the ratio of FX debt to the total government debt had dropped to 24.6 per cent, nearly half of the corresponding figure recorded at the end of 2011. This development is illustrated in Chart 4.

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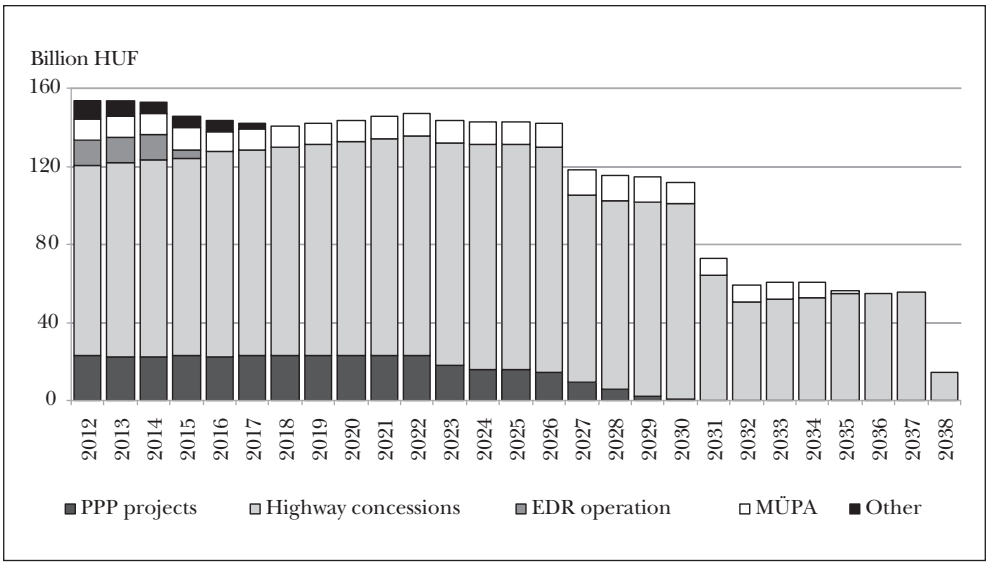
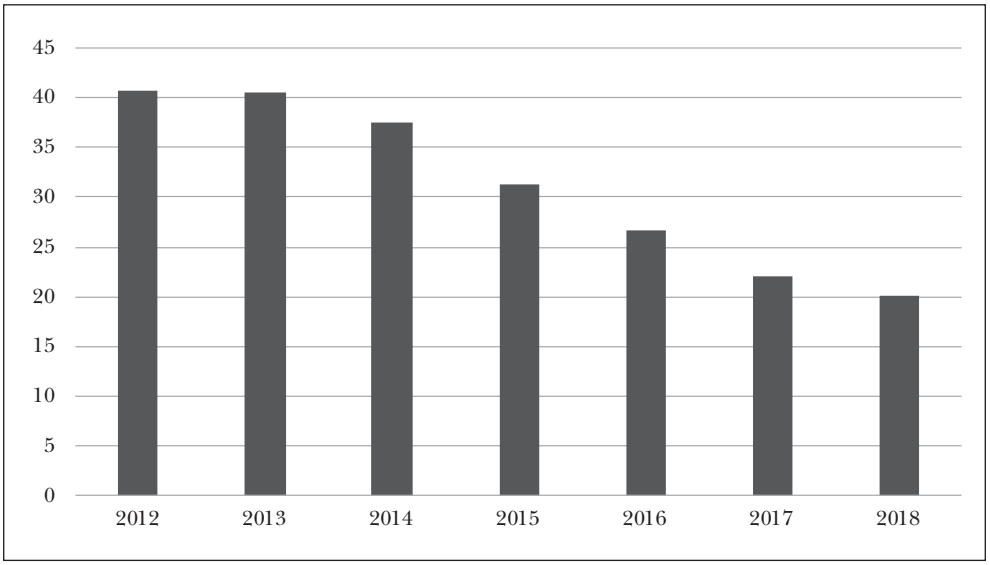
Chart 3: Planned annual budget expenses from long-term commitments



Source: SAO Report no. 1294, p. 25
On the Audit on the Debt of the Central Subsystem of Public Finances and its Commitments for Periods Exceeding one Year.) State Audit Office of Hungary, August 2012 (Report No. 1294)

Chart 4: FX debt to the gross government debt



Source: Edited by the author, on the basis of data by ÁKK Zrt.

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In addition to local governments and the central budget, indebtedness in foreign exchange also affected society at large. The actions taken to help them cost hundreds of millions of forints and/or resulted in losses in revenues for the central budget. SAO verified the implementation of these measures in the framework of an audit of the annual budget accounts. SAO separately audited Nemzeti Eszközkezelő Zrt.'s (the national asset manager's) safeguarding of assets and business management between 2011 and 2014, and found them compliant with the relevant regulations. This was instrumental in ensuring housing for the families in the worst debt trap.

Analysis of the fiscal risks involved in monetary policy

As a result of indebtedness in foreign exchange, commercial banks' liquidity measured in HUF increased significantly, and they deposited such funds with the National Bank of Hungary, which paid high interest on them. As SAO is not authorised to audit monetary policy, it called the attention to the fiscal risks of the monetary policy of the time in an analysis (Pulay et al., 2013). In this analysis we demonstrated the rapid rise in interest burdens, as plotted in Table 3.

Table 3: Amounts paid by the National Bank of Hungary (MNB) for monetary assets (2007–2011)

Description of the monetary asset	(Net) interest paid by MNB (HUF billion)					
	2007	**2008**	**2009**	**2010**	**2011**	**5 years, total**
Minimum reserve requirements	49.6	60.9	29.4	20.0	54.6	214.5
Two-week bond	75.1	71.4	226.7	213.8	255.2	842.2
Overnight deposit	0.5	12.1	24.8	4.8	8.2	50.4
Total	125.2	144.4	280.9	238.6	318.0	1107.1

Source: Edited by the author, on the basis of data by the National Bank of Hungary

The analysis raised the necessity of regulatory changes that would lower the interest payable by the National Bank of Hungary, and simultaneously channel part of the liquid funds for financing the government debt. From 2013, the central bank's new management found the monetary policy actions that led in the direction we recommended.

Audit of other organisations classified into the government sector

SAO audits an increasing number of business associations in state and local government ownership, as according to the regulations of the European Union, part of them fall in the government sector and thus their debts increase government debt. In the case of other organisations included in the government sector (i.e. not included in public finances), we can speak of rising numbers, as an increasing number or organisations are found that should be classified in the public finance sector based on the

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features of their business management. Simultaneously with rise in their number, the debt they represent is also on the increase, and this is further increased by a rise in the debt of the individual business associations.

Table 4: Debts of other organisations classified into the government sector, 2010–2016

Year	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Debt, total (HUF billion)	70.3	62.5	123.5	154.9	190	319	332.6

Source: Data by the Ministry for the National Economy

The data clearly show that these are no insignificant amounts, as in 2016 the aggregate debt portfolio already exceeded 1 per cent of GDP. SAO monitors this process and in the course of its other audits of entities classified in the government sector, it assigns priority to exploring whether or not the particular audited business association had any transaction generating government debt and if it was duly authorised. It was high time we inspected these matters, as we also found gross deficiencies in this field. For example, there was a business organisation which was not aware of the fact that it had been classified into the government sector. Some companies were not aware of the serious consequences of such transactions, e.g. the obligation to seek authorisation for loans and to build an information retrieval system or a more stringent internal control system.

Another important criterion applied during the audit of business associations was the how public utility companies could react to the challenge posed by mandatory reductions in utility bills. In numerous cases we established that public functions had not been separated from other functions; the fees charged for public services were not underpinned by cost accounting calculations; and deficient management coupled with unregulated asset management posed a risk. Consequently, a more accurate accounting and a more efficient business management still offer considerable opportunities. In business management and operation we identified numerous risks that were traceable to regulatory gaps in the exercise of rights by the corporate management and by the owners.

Our audits of business associations in public ownership confirmed that there was a need to renew the state management. The Government accepted our recommendations and integrated them in the relevant statutory regulations at several points.

Opinion on the merits of the draft budget act

In order to give an opinion on the grounding of the budget appropriations, the State Audit Office developed and published a method based on solid foundations. With the help of this method, SAO can quantify the risk of underperforming or overperforming the planned appropriations, and then compares the aggregated risks with the planned budget reserves. If the latter provide coverage for the management of reasonably arising risks, it does not consider the fulfilment of the debt rule as prob-

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lematic, and if the reserves are insufficient, it motions for their increase. Why is this important? The aim of this method is to bring reserve maintenance into the focus of the opinion about the draft budget act. This method can ensure sufficient reserves simultaneously with predictability and flexibility in fiscal management. Reserves create the opportunity for the elimination of interim tightening measures (taxes and blockings), in other words, wartime budgeting.

In my opinion, the most significant outcome of the State Audit Office's initiatives is that in recent years a multi-tier provisioning system has evolved in budgeting. In addition to the general reserve that covers contingent expenses, currently termed as an "appropriation for special government actions", the County Protection Fund was also set up primarily to manage macro-economic risks. It has become general practice also for budgetary chapters to plan a reserve for the management of risks at a chapter level. However, I consider the appearance of "implicit reserves" as the most momentous development. As far as I am aware, the Hungarian State Audit Office was the first ever to coin this term in its analysis compiled for the Fiscal Council.

What is an implicit reserve? Both deficit and debt have an implicit reserve. In the case of deficit, the implicit reserve is the difference between the limit set in the relevant budget regulation and the deficit target. According to the European Union's regulation, the government sector deficit may not exceed 3 per cent of GDP. Thus if the government targets a 2.4 per cent deficit, the implicit reserve is 0.6 per cent. In the case of debt, the implicit reserve is the difference between the limit set in the regulation on government debt and the targeted debt indicator. Since 2013 the draft budget acts have always targeted more favourable deficits and debt indicators than allowed. Consequently, the draft act included considerable implicit reserves. Since 2013 this system of reserves has actually eliminated the need to implement interim adjustments. This is one of the most important achievements of fiscal consolidation, as it created the conditions for methodical budget management by fiscal units, so that they can use public funds lawfully, purposefully and efficiently.

The other important factor that contributed to fiscal stabilisation was the stabilisation of tax revenues. The fact that actual tax revenues decreasingly fell short of the plans, and in fact, in 2015 the plan was already considerably exceeded was major contribution to fiscal consolidation. Chart 5 gives a good illustration of the trend of improvement.

The figure shows that between 2010 and 2013 tax revenues fell more than a hundred billion forints short of target. The turning point came in 2014, when in the aggregate, tax revenues were collected slightly in excess of the target. And in 2015, payments considerably exceeded the target in each of the three types of taxes. The taxes and tax-type revenues collected in the amount of HUF 8000 billion in 2015 exceeded the original target by HUF 469 million (i.e. 6.2%).

There are various additional opportunities to increase the efficiency of tax collection and the legitimisation of the shadow economy. During its audits of the National Tax and Customs Authority ("Tax Authority"), the State Audit Office also identified several gross deficiencies – for example, during the audit of tax benefits, in risk management,

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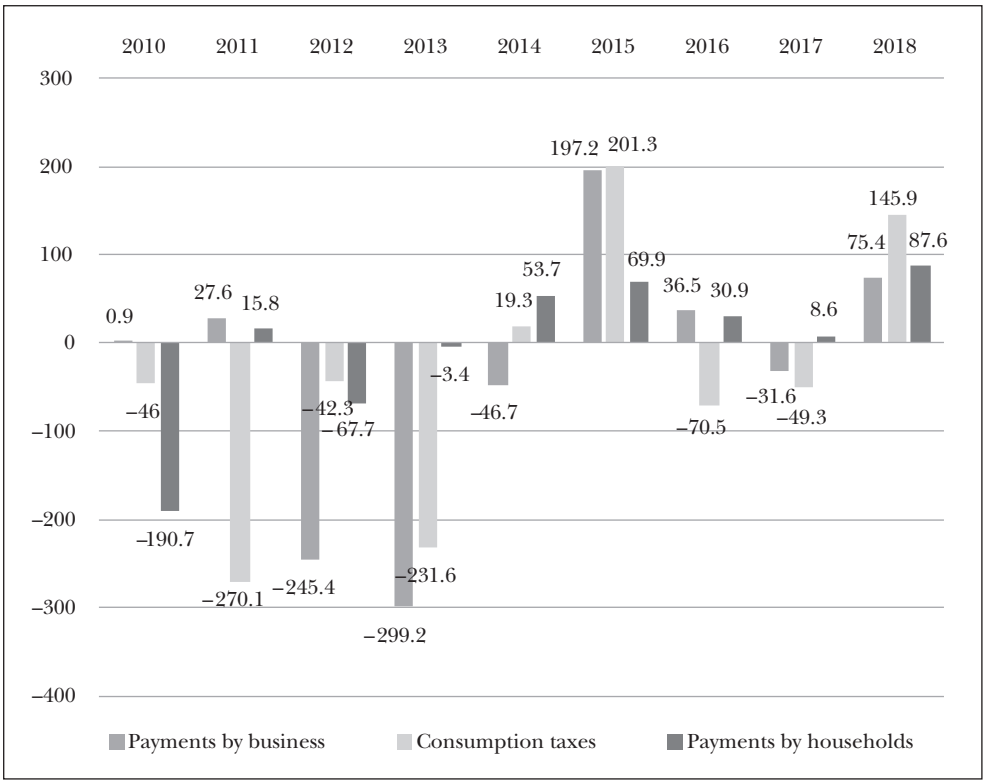
Chart 5: Difference between statutory appropriations and actual performances (HUF billion)



Source: Author's own, based on data from the Ministry of the National Economy

and in the prevention of arrear accumulation –, which may considerably increase the amount of actually collected tax revenues. Based on SAO's audit findings, the management of the Tax Authority took numerous actions that contributed to the improvement in the efficiency of tax collection.

However, improvement in the efficiency of tax collection is not an end in itself; rather it is a means of improving the competitiveness of the economy through cutting tax rates. This was why SAO urged the "sustainable legitimisation" of the shadow economy. In essence this means that in the form of lower tax rates or targeted benefits, the state lets the taxpayers have the surpluses obtained from the legitimisation of the shadow economy, and due to lower tax rates, reduction of the underground economy may continue. The tax policy actions taken in recent years reflect this intention.

Transparency on a macro-economic and micro-economic level

Article 39 (2) of Hungary's Fundamental Law requires transparency in general, when it stipulates that "Every organisation managing public funds shall be obliged to pub-

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licly account for its management of public funds. Public funds and national assets shall be managed according to the principles of transparency and the purity of public life. Data relating to public funds and national assets shall be data of public interest." The principle of integrity in public life means the use of public funds according to their intended purpose, free of corruption and fraud.

The expressions "macro-prudential" and "micro-prudential" supervision are used in relation to finances and the institutions constituting the financial intermediary system. Currently, both are performed by the National Bank of Hungary. The central bank is required to supervise the correct management of one-off risks for financial intermediary institutions, while in the framework of macro-prudential supervision, it monitors the systemic risks jeopardising the financial system and when required, it motions for actions. A prudent, in other words, forward-looking conduct refraining from the assumption of unreasonable risks and its supervision are justified because financial intermediaries invest their depositors' money and not their own, and if they make a loss or have liquidity problems, they put their depositors in a difficult situation.

Similarly, businesses using public funds spend money that does not belong to them as it has been collected by the government from citizens for financing public functions. For this reason it is reasonable to apply more stringent rules to institutions using public funds than to those using their own money. As prudent operation is a fundamental condition for financial intermediaries, so the organisations managing public funds are required, as a minimum set in the above-referenced provision of the Fundamental Law to act transparently and free of corruption. This must be enforced both at a macro-economic (government) and at a micro-economic (institutional) level. The State Audit Office is responsible for verifying whether or not the requirements of transparency and the integrity in public life are complied with both on the macro-economic and on the micro-economic level. The latter requirement primarily means operation and management without corruption.

The two most significant areas of macro-economic control include the evaluation of the draft central budget act and the audit of the government's report about the implementation of the central budget, in other words, the annual accounts. The former has already been discussed in detail. The audit of annual accounts is the most important duty of every audit office. The predecessor of today's State Audit Office was established in 1870 to audit the annual accounts of the Hungarian government budget, independent within the Austro-Hungarian Monarchy. Currently this remains the kind of audit that requires the largest capacity of the audit office. The State Audit Office perceived it as a professional challenge to check the reliability of a report of several thousands of pages. Previously, the SAO management opted to scrutinise the financial accounts of a different institutions every year in addition to the annual audit of the major items. SAO had been able to develop and apply the method suitable for giving an evaluation of the entire report on duly substantiated grounds every year by the time of the audit of the 2015 financial accounts.

On a micro-economic level the most challenging factor is the large number of organisations using public funds and public assets. This circle includes about twenty

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thousand organisations, from budgetary units through business associations in public ownership to government organisations attending to public functions (e.g. institutions of foundations and churches). With the traditional methods it would take decades for the 500-strong SAO to audit so many organisations. For this reason, the audit of all the twenty thousand organisations by SAO within four or five years cannot be set as a reasonable objective It was, however, important that every organisation financed from public funds should manage its business aware of the fact that the State Audit Office may audit its activity and accounts at any time. In order to accomplish this objective, the number of organisations audited in a year had to increase from around 200 before 2010 above 800, and the public sector should not have any "blots" never subject to an audit by the Office. This was the purpose, for instance, of the audit of minority governments and public bodies (chambers), never previously audited by SAO, and then of the comprehensive audit of business associations in public ownership, which was made legally possible for the Audit Office after 2011. 2017 saw the start of audits at a wide circle of organisations not maintained by the government but providing public services. Developments in the number of organisations audited by SAO are depicted in Table 5.

Table 5: The audit reports published annually by the State Audit Office and the number of organisations audited between 2011 and 2016

	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
Number of audited reports	71	112	194	233	221	260	251	323
Number of audited organisations	387	499	569	966	717	740	874	806

Source: Author's own, based on data from the annual reports of the State Audit Office

The last line in the table reveals that by 2013 we had managed to increase the number of audited organisations above 500, which required raising the audits to nearly 200. (A report is made of every audit, but several organisations may be inspected in the framework of an audit.) The latter was primarily enabled by the adoption of the method we call thematic group audits. In essence this means that SAO audits one or two high-priority areas in the activities (e.g. the deployment and operation of internal controls, and asset management) performed by organisations of similar types (e.g. central budget units, business associations in local government ownership, forestry holdings and museums). This proved useful not only because 10 to 30 organisations could be audited on the basis of a single professional programme, but also because the thematic group audits revealed the typical deficiencies in the individual areas. Consequently, the published reports also served as guidance in the correction of the errors for the organisations of the area that had not been audited. In order to better capitalise on this utilisation opportunity, SAO compiled a report of its experienced gained during numerous thematic group audits, and published them. Moreover, in several cases they were presented in the framework of conferences on "best practices".

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The number of audited organisations peaked in 2014. We do not aim at increasing figures at any cost, as with the given capacity, this would jeopardise the quality of audits. However, the 2015–2018 data suggest that SAO can sustainably conduct more than 200 audits per year, including the audit of 700 to 900 organisations. Currently, we are working on new audit methods that would enable further increase in the number of audited organisations. The essence of the concept is that in the first audit module, risks would be identified and additional audit modules would only be conducted in the case of companies found to be risky.

Following approval of the new law on the State Audit Office, audits focused on internal control, the accounting regime, asset management, the financial position and business management. These topics are all closely related to improvement in the business management by public sector organisations. However, simultaneous macroeconomic improvement has also remained a significant objective: The number of audits focussed on support to good state governance and on improvement in economic competitiveness has exceeded two hundred since 2015.

Facilitating the operation of a well governed state in the fiscal field

One of the most innovative provisions in the act newly adopted in 2011 about the State Audit Office stipulates that "based on its audit experience, the State Audit Office of Hungary assists Parliament, its committees and the work of the audited entities, thus facilitating well-governed state operations."[1] In relation to this the first thing to be reasonably determined is the direction SAO helps government organisations to follow. Since the promulgation of Hungary's Fundamental Law, i.e. 25 April 2011, this is clear, as the Fundamental Law, which has an independent chapter on public finances for the first time ever in Hungary's history, has set the direction of the management of public funds. Above all, the provision on government debt set out in Article 36 (4) and (5) should be highlighted. Whereby:

"(4) Parliament may not adopt an Act on the central budget as a result of which state debt would exceed half of the Gross Domestic Product.

(5) As long as state debt exceeds half of the Gross Domestic Product, Parliament may only adopt an Act on the central budget which provides for state debt reduction in proportion to the Gross Domestic Product."

As Hungary's government debt still considerably exceeds 50 per cent of the gross domestic product (GDP), the current task is to continuously improve the government debt-to-GDP ratio. With a view to this, it considers the promotion of compliance with the government debt requirement as its No. 1 priority in the course of its audits and consultancy. In the case of audits this means that the areas with a business management and operation that have direct impact on government debt are given priority during selection, and in their case the audit focuses, among others, exactly on revealing impact on the government debt and the compliance and reliability of data in this respect. Particular consideration is given to the impact on government debt during

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topic selection, but the audits also include the denominator of the debt ratio, i.e. the factors determining GDP developments. Examples include SAO's studies analysing the encouragement of research, development and innovation, and the financial role undertaken by the state (Pulay et al., 2015; 2016; 2017).

The other provisions in the chapter on public finances in the Fundamental Law further clarify the concept of good state governance in the fiscal field. Article 37 (1) of the Fundamental Law stipulates that "[t]he Government shall be obliged to implement the central budget in a lawful and expedient manner, with efficient management of public funds and by ensuring transparency." This is in agreement with Article 43 (1) of the Fundamental Law, which lists SAO's most significant tasks as follows: "Acting within its functions laid down in an Act, the State Audit Office shall audit the implementation of the central budget, the management of public finances, the use of funds from public finances and the management of national assets. The State Audit Office shall carry out its audits according to the criteria of lawfulness, expediency and efficiency." It follows from the co-occurrence of the two referenced provisions in the Fundamental Law that a well-functioning state manages public funds lawfully, expediently, efficiently and transparently, and this is guaranteed exactly by SAO's audit activity, which may review compliance, reasonableness and efficiency, and may also contribute to transparency as its reports are public.

In addition to audits, SAO also supports the operation of a well governed state by its analyses laying the foundations for its consultancy. Its regulatory basis was laid down in Article 5 (13) of the Act on the State Audit Office, which provides the following: "Within its competence, the State Audit Office of Hungary may prepare analyses and studies. In connection with the tasks of the President laid down in subsection 13(2)l), the State Audit Office of Hungary prepares analyses and studies and by the provision thereof it assists the Fiscal Council with the performance of its tasks." The referenced Article 13 (2) l) stipulates that the President of SAO "acting as a member of the Fiscal Council, shall perform the tasks assigned to them to this end in a separate act."

This co-occurrence of statutory provisions sheds light on the fact that SAO has been assigned an extremely important responsibility and powers to indicate fiscal risks by the appointment of its president to act ex officio as a member of the Fiscal Council (hereinafter: "Council"). This is because through the president's membership, the entire organisation is obliged to compile analyses and studies that help the Council in its attendance to its duties. If we continue reading the chain of provisions in the referenced act, it can be established that these analyses must be based on SAO's audit experiences, but at least they must relate to SAO's functions. It is fair to say that in order to implement the above-referenced provisions of the SAO Act, SAO had to create a new genre of analysis. These are fundamentally characterised by their link to SAO's audit activity and facilitate the operation of good state governance in the fiscal field.

One should also understand that with the establishment of this right and obligation, SAO's opportunities to indicate fiscal risks and to motion for the elimination of shortfalls have doubled. On the one hand, since SAO's re-establishment in 1990, year

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after year it has given its opinion on the draft budget act submitted to Parliament. It substantiates its opinion by an audit conducted with a special method. (SAO displays the methodology renewed in 2014 and its supplements on its website.)[2] In addition, every year it audits the final accounts. On the other, with its analysis SAO contributes to the Council's work related to opining the budget.

The Councils gives its opinion twice during the elaboration and approval of the budget. Firstly, it gives an opinion on the draft budget act, in other words, the version that has already been discussed and reconciled by the various ministries, but has not yet been submitted by the Government to Parliament. Thus the Council has the opportunity to call the Government's attention to the risks related to the planned budget before the final decision. Secondly, the Council gives its opinion on the draft budget act before it is put to the vote, after incorporation of the approved amendments proposed by the Members of Parliament.

This evaluation represents a highly important progress in comparison to the previous regulation, which did not require an organisation independent of the Government to give its opinion on the draft act amended by the proposals of the Members of Parliament, and therefore it could (and actually did) happen that the approved act involved considerably higher risks than the version submitted by the Government. Among others the reason for this is that the Members of Parliament drafted proposals to increase expenses in good faith, however, coverage was withdrawn from reserves or overstraining the target revenue. In order to preclude this risk, in addition to its right to report, the Council was granted the right of veto: Parliament is only allowed to approve the draft act if the latter complies with the debt rule, in other words, if as a result of the expected deficit the government debt increases less than GDP at current price, and consequently, the government debt improves. If this condition is not met, the government must make amending proposals and pass them through Parliament until the expected deficit is reduced to the level required for meeting the debt ratio.

Another stride included the fact that in addition to the approval of the original budget, the Council also has the above-mentioned powers during the approval of the draft act on the interim amendment of the budget act.

In addition to the evaluation of the various versions of the draft budget acts, once in six months the Council also gives its opinion on the progress made in the implementation of the act on the central budget and on the developments expected in government debt. In addition, it may give an opinion on

– The draft acts containing the amendments required for laying the basis for the provisions of the draft act on the central budget, including the draft acts that specify public dues.

– Any issue related to the planning and implementation of the central budget and to other ways of using public funds.

This broad evaluation function of the Council also expands the scope of topics analysed by SAO, since pursuant to the above-referenced statutory provision, SAO assists the Council in the performance of its functions by analyses and studies.

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It is important to note that SAO's analyses are based primarily on its on audit findings, although naturally, statistical data and literature findings are also processed in them. It should be highlighted that the analyses prepared for the Council to promote budget evaluation are nearly completely based on audit evidences collected and processed during SAO audits, and as such, they are more reliable than any other reported statistical data or academic estimate. Previously, SAO had also substantiated its opinion on the draft budget act by audits. In order to fulfil its function in the Fiscal Council, it has extended its audit performed in support of budget evaluation in two directions: it begins audit earlier and finishes it later. Earlier beginning enables it to collect audit evidences for the analysis of the draft budget act. At the end of the extended audit, on the other hand, it checks whether or not the ministry in charge of public finances has substantiated the decisions in support of amending motions made in the Government's name by the required calculations and impact analyses. The audit enables SAO to be satisfied that the conditions of the implementation of the amending motions (e.g. an IT development serving the legitimisation of the economy) are in place. The Council can only take a stand in the question whether or not the deficit exceeds the level required for compliance with the government debt rule on the basis of factual evidence. The fundamental factor in exercising veto is the reasonableness of the budget appropriations, as the numerical information in the draft act waiting for a vote formally obviously always meet the requirements arising from the government debt rule.

This new function of SAO is also important for good state governance because SAO regularly conducts audits in relation to the individual budget appropriations. For example, SAO obtains information that is essential for budget evaluation during its audits of the National Tax and Customs Administration's tax revenue appropriations and the Government Debt Management Agency's debt management appropriations. This information is regularly incorporated in the analyses compiled by SAO to support the Council's work and also sent to the heads of the competent government organisations.

Summary conclusion

The 2008–2009 financial and economic crisis undermined sustainable cooperation between the countries that follow an economic policy that is neoliberal in terms of the fundamental welfare state expectations. The previous concept of the state playing a rather passive supervisor, or a kind of a "watchman", emphasis in government action was shifted to the proactive, crisis managing role of the state in the provision of sustainable development. This paradigm change was characterised by a series of government action plans. Increasing central bank intervention in the field of monetary policy was followed by actions falling within the scope of fiscal policy implements, e.g. extensive reorganisation projects to support the consolidation of the financial intermediary system, companies employing large numbers of people and the financial position of indebted households.

The more proactive involvement of the state also had a significant impact on the activities of the supreme supervisory organisations. In contrast to "watchman" organisations, the public expectation that they should have a kind of a "steering" and guiding

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function was increasingly voiced. Simultaneously, demand also increased for step-up in audits and for extending the period and expanding the areas subject to audit. In addition to subsequent, or *ex post,* audits, considered as the basic type, *ex ante* activities also appeared in the form of analyses, consultancy, risk analyses and studies to lay foundations.

A proactive state also galvanises action by the supreme supervisory organisation urging it to become more engaged than previously in order to support good governance, and to contribute to the creation of a sustainable welfare state and thus to improvement in the life and security of citizens through the expansion of its activity and functions. The audit office should become a model institution and its exemplary operation should inspire the transformation of other public sector institutions. In summary: a proactive state requires a proactive audit office.

Notes

[1] Article 1 (4) of the Act on the State Audit Office.

[2] Módszertani útmutató a Magyarország központi költségvetéséről szóló törvényjavaslat véleményezését megalapozó ellenőrzéshez [Methodological guide to the audit providing a basis for an opinion on the draft budget act of Hungary, and the supplements applicable to the 2015 and 2016 audits]. https://asz.hu/hu/egyeb-utmutatok.

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Civic Review, Vol. 15, Special Issue, 2019, 63–92, DOI: 10.24307/psz.2020.0204

Árpád Kovács

The Career of Rule Based Budgeting in Hungary[1]

The Success of an European Solution in Fiscal Stability, Sustainable Development and in Improving Efficiency

Summary

Starting from the macro processes of the national economy and public finances the article examines three economic-public finance turnarounds in Hungary: the improvement of financial stability, the sustainability of the outstanding economic growth and the improvement of efficiency to be achieved and in all of this the role of rule-based budgeting. It shall introduce the regulatory and institutional solutions of the latter i.e. how this service, as a logical consequence of a framework, became a useful part of the financial policy by implementing its rules and – as an annual realisation of the above – a useful part of the budgeting practice. The article reaches the conclusion that it was unavoidable to "elevate" the major stipulations of the rule-based budgeting and the rules of the guarantee-like operation of the institution guarding over the implementation of these rules in the Fundamental Law of Hungary in 2011 to thus strengthen budgetary responsibility. Additionally, the article is dealing with the relations of the Hungarian and EU regulations, the main characteristic features of the work of the Fiscal Council, the FC's recommendations made during the past nine years and the effects of the said recommendations.

Journal of Economc Literature (JEL) codes: B15, E62, H15, H61, H63, L38, P48
Keywords: fiscal policy, crisis management, debt management fiscal stability

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Introduction, the essence of rule-based budgeting

The approach to the development of economic history is related to *"theories"* (Sombart, 1929). However, to the majority of the social-economic actors it is not *theory,* rather the actually used *instruments* and, primarily, the *result* itself is important. And the latter can be captured mostly in the sustainability of the social-economic functioning, the stability and the services provided by public finance. Thus the truth of the motto[2] of the Parliamentary Budget Officials (PBO-s) and of the Independent Fiscal Institutions (IFI-s): *Better budget – Better life* is hardly disputable. As regards their essence the direct social values and interests directly related to public finance can be associated with the quality, expansion and availability of services – *with better life* – and, indirectly with its basic condition, *financial stability – with better budget.* It is common knowledge that the pre-condition of the realisation of the target system of fiscal policy is the continued position of the budget (public finance) close to balance, the funding of social services respectively, keeping the degree of state re-distribution on a level required for reaching the above goals. Their role is decisive not only from the aspect of decreasing government debt but also from the aspect of the competitiveness of the whole of the national economy. Ultimately the sustainability of the social-economic development depends on these factors (Kovács, 2019).

In the course of the past decades *budgetary slippages* and, as a consequence, problems of sustainability and growing indebtedness – accompanied by bank crises too – appeared not only in the emerging countries but also in a line of developed countries (Antal, 2004; Bod, 2013; Muraközy, 2010; Kovács O., 2013).[3]

Lack of financial stability can paralyse the social-economic functioning of a country already within a few years. That's why regaining and maintaining financial stability has become such an important strategic issue all over the world that demanded new solutions – regulations and institutions. The so-called *rule-based budgeting* fits into this framework of fiscal policy (Kutasi, 2012). Implementing this has spread first in the economic crisis ridden countries of Latin America then, from the 80s, all over the worlds, thus also in Europe. Each member states of the European Union, thus Hungary as well, are following these set of rules – naturally with smaller or bigger departures, but alongside tangible principles – in their respective fiscal policies. The so-called "rule-based fiscal policy" means more than merely following the rules governing the preparation and execution of the budget as it dictates *the framework of budgetary responsibility* via the rules of budgetary-political, procedural-transparency regulations as well as via the institutional mechanism of the institutions set up to guarantee the observance of these rules (Kutasi, 2012). The system used in the practice is consisting of these rules and mechanisms –observing naturally the peculiarities of the given country (Ódor, 2014).

From the middle of the first decade of the 2000s it became clear also in Hungary that the more disciplined realisation of the current budget was far from enough to prevent the slippages of the budget that broke away from the performance. That's why regaining and maintaining the financial stability of the Hungarian public financ-

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es that was close to national bankruptcy, became such a strategic issue that called for a new, constitutional stipulations and high level legal norms built on those stipulations that uniformly regulated public finances. The domestic endeavours, following international examples to stop public finance over-expenditures and set solid foundations for the finances of the country served this purpose successfully, followed in 2011 by the regulations stipulated by the Fundamental Law of Hungary[4] and in the Stability Act[5]. Before describing in detail the Hungarian solutions, the domestic practice of rule-based budgeting, we should briefly mention the international career of the *regulatory and institutional system* that has been often referred to as a "magic fiscal weapon".

Sketchy international outlook

Principles of rule-based budgeting practice as a therapy

Rule-based budgeting and the financing built on this principle imply the better harmony of resources and are undoubtedly mitigating the cyclical nature of budgeting (Kopits, 2013). The lessons of the crisis have completed this "classic function" by the fact that introducing rule-based fiscal policy could be a tool of crisis management (Reinhart and Rogoff, 2010; Kovács, Á., 2013).

Governments of several countries opted for the introduction of rule-based budgeting hoping that with the assistance of this method the balance tensions will be contained and conditions of *lasting funding,* growth and sustainable development can be created. To this end they laid down in law, even in constitutional stipulations – in the form of numeric rules, planned according to a specific rule of procedure and supervising them institutionally – the revenue and expenditure proportions of the budget and the acceptable degree of the indebtedness (Kopits, 2013).

In our practice all this meant that

– fiscal policy regulations are being used (for example, expenditure limits to maintain the budgetary balance),

– fiscal procedural regulations were introduced (for example, medium term fiscal planning, the obligatory compensation of expenditures),

– enforced transparency norms (for example, accrual based accounting, reporting system),

– established institutional guarantees to enforce transparency and the observance of regulations respectively, the "supervision" of the macro and micro economy (for example, apart from the SAI of the country – or within its organisation – operating a parliamentary institution and/or fiscal council that is independent from the government and empowered by the right to express an opinion on the central budget).

Naturally, there are essential differences depending on how rapid and deep the worsening of the national economy and financial conditions were and to what extend the new circumstances have become pressing and calling for instant action. Apart from the abilities of the existing financial system and its flexibility as regards modernisation and absorption, it was the above that essentially determined the contents, the

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tempo of its introduction as well as the circumstances of its functioning, the authorisations of the institution guarding over the observance of the rules and the entitlement of the institution within the public authorities. Apart from the limiting factors as regards the implementation of the system that were also related to the differences of the national public finances systems, the international experiences also indicated that by the consistent operation of the system the trend that was apparent in the past decades both in the emerging and the developed countries and was embodied by budgetary over-expenditure, the un-sustainability of the budget and the growing sovereign debt could be reversed (Orbán and Szapáry, 2006).

Solutions to be found in international practice

The practice of rule based budget thus started from South America but by today more than 50 countries in the world are employing such solutions with more or less consistency and a rather varied status of "supervisory" organisations, bodies. We should add that the dominant employment of such a framework, serving the purpose of financial stability that – classified according to their specific, common characteristic features, their functioning norms and attempts to build an institutional cooperation – are typical for the countries of the European Union and, as of 2015, the fiscal functioning of the Commission of the European Union.[6] We can find more than half of such fiscal policy, procedural and institutional solutions within the European Union. That's why we can talk about a "European" solution that proved to be successful in maintaining financial matters – referring to the title of the present article. Namely, thanks to its main characteristics, operational characteristic features and by establishing financial stability, the Hungarian practice falls in this category as well.

Here we mention that the Maastricht system of criteria of the European Union itself is working as a specific network. We can regard its requirements as "numerical and procedural regulations" employed as a compulsory and uniformed system of rules. Let's just think about the 3 percent deficit limit – compared to the gross domestic product (GDP), or the target of the GDP proportionate government debt set in 60%, in case of the latter stipulation, the rule that the debt exceeding this limit shall have to be decreased annually by 1/20th part, or the European Fiscal Board established as an advisory body in 2015 for the member countries of the euro area, that is an independent fiscal institution of the European Commission.

Some European countries have introduced it well before the 2008 crisis and have established Independent Fiscal Institutions (IFIs) i.e. fiscal institutions independent from the government and bearing budgetary responsibility.

As it's apparent from Table 1, elements of the rule-based budgeting were used in a variety of ways. It's the requirements of maintaining balance that are predominant however, we can find more concrete stipulations, like limiting expenditures, deficit and indebtedness (ceiling) as well as calling for medium term planning. Loss of reputation, as a consequence of sanctions applied by fiscal institutions is common. In case of Poland we can see the option of legal sanctioning – for example, the possibility of

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re-discussing the budget – while financial sanctioning – for example, the suspension of EU resources – is applicable in the countries of the euro area (Franco, 2011).

The method of creating fiscal institutions was differed. Mostly it happened by a law adopted by simple parliamentary majority or political guideline (agreement), respectively by constitutional regulation.

Table 1: Functions and competence of the independent fiscal institutions guarding over the compliance with the budget in the individual EU Member States prior to the 2008 financial crisis

	Country	**DK**	**BE**	**LV**	**SE**	**BG**	**EE**	**PL**	**UK**
	Date of introducing the Fiscal Rule	**1962**	**1989**	**1990**	**1997–98, 2007**	**1998**	**1998**	**1998**	**1998**
Fiscal Political Rule	Deficit Limit					X			
	Structural Surplus or Deficit		X		X				
	Limit of Expenditures		X		X				
	Limit of Total Expenditures								
	Current Balance								X
	General Balance	X	X	X			X		
	Efficiency Investigations								
	Medium Term Planning	X							X
	Debt Limit							X	X
	Sustainability								
	Stability Fund					X	X		
Compe-tence	Public Finance	X	X	X	X	X	X	X	X
	National (Central, Federal)		X						
	Subnational governments		X					X	
Basis of creation	Constitution							X	
	Law	X	X	X	X				
	International Agreement								
	Political Guideline, Agreement				X	X	X		X
Public Classifi-cation	Independent, Parliamentary Organisation	X	X	X	X	X	X		X
	Belonging to the Executive Branch							X	
Sanctions implied by the IFI	Right to Veto								
	Loss of Reputation	X	X	X	X	X	X	X	X
	Legal							X	
	Financial								

Note: The abbreviation of the individual countries according to internationally used abbreviations.
Source: European Commission, 2012b; FC homepages

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Table 2: Functions and competence of the independent fiscal institutions guarding over the compliance with the budget in the individual EU Member States in the EU Countries on 31st December 2019

	Country	**NL**	**BE**	**LU**	**LV**	**LT**	**SE**	**UK**	**BG**	**EE**	**PL***	**ES**	**HU**
	Date of the Introduction of the Fiscal Rule	**1945**	**1989**	**1990**	**1990**	**1997**	**1997–98, 2007**	**1998, 2010**	**1998**	**1998**	**1998**	**2001**	**2009**
Fiscal Political Rule	Deficit Limit								X				X
	Stability Fund								X	X			
	Structural Surplus						X						
	Primary Expenditure Limit		X				X					X	
	Total Expenditure Limit			X					X				
	Current Balance							X					
	General Balance	X	X	X	X	X				X	X	X	
	Efficiency Investigation	X											
	Medium Term Planning	X						X					X
	Debt Limit	X		X		X		X			X	X	X
	Sutainability												
Competence	Public Finance	X	X	X	X	X	X	X	X	X	X	X	X
	National (Central, Federal)	X					X					X	X
	Sub-national Government	X	X								X	X	
Basis of creation	Constitution				X	X					X		X
	Law	X	X			X	X	X	X	X		X	X
	International Agreement												
	Political Guideline, Agreement		X	X									
Public Classification	Independent, Parlaimentary Organisation	X	X	X	X	X	X	X	X	X		X	X
	Belonging to the Executive Branch										X		
Sanctions implied by the IFI	Right to Veto												X
	Loss of Reputation	X	X	X	X	X	X	X	X	X	X	X	X
	Legal		X		X	X				X	X		X
	Financial												

Note: The abbreviation of the individual countries according to internationally used abbreviations.
** In Austria there are two institutions functioning: Fiscalrat (Fiscal Council) using the technical background of the Central Bank of Austria and Budgetdienst (the Fiscal Institution of the Austrian Parliament).*
*** By inviting the IFI of Poland that is functioning as a governmental institutions OECD essentially "adopted" it in the group of the IFI institutions.*
Source: European Commission, 2012b; FC websites

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	SI	FI	DK	RO	DE	IE	GR	HR	AT**	IT	SK	PT	FR	MT	CY	EA	CZ
	2009	2010	2010	2010	2010	2011	2011	2011	2012	2012	2012	2012	2013	2014	2014	2015	2017
					X	X			X			X				X	
							X										
													X				
					X												
	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
	X	X	X	X			X		X				X				
	X	X		X					X		X				X	X	X
	X								X	X							X
	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
		X			X		X						X			X	
					X				X			X					
			X		X					X	X		X	X			
	X	X		X		X	X		X		X	X	X		X		X
																X	
		X			X			X									
	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X		X
			X	X	X		X		X		X	X	X	X			
																X	

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In the European practice institutions safeguarding the observance of rules – the fiscal councils – are partly or completely separated from governments and are *independent* from the governments and their independence is protected by constitutional guarantees, even from the *internal* organisations of the parliaments (congress, national assembly) that have a role to support and assist the preparation of the budget (the budget offices of the parliaments) that the international terminology is referring to as Budget Office/s (BPO). As we are going to address this issue later the independent fiscal institutions have various opportunities to enforce their opinions and have public law mandates of different strength.

In the public law classification of organisations guarding over the compliance of the regulations, independence from the government was generally applicable however, we see Poland as the "odd one out" where it was established ten years prior to the crisis, as part of the executive branch.[7] Table 2 shows that among the countries accessing the European Union lately that the number of countries employing such budgetary stipulations and institutional guarantees has significantly grown in the period following the crisis,[8] due to the developing integration and the example of those countries that having followed the practice of rule-based budgeting successfully managed the crisis (Kovács Á., 2013).

From the 13 countries having accessed the EU following 2004 rule-based budgeting is the rule and the compliance is guaranteed by independent institutions. In 5 countries the system was launched before the outbreak of the 2008 crisis, while in seven countries – among them in Hungary – it was introduced in the period 2009–2014. In the 13th country – in the Czech Republic – the fiscal council was established in 2017.[9]

The institutional operation alongside the general principles mentioned under point 2.1 offers an opportunity for the cooperation of national institutions.[10] The predominance of identities is a characteristic feature however, as regards the utilisation of the budget elements in the practice as well as the responsibilities, competence and authorisation the picture is more varied.[11]

Let us finish this considerably sketchy international outlook with the question whether with the introduction of fiscal regulations and institutions (fiscal councils) has *financial management became more disciplined* in the fiscal sector? It is a fact that opting for the introduction of a stricter regime has followed the road of mitigation (see Chart 1) in the majority of the countries. Although some countries of Southern Europe that are EU members are running their respective financial system by a specific "compulsory solidarity", the practice of rule-based budgeting produced certain results nevertheless.

The change is even more plastic if we examine separately the sovereign debt data of the so-called Visegrád Group countries[12] (see Chart 2). Following the 2008 crisis these countries witnessed the start of an economic growth that was nearly three times bigger that the EU average.

In these countries it could become an objective that the new fiscal policy should serve also the strengthening of efficiency in the social-economic operation, beyond

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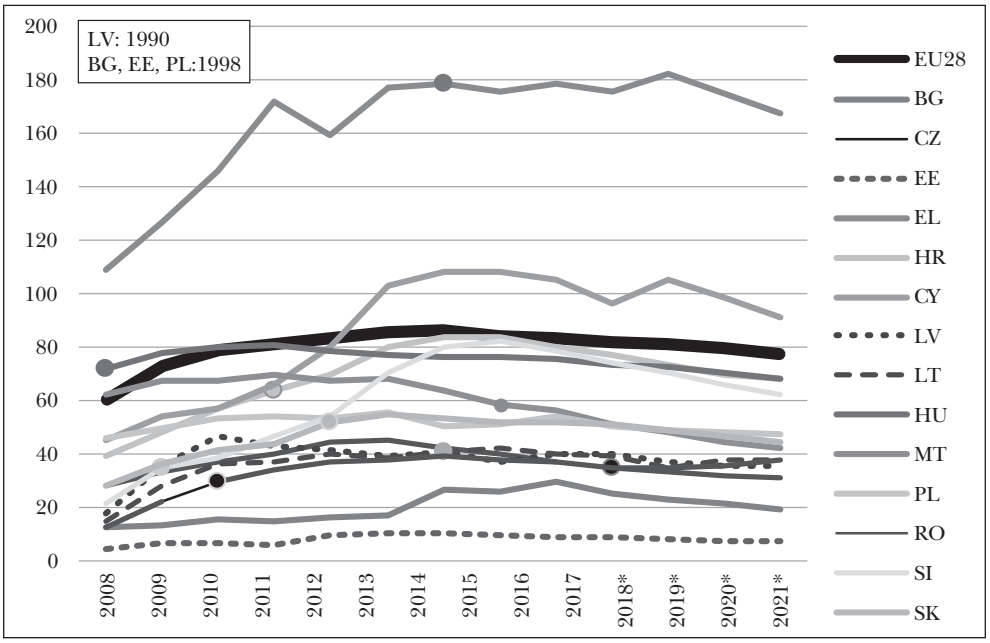
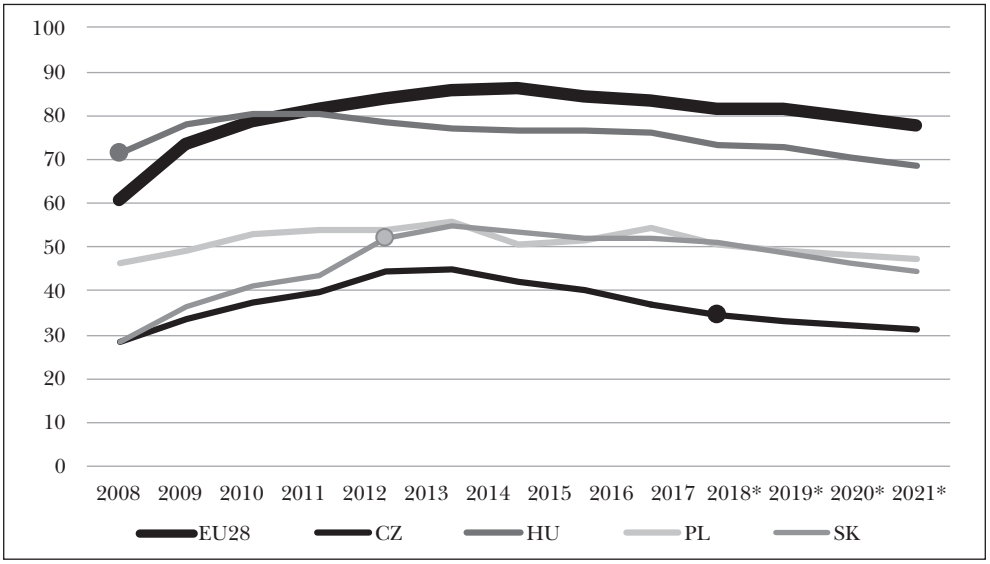
Chart 1: The Gross National Product (GDP) proportionate sovereign debt of some of the European Union countries and the date of the establishing of their independent fiscal institutions



Source: Eurostat, 2019–2021, on the basis of the autumn 2019 forecast of the EC

Chart 2: The GDP proportionate sovereign debt of the Visegrád Group of countries and the date of establishing the independent fiscal institutions



Source: Eurostat, 2019–2020, on the basis of the autumn 2019 forecast of the EC

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promoting the support of stability and growth conditions by fiscal means. Clearly we can reach the conclusion that the use of rule-based budgeting is favourably affecting problem solution, the promotion of strengthening financial management discipline and this favourable effect can be directly experienced mostly in the gradual easing of the burdens of indebtedness. We should note however, that the degree of the contribution of rule-based budgeting in the strengthening of financial stability to a large extent depends on the social-political will and, naturally, on the public authority respectively the strength of the said authorities of the institutions guarding over the compliance with this set of rules.[13]

Domestic fiscal policy, introduction of rule-based budgeting

Problems of managing public finances and the human factor

Earlier we mentioned that specific national characteristic features and the lack of financial stability in the immediately preceding period are defining essentially the circumstances of the introduction. Having in mind this we cannot escape mentioning, why and how we have reached the conclusion in Hungary that in order to establish stability in the fiscal (budgetary) policy the introduction of rule-based budgetary frame is inevitable?

After the millennium Hungary was not the only country that had to face those increasingly hard to handle public finance, over expenditure and – as a consequence – ever deepening indebtedness issues that all led to the ambiguity of the financial stability of the country. However, the situation was somewhat different in case of our country because of the synergistic/antagonistic processes of the overlaps between the political and economic cycles that very likely have had a crucial role in over-expenditure – due to endeavours to maximise and/or get more votes – and thus in the growing indebtedness compared to other countries of similar fate[14] (Karsai, 2006) .

As regards our fiscal policy it remained a fundamental feature that parallel with the amendment of our Constitution in 1989, then the signing in 1994 of the Contract of Association that was an opening step in the direction of the European Union and finally, in our determinations listed by the 2005 Accession Agreement to the EU that contained those requirements regarding the goals and the tools to be used in the course of the accession that expressed our connecting to a bigger group of those European countries that formed a social-economic-political community.[15] The association implied harmonisation obligations, incorporating the *financial balance related* requirements among joint European integration values and norms.[16]

In the context of our article it is obvious that reaching the desired goals depends not only on creating the appropriate regulations but also on the disciplined observance and enforcement of the said regulations. And in this *the human factors, the ability of recognising social interest and the will to follow this road* are getting an important role without the support of what the financial stability of a country can hardly be realised (Kovács, 2016).

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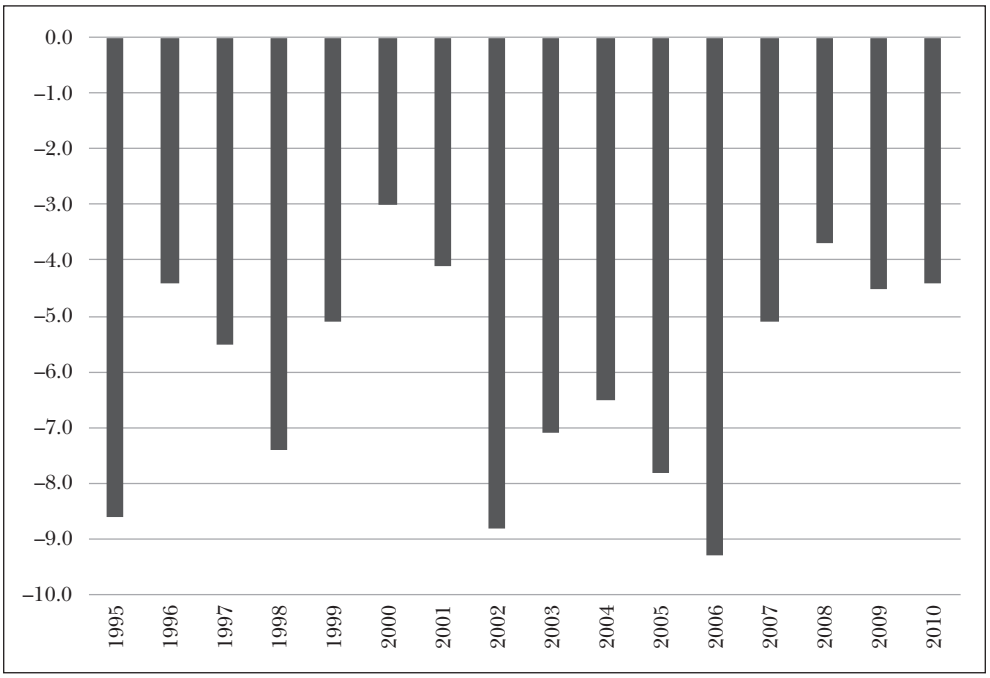
In Hungary, following the regime change, the fiscal policies of the subsequent governments were characterised by bargaining mechanisms, planning and financial management built on political promises and dogmas. This presented an obstacle for public finance stability as well as for sustainable development (Antal, 2004; Karsai, 2006; Lentner, 2008; Matolcsy, 2008; Muraközy, 2010).

From time to time public finance deficit was "skyrocketing" in Hungary (mostly in years around parliamentary elections). In 2002 and 2006 it reached close to the 10 percent of the GDP (Chart 3).[17]

Chart 3: Hungarian public finance deficit calculated by the EU methodology (ESA 2010) from 1995 to 2010 (in the proportion of the GDP)



Source: Eurostat, FC Secretariat edition

It was the direct consequence of the high deficit that the degree of the GDP proportionate government debt (government debt rate) that beginning with 2000 years up to the introduction of the rule-based fiscal politics in 2010, the rate had increased continuously. Contrary to the ongoing emphasising of our European orientation and the country's commitment to follow the European examples, the promises made in the convergence programmes, the indicators regarding the balance of Hungarian public finance were getting farther and farther from those fiscal policy and technical balance regulations that the country had undertaken.

Not only the repayment of the government debt that skyrocketed in the first half of the 1990s – to be followed by a temporary decline – and jumping up again in the

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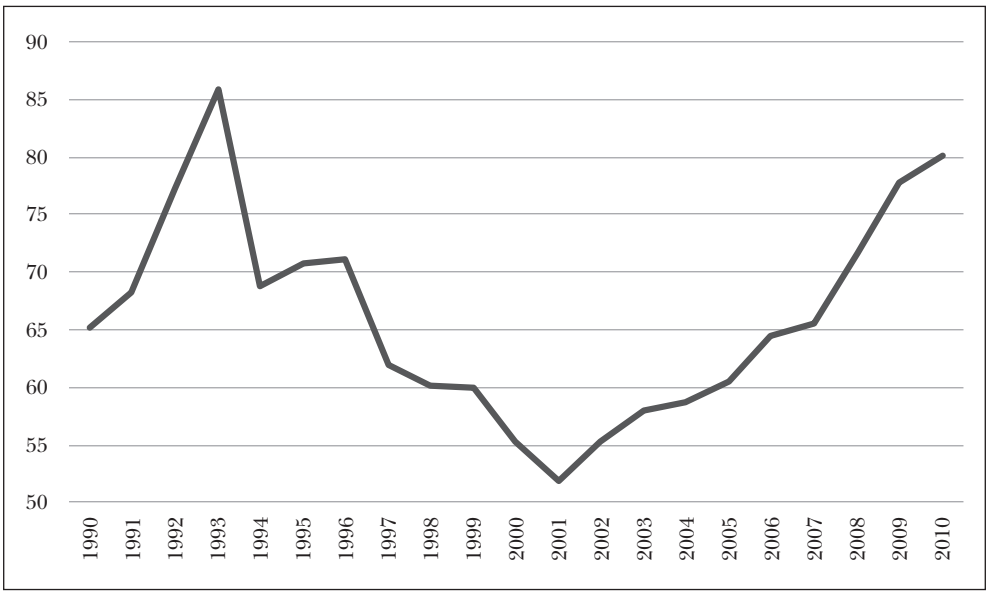
years 2000, but also the very expensive financing of this debt (the debt service, i.e. the interest) meant/means an enormous burden for the country. "In the period of 1993–1999 the interest expenditures exceeded the amounts used for education, culture and health care" (György and Veress, 2016).

All we can add is that the debt service tied up the same proportion – 8–9 percent – from the public finance expenditures allocated for healthcare and was hardly lagging behind the 10–11 percent allocated for the total of education expenditures for several years, even after 2010. (Today this burden represents 5 percent!)

Chart 4: GDP proportionate sovereign deficit, 1990–2010



Source: Eurostat, FC Secretariat edition

The exceptionally high degree of Hungarian *redistribution* – around the outstanding 50 percent of the GDP – compared to the neighbouring countries but even to the average of the EU countries was the direct consequence of our fiscal policy.

It was inevitable that the significant *income depletion* (and within this the high tax centralisation) encouraged the amplification of black economy that led to the narrowing of the number of taxpayers, the erosion of tax bases and even higher tax rates. As a consequence, *market sector investments* decreased. The phasing out of companies from the credit markets was a factor in this.

Lack of social acceptance and support of the society were also playing a part in the fact that the public finance reforms and consolidation attempts announced by the succeeding governments following the change of regime proved to be unsuccessful or were merely partially successful during twenty years – with the exception of the 1996–2002 period that overreached governments. Another factor of this failure was that at

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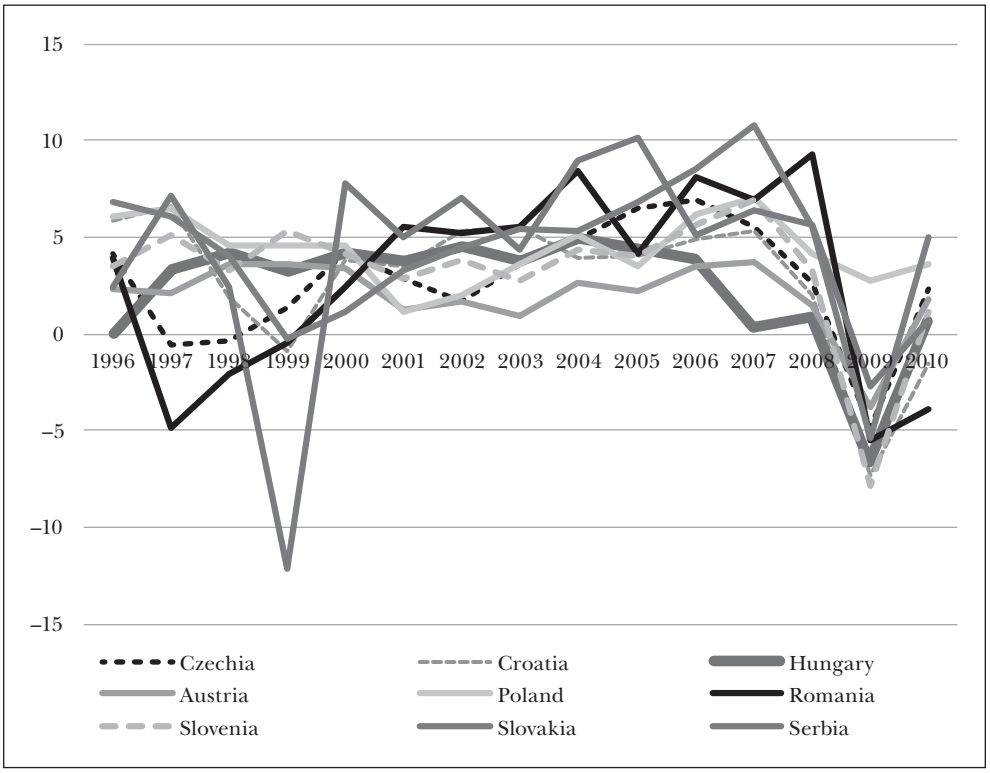
that time there were no appropriate fiscal-political regulations, i.e. those checks that that could have adjusted the tasks undertaken by the state to the capabilities (taxation) of the country were missing and no requirements existed at the time that might have promoted the more efficient utilisation of public moneys and accountability.

The competitiveness of the country also worsened due to the (aforementioned) oversize public finances and its subsequent "greed", the non-efficient operation affected the national economy negatively.[18]

The above causes – together with a number of additional factors like, for example the lowering productivity – all present together in our county *contributed to a more moderate growth rate and often, to the downturn of the growth rate* respectively, maintaining the growth required ongoing mobilisation of external funds and indebtedness (see Chart 5).

Chart 5: Economic development of Hungary and the Visegrád Group countries from 1996 to 2010 (change of volume compared to the previous year, percent)



Source: Eurostat, European Commission, FC Secretariat Edition

Despite the predominance of public finances the population had the perception that the level of public services and thus their quality of life has been constantly worsening. In other words the perception was that their expectations were not met despite

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seeing/hearing them repeatedly in the election promises (Kovács, 2016). On top of this, the 2008 crisis that started from the money markets and became an ever more encompassing economic crisis found our country in this situation and thus contributed to further weakening our position.

Introduction of the rule-based budgeting in Hungary – antecedents, institutional solutions

As a result of the worsening problems of Hungarian public finances that had endangered the sustainable financing of the public finances and had a destructive effect on the competitiveness of the real economy, by 2006 it became clear that the budgeting practice being applied ever since the change of the regime excluded the chances of following the course of sustainable development. Change could not be postponed any longer and a substantial turnaround was necessary in fiscal policy; the question was what should be the content of this change.

Balancing on the brink of fiscal unsustainability led to the recognition that in order to maintain the financing public finances in a longer run government control shall have to ensure a regulation that was internally consistent and corresponding with the chosen scenario as well as a budget planning that was "thinking" about a longer period of time within the financial system of public finances, together with independent control guarding over the observance of the regulations.

Double reflection period (2006–2007)

As regards the character of the rules required for fiscal sustainability and the institutional guaranteed necessary for their observance experts were fundamentally thinking along two directions.

The *Theses on the Regulation of Public Finances* elaborated by the State Audit Office of Hungary assumed that in order to implement substantial changes, the whole of public finance management has to be regulated and made transparent and accountable. Namely, the experiences of this institution gained from its work proved that the weak effectiveness of the utilisation of public moneys due to the structure of public finances or the over expenditure guided by political purposes was impossible to correct subsequently and essentially *by means of control*. However, the understanding as regards the necessity and usefulness of comprehensive re-regulation proved to be insufficient for the realisation, due to the political division and under the conditions of a coalition government burdened by debates.

The other initiative that can be associated with the Central Bank of Hungary in its concept was focusing on the most important factor of fiscal tensions, i.e. the prevention of over-expenditure and considered the introduction the elements of *rule-based budgeting* – that proved to be successful in international practice – as a solution of the domestic problems. In 2007 and 2008 a lively professional debate evolved that was moving towards concrete solutions.

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The proposal combined by the Ministry of Finance, as an adaptation of the USA Congressional Budget Office, would have established the Budget Office of the National Assembly. Protracted consultations took place. According to the critics this concept could not find an adequate answer to the fundamental issue, how it would be possible to keep in harmony the undivided political decision-making authority and responsibility with professional control. According to other critics a decisive condition of observing the rules was missing, namely that they succeeded introducing reforms concerning the tax system and the great entitlement system in "critical mass". Apart from this they were of the opinion that from the aspect of implementation and efficiency this concept raised concerns.

After the proposal of the Ministry of Finance was taken off the agenda, the concept that aimed at the introduction of a regulatory framework targeting the mitigation of the deficit inclination and the prevention of over-expenditure became the sole concept on the table.

In the shadow of the threatening national insolvency and the pressure of the IMF–EU borrowings, by the end of 2008 *the act on cost-efficient state management* was born that is often referred to as "ceiling act" due to its perception and intervention mechanisms (expenditure limits). Namely, by this act they were limiting the expenditure grand total of the budget for the next year (the amount planned for year 2009 had to be the same as the 2008 appropriation, while later the real value of the planned amount was allowed to grow by the half of the expected real growth of the GDP). Apart from this they created complicated rules for the envisaged balance of the budget just like for the envisaged degree of government debt.[19]

There were two different concepts *as regards the Fiscal Council and its organisation*. Although there was agreement that the chairman of the body should be an expert representing the head of the state however, as regards the members, there were different ideas. According to one concept the members should be the *incumbent heads* of two financial institutions, independent from the government, i.e. those of the SAO and the Central Bank of Hungary (MNB). In this concept the small secretariat basically should be focusing on summarising and planning tasks as the professional support of the Council's decision making work and would rely on the high level and significant macroeconomic analysing capacities of the SAO and MNB that otherwise have their respective, independent research and analysing staff and regularly analyse the soundness of budget planning.[20]

The other solution was essentially different from the above. In this case the expert representing the head of the state, heads of the SAO and MNB would make recommendations for the members of the FC. According to this concept the secretariat would be an apparatus with a significant staff funded by an independent budgetary source and had a distinct ability to do macroeconomic analyses.

Finally, in the "ceiling act" they opted for the latter version and that existed up to the end of 2010. From year 2011 they returned to the first concept and the conditions of the transitory period were regulated by the 2011 budget.[21] The new Government established following the 2010 elections undertook the task of reviewing and setting

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in a new framework the whole of the legal system and within this of public finances, supported by a two-third majority in the parliament. This solution opened a new chapter in the regulation of the rule-based budgeting system that was in harmony with the importance of this issue.

The Fundamental Law of Hungary and the Act on the Economic Stability of Hungary about rule-based budgeting

The *Fundamental Law* of Hungary adopted on 18th of April 2011 dedicated a whole chapter to public finances. In this it stipulated the budgeting right of the National Assembly. Additionally it laid down that public finances should be managed in a transparent and in a verifiable manner, having in mind the requirements of legality, expediency and efficiency. At the same time it set up a barrier for indebtedness not only concerning the whole of public finance but within that for the local governments as well.

The Fundamental Law also defined the annually predictable measure of government debt when it created the *government debt rule*. According to this rule the National Assembly should not adopt such an act on the central budget as a result of what the government debt would exceed half of the GDP. As long as the degree of government debt exceeds this measure the National Assembly should adopt only such a central budget bill that contains the decreasing of the GDP proportionate government debt.[22]

The Stability Act concretely stipulates the government debt rule in a "debt formula" (see also the note no. 23). This rule *formulated* requirements *not only regarding the planning and adoption of the budget but also regarding its execution*. It determines that as long as the government debt is exceeding half of the GDP – with the exceptions laid down – no such loans shall be taken and no such obligations shall be undertaken as a consequence of what the proportion of the government debt to the total of the gross domestic product would increase the proportion of the previous year.

The Fiscal Council (or: Council, FC) guarding over the compliance with the rules of fiscal stability was elevated to the rank of the preconditions of constitutional operating by the Fundamental Law. The Council is a body that's task is supporting the legislative work of the National Assembly and carries out its work subject to the law. Among these tasks it is participating in the preparation of the central budget act and as an organisation supporting the legislative activities of the National Assembly it examines – formulates its opinion on – the soundness of the central budget on the one hand while, on the other hand *it gives (or does not give) its preliminary consent* for *the adoption of the central budget act* having in mind the compliance with the so-called government debt rule. In the process of creating the law by the latter task and mandate the Council, as an independent fiscal institution was endorsed by a public role, i.e. the so-called "right to veto" together with the responsibility that goes with it. The quotation mark is justified because the Council shall not annulate a decision, merely shall help it in the right direction.

This solution that implies a strong public mandate surpasses the practice existing in the majority of the EU countries where – as we could see in Tables 1 and 2 – the

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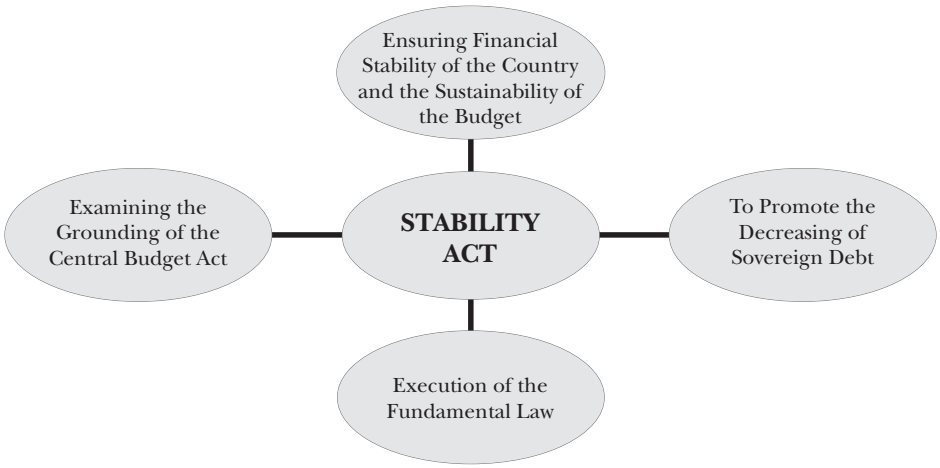
institution has a more of an awareness raising, advisory role that could be emphasised in a limited way by attaching them to a SAI or the parliament. The possibilities of direct intervention of the given institutions, bodies are modest most of the time. They can be characterised by an independent macro-analysing, forecasting (projection) work; the strength of the utilisation of their findings primarily are defined by the respect of the given institution, respectively the attention given to them by the actual government of the given country and/or parliament. Accordingly, the given fiscal institution characteristically puts the emphasis in its work on the preparation of multi-annual forecasts. Contrary to the Hungarian institution, where such longer term outlooks prepared by the experts assisting the work of the Council, are being used in the assessments of the body regarding the budget of the current year (Kovács, 2014; 2016).

As regards the tasks of the Council, the framework set by the Fundamental Law was detailed also by the Stability Act (see Chart 6).

Chart 6: Tasks of the Fiscal Council in the Stability Act



Source: www.kormanyhivatal.hu/download/3/de/20000/6%20Stabilit%C3%A1si%20t%C3%B6rv.pdf

It is the Stability Act that expounds in detail the procedural order to fulfilling the *obligatory tasks* of the Fiscal Council and the related tasks of the Government, focusing, first of all, on the adoption of the central budget bill (and its amendments). If, in case of formulating its opinion on the draft bill, the FC expresses its disagreement then the Government has to re-negotiate the bill and conciliate it with the Council. The procedural rule concerning the preliminary consent of the Council about the compliance of the draft budget with the government debt rule is even "tougher" if the FC – enforcing its veto right – refuses granting its preliminary consent the final voting has to be postponed and the procedure should be repeated until the Council gives its consent.

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Organically completing all the above, it is a priority task of the Council to formulate its opinion on the execution of the central budget act and the expected trend of sovereign debt every six months.

The FC is monitoring the planning and execution of the budget also in the context of the longer term macroeconomic processes. In this, beyond the analysing abilities of the SAO and MNB the Council is relying on the contributions of research institutions, external experts, professional fora and advisory bodies as well.

As regards the *other, non-mandatory tasks* of the Fiscal Council the Stability Act defines that it may express its opinion on the amendment of laws related to the budget act and any other issues that are related to the planning and execution of the budget, the use of public funds and the state of the public finances. In a wider context satisfying the interest of experts and the media, seeking the opinion of economists, fulfilling the demand for information by international organisations, cooperation with the independent fiscal institutions of other countries, promoting the public finance stability by means of publicity also belong among the duties of the Council (the resolutions, the annual action plan, other documents and used researches can be found on the Council's website).[23]

The activity of the Fiscal Council following the adoption of the Fundamental Law of Hungary and the Stability Act

By its tools, not least by its strong mandates that serve fiscal discipline, or we can say, by its guarantee-like presence, the activities of the FC have also *contributed to the policy of fiscal balance* as a significant consequence of what the proceeding of Excessive Deficit Procedure (EDP) against Hungary was terminated in 2013, respectively the parameters that allowed that the big international credit rating companies uniformly put Hungary in 2016 back to the category of recommended for investments were met.[24]

According to Point (3) Article 44 of the Fundamental Law the Fiscal Council's primary goal of operation can be summarised in ensuring the implementation of the rule about the decrease of sovereign debt. In its work the Fiscal Council has been consequent in focusing on this task. Accordingly, it was the annual analysis of the implementation of the compliance with the respective stipulations (expectations) of the Fundamental Law and the Stability Act promoting and maintaining public finance balance, the creating of budget laws and checking their execution that made up the focus of the Council's activities.

The annual and continuous GDP proportionate government debt is reflecting also the work of the Council (Chart 7).

The end of the year level of the GDP proportionate sovereign debt has been declining since 2011 and by 2019 it was below 67 percent (9 percent decrease). On the basis of the fiscal and macroeconomic processes the debt rate might fall below 60 percent by 2022, i.e. below the Maastrich criteria. It is now within reach that the euro area would be a result of many-facet (economic) political pondering and not merely the meeting of the accession's criteria.

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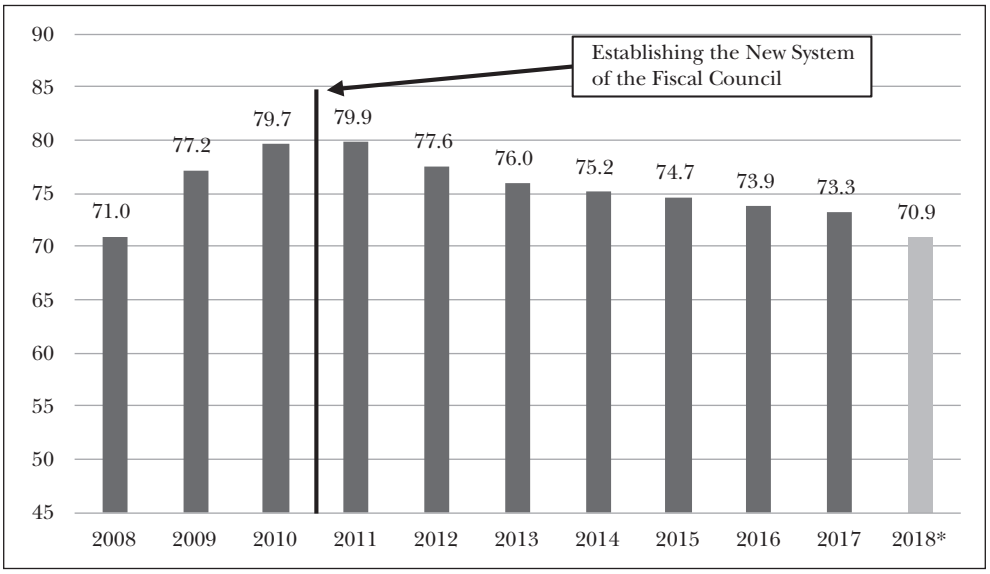
Chart 7: Trend of the GDP proportionate sovereign debt (percent) from 2008 to 2021



Source: Annual Discharges, MNB, FC Secretariat, 2019–2023 Preliminary Data

The effect of the FC's work was reflected also in the improving validity of the planning work of the government. Namely, in the second part of the reviewed period the need for amendments decreased and even then the reason was development and wages and salaries' oriented due to the improving revenue collection and the ensuing greater room to manoeuvre. Naturally, the strengthening of the stability of the budget and the fact that the macroeconomic growth was beginning to be sustainable, were important factors in this respect as well.

As regards the planning and execution of the budgeting process it was also favourable that contrary to the earlier legislative practice of doing it during the autumn and winter months, the adoption of the budget act was completed already in June–July. This has a positive impact not only on the public finance sector but also on the national economy in a wider sense as the business entities have a significantly longer period of time for the preparation of running the business in the next year.

Year after year the Council was paying attention not only to the exact planning of revenues, expenditures, deficit and sovereign debt but also made sure that aspects of efficiency were enforced on both the revenue and expenditure sides of public finance. The FC did this parallel with repeatedly emphasising that the competitiveness turn was unavoidable in the economy.

Additional technical and substantial characteristic features of the eight years' of functioning

In the period from 2012 to 2019 the Fiscal Council altogether made 71 resolutions (14 in 2012, 17 in 2014, 9 in 2015, 6 in 2016, 6 in 2017, 6 in 2018 and 6 in 2019)

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when, in the course of performing its tasks was focusing on the balance, authenticity, reliability and the implementation of the government debt rule. From among these resolutions 61 were related to their opinion on the draft of the central budget bill (and the related amendments), the half-year evaluation of the implementation of the central budget act respectively, in connection with the final voting, granting the FC's preliminary consent; 10 resolutions were brought regarding the operation of the Council and the report on the body's activities in the previous year as well as the board resolution about the adoption of the FC Action Plan for the next year.

Taking a look at the decreasing number of resolutions and the contents of these documents the process of the stabilisation of Hungarian public finance can be traced. It shows that with the passing years there was less and less and finally no need at all for mid-year corrections or the amendment of the budget. The differences between the implementation data of the planned and realised budgets in 2016 and 2017 were the result of the changes in the EU financing cycles and not of internal, planning errors.[25]

On a basis of legal authorisation the SAO and MNB have continuously supported the Council in formulating its well-founded decisions by a number of studies, analyses (findings) prepared by the staff of these two institutions. Apart from these documents the 56 studies commissioned and utilised by FC from scientific, research institutes and market analysing companies dealing with a variety of issues were also playing an important part in these years.

In each year of the reviewed period, beyond enforcing the direct, governmental and parliamentary enforcement of FC's public law effect resolutions the Council was also affecting *indirectly* public finance and economy when the Chairman of FC, the staff of the Council and their representatives, as well as the heads and staff members of institutions that contributed to the work of the Council by researches, have held presentations that evoked great interest at conferences organised together with the Hungarian Economic Association. They regularly appeared in the media as well.

Following the emergence from the EDP procedure the Chairman of the Council initiated a line of consultations about the issues concerning the methodological rules of procedure and their topical changes with the President of the Hungarian Central Statistical Office and her experts. In these consultations they reviewed the types of national accounts, the respective issues of substance, the requirements of the EU Regulations 549/2013 issued by the European Parliament and the Commission (21st of May, 2013), and the effect of the topical Eurostat corrections on the GDP and GNI calculations. Members of the FC, respectively experts representing them were attended the consultations.

The Chairman of the FC ensured the opportunity for international financial organisations for meetings and exchange of opinions. Thus it informed the experts of IMF and OECD who regularly visit the country about the state of the central budget and issues of sustainability. Apart from this several time he received representatives of the EU Commission and the experts of international credit raging companies (Moody's, Fitch Rating, Japan Credit Rating Agency Ltd.) seeking information. Mem-

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bers of the FC and its experts were also attending these meetings or were informed about these events.

Apart from introducing the general characteristic features of the Council's work it is reasonable to include some concrete key decisions of the Fiscal Council too:

– In 2012 the FC asked for the elaboration of an alternative macroeconomic course and the significant increase of the so-called Country Protection Fund[26] in connection with the year 2013 draft central budget bill as in the course of formulating the body's opinion they considered that the macro forecast used as a basis for the budget planning was not duly substantiated. As a consequence the Government prepared a new proposal with and amended macroeconomic background, targeted deficit and additional measures to improve the balance of revenues (tax system) and expenditures.

– In 2013 in the FC opinion on the draft of the 2014 central budget bill the body identified risks both on the revenue and expenditure sides. Thus they were on the opinion that strict and efficient financial management was necessary at all levels of public finance in order to comply with the implementation of the targeted balance. The FC also indicated that even if justified, the frequent amendments of laws resulted in decreasing accountability.

– In 2014 the Council called the attention to the necessity of more robust reserve maintenance as regards the 2015 budget bill to protect the macroeconomic course from external effects.

– As regards the aforementioned debt formula the FC wrote a letter to the Prime Minister in 2013 and initiated reviewing the formula as its methodology proved to be too strict and would have called for fiscal steps that might have endangered public finance balance and economic growth in 2016. In later years the FC repeated its recommendation several time. In 2015 it called the attention once again when analysing the 2016 draft of the central budget bill they were on the opinion that compliance with the debt formula was impossible to meet. Having in mind these antecedents finally the National Assembly adopted a new debt rule that was supporting growth.

– In 2016 in the debate of the draft of the 2017 central budget bill the Council welcomed this as a step taken towards a balanced budget (the separation of the operational and capital formation budget, recognising deficit only in case of the latter). This was the first time when the FC called the attention of the Government to the improper performance of the requirement concerning the so-called structural deficit.[27]

– When formulating an opinion in 2017 on the year 2018, and in 2018, on the year 2019 draft budget bill it was the issue of the examination of structural deficit that got in focus. The FC stated that it was exceeding the medium term targeted value. At the same time the body deemed it a positive sign that the difference has been decreasing every year.

– Furthermore, in connection with the draft budget bills of years 2018, 2019 and 2020, it emphasised that the planned decrease of the GDP proportionate sovereign debt was meeting not only the domestic requirements but was also in harmony with the EU stipulations.[28]

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– In 2019 – according to the Council's emphatic opinion concerning the 2020 budget bill, the FC "deems it justified … to take those measures that would ensure the improvement of productivity and efficiency as a result of what the growth rate exceeding the average of the European Union not only in 2020 but in the medium term as well".

– As a result of multiannual efforts it could be stated that in the course of the past years the share of foreign currency denominated debt within government debt exceeding 50 percent in the years of 2010 has decreased by the end of 2019 to approximately 10 percent and has significantly contributed to the mitigation of the external vulnerability of the county.

Stability of Hungarian finances as the basis of the ability to grow and of efficient functioning

The improvement of public finance balance is acting as a stimulus as regards growth both in our country and our neighbours. The success of our rule-based budgeting policy is reflected not only in the decreasing public finance debt but also in the fact that ever since 2012 our primary balance has been continuously positive in contrast to the previous years when we succeeded reaching such a favourable result only in certain years (Chart 8).

The improvement of public finance balance is acting as a stimulus as regards growth both in our country and our neighbours. The success of our rule-based budgeting policy is reflected not only in the decreasing public finance debt but also in the fact that ever since 2012 our primary balance has been continuously positive in contrast to the previous years when we succeeded reaching such a favourable result only in certain years (Chart 9).

As a result of the significant improvement of the work targeting the effectiveness of revenue collecting and keeping expenditures under control contributed to the improvement of deficit indicators and following 2010 the government debt rate has been decreasing each year (as we saw on Chart 7). By the improving balance the budget can be financed by smaller costs. And cheaper financing exempts resources primarily for economic development and thus is a growth factor. This is setting the foundations for the increasing of resources for social and welfare (healthcare, education, social matters) expenditures. From the aspect of the vulnerability of the national economy and judging the public finance the dramatic fall of the foreign currency denominated share of sovereign debt (see Chart 9) is especially advantageous. In this respect it is just as important if not more important that by the end of year 2018 – following a similar path – the share of debt owned by domestic hands has grown to the detriment of external grantors.

The economic growth determining public finance stability has been present ever since 2013. We should emphasise that years 2014 and 2015 were the first two years ever since the early 90s when Hungarian economy was able to grow in such way that the growth was not followed either by the growth of sovereign debt or that of the external indebtedness of the economy. It is favourable that economic recovery is gaining

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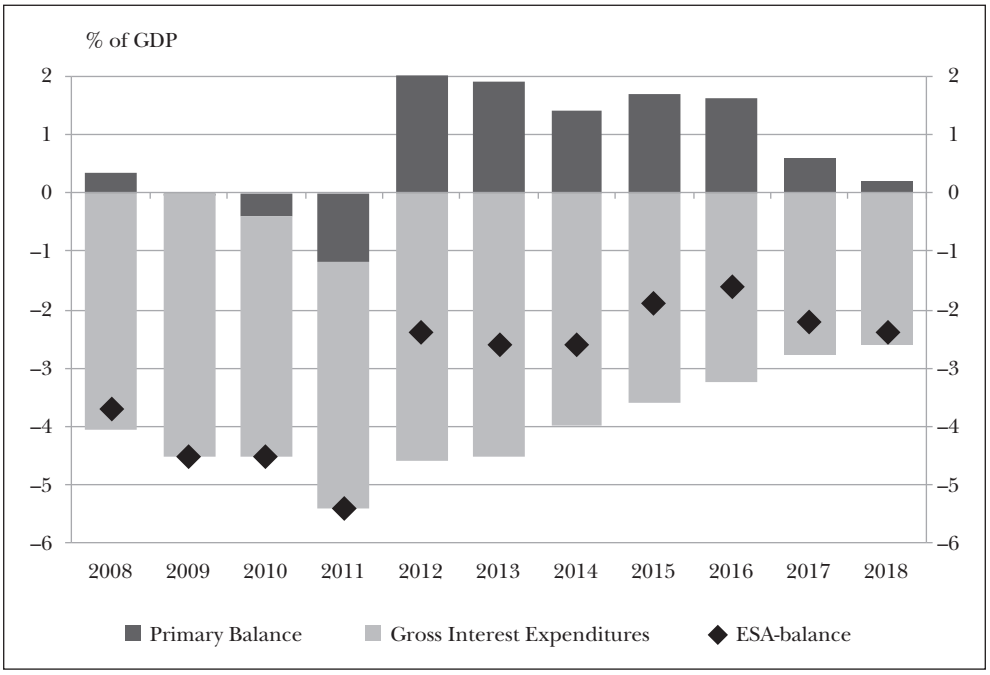
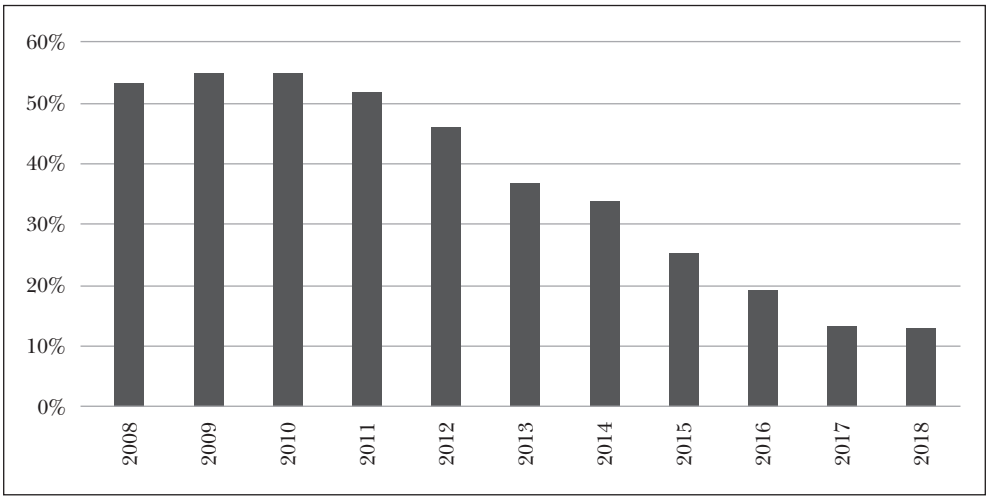
Chart 8: Deficit of the Hungarian Public finance, its net interest expenditures, primary balance in the proportion of the GDP, 2008–2018



Note: At the time of closing the manuscript the 2019 data is not known yet.
Source: MNB

Chart 9: GDP proportionate sovereign debt of Hungary denominated in foreign currency



Note: By 2019 it decreased further (no concrete data was available yet at the time of finishing the manuscript).
Source: ÁKK, FC Secretariat Edition

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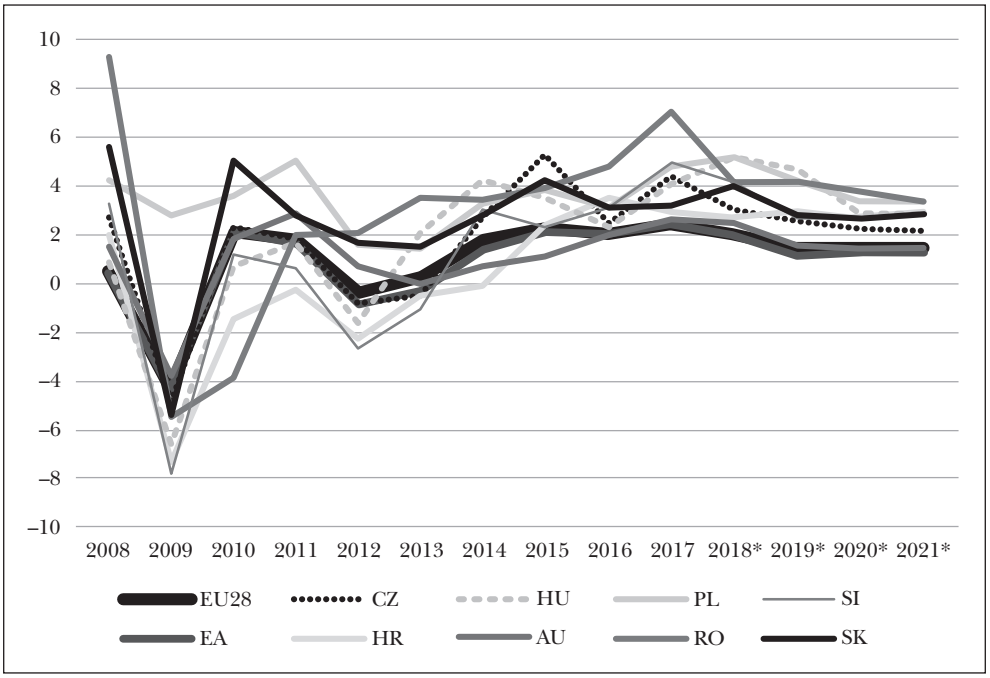
strength and the economic growth of the region is exceeding the average of the euro area (see Chart 10). As regards the chart, we should note that the expansion of the Hungarian economy in 2018 reached 4,9–5 percent that exceeded by far the last forecast of the European Commission (2018) and the data from 2019 is similar to this. As regards the following years it is likely that the Hungarian economy will perform above the average of the EU, in the area of 3–4 percent.

Chart 10: Economic growth of the Central-Eastern European regions and the euro area in the period of 2008–2021



Source: Eurostat, European Commission, 2018

Some final thoughts

The specific characteristic of the "Hungarian model" that was renewed in 2011 is that to prevent the earlier fiscal indiscipline the FC was granted public law authorisation (the right to veto) concerning the adoption of the budgets (and their respective amendments). As a consequence, the body is primarily focusing on the risks threatening the stability of the given year and the year beyond. It utilises the medium term outlooks, forecasts subordinated to this philosophy. Although the Council does not elevate such documents to the rank of board decisions, in its work the ideas concerning the sustainability on medium and longer terms are getting more and more in focus concerning the harmonious sustainability rather, increase of the economic, environmental, competitiveness and social welfare.

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It can be said that it is not solely because of the strong authorisations of the strict stipulations, the simple and transparent principles of the Hungarian system, the principles that are focusing on fighting government debt and the stipulations guarding the observance of the rules that make its successful operation possible but also the solutions of the Hungarian regulation that is adjusting to the European practice in a specific context, its effect of moderating over-expenditure, its awareness raising and confidence creating power as well as its timeliness have all contributed to its success. This is how it can contribute to the stability of the country, sustainable development, the improvement of the country's competitiveness, to the efficiency operation of the public finances sector and finally, the rising of the nation, the citizens of the country and material well-being.

Thanks to employing the elements of rule-based budgeting and the activities of the Fiscal Council – strengthening the requirements applicable for them both in the Fundamental Law and the Stability Act – in the years following 2011 the public finance balance clearly started to improve concerning the indicators of deficit and indebtedness. The stability of the central budget makes it possible that public finance assisted the development of the economy to an ever growing degree (today it represents the double of the data of the 2010 years). The competitiveness indicators[29] however are lagging behind the indicators of the Visegrád group of countries even today, despite their having shared a similar fate to us. At the same time, from among the line of our weaknesses those factors that were related to the poor efficiency of the functioning of the Hungarian public finances and that – by withdrawing resources from the economy – were the reason why competitiveness of the Hungarian economy eroded in the period 2004–2010 and embody the causes that are difficult to outgrow.

Our balance situation if exerting a positive effect on our national competitiveness.[30] The development of efficiency enhancing and innovation factor that are able to lay solid foundations for competitiveness and economic growth, like vocational and adult education, higher education, innovation system, optimising the coordinating mechanisms of the economy and cutting back the bureaucratic and administrative burdens of the market actors, can take place if we maintain the balance of stability and growth (György and Veress, 2016).

We can say that thanks to the economic performance of the country and the disciplined, committed to the principles and implementing the practice of rule based public finance management, the observance of the system of financial norms of the EU *stipulated by public, normative regulations* – at least its regulations related to financial stability and sustainability – Hungarian fiscal economy came close to the European standards in a period when a government professing itself to be committed to "national" causes was leading the country.

Notes

[1] The author wants to thank Tünde Gregich and Dániel Csomós, staff members of the Fiscal Council Secretariat, to Messrs. László Kékesi and Sándor Varga, advisers to the Chairman, who assisted him in writing this article. The article is a revised and amended with new experiences version of the paper pub-

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lished in *Polgári Szemle*, issue 13 in 2017 in Hungarian and English languages titled *Rule-Based Budgeting: The Road to Budget Stability* that was followed by a Chinese language edition of *Polgári Szemle* in 2019.

[2] 10th OECD Network of Parliamentary Budget Officials and Independent Fiscal Institutions (PBO) Seoul, 3–4 July 2018

[3] The introduction and application of the rule-based budgeting has a very extensive theoretical literature and the EU Commission – moreover and lately the cooperation forum of the independent fiscal institutions of the EU member-states started to publish documents. This chapter was prepared by using these referred documents.

[4] Indent (1) Article N of the Basic Line of our Fundamental Law („Hungary shall observe the principle of balanced, transparent and sustainable budget management.") and Articles 36, 37 and 44 of the chapter The State on public money.

[5] Act CXCIV of 2011 on the Economic Stability of Hungary.

[6] In October 2015 the European Commission established the independent fiscal institution of the European Union, the European Fiscal Board as an opinion giving, advisory body the activities and mandate of what were limited to the countries of the euro area. According to the resolution this new body functions independent from the national and European institutions but in cooperation with them. Members of the board were appointed a year later, in October 2016 by the European Commission and started its activities following this.

[7] Although in Poland constitutional regulation provided the framework for the rule-based budgeting, it is the government, as an integral part of the executive power responsible for the execution of the budget, is overseeing its observance.

[8] It was after 2008 when they started to use stricter fiscal regulations and established institutions to protect and „oversee" them in Germany, Ireland, Portugal, Finland, Austria and Italy. The countries that have already had such institutions (Sweden in 2007, Denmark and the United Kingdom in 2010) they further developed the system.

[9] Up to 2017 none of the rule based fiscal framework elements have been used and the fact that the former Czechoslovakia could not get external resources due to political reasons was playing a significant part in this. The change of the regime here took place in a country where the economy was relatively developed, the standard of living was low however, the level of indebtedness was minimal.

[10] The cooperation forum of the IFIs offers an organisational framework for this, and works with the ECFIN in the background. From 2015 the professional and consultation forum established as a self-assembly initiated mutual exchange of experiences with the European Fiscal Board to share best practices.

[11] There are no international (European) best practices regarding the concepts of professional background or public law status of independent fiscal institutions. The important thing is the ability of institutionalised preservation of rules that varies from country to country as regards the strength of the employed public law tools, the degree of relying on different confidentiality and authenticity (respect) values and traditions, differently organised professional support, using different public law or institutional tools. One difference however is especially obvious that concerns the strong public law authorisations and the right to veto as regards the adoption of the budget when it comes to the Hungarian Fiscal Council. (We are going to deal with this later.) The guaranteed to keep budget deficit under control, to prevent over-expenditure or the regulations intended to limit the investment expenditure (Benczes and Váradi, 2011) can be interpreted together with the structure of the state organisation and its fiscal system (Török, 2011). There are a number of experiences in international practice where the basic analyses serving the validation of the body's decisions are acquired from the business sector or other, independent institutions – SAI, national bank, professional task force. From the countries of the European Union France, Finland, Lithuania, Latvia and Italy are building on their respective SAIs, while Slovakia and Austria opted for their national banks as professional background. In case of the latter solution we also have to note that in these countries an institution with parliamentary powers is also guarding the rule-based budgeting.

[12] The cooperation of the Czech Republic, Poland, Hungary and Slovakia are behind the name "Visegrád" group of countries. In 2017 this group gave 5.6 percent of the GDP of the European Union and the name refers to the cooperation agreement of these countries signed in Hungary, at Visegrád in 1335.

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[13] Such could be for example when the IFI prepares the macroeconomic forecast that serves as the basis of the budget plan, gives its opinion on the draft budget bills, the defined budget parameters (proportion of the sovereign debt compared to the GDP, deficit ceiling, etc

[14] Gábor Karsai wrote in 2005: „In Hungary the amplitude of the cycles of domestic politics appears more powerful than it is common in the old EU member states. Very likely this is partly the consequence of the greater tensions brought along by the transformation and partly of the more modest democratic traditions. … The declared principles and practice the programmes announced in the election campaigns and those declared in the government programmes and laws should be clearly differentiated in the Hungarian economic and privatisation policy. This has two important elements. On the one hand these processes took place without parliamentary regulation" (Karsai, 2005, p. 510).

[15] See Act XXXI of 1989, Association Agreement, Act I of 1994 EU Accession Treaty, Act XXX of 2004.

[16] Acquis Communautaire, the basic principle of the community law. Literally it stands of „jointly achieved" things and according to the Hungarian translation means „community achievements". Instead of the expression 'acquis communautaire' lately they are often referring to it as 'acuis de l'Union' that is encompassing the „achievements" born in the second and third pillars of the European Union

[17] Chart 3 shows the evolution of the accrual-based deficit (according to ESA 2010). We are aware that the public debt ratio is not directly affected by this, but by the cash flow deficit. The bottom line is that the effect is evened out over a longer period.

[18] Naturally, this problem is present in a far wider context than this however, discussing it – amount them especially the impact assessment of productivity efficiency – far exceeds the frames of this article.

[19] Act LXXV of 2008 on the Cost-efficient State Management and Fiscal Responsibility.

[20] The small secretariat can be linked either to the SAO or MNB to thus ensure the technical conditions of the FC operation but it could also be expedient if the office of the National Assembly ensures the technical background for the operation. There are examples for all the above in international practice.

[21] The changing ideas of establishing an institution or the concept of formulating its mission exceed the frames of this article. The Fiscal Council can be found in the Kovács, 2016.

[22] According to Article 36 of the Fundamental Law as long as the government debt is exceeding half of the total gross domestic product the National Assembly shall adopt only such a budget act that contains the decrease of the proportion of government debt to the total gross domestic product. According to § 4 of the Stability Act the amount of the government debt planned for the last day of the budget year. According to the valid regulation in 2019 if the rate of inflation forecasted for the budget year and the real growth rate of the gross national product (GDP) equally are exceeding 3 percent, the growth rate of government debt compared to the previous year shall not exceed the difference of the expected inflation of the budget year stipulated by the budget act and the half of the real GDP growth. In case from among the inflation rate forecasted for the budget year and the real GDP growth rate at least one does not exceed 3 percent the government debt decrease shall have to be at least 0.1 percent. According to the amendment of the Stability Act valid from January 1, 2020 and to be considered when preparing and adopting the year 2021 central budget of Hungary the degree of government debt shall have to be defined so that the decrease of the value of the government debt indicator compared to the reference year should reach minimum 0.1 percent apart from the observance of the EU regulations concerning the decreasing of government debt.

[23] www.parlament.hu/web/koltsegvetesi-tanacs.

[24] Most recently (15th of February, 2019) Standard & Poor's upgraded Hungary from BBB/A-3 to BBB/A-2 while Fitch Ratings upgraded the country from BBB minus to BBB (22nd of February 2019).

[25] In 2016 the growth rate that determined the micro course of the national economy was 2.3% and was realized on the level of potential emission. And in 2017 the cash flow deficit was significantly better than the planned degree.

[26] Apart from the nominated, reserves to be constituted compulsively the central budget bill may provide regulations for the establishment of other reserves. Such is the Country Protection Fund that ensures the maintaining of fiscal balance.

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[27] Structural deficit: the balance of the governmental sector cleaned of the effects of the economic cycles and individual items (Áht. Point y) Indent (1) § 2). Its extent shall not be higher than the 1.5 percent stipulated as a medium term fiscal goal by Point a) Indent (2) § 3/A of the Stability Act.

[28] According to the so-called one-twentieth rule of the EU the GDP proportionate government debt shall not exceed 60 percent. In case it is higher than this limit then the difference shall have to be decrease annually by one twentieth part of the reference framework of the previous three years.

[29] Attila Chikán wrote: „a fairly strong correlation exists between labour productivity and competitiveness. We are hardly making a mistake when we say that one of the important factors of our country's significant lagging behind is that in the rank of the 33 OECD countries only five countries are behind us and Hungary's indicator is not reaching half of the USA data and represents exactly 60 percent of the OECD average. Having such results it is inevitable to detect overall backlog and it is an especially regretful fact that the growth rate of productivity is also showing a downward trend" (Chikán, 2014).

[30] Continuing the thought of linking competitiveness and the rising of the material and spiritual wellbeing of the citizens we have to agree with the definition of Prof Dr Magdolna Csath according to what: „economy is competitive if the abilities of the nation are used well and keep gaining strength in a longer run, the firms are producing big additional value and as a consequence of these factors the standard of living and the quality of lives of the people is constantly improving" (Csath, 2016, pp. 5–6).

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Csaba Kandrács

The Renewal of Banking Supervision

Summary
Financial supervision, including banking supervision, has evolved over the last hundred years in terms of both its institutional system and its methodology and approach. The biggest impact on development was caused by various economic crises and scandals at certain financial institutions. In order to be able to mitigate the impact of financial crises on the banking system and to detect and deal with banks' problems in a timely manner, financial institutions must be subject to continuous supervision. The most recent era in Hungarian banking supervision began on 1 October 2013, when the Magyar Nemzeti Bank took over the role of the Hungarian Financial Supervisory Authority, thereby integrating micro-prudential supervision into the Hungarian central bank. Renewal can be identified throughout the set of instruments for Hungarian supervision, including continuous supervision and investigation methodologies. The entire set of instruments is characterised by a change of approaches, i.e. the reactive, "retrospective risk management" approach has been replaced by a proactive approach. As technology develops, it has become possible for the Supervisory Authority to use solutions that enable it to be present in the life of an institution without interfering with its business. In addition, the spread of digital channels has dramatically changed the financial habits of people and institutions. Information technology is becoming indispensable in more and more areas of life. Managing and monitoring the inherent risks is a major challenge that requires innovative solutions. The only constant is change. This paper presents a detailed overview of the latest supervisory developments and regulations.

Journal of Economic Literature (JEL) codes: G01, G21, G29, O30/39
Keywords: renewed banking supervision, innovations in supervision, MNB Supervision

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Brief overview of international banking supervision

Generally speaking, the development of the supervision of financial markets – including the development of banking supervision – occurred hand in hand with various scandals at financial institutions, banking crises and, in some cases, turbulences affecting entire banking systems. Both the changes in the institutional framework for financial supervision and the innovations in its supervisory instruments are generally responses to unfortunate institutional bankruptcies and the resultant depositor or taxpayer losses. These milestones are easily identifiable. One such event was the depression of 1929–1933, following which the regulation of supervising organisations was raised to the level of legislation in some countries, while development remained at the level of the national states, with the most advanced financial markets of the time at the forefront, such as the United States, the Netherlands and Belgium. The meaningful launch of a uniform regulatory approach at the international level can also be attributed to the crisis of a well-known bank, the Herstatt Bank House, which triggered the international coordination of banking supervision and banking regulation in the 1970s. Establishment of the Basel Committee on Banking Supervision at the end of 1974 was a huge step towards a unified global regulatory approach. There should be unified approaches and principles that define the fundamentals of banking all over the world. There is special literature on how the Basel Commission recommendations have become more complex and how they have advanced from capital requirements through credit risk requirements to other risk segments. The economic crisis of 2008 was the latest international event that led to the termination of many banks around the world, which put entire banking systems and countries in distress and had a significant impact on supervisory institutions. After that, more and more countries decided to transfer banking supervision to central banks, thereby reinforcing their independence.

Institutional, regulatory and methodological innovations were thus generally driven by crises at financial institutions and major economic crises, while technological advances continue to support the development of supervisory authorities. As in all other sectors, IT innovations play a key role in this regard, preparing the regulatory authority for a deeper, more up-to-date involvement in the day-to-day operations of institutions and, and to intervene in good time, where necessary. Continuous presence, the earliest possible recognition of problems and addressing them as quickly as reasonably possible were demands manifest in every age, but technological progress in the 21th century has offered solutions that make these more feasible than in any previous period.

Banking supervision in Hungary

Hungary and Hungarian banking supervision could not have avoided the international mega-trends, even though the changes began later compared to the developed financial markets. On the institutional side, entities overseeing different sectors of the

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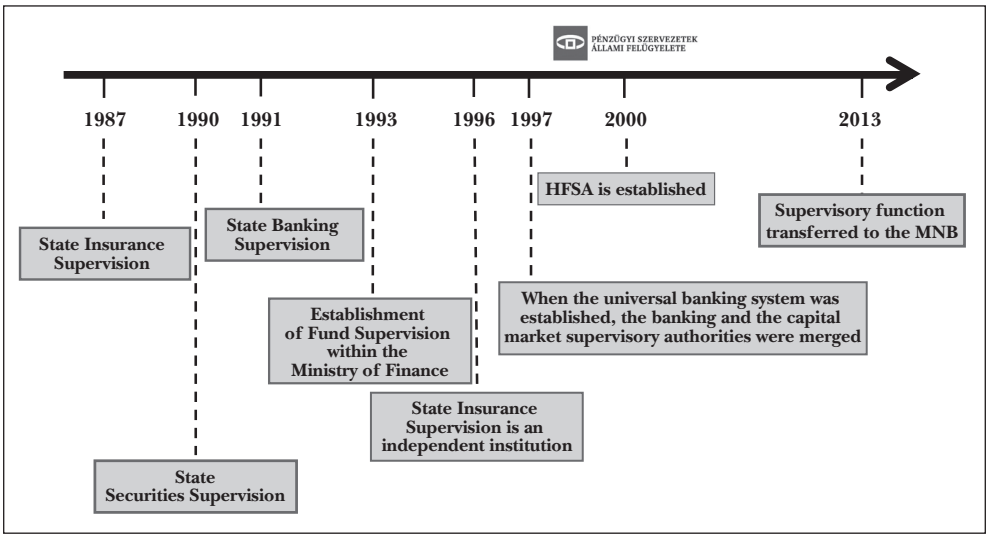
financial system were created around the political changes of 1989–1990, initially independently of one another. Subsequently, starting from the second half of the 1990s, the merger of supervisory authorities related to different markets in the financial sector began. First, the banking supervision and capital market supervision were merged, and from 2000, the Hungarian Financial Supervisory Authority was established, which also included insurance supervision. As in many other countries of the world, the economic crisis of 2008 highlighted the need for a new supervisory strategy to detect the risks in good time. However, an integrated supervisory approach, separate from the central bank, was in place until 2013. The milestone on the path to renewal was 1 October 2013, when upon the termination of the Hungarian Financial Supervisory Authority, the tasks of the Magyar Nemzeti Bank were supplemented with the supervision and consumer protection functions of the Hungarian Financial Supervisory Authority, thus making it possible to concentrate the macro- and micro-prudential mandate in a single institution. In 2014, the Magyar Nemzeti Bank (MNB) also established a resolution division, through which efficient crisis management could be provided for institutes that were struggling with problems, but were economically viable. Overall, in line with international trends, the supervisory function of the financial system was thus integrated into the Magyar Nemzeti Bank, establishing a central bank with one of the most sophisticated toolkits in the world, consolidating the micro-prudential supervision of all markets of the financial system, including the micro-prudential oversight of the banking, insurance, fund, capital and intermediary markets, the macro-prudential oversight of the financial system, the function of resolution, as well as financial consumer protection, and including the complete set of monetary policy instruments.

Figure 1: History of the Supervisory Authority



Source: MNB

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Starting from the second half of 2013, the MNB, which had been strengthened in its financial stability toolkit, has taken a number of steps to develop new approaches and methods to address risks to the financial system, including the banking system, in an appropriate and timely manner. Thanks to continuous improvements, the earlier periodic control approach, which mainly addressed existing risks, was replaced by a forward-looking approach, i.e. forward-looking supervision, and a continuous, risk-based, close presence in the institutions. The financial crisis of 2008 demonstrated that the market's self-regulatory capacity is low, and it is up to supervisory authorities to detect and address signs and practices of unhealthy financial intermediary systems before they become widespread.

Renewal of continuous supervision, basic monitoring and early warning system in continuous supervision

The basic pillar of effective supervisory activity is the ability to intervene in time. The primary means of transitioning from a reactive to a proactive practice is to shift the focus of supervision from periodic on-site audits to continuous supervision. Technological tools support this process, and someday it may be possible to receive information automatically online, twenty-four hours a day, without physical presence, from a supervised credit institution. However, one prerequisite for this is that the supervisory authorities have more detailed information on the functioning of the supervised institutions than in the past. To accomplish that, the volume of data requested from institutions has increased several-fold in Hungary, as in other EU member states. However, this in itself is not enough, as it must also be possible to process the incoming data and analyse the mass of information, extracting those elements that reveal in a timely manner when an institution is exposed to risks, including risks which need to be managed. This required the development of a basic monitoring system and the establishment of an early warning system based on such, which indicates problems by means of dozens of indicators, on the basis of the incoming data. After that, the need for supervisory intervention is examined. This basic monitoring system, which is under constant methodological development, is a kind of continuous forecasting system. Over time, more and more indicators are activated in the monitoring instruments. The reason for this is the recognition that it is not sufficient to capture the operation of a bank by risk segment, such as credit risk, operational risk, market risk, etc. ... it should also be assessed what are those relations in an upswing economic environment or even in a crisis or post-crisis situation, which best capture the current situation and the anticipated future risks of a bank. The technological advances of the 21th century provide the opportunity for a monitoring system to be IT-based as much as possible, and increasingly automated, and for a kind of *alert system* as well, to be based on the monitoring information. The new dimensions opening up to us with the rise of artificial intelligence in the field of automation and a forward-looking approach are now evolving in front of our eyes. The essence of the alert system is that in the case of sudden and unexpected changes in the data of interest and value to the

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supervisory authority, a different pattern than before emerges, the system will send an alert to the data evaluation officer, who will then investigate the cause for the alert and, if necessary, take action to fix the problem. Since 2013, several new, complex indicators have been developed that assess and evaluate different risk segments, in order to detect problems as soon as possible when the riskiness of a bank shifts in an adverse direction.

But such a system alone would not be able to fulfil its function if this numerical information was not supplemented by qualitative information which, on the one hand, is received through the regularly conducted *prudential interviews*, and on the other hand, by requesting materials submitted to the meetings of the supreme decision-making bodies, which constitute an important pillar of regular reporting. Regular institutional interviews, which are conducted quarterly for institutions of systemic importance, provide an excellent opportunity to uncover information and changes in business model and strategy that cannot be inferred from the numbers. During the conversations, the representatives of the institutions have a chance to respond to the trends that can be inferred from the monitoring system, to one-off outliers, and the supervisory authority can also express their opinion on the operation of the institution.

The documents *submitted to meetings of the supreme decision-making bodies,* such as proposals and minutes prepared for meetings of the Board of Directors, the Supervisory Board and the Senior Lending Committee, ensure that the Authority can very closely follow and detect the direction in which the institution is moving. Naturally, in the course of its operations a bank makes many decisions that require significant resources to process, and the Authority's capacity to process these fully is limited, but technological advances and the risk-based approach support increasingly close monitoring of the activities of institutions of systemic importance. Development is clearly heading in the direction of having more and more institutions subject to continuous monitoring, which does not seem to be an impossible mission with the development of technology. Other information obtained by institutions in larger volume and increased frequency, such as *more frequent physical presence* in meetings of various bodies, furthermore, *indications received from customers* and channelled in the process of *supervision also support early intervention.* By processing these data, MNB staff can keep up-to-date with the activities and operations of the given financial institution and, if necessary, intervene in a timely manner in order to prevent risks and violations of the law. Due to the regular quarterly evaluation of the basic information sources described above (monitoring system, prudential interviews, participation in board meetings and their materials, consumer indications), the Authority is indeed able to forecast the main directions of operation of institutions, and therefore detect any potential negative trends. In practice, as part of the quarterly evaluations, the expert responsible for processing these sources of information for the institution in question will provide the management with a summary of the most significant changes and events that deserve mention on a risk basis over the past period, and propose additional steps to be implemented by the Authority, if necessary. It should be noted that due to the lim-

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ited resources, supervisory activity is performed on a risk basis. The idea is that each institution is ranked annually in terms of its impact on the financial sector. The more significant the impact of the operation of an institution on the domestic financial sector and the economy, the more emphasis should be placed on it in the course of supervision. In its risk-based oversight, the MNB oversees and audits individual institutions based on their weight in the financial system and their risk profile.

Inspection methods, with special regard to the renewal of on-site inspections

The previous section outlined the tools and channels of information available to financial supervision in Hungary today to reach the institutional actors of the banking system and to monitor their activities, in order to obtain up-to-date information and draw forward-looking conclusions on the operation of banks, and where appropriate, to be able to intervene in due time. However, these fall into the category of so-called ongoing supervision, and at present are not sufficient in themselves to provide a comprehensive picture of a credit institution. They are complemented by various on-site inspections. On these occasions, the supervisory staff will review certain aspects of the operation of the given institution at the premises. It is a legal obligation of the MNB to conduct, at specified intervals, a comprehensive on-site investigation of the various supervised institutions. As a result of the supervisory operating regime renewed after October 2013, the Authority has moved towards conducting more and more investigations in the banking system, other than the comprehensive investigations required by law. In line with the MNB's general operational approach, these investigations are much more targeted events focusing on specific problems and risks. The background to this renewed approach is that, due to the demands of today's economic and regulatory environment, the processes and internal control systems of supervised institutions are changing so rapidly that it is necessary to assess the risks of institutions on particular subjects. Simply put, the financial world is changing too fast for a detailed on-site inspection of institutions conducted once every 3-5 years to be sufficient. In order to obtain an accurate picture of the daily business of an institution and the directions of its development, we had to increase our presence. Of course, this is a resource-intensive task, and the available capacities of the Authority are finite, but with the help of risk-based audit design, we have been able to make significant steps towards our goal, by enhancing our targeted and thematic inspections with a narrower focus.

The advantage of the new approach is that risks can be investigated shortly after their occurrence, and if necessary, intervention can be launched before the escalation of negative events, thereby preventing a systemic accumulation of risks. As a result of the thematic investigations, the MNB is able to obtain a sector-wide, horizontal information base and assessment of the evaluated risk, thereby facilitating more standardised supervisory action. Risks are identified by evaluating information received from ongoing supervision and processing data reports to the authority, meaning that

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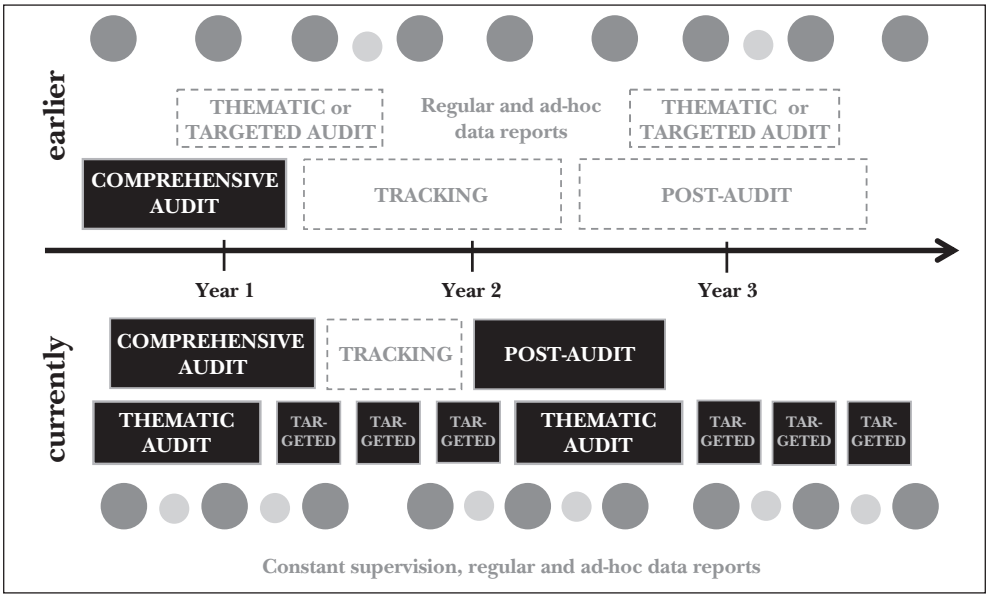
Figure 2: Supervision from an institutional perspective



Source: MNB

ongoing supervision substantially supports and influences when and what type of investigation is conducted at a bank, along with the regular comprehensive review.

In order to facilitate fast and effective supervisory responses, so-called operational investigating units have been set up, which *specialise in rapid, on-site risk assessment*. The purpose of their activities is to provide immediate on-site inspection and intervention based on the information and risks reported during ongoing monitoring. In the case of operational investigations, the difference from other inspections is that there is no need to notify the institution in advance of the initiation of the investigation, and the investigation is carried out on an identified, specific topic, which often involves copying the contents of the institution's data media (e.g. computer, telephone) (Lehmann et al., 2017).

Using *the tool of thematic inspection*, in 2015 for eleven banks the MNB investigated whether their remuneration practices were in compliance with the law and did not encourage excessive risk-taking, and whether the banks that acted as group leaders were enforcing their remuneration policies for group members subject to consolidated supervision. In 2016, by way of a thematic investigation on non-performing loans (NPL), the MNB sought to determine whether banks have a strategy in place to reduce their NPL portfolios, as well as the necessary resources and appropriate tools, by reviewing the practices of eleven institutions. In addition to the investigations, in-depth analysis of various risk-related topics by surveys was promoted, in order to explore the sector-level risks and market practice. In 2017, institutions conducted an analysis of their impairment recognition methodology and collateral management

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practices, the direct result of which was the entry into force of a comprehensive property valuation supervisory authority recommendation in 2018.[1]

Of course, *comprehensive investigations* have not lost their significance over the years, but as a result of several methodological innovations, they have become more targeted and focused. In the context of renewing comprehensive investigations, the following methodological changes have recently strengthened the MNB's functions in the credit institution sector:

– With regard to the investigation programme of comprehensive audits, risk-based planning has been reinforced, including the assessment of information from ongoing oversight; furthermore, the investigative focuses designated on the basis of the processing of data reports to the supervisory authority will play a more prominent role in conducting investigations. As a result, there are risk segments within the comprehensive investigations that are explored more deeply, in greater detail, and in some cases through a larger sample, for greater certainty.

– The role of addressing annual supervisory priorities in comprehensive investigations has also increased in recent years. This is based on the fact that each year the MNB evaluates the previous year's supervisory events and experiences, as part of the planning period for the upcoming supervisory year, considers the anticipated economic environment, future trends and risks, and sets out its comprehensive supervisory priorities on that basis. Such priorities included, for example, promoting the deleveraging of the NPL portfolios that developed after the crisis, monitoring the transition to IFRS standards as a result of changes in global accounting requirements, and tight monitoring of new lending processes emerging as a result of the resumption of lending. These horizontal priorities appear more prominently in the audit programme of comprehensive investigations.

– The previous audit practice based on the assessment of transactions and purely focusing on legal compliance has been replaced with a multi-step audit approach:

a) In order to ensure that – above and beyond legal compliance – the individual prudential compliance audits can be implemented in the widest possible scope at the level of the given institution, the MNB recently established the framework for examining compliance with regulatory and prudential requirements at the portfolio level, using analytical tools, which are implemented using the highly granular inspection analytics generated by the credit institutions. After having been tested by the MNB for thoroughness through agreement with the general ledger, the credit and coverage analytics generated by the institutions, with detailed data contents, go through a filtering package containing hundreds of checks, including a review of the following: are the given data fields populated in the correct format; equivalence of the institution's value sets with the values expected by the MNB; proper application of logical relationships between individual data fields; application of the loan coverage value and income-rated instalment rules; conduct of the customer, transaction and collateral reviews in a timely manner; correct application of customer and transaction rating categories; adequacy of collateral allocation; proper application of segmentation; adequacy of the level of group impairment; the adequacy of the risk weights used in capital calculation.

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b) the MNB carries out audits of individual risk processes in a process-oriented manner, thereby facilitating the identification of systemic deficiencies,

c) in support of the above, the MNB applies statistical, expert and focused sampling on the basis of a complex methodology, in order to explore deficiencies that can be observed in practice,

d) during the process audits, the MNB pays special attention to monitoring the IT support of risk assumption activities and, in close cooperation with IT security oversight areas, verifies the prudential compliance of the relevant IT applications,

e) the MNB conducts proactive communication in order to remedy the deficiencies discovered in the course of investigations as soon as possible, and reports the errors observed in their operation to the audited institutions.

In line with international requirements, another important innovation of the renewed banking supervision is the so-called *ILAAP*[2] *reviews, used to audit the liquidity positions of institutions and the management of liquidity risks,* which take place – in addition to analysing information obtained from regular data reports – in the form of on-site investigations. Previously, the MNB had used balance sheet and deposit coverage ratios to monitor the liquidity of the banking system and measure systemic risks related to liquidity, but this was discontinued based on the experiences from the 2008 global financial crisis. Balance sheet and deposit coverage ratios have been replaced with the so-called Liquidity Coverage Ratio – LCR, compliant with the international regulatory standards, enabling a more segmented, more in-depth analysis of items affecting liquidity (Lehmann et al., 2017). "Pursuant to the liquidity coverage requirement prescribed by the rules of law in force, institutions shall possess such a volume of liquid assets, the total value of which covers, in a situation of distress, the difference between liquidity outflows and inflows, ensuring that such a level of liquidity buffer is maintained which may be appropriate, in times of severe distress, to bridge any imbalance between outflows and inflows for a period of thirty days" (Lehmann, Palotai and Virág, 2017, p. 883). However, practical experience with the application of the LCR indicator has also highlighted certain shortcomings of the indicator, notably that it does not take into account the risk of deposit concentration, and therefore the supervisory authority has provided guidance in that context as well to the sector, through the modification of the regularly renewed ICAAP / ILAAP manual. The essence of the modification is that it has been formulated as an expectation from the institutions that the part above the threshold of individual deposits exceeding a certain percentage of the deposit portfolio should be fully covered by liquid assets. The key areas of liquidity risk management are changing dynamically as a result of factors affecting the banking system, thereby adapting to the risks inherent in banking practices. An example of such an identified risk is the failure to take into account fixed but callable deposits in the LCR. Therefore, the MNB expects the institution not to automatically classify its liabilities into LCR categories based on their maturity, but to review whether they have any call option. Also, an inadequate assessment of the operational relationship also leads to underestimating the risks. In the LCR calculation, "only that portion of the deposit that is required for using the service for which the deposit is a

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by-product, shall be treated as an operational deposit." Accordingly, the MNB expects the institution using the operational deposit category to have a methodology to determine the balance needed to maintain the operational relationship. On the other hand, it should make a statistical estimate to determine whether the average outflow factor of the deposit holdings, divided up into an operational and a non-operational part, reflects the risk of the entire deposit holdings appropriately. The MNB also assists the institutions by publishing these priority topics, by defining the legal requirements accurately, and by identifying and managing the liquidity risks that affect them.

The MNB also complies with international expectations by conducting ICAAP [3] reviews at the banks, which assess the capital requirements set by credit institutions to cover the risks assumed by them and, if necessary, determines additional capital requirements for the institution. The starting point for this is that all credit institutions are required by international rules to assess their internal capital requirements and to develop calculation procedures that will enable the institution to assess the level of its capital requirements. The European Supervisory Authorities, including the Hungarian Authority, expect the institutions to regularly review whether their available capital covers their losses in times of stress. These tests are conducted by risk type. Credit risks carry the most weight, which are the effects of the risk of default of contractual counterparties on the profitability of the institution and on losses affecting its capital position. It is in this context that the default, counterparty, foreign currency lending, settlement, equity, concentration, country, and residual risks are assessed. In addition to credit risks, special consideration is also given to operational risks, market risks, bank interest rate, business risks, strategic risks and regulatory risk, as risk types. The MNB evaluates the capital requirements of credit institutions calculated for themselves, for each type of risk annually. Its methodology has been constantly evolving over the past five years, influenced by the experiences from the crisis. In the past, ICAAP reviews for non-systemically significant institutions with a weak impact took place annually, on a desktop basis, without any on-site inspection, but each systemically significant institution underwent an annual on-site assessment. In recent years, the central bank has developed a transparent and compelling view on both risk management and the calculation of capital requirements covering the risks. For the latter, benchmark methodologies have been developed to support the acceptability or rejection of the several different calculation methods used by institutions for the risk models. This ensures transparency vis-à-vis the institutions on the one hand, and helps with the comparison of the models based on mathematics and statistics on the other hand. In conclusion, the ICAAP review methodology was a function of the size and risk profile of the institutions. However, given that systemically important credit institutions have, over the years, understood and learned the MNB's expectations and methodology for ICAAP calculations, and through annual reviews it became clear that the ICAAP calculations had been built into the everyday operation of the institutions, it became possible to shift in the direction of having every institution evaluated by on-site investigations as well. Naturally, due to the limited capacities available, these can only be conducted at certain intervals. Another argument for the change was that there is no such thing as a

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small or large bank, a systemically significant or not so significant institution from the perspective of the customer, depositor, creditor, depositors authorised their banks to manage their funds trusting that they will certainly get their funds back, and it is the responsibility of the Supervisory Authority to ensure that every institution should have this kind of public trust. The new approach essentially consists of classifying institutions into three categories, depending on their size and risk profile. The first category is subject to a comprehensive, full ICAAP review, the second group of credit institutions are subject to targeted investigations with a narrower focus, but the Authority will still make on-site visits, while the third category will be subject to evaluation without an on-site investigation. Based on the methodology, every institution undergoes a comprehensive review every three years, but the systemically most significant and the most risky institutions continue to be evaluated by on-site investigation.

Data backup, data analysis support during on-site inspections

In addition to data analysis carried out as part of its ongoing oversight, the MNB also performs data collection and analysis as part of the investigations and procedures it conducts. This type of data collection can be divided into two groups according to the processing of the information: when the selection of the data is performed by the supervised institution, and when the selection is performed by the MNB at its branch office in order to ensure and control completeness. "The highest level of data collection is when the MNB makes a physical mirror copy or a certified copy of the data owned by the institution or its staff, including data stored by a hosting provider, and uses the copy to scrutinise the saved data. In this case, MNB is not only responsible for the restoration and processing of the data, but also for demonstrating the integrity and authenticity of the data, which is currently guaranteed by the MNB by using so-called hash codes and hash functions. The first step in processing database backups is to establish the same IT environment as the platform of the backup database, and then restore the database in the same way as the one at the supervised institution's site. After this, filters, reports and analyses are prepared, which is performed using the same logic as during data requests. Querying data from a restored database has many advantages over obtaining the data files. On the one hand, the risk of data falsification is significantly lower; everything can be audited; sampling is possible on the basis of a more precise risk classification, for more in-depth investigations, on the other hand, it is possible to eliminate problems due to information asymmetry between the requester and provider of the data (e.g. the data provider does not prepare the statement with the required logic/content).

However, there are special requirements for database backup, such as higher IT infrastructure, the information security risk is higher, increased needs for human resources, and the Supervisory Authority needs to have a broader scope of information and skills concerning the individual operation of the investigated institutions. Processing of the physical mirror copy or certified copy differs from the processing of database backups in that in this case the content of the copy remains unknown to

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the Authority until the beginning of processing, furthermore, the content of the copy is unstructured, and therefore the MNB must have the necessary data analysis infrastructure and the required expertise " (Lehmann, Palotai and Virág, 2017, pp. 876–877). At the same time, the MNB has also moved towards the collection of granular data for regular data reporting, as much more detailed and accurate analyses can be conducted on this basis, both by the Authority and other areas of the MNB. A major milestone in this ongoing journey will be the launch, in 2020, of a project initiated by the MNB, which will provide the MNB with regular elementary information on virtually the entire credit portfolio of the supervised institutions, thereby replacing a large number of data reporting tables currently containing aggregate data.

Supervisory stress testing

It has already been mentioned that according to the MNB's view a forward-looking approach contributes significantly to the stability of the financial sector. One way to do this is to apply stress tests. These stress tests are designed to verify whether in the event of a significant macroeconomic shock the supervised credit institutions would remain sufficiently liquid and capitalised. Since the outbreak of the last financial crisis, special attention has been given to banks' ability to withstand shocks and absorb losses. With the help of the national micro-prudential authorities, the European Banking Authority (EBA) has been investigating this for larger European banking groups since 2009, but to date there have been no material consequences of these tests. One of the major accomplishments of the common European banking supervision has been the harmonisation of the supervisory review and evaluate procedure and its incorporation into a recommendation, based on which the supervisory authorities work in a uniform manner to identify risks to banks. In order to ensure that stress resistance of financial institutions with foreign parent banks and domestically-owned financial institutions operating in the respective countries can be tested directly by the national supervisory authorities, the EBA supplemented its aforementioned recommendation, which was published on 19 July 2018 (EBA, 2018). Having taken effect officially from 1 January 2019, the guidance requires the relevant authorities to establish a Pillar II capital recommendation (in short: Capital Guidance or P2G) for credit institutions or groups of credit institutions. As a result, the financial system, taking shape since 2017, and separately each of the innovations aimed at ensuring the stability and more secure operation of banks, have been incorporated into the regulation. To determine that, supervisory solvency stress tests had to be developed, which the MNB did in early 2018. The micro-prudential authority will run the first stress test developed by it and determine Capital Guidance on the basis of the balance sheet total of the complex SREP for the largest Hungarian-based banks in the first year, and from 2019 onwards, for small and medium-sized banks. P2G is a supervisory guideline whereby the micro-prudential authority determines the amount of capital buffers it considers justified in addition to the prescribed SREP capital requirements (TSCR) and macroprudential capital

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buffers (collectively OCR), so that the supervised institution does not violate its requirements under stress conditions. So this is a kind of "proper safe distance". The management of the banks has so far held additional capital to avoid the violation of the capital requirement (OCR), but this is now being quantified by the supervisory authorities in a single stress test and imposed on the banks in the form of a recommendation. It is important to underline that the new instrument is a guideline and does not constitute a direct capital requirement, but merely determines the amount of additional capital that the supervisory authority deems desirable based on the results of the stress test. The supervisory authority strictly penalises any violation of capital (quasi-car crash), and only declares keeping the "proper safe distance" as desirable. At the same time, the MNB will closely monitor institutions where it finds that this buffer is inadequate and that there may be a risk of a capital infringement on the planning horizon, i.e. the institution stays within the proper safe distance defined by the Supervisory Authority. In the default case, the P2G valid for a given year is determined based on the stress test conducted in the previous year. Therefore, the MNB calculates the P2G values determined at level of the individual bank (sub-consolidated level,) effective from 1 January 2019 as a result of the stress tests conducted in 2018. Since P2G has been formulated at recommendation level only, in the beginning any violation of the established value only results in intensive communication between the Supervisory Authority and the bank, and the preparation of a capital position recovery plan. However, in the absence of a willingness to cooperate, the Supervisory Authority may even apply the tools reserved for capital infringement.

The supervisory stress test methodology is based on a European-level equivalent developed by the EBA. However, in order for testing to be fully applicable to all actors in the Hungarian financial sector, the generalised framework for larger European banking groups had to be slightly revised. The main methodological difference was the shift from an approach based on the use of partial bottom-up, that is, the use of internal banking models constrained by a certain framework. The stress test developed by the Hungarian supervisory authority is fully centralised, in order to ensure better comparability between banks, i.e. both the definition of the macro scenario and the models used for forecasting and populating with data are ultimately controlled by the MNB. The aim of banking regulation is to further strengthen the forward-looking approach, which has also been supported by a change in the accounting standard to be used by credit institutions. For European credit institutions, one of the major innovations of IFRS9, introduced in 2018, was the provision for the calculation of impairment of loans. While the previous impairment model was capable of handling only actual, evidence-based losses, the new standard models expected credit losses, which brings forward the recognition of impairment in time. The supervisory stress test has joined this direction since 2019, which can therefore simulate properly and more realistically the recognition of impairment occurring differently in terms of dynamics and extent, in the case of simulating a possible crisis or deteriorating macroeconomic environment.

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Viability assessment based on ongoing monitoring and inspections

The previous sections described the activities covered by constant supervision, constituting the backbone of the activity of the Supervisory Authority, and by the various investigations. However, these are not a series of point events, but rather the information extracted from them culminate in a complex, annual institutional assessment. This is a representation of the concept that monitoring is an uninterrupted process. The closing moment of this process for a given year is the *viability or SREP dialog,* which systematises all activities carried out by the supervisory authority in the given year, from the processing of regular data reports, through completed inspections, through prudential interviews, to the on-site inspections of the given year, all the way to ILAAP, ICAAP evaluations. Since the end of 2017, the system, built on a methodology developed by the European Banking Authority, provides a clear view of the viability of institutions, key aspects of their operations such as corporate governance, credit risk, operational risk, capital position and liquidity, based on more than 70 indicators and qualitative information, and through evaluating these by applying transparent and comparable principles. The subject matter of the SREP CEO meetings, which is a summary of the SREP dialogue covering the entire supervisory system for a given year, is attached to this evaluation because it provides a complete overview of the institution's operation and its assessment by the supervisory authority, through the composition of the set of indicators. In respect of systemically important institutions, the indicators are updated quarterly, but even for smaller institutions, the analysis and the resulting assessment are performed annually. The annual evaluation discussions take place at the supreme level of governance of the institutions, to ensure that the senior management of the credit institution sees and hears at least once a year what the Supervisory Authority thinks of the institution they manage, its weaknesses, areas for improvement, major risks, and the focal points of the next year from the aspect of the supervisory authority. The information received in the course of ongoing supervision, as well as on-the-spot and other investigations that have established the viability value of a given institution for the given year, are presented here. This kind of approach, formulated in a logically closed system, is one of the supervisory achievements of recent years, helping the Authority to understand and evaluate banks in a complex way, and to allowing credit institutions to understand what they need to do to ensure the development of areas considered by the Authority as the carrying the highest risk.

Regulatory activity

It is the primary responsibility of the incumbent supervisory authority to channel the information obtained from the sector through ongoing supervision and investigations to the institutions in the form of legislation, recommendations and management circulars, to ensure that the practices of the institutions meet the prudential and other requirements as much as possible. The Authority has prepared extensive

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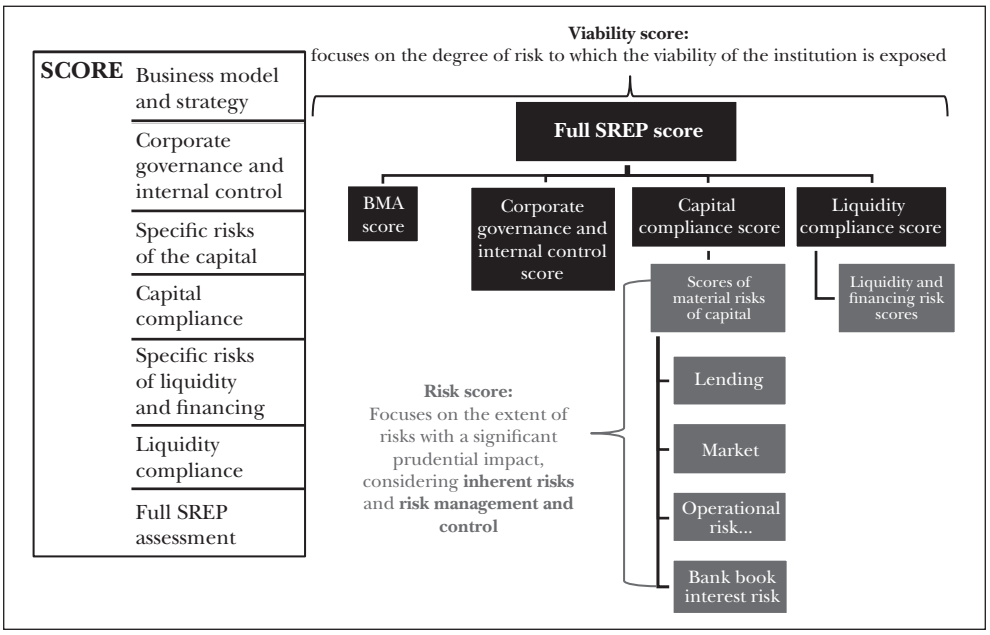
Figure 3: Risk and viability assessment



Source: MNB

recommendations to the sector in the recent period, one of the key motives of which was to communicate the lessons learned from the crisis and post-crisis period to the supervised institutions. Although the former financial supervisory institution had had a similar tool before the supervisory task was delegated to the MNB, due to the previously mentioned complex financial stability toolkit employed by the MNB, the published recommendations can be more attentive not only to the problems occurring in micro-prudential supervision, but also to the macro-level risks. The NPL (Non-performing Loan) package, which came into force in July 2018, is of particular importance in this respect. The Recommendation package is a coherent system of multiple recommendations built on one another. The set of recommendations is intended to prevent the bad practices observed during and after the crisis, so the key objective is to prevent high non-performing loan portfolios from developing in the sector in an uncontrolled way, and to keep the institutions prepared to write off the portfolio of non-performing loans, to prevent these from being entrenched in the books of the institutions, as these portfolios draw off significant resources from their core business, thereby undermining the efficiency of the financial intermediary system. The central element of the package is MNB Recommendation no. 10/2018 (II.27.), implementing the NLP recommendation of the European Central Bank, which requires supervised institutions with a high non-performing portfolio to have a strategy for deleveraging their NLP portfolio, which they are required to submit to the Supervisory Authority. In addition to the preparation of the strategy, the recommendation also

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sets out organisational and process expectations, in order to ensure that the strategy's realistic but ambitious goals remain achievable.

The other pillar of the package is Recommendation 12/2018 (Part II) on the structuring, monitoring and proper valuation of real estate-based project funding transactions. Real estate-based project financing was a major problem for the domestic banking sector during the crisis, and therefore it is crucial that lessons learned from the crisis are embedded in the practice of both institutions and the supervisory authority, which is implemented in practice by the Recommendation.

Closely related to this is Recommendation no. 11/2018 (II.27.), which provides practical guidance for the valuation of real estate collateral, both for supervised institutions and the real estate appraisal trade, defining such cornerstones, concerning both the professional content of real estate appraisals and how the banks should treat real estate appraisals and appraisers, which, when applied properly, are capable of ensuring that the real properties used by the institutions as collateral are taken into account at an adequate value when lending decisions are made.

Purposes and means of the digital renewal of supervision

From the previous sections, a kind of new approach can be inferred, i.e. that the MNB, as the supervisory authority, attempts to be present in the lives of institutions without hindering, slowing down or disabling their prudent business operations. In today's modern, computerised world, this kind of approach can work, but it requires further development of methodologies and further shaping of the set of supervision instruments. The keyword is digitisation. The strategic goal of the MNB and the defining element of its mission is the realisation of "Digital Supervision". In practice, Digital Supervision means that the Supervisory Authority continually seeks and implements technical solutions and innovations that can make its operations more efficient. On the one hand, a supervisory solution is considered effective if it can transform the inherently reactive, subsequent nature of supervision into a proactive one that focuses not on managing existing risks, but rather on preventing such risks from emerging. On the other hand, a supervisory solution is considered effective if it succeeds in replacing random supervision or supervision by expert sampling with a risk-based solution that involves the full or the most comprehensive processing of the data. Thirdly, it is effective if the data to be processed are collected and processed in the most raw, genuine form possible, thereby reducing the possibility of fraud and data manipulation. Fourthly, it is effective if the automation of the processes reduces either the need for human resources or the number of human errors.

IT supervision – the only constant is change

IT supervision is another one of the areas that is constantly changing and thus requires continuous professional development to keep experts abreast of the latest technologies. At the same time, the methodological foundations of IT supervision need

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to be updated from time to time, proactively anticipating the changes. Meanwhile, supervised institutions must be provided with a stable, predictable regulatory environment that allows for technical innovation and delivers a secure framework for new developments, since a major system change or implementation of a new system is usually a multi-year project. The IT Supervision Department of the Magyar Nemzeti Bank operates in this challenging professional environment. In the following sections, we will discuss IT as a supervisory area, but there seems to be a clear direction that we cannot talk about state-of-the-art supervision without having every major function of supervision (constant monitoring, area of investigations) turning more and more into an IT function. Today, IT solutions have emerged that can automate many processes, and artificial intelligence can open up unprecedented opportunities for the continuous monitoring of prudent banking operations.

Methodological developments in IT supervision

The spread of IT tools, the increasing penetration of smartphones and the emergence of generations of "digital natives" have resulted in IT becoming a part of our everyday lives, and we increasingly manage our finances through electronic channels. This trend has been recognised by both financial institutions and regulatory authorities, which is why banking digitisation is increasingly promoted in institutions' strategic plans. One example for that, which has been increasingly widespread, is the conclusion of a paperless contract or making legal statements without paper, sometimes even without the physical presence of the customer. Another frequent digitisation goal of financial institutions is to implement remote client identification, in accordance with anti-money laundering regulations, necessary for remote account opening or borrowing. These solutions require application of available state-of-the-art technology, while the current underlying IT systems have often operated unchanged for many years, following a system logic that is several decades old. This duality poses a daily challenge, not only for financial institutions, but also for IT supervision, as it has to examine objectively, with a focus on risks, systems that are very divergent, representing very different worlds in terms of approach and technology, even within a single company. In practice, this means continually reconsidering the system of requirements and testing methodology: each new technology raises the question of whether the previously expected control measures are relevant, or whether there is already some kind of better and more up-to-date risk mitigation measure that the Supervisory Authority can expect or recommend. Can the same set of expectations apply to agile software development, as it does to applications made in the traditional cascade model? The answer depends on many other factors as well (such as the size of the development team, the purpose of the software, etc.), so supervision requires a flexible methodological approach that experts can apply in possession of accurate knowledge of the specific situation and circumstances.

In addition to the technical solutions and the methodologies of development and operation, the system of expectations of IT control itself is also changing. For ex-

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ample, a password policy that any auditor would have regarded as appropriate ten years ago may no longer be considered secure. Today, entry by password is no longer considered as strong authentication in itself, no matter what password complexity requirements the administrator has set. The expected control measures in other areas of information technology are changing in the same way, although the control objectives to be accomplished (such as proper identification of the user) remain the same. For this reason, supervision methodologies are also constantly evolving, extending across the entire framework of investigations and requiring that the guidelines used in technological audits be constantly updated.

In addition to the continuous improvement of its own IT supervisory methodology, the awareness and tracking of international regulatory trends and directions, or even proactive participation in their development, has been an increasingly prominent task. Financial services provided over the Internet are often available across national borders, so it is important for domestic financial institutions and fintech firms to avoid a competitive disadvantage because of a possibly more stringent regulatory background. At the same time, the Supervisory Authority must also take care not to make the mistake of introducing too relaxed regulations, and thus exposing customers to excessive risk or opening up money laundering opportunities. This is particularly true in the field of IT supervision, as financial technology innovation is emerging primarily in this area, and such innovations are being explored by the Authority during licensing procedures and in the investigation of the supervised institutions. Another important driver of participation in international regulatory work is the pursuit of a unified approach and set of rules. All over the world, more and more attention is being paid to cyber security breaches, and many international organisations feel the need to develop regulations, in order to raise the overall cyber security level of maturity. However, this regulatory tendency carries the danger that contradictory, practically unworkable regulations are created that, all in all, do not improve, but rather erode, the cyber security resilience of the financial system. That is why it is important that integrated supervisory authorities with an overview of several sectors, such as the MNB, are more involved in international regulatory and methodological work, share their experience and seek synergies between existing and emerging regulatory frameworks.

New tools in IT supervision

Traditionally, IT supervisors visit the supervised institutions during on-site inspections, especially during IT sub-audits of comprehensive investigations, or during themed and targeted audits. In addition, institutions may receive IT-related expert opinions during licensing procedures and requests for official position, which are prepared with the involvement of the IT supervisory function, but in these cases usually there is no direct connection between the institutions' IT managers, experts and the IT supervisors. Over the past two years, the MNB has sought to establish a more direct connection with the institutions supervised by it. On a number of occasions, the experts of the IT supervisory function provided consultations on the inspection reports

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prepared by the Supervisory Authority, as well as on planned major developments, system replacements and data centre relocations. With regard to priority IT projects, the MNB considers it a good practice for institutions to report regularly on the progress of the project in the context of ongoing monitoring. During such personal consultations, the HFSA staff responds to any questions that may arise, in order to help institutions comply with the regulatory and supervisory requirements. As part of more interactive supervisory relationships, the MNB also seeks to assist and monitor major system replacements, data centre relocations, outsourced IT operations, and system and data migration associated with mergers and acquisitions of institutions. At the same time, the Supervisory Authority also strives to ensure that the monitoring of projects that require such a high level of attention and resources should cause no unnecessary drain on the resources devoted to actual objectives, possibly by imposing additional obligations (data requests, reports, on-site interviews) on the institutions. Therefore, supervisory authorities strive to become familiar with the ongoing project, so that they can process information and decision preparation materials designed for the institution's own decision-makers.

When inspecting data migrations, in addition to enhancing traditional sampling control testing IT monitoring also applies procedures based on full data population testing, with the support of appropriate audit/data analysing software. In this way, supervisory controls can gain very high assurance that data migration has taken place properly, without data loss or inappropriate modification. The correctness of the data is also important, in order to ensure that the relevant rights of the data subject in the processing of personal data are not violated.

Supervision of clouds

In IT, the "cloud" is a solution that enables on-demand access to shared, configurable computing resources that can be quickly allocated and their use can be stopped, with minimum management expenditures or service provider's involvement. In this way, using the cloud can deliver new business or IT services relatively quickly, even without in-house IT development capacity. Due to its flexibility, more and more financial institutions are opting for cloud solutions, either inside the company or company group (private or community cloud), or outside (public cloud). However, use of the cloud always entails some loss of control over the IT environment, and if the entire in-house IT assets remain outside of the cloud (since that is also an option), then even the available or easy-to-implement control measures might not be implemented. Depending on the chosen cloud service model, the entire infrastructure (Infrastructure as a Service (IaaS), Platform as a Service (PaaS) or only the software (SaaS) is used by the cloud provider's client, the supervised institution. The model determines the level at which the supervised institution itself controls the data, accesses and services, and the degree to which it relies on the cloud provider's own services. When supervised institutions start developing a new solution based on a cloud-based service model, they face technical and compliance issues that do not arise during the deployment and

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operation of traditional IT solutions installed physically on one server. For example, in a virtualised world of clouds, even the continent where the data are stored physically cannot be located by the owner of the data. In order to avoid such situations, the MNB resorted to the regulatory tool presented earlier, and issue a recommendation [4] to financial organisations, with the aim of providing practical assistance in managing the risks arising from the use of community and public cloud services, and to ensure the uniform interpretation of the application of the relevant legal provisions. The Recommendation provides guidance on compliance with legal requirements, sets out the minimal contractual requirements, describes the risks to be managed, the control measures required and the main aspects of the supervisory authority's audits, and is consistent with other European regulations. The MNB issued the most recent, revised version of the Cloud Recommendation[5] in March 2019.

Regulatory and fintech innovations

It is often said that development is unstoppable. This is especially true for the beginning of the 21st century. Technological progress has reached an unprecedented speed. Almost every novelty becomes relatively easily available for the average person as well. Information channels – the Internet, Facebook, Twitter, Tumblr and many others – keep releasing news of the world.

In many cases it is not easy get oriented in this flood of information, and to obtain the relevant and useful information that we are interested in, however, this much-resented flood of information also has some beneficial impacts: The innovations that mean faster, more comfortable services and solutions containing added value and importantly, carry a lower price tag, become available for the consumers – or customers, through the lens of the service provider – almost immediately. Additionally, considering the customer side, the requirements communicated from the side of the consumers may also appear for the other side almost immediately. In the virtual space, the demand and supply side can thus respond almost immediately to consumer demands on the one hand, and to new opportunities, on the other hand. Of course, in order for an idea/need to become a "product", sharing information is not enough, on both sides listening ears, the intention of implementation and such a regulatory environment, mindset and a system of tools are required that support the implementation of the novelties in the market environment on the one hand, on the other hand, guarantees for the market players that they can operate safely, given the risks that emerge with the new products, services. According to our current knowledge, the two most state-of-the-art tools operated by regulatory, supervisory authorities are the "Innovation Hub" and the "Regulatory Sandbox".

Innovation HUB

Financial regulators in many countries around the world have recognised that, similarly to other industries, without supporting and regulating the market entry of inno-

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vations, they will lag behind in the competition in the field of services, and the accomplishment of country-specific economic aims may also be jeopardised. One element of the regulatory tools supporting innovation is the so-called Innovation Hub. In most cases, the Innovation Hub is an electronic interface that enables direct information exchange between regulators and market players, as well as between market players. There is no generally accepted scheme for the operation of Innovation Hubs, the operating mechanism may vary from country to country, but we can find the identical elements. The Innovation HUB operated by the MNB summarises international best practices, via a web site with an easy-to-use user interface that includes the following features:

– It acts as a repository of information, i.e. it shows the exact legal environment for each development, indicating the relevant MNB expectations. It contains information on how to obtain the various licenses.

– This is the area where the regulatory authority may be asked questions on matters that are not or are not fully regulated in the legislation belonging to the innovation solution.

– It is a Communication Hub, as well as an international collaboration platform where information can be shared between market participants.

In addition to facilitating information flow between actors, the main function of the interface is to request regulatory support to ensure compliance with the legislation. Obviously, the platform can only be operated efficiently under predetermined conditions. The applicant can submit the question using an electronic form that is easy to understand and fill out.

Regulatory Sandbox (Innovation Financial Testing Environment, IPT)

Another element of the modern regulatory toolbox is the provision of the Regulatory Sandbox, which is not a unique tool operated exclusively in Hungary, as this solution is already available in many countries. At the same time, Hungary was the second country in Europe after the United Kingdom to introduce a Regulatory Sandbox operating within a regulated framework in December 2018, and the first in the CEE region.

By Sandbox, we mean a regulated market test environment for financial products and services that enables the provider of the service/product to test innovations within a limited time frame, on a specific customer base, in such a manner that during the test period it is exempted from compliance with the predefined legislative requirements. The purpose of the Innovative Financial Testing Environment is to prevent excessive risk-taking by market players and, if necessary, to adapt the relevant regulatory environment in the light of experience gained during the test period. It was also mentioned in the case of the Innovation Hub that, in order to facilitate efficient operation, the regulatory side defines the admission criteria, whereas the admission criteria for new products/services have also been defined for the IPT:

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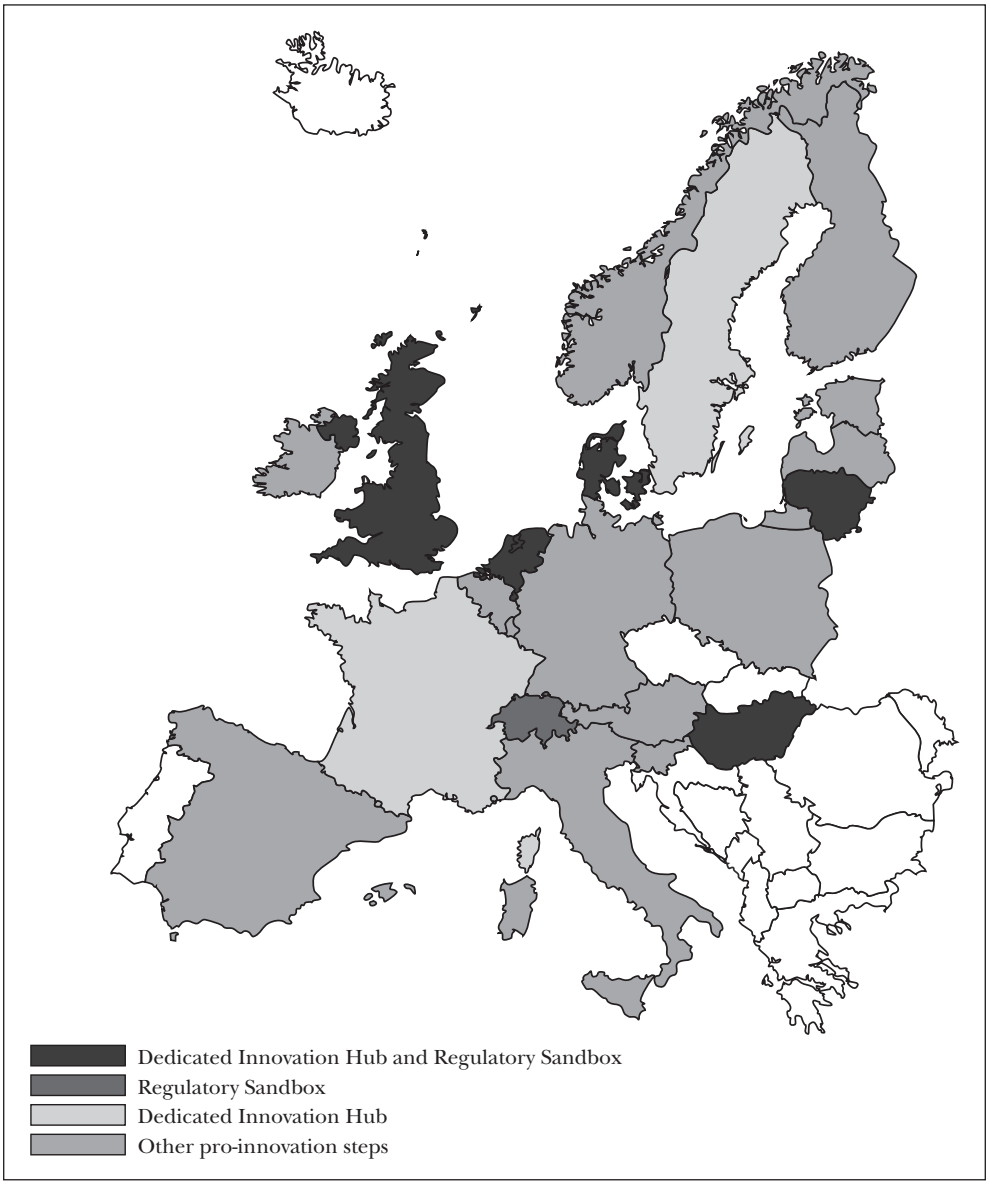
Figure 4: Innovation HUBs and Regulatory Sandboxes in Europe



Source: MNB, EBA[6]

– The product/service must be innovative,

– The product/service needs to be introduced to the Hungarian market after a successful test period,

– The product/service to be tested in the IPT must be ready for testing.

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The regulatory authority consults with the service provider prior to the test period, and will continue to monitor constantly the test results until the end of the test period, following the IPT entry statement.

Testing may have three different outcomes:

– The product/service complies with the current regulatory environment and is therefore fully marketable.

– In relation to the product/service, the relevant MNB decree or decrees are amended and subsequently become available without restriction. Also,

– The service does not comply with the legal environment and the regulations cannot be amended, so the service/product is not allowed to be provided.

The Innovation Hub and Regulatory Sandbox tools allow regulatory authorities in our fast-changing world to shorten the time it takes to bring financial developments to the market, maintaining the security that is essential for the market players – and is of outstanding significance – and to facilitate future supervisory activities, by enabling the competent authorities to know, learn about and understand the nature of innovations in a timely manner, to support their operation by new supervisory methods, and that way all users can use the various financial innovations in a secure context.

Notes

[1] Recommendation no. 12/2018. (II.27.) of the Magyar Nemzeti Bank on the evaluation of real property financing project loans and certain matters of their management.

[2] ILAAP – internal liquidity adequacy assessment process.

[3] ICAAP – internal capital adequacy assessment process.

[4] Recommendation No. 2/2017 of the Magyar Nemzeti Bank (I.12.) On the use of community and public cloud services - repealed with effect from 1 May 2019, see recommendation 4/2019.

[5] Recommendation no. 4/2019. (IV.1.) of the MNB on the use of community and public cloud services.

[6] https://eba.europa.eu/-/esas-publish-joint-report-on-regulatory-sandboxes-and-innovation-hubs.

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Katalin Botos

More than 30 Years of the Hungarian Banking System

Summary
The two-tier banking system was (newly) born in Hungary in 1987. The advent of political changes arrived when the over-indebted country had been left without reserves, and nearly went bankrupt. From such a difficult position a functioning banking system had to be built up after the first free elections held in 1990. During the second term, between 1994 and 1998, most of the Hungarian banks were privatised (after consolidation of the individual banks during the first government with the help of government bonds.) In the third cycle there appeared to be too many banks in the country, and most of them were below the optimum. In the period between 2002 and 2010, banks flourished and created a credit boom based on foreign currency. Following the international financial crisis this led to great troubles. The forint was devaluated against the Swiss franc, and numerous clients became insolvent and lost their homes. The government elected in 2010 made efforts at resolving the situation to help citizens by programmes including several steps. Banks were required to take part in this effort by paying special taxes and for a time this cut back on their profitability. The last three governments since 2010 modified the deconcentrated banking structure and repurchased some of the previously privatised banks. In 2013 the government set the goal of increasing the share of Hungarian-owned banks to above 50%, which was achieved in 2019. The profitability of banks has recovered, and their capital position is now strong. The National Bank of Hungary fulfils the supervisory function. Through its monetary policy, unorthodox measures and credit programmes, it helps the smooth functioning of the sector and thus the financing of Hungarian SME's.

Journal of Economic Literature (JEL) codes: G21, G28, E47
Keywords: banking history, banking structure, privatisation, state banks, crisis management, central bank's policy

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Introduction

The two-tier banking system was born in Hungary in 1987, a few years before the 1989–1990 political change of regime led to a new, democratic society and a market economy. The importance of financial matters became clear very soon. Short-term foreign deposits (which the National Bank of Hungary, MNB recognised as "reserves") left the country in the springof 1990, a few weeks before the final elections. The National Bank did not have a sufficient amount of foreign currency to finance debt service to the country's creditors. The public promise made by the reform politicians of the Hungarian Democratic Forum on television to fulfill debt service if they were elected finally convinced investors to return the money.

Initial years: 1990–1991

All this awakened Hungarians to the importance of the banking system and monetary and finances for the country. Experienced in international banking, Pál Tar, a friend and adviser of Prime Minister József Antall, convinced him to place emphasis on this sector. A Bank Privatisation Committee was established with the task to consolidate the existing system and prepare the privatisation of banks. (Actually, the Committee was not engaged in privatisation, but created the legal framework for the genuinely market-conform functioning of commercial banking in the country.)

The system existing in 1990 comprised the following members: three commercial banks detached from the MNB : the Hungarian Credit Bank (Magyar Hitelbank, MHB), the National Commercial and Credit Bank (Országos Kereskedelmi és Hitelbank, OKHB) and Budapest Bank (BB); completed by the Foreign Trade Bank (Magyar Kereskedelmi Bank, MKB), the General Banking and Trust Ltd. (Általános Értékforgalmi Bank), OTP (the National Savings Bank), the network of smaller saving co-operatives, and a few smaller joint venture banks (Citibank, CIB, Unicbank). Later on, new Hungarian banks (e.g. Ybl Bank, the first private bank after 1990 in Hungarian hands) were also established. At the beginning, the legal regulation of the sector was very poor. The Banking Act was only passed by the Hungarian National Assembly at the end of 1991.

Today it is difficult to imagine how little idea the Hungarian economists and financial specialist of the time had about the functioning of a genuine commercial bank in the 1980's. Very few old experts had still been living who had some practice in banking before the nationalisation of banks in Hungary (Act XXX of 1947). A few employees of the National Bank at the arbitrage department had some understanding of foreign exchange transactions, but 40 years of a monolithic banking system nearly killed all the simple routines which any clerk in an Austrian or French bank had. In the Finance Research Institute young colleagues studied the specialised literature and they became members of the Committee that established the two- tier banking system recommended by Finance Minister István Hetényi. However, there was nowhere to learn the necessary expertise in everyday activity from. Not to mention the methods

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and practices of surveillance and supervision. Board-members who were supposed to fulfil the role of internal control at banks were also people without any specific practical banking knowledge. To be quite honest, it was a surprise for us when similar problems turned out even in the most advanced market economies later on. The investigation after the collapse of the Lehman Brothers made it clear that the external board members *did not have any useful knowledge* on banking business at this big US bank.

In the 1980's the World Bank assisted a due diligence of Hungarian banks. Under severe banking confidentiality, some of the members in the banking supervisory group at the Finance Ministry were actually aware of the amount of non-performing assets held by big Hungarian commercial banks. Everybody was afraid of the public reaction when and if it were disclosed that Hungarian banks wer technically bankrupt.

The causes of the disastrous shortage of capital were rooted in the situation inherited from the socialist economy planning mechanism. The so-called New Economic Mechanism adopted in 1968 was insufficient for either convertibility or the internal capitalisation of enterprises. The firms no longer received sufficient working capital for their activities from the state when they were declared to be autonomous. Only the MNB's credit lines helped bridge the shortage of capital. Firms were burdened by credits. Inadequate capital represented the legacy of the past. And the future was not rosy at all.

Parallel to the capital shortage of Hungarian firms, their export partners' solvency abroad was also a big problem. The buyers of Hungarian industrial and agricultural products were mostly firms in former socialist countries, themselves insolvent as a result of the political changes in their own countries. They could not pay for the exported Hungarian goods, so our firms also became insolvent. This led to the non-performing assets in our banks. Due to budget constraints, the Finance Ministry did not allow to create some reserves for covering the losses, accounting it as cost. So the picture was very gloomy.

At the beginning of 1991, the government commissioned a minister without portfolio responsible for the banking sector, who, with the help of a team of Hungarian experts, drafted a modern banking regulation which was handed in and accepted by the Parliament at the end of the year. This revealed the genuine portfolios of big Hungarian banks. The Banking Supervision established by the Banking Act started to control and survey the activity of the banks. It was not an easy task, because of lack of professional employees, both in the Supervision and in the banks themselves.

The public that time was not concerned with the professional issues of the conducting of banking business but of the privatisation of the banks. This process was not in the competence of the Supervision but in the hands of the Finance Ministry.

In 1991 the Banking Committee consulted a lot of Hungarian and foreign financial experts and the Banking Association representatives about the amount of potential losses, and the methods and forms of the consolidation of the Hungarian banks. The Supervision had completed its task by showing the realistic capital situation of banks. It became clear that the state could not sell them in their current position for any significant amount of money although the budget and the debt situation of the country would have demanded capital income from privatisation, possibly in foreign currency.

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The Finance Ministry therefore worked out different steps for the consolidation of banks' capitalisation. This included *credit-consolidation*, *client-consolidation* and *bank-consolidation*, by removing non-performing loans from banks' portfolios in exchange of long-term government bonds. In the first step a *buyout* was performed, the second one included *raising the capital of state banks* by adding long-term state securities to the initial capital, followed by *writing off* non-performing loans. Client consolidation was a direct help offered by the state to the clients of banks making them capable of debt service.

In the deteriorating situation two main factors played a role: the collapse of Eastern-European markets and the *fundamental ideology of market economy*. Both the ruling and the opposition parties based their policies on belief in the allocating function of the market forces. (In this spirit sometimes Hungary set stricter than necessary rules; for instance in the Bankruptcy Act.) Most experts pressed for privatisation. Liberal economists in the country firmly believed that the quicker state ownership is replaced by private the better. The other dilemma was also decisive: Should we invite strategic or portfolio investors as bank owners? Liberal politicians stressed that only *strategic foreign investors* have the required professionalism at Hungarian banks. (It was deliberately disregarded that the *realised seniorage* through lending and money generation included in the future profit would then also belong to the foreign owners.)

On the other hand, some who advocated "etatist" views did not understand the pressure made by both private and international financial institutions. The latter preferred foreign ownership, in other words, selling the Hungarian capital for foreign exchange to increase the country's reserves. Looking back, it seems a deliberate action to get hold of this profitable sector in transition economies for the benefit of foreign owners. But one has to acknowledge that it happened at the same in every CEE country, partly because of the inherited socialist capital shortage seen everywhere, and partly due to the lack of professional banking knowledge. But the ratio of foreign ownership at banks in Hungary was even higher than in the other countries of the region. (Hungary has always been a "trailblazer" or a "good pupil" during Central and Eastern European transformation.)

The first government after the change of regime would have preferred Hungarian ownership, and if foreign ownership was a must, at best they should be portfolio investors. But this strategy was only successful at OTP, where the management itself had been working according to a strategy for privatisation. It must be added that OTP did not need a large amount of money in consolidation, as it did not perform significant corporate lending activity and thus did not realise considerable losses, and so the sale of its capital was far easier. All the same OTP, too, received consolidation bonds, and they may have used them for technical development to get the necessary improvement in modernisation of the bank. It was actually a hidden assistance to the big Hungarian bank to become competitive.

OTP had a different problem: it had great many housing credits at very low, state-guaranteed interest. This was a big burden, although not for the bank, but for the guarantor, the State Treasury. The problem had been solved by a statute that allowed

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the repayment of loans at a large discount. This offer was accepted by the large majority of the debtors. (The superfluous nature of the formerly granted government-guaranteed loans at low interest rate became obvious: most people actually had the money required to buy their homes, and they simply enjoyed the cheap loans, as money in deposit brought higher interest rates than the repayment of the subsidised loans.) As an interesting fact it is worth mentioning that for those who were unable to repay half of their loans, the interest rate was unilaterally raised five times the original. But the (few) who were aware of the legal proceedings and went to court won the lawsuits against the state. So the consolidation made Hungarian banks "marriageable", that is, ready for sale in the framework of privatisation.

When banks were offerd for sale, the immaterial part of the capital was not taken into consideration in the price. (For instance in 1994, MKB's sales price was 100%, which only included the clientele, and the expertise of the management was not at all included in the price. True, the buyer simply wanted a banking licence.) The sale of Hungarian banks to state-owned or international banks (e.g. the EIB) can hardly be considered genuine privatisation. For example, the Landesbanks of Germany were institutions based on public and not private law. The EIB is an institution based on interstate contract. So why was this considered "privatisation" and how does the market's magical "private" ownership work through them?

Nevertheless, privatisation and bank consolidation are seen as success stories both by Hungarian liberal economists and international experts. To evaluate consolidation, let us quote a Hungarian researcher: "There are more than one answers to the question of whether the final bill for the major state bank rescue programme was too much, at around USD 4 billion or 10% of Hungary's annual GDP. If we consider that this amounted to almost one tenth of the country's annual gross national product, then the burden seems considerable. If, on the other hand, we consider that without the state's rescue plan the banking system would have collapsed, and would have dragged along the entire economy, then we can safely say that the government chose the lesser of two evils" (Várhegyi, 2019, p. 47).

Privatisation: 1994–1997

Bank privatisation only accelerated after 1994 and had nearly been completed by 1997. By the millennium there had been 42 credit institutions, with foreigners holding majority in 33 banks. In addition to commercial banks, there were nearly 200 small Hungarian savings and credit co-operatives with limited licences. Their market share was fairly small up to 2019.

The period between 1994 and 1997 can be characterized by foreign ownership of the Hungarian banking system.

How can the role and importance of foreign ownership in banks be evaluated? In the 2000's one could often read praises of foreign-owned banks, claiming that they defended the country from the effects of the 1998 international emerging-market crisis. But the pros and cons show a different picture.

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As an ECB document reads: "Foreign ownership may have also been one of the important factors that recently helped shelter accession countries' banking and financial sectors from spill-overs from the crises in other emerging markets. However, foreign ownership was not entirely without drawbacks. For example, in many of the foreign-owned banks, trading and other key activities were shifted to the headquarters, so that the subsidiaries in the accession countries lost some of their important functions. Moreover, the stability of the system would now depend largely on the stability of the home institutions as well as the home regulators. It was also pointed out that the presence of foreign-owned banks would in itself not guarantee stability in the banking system, as evidenced by the fact that a relatively high level of non-performing loans had persisted even in foreign-owned banks. Finally, foreign ownership should also not be seen as necessarily perpetual as disinvestment – for example, as a result of a domestic crisis or a change in the commercial strategy of the owner – always remains a possibility, and indeed disinvestment in accession countries by a strategic foreign owner had already occurred" (ECB, 2002, p. 10).

The role of the management is always critical. Sometimes foreign strategic owners did not send the most qualified persons to the banks they had purchased, and changed them too often. Measured by achievement and the economic successes of bank CEO's, it turns out that Hungarian CEO's were often better than the foreign directors.

The system also included a few newly established ("green grass") banks. At around the turn of the millennium, specialized institutions also existed in the Hungarian banking sector. The activities and performance of the state-owned Land Credit and Mortgage Bank and the Hungarian Development Bank were primarily driven by government programmes, which contributed to high growth in their balance sheet total. Nevertheless, the market share of specialised credit institutions was still relatively modest, amounting to only 6% in 2001.

The year 2001 witnessed only minor changes in the ownership structure in the Hungarian banking system. The share of *state ownership* within residents' domestic equity holdings rose at the expense of credit institutions, enterprises and individuals. *Foreign ownership*, in the middle of 1990's decreased to 63%, but it was still very high. Excluding the Hungarian Development Bank, a special-purpose state development institution, and only including commercial banks, foreign ownership amounted to 76% (ECB, 2002).

Bank failures

In the early stages of building the commercial banking system in Hungary in the 1990's, only a very few banks went bankrupt. Such cases (Ybl Bank, West LB, Gyomaendrőd Savings Cooperative) were due to the absence of professionalism, and fraud also played a role. Ybl Bank was established for the purposes of the planned World Expo, which ultimately did not take place in 1992. The debtors could not repay the loans taken for building new hotels and similar investment projects. The

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bank's portfolio deteriorated, and its capital was shrinking. To restore liquidity, the leadership of the bank used *bogus contracts* with various ministries and state institutions to use their temporarily disposable money for buying state bonds. For their "clients", i.e. ministries, it was not allowed to deposit their temporarily disposable money in commercial bank deposits, but it was legal to commission a bank to buy government bonds for them. This was a legal loophole, but only bogus contracts. Ministries should have known that there were no government bonds for sale in the market. But in such contracts there was a paragraph guaranteeing *market interest rates* for the commissioned bank *in any case*. Interest rates were very high because of peaking inflation. It was absolutely flagrant that even the Finance Ministry had been involved in such tricky businesses to get some extra money. They used it to compensate the overburdened staff for overwork. In their defence they claimed that it was very difficult to retain the workforce for the administrative staff in the ministry. Anyone with some financial knowledge went to work for better paying, newly created banks and other financial institutions (Botos, 1996). Bank crashes challenged the central budget, which had already been overstretched. It was clear that the government would not allow major losses in the depositors' money, as that would "go against" the recent political changes. People had no practice in a functioning market economy, and were unable to assess the possible risks at banks. They were grown up in a climate with huge posters on the walls of OTP reading: "Deposits are guaranteed by the state." So bank crashes urged the establishment of a Deposit Insurance Fund, which was anyhow foreseen in the Banking Act of 1991. ("The main responsibility of the Deposit Insurance Fund is to compensate depositors if the Authority has delivered its decision adopted under Section 33(1) of the Credit Institutions Act".) The fee for deposit insurance came from the banking community, so any subsequent problems remained to be solved at the taxpayers' cost.

After 1993, certain amendments were made (e.g. the operative functions of the Investment Insurance Fund were taken over), but since then a bank failure may not cause huge losses to an ordinary depositor. (Small investors are now also protected by the Investment Insurance Fund.)

One of the major bankruptcies in the second half of the 1990s was the *case of Postabank* (SAO, 1999; 2003). The accumulated losses in this bank were so grea that special state intervention was required. The audit performed by the State Audit Office (SAO) after the collapse of Postabank shed light on a lot of moral, regulating and political problems. The supervision and regulation of banks have always been based on the law-abiding behaviour of the market actors. As Gerald Corrigan, director at the New York Fed, once said: if the leadership in a bank wants to mislead the supervision, it can always easily do it (Botos, 1996). This is why the *moral standard* of the management is so iportant. In the case of Postabank, a large number of mistakes were traceable to the management behaviour. (The extremely lenient punishment imposed on the CO of the bank after the trials and the investigation by the State Audit Office were absolutely shocking.) In addition to the bank's management, politicians also played a role in preventing the Supervision's activity when they wanted to performe on-site

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inspection. It was against the law to intervene in the Banking Supervision's activity by any external authority or person, but as the Supervision was dependant on the government, it did not have sufficient power to combat pressure. It may be credited to the leadership of the Supervision that they remained firm during the disclosure of the "ownership structure". The management wanted to conceal the investors of the bank who would strengthen the capital position of the institution. There was a suspicion that the management wanted to help them by using a man of straw, and perform a kind of "baron Munchausen" escape, who pulled himself out of the situation by his own hair. The bank made a lot of similar other tricks, e.g. offering cheap and higher amounts of loans than requested by clients, even to parish clerks, if they deposited the money above the loan amount as subordinated capital. This was to raise *capital from deposits* made by the clients. Many other procedural problems were discovered during the audit. The bail-out cost for the public more than HUF 150 billion (and the CO's legal punishment was only HUF 3 million, absolutely abhorring.)

A change in the legal status of the banking supervision and its incorporation in the National Bank has strengthened its position against everyday political influences.

The 1990's and the following decade was a period of illusions. The firm belief in market economy, the belief that the West would help us adapt to the market challenges, and perhaps reduce our debt in return for the *Paneuropean Picnic* turned into disappointment. Part of the talented liberal economists continued to insist on their belief that the best solution for all our problems was the "marketisation" of all aspects of life and first of all, the economy. The less the state intervention, the better, they claimed. In banking the clearest sign of that ideology was reflected in giving increasing ground to foreign banks in the internal market and in minimising state ownership.

The other scenario: 1998–2002

A more conservative, patriotist economic policy was implemented in the period under the Fidesz government between 1998 and 2002. This government had a scenario that differed from that of liberal economists. Without a complex evaluation of the economic situation of that period, only one aspect, which deserves special attention, is discussed here: *economic development based on domestic factors.*

Although the export-capacity of the country was as important as before, the government also stressed the role of the internal market. A glimpse at the macro-economic data of the time reveals that the country had not reached the pre-transition levels by 1998 in many respects. Only GDP had reached the level of 1990 by 1999, but wages had only in 2002, and pensions in 2004. Thus there was insufficient demand because of the low level of personal incomes. There was only one option to boost internal demand: by offering *subsidies to home-building.* Families were planning new houses and buying new flats. The construction industry flourished. (It is remarkable that this was also the method applied in the US, in the form of low-interest rate lons to support home-building.) The growth-rate was surprisingly high; the export surplus consoli-

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dated the external balance, so the indebtedness of the country decreased in relative terms. No wonder the political leaders were convinced they would be re-elected in 2002. But as mentioned earlier, wages and pensions were still lagging behind, and this explains the lost election of 2002. In their living standards, voters did not feel the government's undeniable macroeconomic achievements.

Repeatied liberal line: 2002–2010

After the conservatives' lost 2002 elections the country returned to the liberal market economists' trajectory.

In the years after 1990, a decreasing concentration was seen in banking. By the end of the nineties, several acquisitions and mergers had taken place and resulted in concentration increase as some saving co-operatives had ceased their operation, had merged or had transformed into banks. Based on a study by McKinsey and Company, in 2005 the market share of the three biggest banks was 43.8% in Hungary, while the HHI for the whole sector was 1007. What concerns the banking industry's ownership structure, state ownership in the banks was below 20%. State banks' share was about 10%

Balázs Zsámboki assess the situation in the pre-accession stage of the banking sector as follows: "With regard to the current level of balance sheet total, there appear to be too many banks, implying that the average size of banks is below the optimum level. However, looking at the density of branches, Hungary is not overbanked, although technological development will certainly make a few branches redundant" (ECB, 2002, p. 113). We may agree with the other statement of Zsámboki that the relation between the level of concentration in the banking sector and its vulnerability in the case of shocks and crises has not been adequately assessed in Hungary so far.

In addition to the structure of the banking sector, growing foreign currency lending created great problems. This has not been given sufficient emphasis in contemporary or current professional supervisors' publications. Few authors draw attention to this dangerous phenomenon, despite the fact that retrospective analyses reveal its importance (Lentner, 2015). As an exception, Botos and Halmosi gave an evaluation on the risk climate in the second half of the 2000's: "Inflationary expectations … will bring further depreciation. It is hard to precisely establish trends, but we may declare that *this will bring great suprises for housholds running up huge foreign currency loans*" (Botos and Halmosi, 2009, p. 109, italicised by the author). The subprime crisis came as a surprise and also hit Hungarian banking, despite the fact that Hungarian banks were not involved in the so called toxic assets business. But lending in foreign currency and the coming overvaluation of the Swiss frank made this type of business very costly, concerning redemption for the clients of banks. Many were unable to repay their debts. This raised the portfolios of non-performing loans at banks. But the problem which was emerging in the society was even greater. Citizens who thought that they had found a cheap financing for their housing were divested from their home ownerships

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and fallen into deep poverty. Discontent was growing and the banks were blamed along with the government.

Why did such a very quick growth in lending based on foreign currency happen?

As was mentioned before, the first Orbán government supported housing from the budget. Families with children intending to buy flats or houses, were given subsidies. This idea matched the policy of the incumbent political party, namely that they intended to base the society on *families* instead of the full individualism. (The government intended not only to stimulate growth, but also parenting, as the birth rate was extremely low in Hungary. Population decline has been threatening the country.) But after 2002 the liberal government terminated this type of budget subsidy. Those who wanted a new flat had no access to anything else than bank loans. It came in handy to offer low interest rateloans from abroad to Hungarian banks, so they started lending based on Swiss francs. This did not mean that the debtor actually received Swiss francs, only the lending transaction was based on Swiss franc credit lines taken by the banks (Lentner, 2015). That way they realized an extra margin and an extra profit. Profitability of the banking sector was soaring.

But the country's macro-economic situation deteriorated year by year in this period. In relative terms, state indebtedness strated to rise again to the pre-1990 levels, and deficits were high. Vulnerability to external financing was intensive. Despite all of that, the banking sector had flourished up to the eruption of the crisis. Due to international financial problems, the country had to turn to the IMF again to be able to fulfil its obligations to the rest of the world. (The first Orbán Government terminated the contract.) People's living standard failed to improve and housing problems were challenging. This is why 2010 brought changes in the political leadership of the country.

After 2010

After the eruption of the crisis relate to the Swiss franc started to revaluate and the Hungarian forint was devaluated. The loans denominated in Swiss franc became very costly, and nevertheless, Swiss franc loans expanded even in the couple of months after the outbreak of the lending crisis. Only the elections brought radical stop.

The new government very soon banned forex-based lending, and the IMF-contract, introduced extra taxes on banks, starting to consolidate the government's unsound budget. The banking tax was under heavy criticism by liberal economists inside and outside the country. (While nobody criticised the *unhealthy lending activity* of foreign-owned banks in Hungary.)

The government decided to consolidate the banking sector, eliminate the too much banks, create a healthy concentration in the savings co-operate sector, raise a bit – maybe only for temporarily – the share of the state-owned banks.

The government set a goal in 2013 to raise the share of Hungarian-owned banks above 50%. Some foreign banks left the country, as a consequence of deteriorating profitability (caused by bank taxes) and Hungarian-controlled (or owned) banks gained ground.

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Table 1: Foreign and government ownership, 1995–2013

	Foreign-owned banks					State-owned banks			
Hungary	1995	1999–2001	2008	2010	2012–2013	1995	1999–2001	2008	2010
	22%	75%	85%	83%	59%	61%	6%	3%	4%

Source: Cull et al., 2017

In 2012, MFB was ordered by the state to buy out the stake of Germany's DZ Bank in the umbrella bank of the savings co-operatives, so that it could act as an "integrator" of saving co-operatives. The government intended to unite savings co-operatives into a "commercial bank" with a nationwide network (which was actually performed in 2019).

In 2014 the state purchased MKB Bank from its Bavarian owner. In 2015, Budapest Bank was also bought by state-owned MFB on behalf of the Hungarian government from its American owner GE (which was planning its further privatisation).

The state agreed with the owners of Erste Bank to purchase a stake in the bank, through the Corvinus Investment Zrt., parallel with EBRD (each having a 15% share). The government promised by an aggreeement with the EBRD to stop introducing unfavorable measures against banking activity in Hungary. Based on the balance sheets share of the banks under Hungarian management, *the ratio was raised in seven years* from 13.55 to 55.7%. So the government has achieved the aim to bring the share of Hungarian-owned banks above 50%.

Some critics were recently published against the banks having Hungarian owners (and management), that they are under controll of economic forces close to the government. "From the perspective of the future stability of the banking system, two crucial questions arise: first, whether the newly nationalised credit institutions have sufficiently well-capitalised owners to stand firm should the need arise; and second, what is the impact on prudent bank operations of close interlocking with the centre of political power, and how much has the moral hazard been exacerbated" (Várhegyi, 2019, p. 59). It looks as if the concerns were exaggerated.

The most recent developments

Let us summarize the situation in the Hungarian banking sector based on the report made for the European Banking Federation: "The Hungarian banking sector consists of 69 institutions. Among them are 26 commercial banks, nine foreign bank branches, five mortgage banks, four building societies, three specialized banks and –as a result of massive consolidation – 22 credit or saving cooperatives. At the end of 2017, 50.5% of the banking sector's shareholding was kept by domestic entities with almost two-thirds of that in the hands of the state.The banking sector has 2,420 branches and employs around 39,000 people (0.88% of the total employment in Hungary). For the country's population of 9.8 million in 2017, there are 10.5 million bank

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accounts, 9.1 million payment cards (of which 72% are contactless), 5,100 ATMs and 136,400 POS terminals. Electronic payments increased dynamically in 2017. The payment card accepting network grew significantly by 25% which also means that 83% of the POS terminals support contactless card acceptance. In 2017, two-thirds of retail payments were made by contactless cards. The rate of access to payment accounts by internet and mobile banking services increased by 2.5% which means that 82% of the payment accounts can be accessed by one of them. The National Bank of Hungary has launched a project to implement a domestic (denominated in HUF) instant payment (IP) solution. The new payment system will be available to make payments between Hungarian payment accounts within seconds, on a 24/7/365 basis. It will also be possible for market participants to provide a range of additional services. The IP service will start on 1 July 2019. The new basic infrastructure supports innovative payment services. One-third of the banking sector's total loan portfolio is provided to non-financial corporates, one-third to households and organisations closely linked to households and one-sixth to the foreign sector (half of it to foreign corporate sector). In 2017, corporate lending grew at a rate unseen since the crisis, expanding by more than 13% in annual terms, while retail lending almost stagnated with an increase slightly over 1%.The deposit value of the banking sector remarkably increased in 2017 (by 7.7%) in total, each major sector (local state, corporate and household as well as foreign) contributed positively.The capital position of the Hungarian banking sector is stable. The Tier 1 capital adequacy ratio (CAR) is over 18%, while the total CAR is a bit over 20%. In 2017 profits reached a new high in nominal terms, mainly due to extraordinary or external factors, before tax ROE remained over 14.5%. Major extra contributors to the unexpectedly good performances are the good profitability of local banks' foreign affiliates and releasing impairments. The banking sector has a relatively high contribution to the central budget in Hungary. It provides almost 4% of the total budget revenue (approximately 1.5% of the GDP), half of it coming from sectorial taxes" (Vass, 2018).

The above long list shows that the Hungarian banking sector is for today in a well-balanced situation, concerning forein and Hungarian ownership. Banks work profitably, have strong capital base. Hopefully the sector will help further on the smoose financing the development in our country. The latest data on the activity of the Hungarian banking sector are also promising. The most important is how leding was developing.

We may outline the situation based on the latest Inflation Report by the National Bank of Hungary (MNB, 2019).

In 2019 parallel with output and investment, the outstanding loans of the private sector exhibited a remarkable expansion during the year – just as we have seen in 2017 – both in historical and international comparison. There was a rapid growth to be seen on the demand side, both in corporate and household lending. The supply side was characterised by loosening of credit conditions and price competition. This credit expansion was really unprecedented since the crisis already in the preceding year, but it strengthened in 2019 further on.

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The MNB overviewed the structure of changes in loan portfolios. Over the past 12 months, the outstanding loans of non-financial corporations vis-a-vis the Hungarian financial intermediary system have increased rapidly, by almost 17 percent. By international comparison, this is remarkable. Credit expansion primarily occurred in longer term loans, with had a maturity of over 1 year. They gave more than two thirds of the growth in the credit volume. And the majority of the credit-growth (2/3) was offered in HUF. This is favourable from a stability standpoint...

Last year's contribution of gross fixed capital formation to GDP growth was considerably higher in Hungary than in the other Visegrád countries. Business cycles and corporate lending in the Visegrád countries have typically been in sync in the past decades. This is explained by the fact that there must be country-specific factors behind the extremely rapid increase in lending seen in Hungary at present compared to other countries of the region.

Growth in corporate credit is broad-based in all sectors of the economy. Loans for the manufacturing sector has shown the largest increase. Expansion in landing in the manufacturing happened first of all by the borrowing of several international corporations in Hungary, linked to their Hungarian projects. The second sector included the firms providing financial and insurance services. The credit demand of the agricultural sector was also supported by the supplementary financing of EU transfers. The robust activity in construction and the real estate sector raised the credit portfolio of these sectors too, but a lesser degree. This was the consequence of the investment activity of *real estate funds*. Developments in the CRE market also affect the functioning of the financial system. This is primarily due to the fact that most banks' corporate loan portfolios are CRE-collateralised loans, accounting for almost 40 per cent of the portfolios in Hungary in 2018. The Hungarian corporate sector's low aggregate indebtedness provides further room for rapid credit expansion.

In the household sector the portfolio had not increased until 2017, as repayments consistently exceeded disbursements. This is because these loans were annuity loans: as the maturity of loans disbursed before the crisis progresses – accounting for a substantial proportion of existing debt – the share of principal repayments grow progressively in the monthly instalments paid by debtors. From mid-2017, however, the new credit outflows already exceed the repayments of existing contracts, and the outstanding borrowing of households began to grow. It should be emphasised that lending tends to exert its impact primarily in household investment rather than consumption.

The current growth is driven by the double-digit increase in new housing and personal loans. In addition to the low interest environment, demand is supported by the family policy programmes of the government, such as the Family Housing Allowance (CSOK) available since 2016 – and the extension thereof – and the Prenatal Baby Support available since July 2019. The number of home purchases from credit increased over the past few years, although still less than one half of all home purchases are financed with credit. However, not only housing loans, but also personal loans can finance housing investment, despite the fact that the cost associated with personal loans is still three times higher than that of mortgage loans. But fast loan assessment

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and disbursement encourage households to take out personal loans for lower-value housing purposes as well. The nearly 7% expansion in household lending is driven by demand: supply conditions have not eased significantly since the crisis.

The over-indebtedness is controlled by the *debt cap rules* introduced in 2015 which have been recalibrated several times since. This prevents excessive indebtedness.

Due to the relatively high share of variable-rate loans, debtors in both the household and the corporate sector are sensitive to interest rate fluctuations. The consumer credits-takers are often not aware enough of the risk. The MNB issued therefore a recommendation to financial institutions, trying to suggest them to convince the most affected customers who have variable-rate mortgage loans, to change a transition to a fixed-rate scheme with an amendment to the already existing contract.

On the whole, thanks to the favourable financing environment and buoyant investment demand, rapid expansion may be expected to continue both in the corporate and in the household sector in Hungary in the coming period.

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Audit Experiences of State-Owned Business Organisations in Service of the State Management Approach

Summary
Business associations in government ownership attend to significant public duties. Their activities, the quality, efficiency and fruitfulness of their business management have a considerable impact on the quality of life, security, health and welfare of the population using their services and contribute to the responsible management of public funds. In other words, the reasonable, compliant and effective operation of businesses operating in public interest is one of the most important social objectives. The State Audit Office's contribution includes its audits, analyses, studies, consultancy to management systems, performed on the basis of the Hungarian National Assembly's authorisation given in a resolution, and its support to training executives in the field of public finances. The article presents their valuegenerating utilisation.

Journal of Economic Literature (JEL) codes: H83, E01, G38, H30, M1
Keywords: business association, public duty, State Audit Office of Hungary, national asset, ethical management system

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Significance of the topic

The Fundamental Law, which entered into force on 1 January 2012, is the basis of Hungary's legal system and the highest-standard precept in Hungary. The provisions of the Fundamental Law should be understood in agreement with the National Avowal included in it, and with the achievements of our historical constitution. The Fundamental Law ensures special protection for public funds and national assets, and provides guarantees for their prudent and transparent management. The Fundamental Law identifies the assets held by the Hungarian state and the local governments as national property, and establishes the purpose of its management accordingly. Thus, national assets may not be managed in private interests but must serve the benefits of the community, with special consideration for the need to protect natural resources, due to their being exhaustible, and to the fact that national assets must remain available in an amount sufficient to meet the needs of future generations.

National property also includes economic stakeholder organisations that are owned by the state and must be managed under the Fundamental Law according to requirements nearly identical to those applicable to the implementation of the central budget, although they are given greater independence than budgetary organisations. It is primordial that only well, efficiently and effectively managed state-owned business organisations serve public interest. The assets they managed constitute public property, and the standard, efficiency and performance of their activity and management contribute to responsible public funds management.

As Parliament only has limited powers to directly control the business management performed by the executive power, the Fundamental Law identifies the State Audit Office as an independent institution that attends to this task. The State Audit Office is authorised to fully supervise the use and utilisation of all public funds and national assets. Thus the State Audit Office is the supreme guard of public funds. It helps the creation of a well-governed state by its audits, by sharing its audit experiences and by analyses and evaluations of the latter. This institution holds up a mirror, presents mistakes, the international trends and the directions of moving forward.

In Hungary public duties are performed, on the one hand, by budgetary institutions founded and operated by the state. On the other hand, organisations falling outside the scope of public finances may also contribute to the – according to rules determined by law – performance of public duties and the state provides part or whole of the funds required for the performance of such duties (Lentner, 2017, pp. 75–90). In addition to institutions, business organisations operating outside the scope of public finances increasingly participate in the performance of duties. Approximately 300 business organisations in the majority ownership of the state operate in Hungary (disregarding their subsidiaries), and a significant number of them perform public duties and manage public assets. The scope of public duties concerned is extremely wide. They include water utility companies, primarily engaged in water supply, wastewater treatment and sewage disposal through utilities. This also includes forestry holdings, which manage forests in government ownership, companies attending to healthcare

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and welfare duties, like spas, old-age homes, and companies in charge of social and cultural duties, among others, education and heritage protection. The government portfolio also contains state-owned companies conducting research and undertaking infrastructure development duties, such as corporations engaged in the operation of public roads and real properties and providing ancillary services. Clearly, state-owned companies and the goods produced and services provided by them affect the living standards, security, health and welfare of the population.

Audit findings

State-owned companies have a significant role in safeguarding and increasing property in state ownership, as the value of the assets they manage is high, a great deal of freedom is left for the companies in management, as they are allowed to make the daily decisions related to assets. With a view to all this, the State Audit Office regularly audits the management activities performed by business organisations in state ownership. During the audits of 221 state-owned companies conducted between 2011 and 2018, the SAO obtained a wealth of experience in relation to company management and governance, in other words, to state management. Based on audit experiences, critical areas could be identified that were inseparable from the responsibilities of the management and of those who exercise ownership and supervisory rights (SAO, 2018).

SAO's audits are aimed primarily at the creation of the conditions for performing public duties and at the assessment of financial and asset management. SAO primarily audited and assessed the financial situation, asset management, the configuration of internal control systems, and compliance with the relevant regulations in areas constituting integral parts of the former. The audits also included the assessment of certain areas in leadership performance.

In the case of state-owned business organisations, the exercise of ownership rights means the exercise of rights and obligations of the owner. The ownership rights of state-owned companies – and the state's share – are fundamentally exercised by Magyar Nemzeti Vagyonkezelő Zrt. (Hungarian National Asset Management Inc) or, in certain cases, other legal entities appointed by law.

Exercise of ownership rights

The relevant statutory regulations require the organisations exercising ownership right on behalf of the state to enforce the corporate management's responsibility and asset management that guarantees the enforcement of public interest. The audits have revealed that the party exercising ownership rights, the supervisory board and the management primarily endeavour to accomplish the obligations required by law, and they make less effort at adding proactive means of governance to their activity to supplement the mandatory requirements set out in statutes. According to the audit findings, ownership rights were exercised basically in compliance with the law. The

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parties exercising ownership rights determined the system of corporate decisions and the duties of the company management in the deed of foundation. The established supervisory boards reinforced the owners' supervision of these companies. Experience shows that the exercise of ownership rights was focused on the approval of company reports and paid less attention to strategic planning and development.

Based on SAO's audit experiences, in the case of companies, the management's responsibility has remained largely unenforced or merely formal. The party exercising ownership rights approved the business plans, reports and accounts, but failed to evaluate and review them.

The current regulatory environment does not specify criteria for performance in asset management, fails to provide considerations for the efficient use of state property in accordance with its intended purpose and for accountability. The parties exercising ownership rights are not obliged by law to set performance objectives and measurable criteria for these companies in order to gauge operation and management, or to set up a monitoring system. For this reason, they do not define any performance objectives or criteria for these companies, and thus performance gauging is not ensured for these companies, in other words, it is unmeasurable whether public funds and public assets have been used efficiently and economically, and the managers' performance cannot be assessed. In the absence of defined efficiency criteria, the stakeholder can only be held accountable for the lawfulness of spending public funds. As the statutes merely set frameworks, the company manager is fundamentally at liberty to fill the framework with content and to decide whether to enforce efficiency and economic viability criteria in the management of assets. All these justify the need to set requirements.

As a significant number of these companies attend to public duties or public benefit duties, lawful and efficient business management on a going concern basis is important. The audit experiences show that these companies have contracts for the performance of public duties, and the contracts have generally been drafted in agreement with the relevant statutory requirements, but in most cases they had not been updated to reflect recent statutory changes.

The party exercising ownership rights is required by law to regularly review such contracts, but the type of review is not specified and the term "regularly" is not defined either. When the ownership right of the assets is exercised, the party exercising ownership rights is required to verify the presence of the assets, their lawful handling, replacement and use for the intended purpose. When the ownership title to shares is exercised, the owner reviews the company's operation and business management, the achievement of the objectives and the lawful performance of duties. The beneficiaries exercised ownership rights by reviewing the information retrieved and the data reported. They rarely exercised their right to check asset management, the retention, increase and use of assets on the site.

Change in the owner's person took place in several audited companies, some within a year, and in some companies several organisations exercised the ownership rights simultaneously in respect of the individual assets of the company. In such cases the

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risk may be run that the expectations of multiple parties exercising ownership rights might be divergent or that the principle of responsible asset management is difficult to enforce if at all. The audit experiences show that the duties of the parties exercising ownership rights of assets and shares are not clear for either the party exercising such rights or for the companies, and they are frequently blurred or confused.

It may also be a problem that the party obliged to perform public duties is frequently the same person as the party exercising ownership rights. In such cases the principles set out in the relevant statutes to govern the duties related to the exercise of ownership rights and competences cannot prevail. The management procedure of exercising ownership rights should reasonably be separated from technical management. It is also important to precisely define, through the application of modern process management principles and methods (internal control system), the owner's duties and competences, and in relation to this, also the functions supporting the individual areas in technical management. In the case of parties exercising ownership rights of several business organisations at a time, the elaboration of portfolio management may be a reasonable solution.

Assets may only be managed after the asset management right has been granted. The right to asset management may be conferred by contract or, exceptionally, by statutory appointment. With a few exceptions, including the ban on alienation, encumbrance and provision as collateral, the asset manager is entitled to the owner's rights and subject to the owner's obligations. The asset management contracts were frequently found to fail to meet the statutory requirements, as they did not specify the volume and/or value of the managed assets or these had not been up-to-date, and this jeopardised the retention and the maintenance of accurate records of the assets. Due to the absence of tracking changes in statutory regulations, these contracts failed to ensure the conditions of lawful asset management. This suggests the party exercising ownership rights is not on the top of things and thus these companies enjoy extremely generous autonomy.

Management

The company audits revealed that the rules of accounting were established deficiently, on the one hand, and the regulations were not updated simultaneously with statutory changes, on the other. Moreover, we even came across a company that had no accounting regulation at all. A regulatory environment and the development of controls are fundamental prerequisites of lawful and efficient management.

In order to preserve the value of national assets, the audited companies implemented capital investment projects and conducted maintenance to increase asset life. These were financed partly from the sum of costs included in service charges and depreciation. The companies raised the remaining financing requirement from external resources (e.g. aids and loans). In general, the companies made efforts at maintaining the value and condition of the assets, however, the inspections of capital investment projects and renovations revealed deficiencies in public procurement

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procedures. In several cases, for the public procurement procedure the companies required the conclusion of contracts exceeding the statutory limit or conducted these procedures in conflict with the relevant regulations.

During the audit of business organisations in (full or partial) state ownership, the absence of correct inventories and failure to use inventories as supporting evidence for balance-sheet items were common. For this reason, neither the principle of giving a true and fair view, nor the protection and safeguarding of property were enforced. In the accounting records, separation was frequently not performed in financial flows (e.g. the absence of reconciliation with aids per financial envelope, the separate financial clearing and monitoring of the individual activities), and as a result, accountability and transparency were not guaranteed.

In order to eliminate the irregularities and deficiencies revealed during its audits and to promote transparent and efficient operation, SAO makes recommendations and in response, the executives of the audited organisations are required to compile action plans. The obligation to act and its supervision by SAO are powerful guarantees for the inclusion of SAO's recommendations into the practice of the audited organisation, thus eliminating the irregularities, deficiencies and inappropriate practices revealed. SAO also verifies the implementation of the recommended actions and of the action plan in the framework of follow-up audits (Domokos, 2014). On average, SAO made 4 or 5 recommendations for a business organisation, to the No. 1 executive of the organisation. The recommendations typically addressed gaps in the internal control, the absence of supporting evidences to the accounting records, or to failure to meet the obligation to publish, and the audited organisations complied with their obligation to make action plans. Thus with its recommendations made to the stakeholders on the basis of its audit experiences, SAO is directing the managers of state-owned companies towards compliant and appropriate operation, which is also the basis of efficient and successful business management.

Consultancy and support by the State Audit Office

In addition to its primary control activity, the law also authorises the State Audit Office to perform a kind of consultancy and deliver its opinion. In addition to audits, the aim is partly to improve transparency and efficiency in the systemic use of public funds with the help of SAO's analyses and studies, and to contribute to the more efficient running of the institutions and systems that provide public services. Another aim is to trigger favourable changes by its audits and analyses in order to improve the citizens' standard of living through the improvement of the public services they use.

Giving an evaluation of its experiences gained from the audit of state-owned business organisations from this perspective, in the framework of its analysis disclosed in July 2018, SAO overviewed the provision of conditions for the performance of duties by state-owned business organisations and the characteristic features of the exercise of ownership rights; and evaluated the operating and management risks run by the companies in terms of the sustainability of operation (profitability, indebtedness and

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liquidity). The analysis also evaluated the requirements and considerations of integrity (which means value-driven conduct/operation, see below), capitalising on the findings of surveys and analyses performed by the audit office in this field.

The State Audit Office shares the trends and recognised good practices revealed during its audits with the interested stakeholders and with the wider public. In order to promote knowledge sharing, it publishes analyses and organises conferences. Sharing "good practices" promotes improvement in the regulation of the operation of the audited companies and development in public finances. In addition, to companies potentially subject to audit, it provides support in compliant operation despite being unaffected by recent SAO audits. Capitalising on its audit experiences, SAO supports the lawful operation of organisations using public funds by the elaboration, publication and annual updating of self-tests. In relation to its support and consulting functions, SAO launched its self-tests in November 2014. The completion of these self-tests is voluntary. With the help of these self-tests, in addition to the audited organisations, unaudited ones also have the opportunity to size up their current situation, adopt "good practices" and improve the regulation and lawfulness of operation.

SAO's experts share their experiences and the "good practices" they have collected at expert and executive conferences, professional lectures and forums in order to provide communication opportunities for companies potentially subject to audit in the interest of more compliant operation.

Pursuant to the act on the State Audit Office, SAO uses its findings, recommendations and advice based on its audit experiences to help the work of Parliament, its committees and the audited organisations in order to promote the operation of a well governed state. SAO also assists legislation at the three topmost levels of the legislative hierarchy, namely, in the adoption of acts by Parliament, decrees by the government and orders by local governments. The State Audit Office endeavours to transfer its audit experiences to legislators for incorporating them into new statutory regulations. Naturally, SAO does not wish to take over the duties and responsibilities of legislators, however, it is supposed to call the attention to risky and poorly regulated or unregulated areas it considers reasonable to address by legislation. Coherent regulation of an appropriate standard and free of legal loopholes is especially important for SAO because in the absence of an applicable rule or in the case of deficient regulation, the organisations cannot be held accountable during compliance audits, even if irresponsible public fund management provides ground for calling them to account.

SAO also supports legislative procedures indirectly. For example, it dispatches its reports and analyses to Members of Parliament, government members and the parties exercising ownership rights over the audited companies. Moreover, by sharing its audit experiences in a way that raises public awareness, it also urges legislators to remedy the deficiencies revealed and any incorrect practices by statutes, if required.

In a resolution, the Hungarian National Assembly authorised the State Audit Office to expand its consultancy on management systems and to support training in ethical public finance management. In order to accomplish this task, the State Audit Office has established a joint department with the University of Miskolc for doing research

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in and for teaching performance measurement in the public sector. In the framework of this cooperation, educational programmes and modules were elaborated for training the current and the next generation of heads of business organisations managing public funds and public assets, with focus on performance assessment, measurement of the value of public services, monitoring, controlling and human resources management, the integrity approach and the dissemination of methods and instruments supporting the reinforcement of integrity controls used in the course of management.

Promoting competitiveness

The intersection between the state's exercise of its ownership right and SAO's efforts is assessing and making public service companies' performance measurable based on unbiased indicators. SAO's baseline is that the avoidance of loss making is a basic requirement in the public sector; however, as profitability is an inaccurate standard for efficiency, it can only be assessed in the light of the set objectives. However, if there are no quantified targets, efficiency is unmeasurable. Experiences show that the use of measurable performance indicators is extremely rare in the public sector, and what is more, numerous organisations do not set performance target either. SAO has taken steps to improve the measurability of public service performances. In cooperation with the Faculty of Economics of the University of Miskolc, it has been working on the elaboration of a model and a measuring system based on the model that enables the setting of 5 to 10 indicators to properly express public service organisations' performance.

The baseline of the model is the competitiveness of public service organisations. The purpose of the model is to identify interventions that improve competitiveness. In this model, performance measurement is not is not an end in itself, rather, it is a means for assessing competitiveness, and a feedback required for successful intervention, which helps identifying the required intervention, the extent of intervention and then the effects of an intervention. A model has been elaborated for the competitiveness of public service provider organisations on the basis of principles laid down during previous research conducted on performance management by the Faculty of Economics of the University of Miskolc. The elaborated model is depicted in Chart 1.

In this model, the outcome, i.e. the socially relevant impact, is considered as a result, and the partial results required to achieve the output (in terms of both the quantity and the quality of service output) and the conditions that need to be created in operation and in the quantity and quality of input to achieve the desired level of output are analysed. In order to determine the competitiveness of public service organisations, the input, operating, output and outcome indicators need to be assigned depending on the organisation/sector. It is important that the indicators should be relevant, quantifiable and measurable. The four pillars are quantifiable based on the public service organisations' data (micro-monitor). The data are, on the one hand, accessible from the data provided by the organisations for statistical purposes, and on the other, quantifiable through surveys by questionnaires. The

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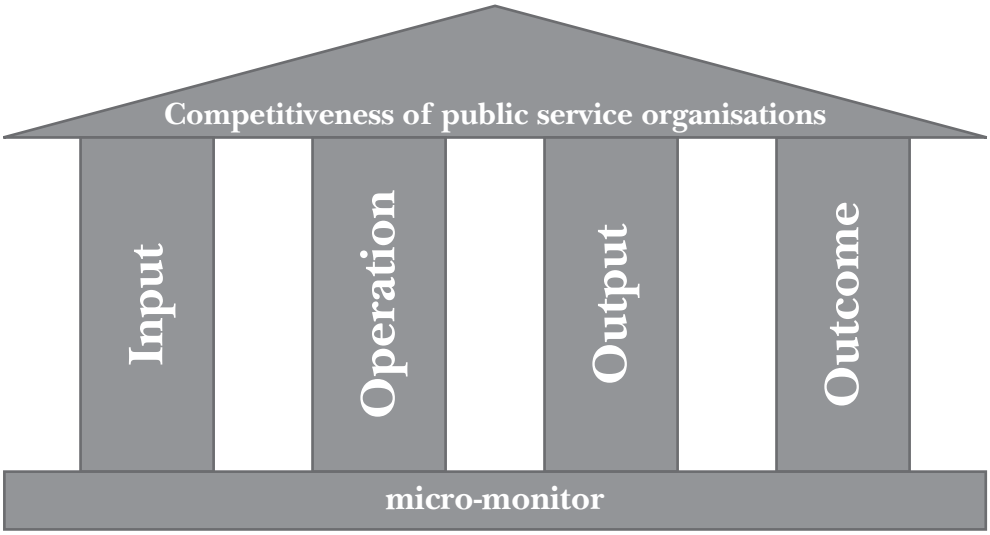
Chart 1: Competitiveness assessment model



Source: Edited by the author on the basis of a model elaborated by SAO and the University of Miskolc

required questionnaire, including all four pillar modules, have been elaborated by the researchers of the University of Miskolc, the small-group tests have been conducted, and the preparation of testing in a wider circle – with the involvement of the State Audit Office – is in progress. The outcome of the measurement enables positioning, temporal and sectoral comparisons and ranking. The retention of or improvement in the position achieved in the given ranking poses a challenge for the organisation's management, and provides a tool for the party exercising ownership rights to assess executive performance on the basis of objective performance indicators. In addition, the indicator is also suitable for predicting the time when the owner needs to intervene.

The purpose of cooperation between SAO and the University of Miskolc is to support a "well-governed state", to train public and civil servants who manage public funds efficiently and transparently, and thus to contribute to the development of state management. In order to spread "good practices", SAO regularly organises series of events to share knowledge, and promotes training ethical public finance managers. Through improving knowledge in public finances and management, the purpose of training top managers is to contribute to the implementation of common objectives and to promote the operation of the well-governed state. SAO and the University of Miskolc also closely cooperate in this topic. The joint endeavour of the two institutions is to lay the scientific foundations of a management training that combines ethical executive behaviour and the measurement and evaluation of managerial performances in both theory and practice. As in addition to professional expertise, the heads of public sector institutions should also be well-versed in management, they need to continuously improve in order to be able to meet the increasingly complex

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expectations towards them. SAO's management training programme offers help in this. Within this framework, the course on good practices is complemented by a 1.5-day training module and by a 5-week remote learning programme.

SAO's contribution to reinforcing the state management approach

In order to improve the efficiency and effectiveness of state-owned business organisations, and ultimately their public recognition, a coordinated cooperation is needed between the owners, owners' representatives and public service organisations attending to the management of state-owned companies. Thus the functions of the individual roles, such as setting and achieving strategic objectives and the verification of their implementation, should constitute a system of incentives to ensure the retention of an increase in public assets and the responsible and frugal use of public funds, in addition to the provision of (public) services and the manufacture of products, both high-standard and sustainably affordable, to the satisfaction of all.

Based on the fundamental and recurrent problems identified during the audit of state-owned business organisations, the State Audit Office has recognised the need for a systemic renewal of state management. SAO has compiled a 4-point recommendation package to renew state management, which required that

– The work done by the managers of state-owned companies should be regularly evaluated for lawfulness, efficiency, efficacy and economy;

– The efficacy, evaluation capacity and activity of the party exercising ownership rights should be improved;

– The managers of state-owned companies should meet strict ethical and integrity requirements;

– The system of remuneration for company managers must be transformed.

The decision adopted by the Government of Hungary in September 2015 about the transformation of the procedure of appointing managers at the head of companies in majority state ownership is of special significance in the application of SAO's recommendations regarding the renewal of state management. It established that the executives' remuneration and requirements need to converge to the market leading salaries and requirements, and a considerable part of the current bonuses should be included in the basic salary. No additional benefit was recommended for the managers of loss-making state-owned companies. The decision underlines that the Government is committed to the creation of the conditions of a transparent, efficient and economical operation of companies in majority state ownership, and – at the proposal of the President of the State Audit Office – it is also committed to the regular evaluation of the activities performed by the managers of business organisations in majority state ownership for lawfulness, efficiency and economy. The decision points out that the managers of state-owned companies must meet strict ethical and integrity requirements.

SAO annually surveys the corruption risks of public sector organisations and suitable controls established by these organisations to prevent or mitigate such risks. Based on these experiences, in 2017 SAO launched a survey of the integrity of business or-

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ganisations in majority state ownership. The findings of the integrity survey have confirmed that corruption risks basically depend on objective factors. They are affected by company size, the provision of public services and the amount of public funds used. In contrast, the firmness of the integrity controls put in place to prevent these risks primarily depends on subjective factors, namely, on the owner and management of the business organisation. Based on the survey findings, the party exercising ownership rights can best improve organisational integrity through the effective operation of a supervisory committee. The most the management can do for the improvement of integrity is the creation of a high-standard internal control. The business organisations of the highest integrity, which were found to endeavour to "improve", analysed and managed risks, including corruption risks, at a system level (Pulay and Lucza, 2018).

In the course of SAO's audits, in addition to the financial situation, asset management and the internal control system, in the framework of a separate module, the performance of the leaders of state-owned business organisations was also checked and evaluated. In addition to the criteria of compliance with the statutory and internal regulations, the evaluation is based on questions supporting the State Audit Office's advisory activity, excluding the evaluation of the performance of basic professional and public duties. SAO's evaluation of management performance was aimed at facilitating improvement in management activity, organisational integrity and the achievement of organisational objectives, and through this, at promoting responsible public fund and public asset management.

Based on the experiences of audits performed in four years, SAO published a series of studies related to the strategic objective of the well-governed state, and including a study about the State Audit Office's contribution to the renewal of state management, published in 2016 (Domokos et al., 2016). Relying on the assumptions of the study, below is a discussion of the areas considered most important on the basis of SAO's audit experiences.

– Companies can be efficiently and successfully manged if its activity is focused on the achievement of the objectives and the mission set for the organisations. This is why it is reasonable for *the party exercising ownership rights to set strategic objectives for each of its companies*. Once the objectives have been set and the mission of the organisation is clear, an action like cost-cutting coupled with quality-related goals will have an effect towards the provision of high-quality services or the sustainability of product manufacturing.

– The fundamental objective is the same for state-owned and private property: to retain and increase assets. The theoretical difference lies in the fact that the beneficial owners of publicly owned companies are citizens, and consequently, *the party exercising ownership rights should represent public interest*. Consequently, the party exercising ownership rights should set clear performance requirements for the management operating the company and for the supervisory committee. SAO's management performance assessments provide some guidance on this, as they mark the areas critical in public finances, where management activity can be improved. The management performance assessment system contributes to the renewal of public administration

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and to the achievement of the strategic objective of creating an efficient national public administration, as set out in Article XXVI of the Fundamental Law.

– Goal-setting only makes sense if it is backed up by accountability. Calling someone to account requires a thorough understanding of its performance. To this end, the party exercising ownership rights should be well-informed and should make a proactive contribution. *The performance of the management and of the supervisory committee,* beyond the expected lawful operation, *should be evaluated time and again, comparing the set performance objectives with the results achieved.* This is the way to successfully, economically and efficiently achieve the objectives set. The owner should set the evaluation criteria in advance and should perform assessment on this basis. The evaluation should feed back to the operation, remuneration and mandate of the management and of the supervisory committee.

– The managers of state-owned business organisations must perform their activity in service of the public, enforcing the principles of integrity and transparency in public life. This is why competence, objectivity, impartiality, moral integrity and giving precedence to public interest are important. In order to enable its enforcement, *the party exercising ownership rights should select the members of the management and of the supervisory committee on the basis of their previous performance, abilities and commitment to the service of the public.*

– Due to the high number of state-owned companies, obtaining appropriate information and proactive contribution pose intrinsic challenges for the state, as the owner. *The state should develop an efficient method for exercising its ownership right.* Based on their strategic significance and other criteria, state-owned business organisations can be classified into several groups, and the various forms of strategic governance can be elaborated for these groups. The fate of the individual constituents can be decided on the basis of the financial and professional evaluation of the corporate portfolio. This can be merger wherever the conditions of the economies of scale can be met, or the sale of minority participations in the case of business enterprises with unjustified state involvement. The benefit of portfolio management is the higher level of coordination. In addition to the harmonisation of the contents of capital investments, this provides an opportunity for planning projects for a period when they can be most economically implemented.

– The feasibility of the objectives set by or for state-owned companies is fundamentally influenced by the owner's decisions. As a basic condition for a good proprietary decision, the owner must recognise the need of a proprietary decision or intervention in time. This requires regular report by the supervisory committee to the owner about the findings of its audits and inspections, taking full responsibility for their content.

– The primary expectation from the managers of state-owned companies is compliance with the rules. Lawful activity in itself is no guarantee for the efficient service of the common good. Adjustment is needed to the quickly changing environment and to challenges. This is why innovative skills and the ability to manage risks have appreciated in the public sector. Public sector managers have roles that go far beyond static management merely required to ensure lawful operation. *The managers of state-owned*

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companies must act with due care, committed to the public, abiding by the rules and respecting budgetary limits, enforcing claims and performing obligations by the deadline.

– The management should compile detailed business plans. They should plan the performance criteria and indicators. *In the business plan, criteria should be set for the efficiency, economy and effectiveness of management* and for the performance of duties to lay the basis for grounded decisions.

– A management can pass the right decisions if it has up-to-date information about the company's operation and the characteristics and quality of its activity and procedures. For this reason *the managers of state-owned companies should build management information systems to support their decisions.* In addition to the external audit of state-owned companies, internal control can also have such a role. This is the most direct method of tracking and monitoring the lawfulness of a company's operation by the management.

– In addition to their reporting obligation, the managers of state-owned companies are also required *to ensure that operation is transparent for both the owners and the public.* The party exercising ownership rights can assess management performance and adopt grounded decisions on the basis of the reports and data related to operation, management, the achievement of the objectives set and to the publicly disclosed data. Citizens can assess the extent of contribution to the service of the public and to the improvement of citizens' welfare on the basis of the data and information disclosed.

– State-owned companies manage public assets, and use public funds for their business management. This is why it is important to only allow *the managers of state-owned companies to perform other activities unrelated to the company's core activity.*

– Due to the state's increasing economic involvement, the interface between the public and private sectors is growing, and unless integrity improves, this increases corruption risks. In order *to reduce corruption risks, focus should be placed on knowledge and meeting the ethical requirements.* The corporate management should set up a management environment to ensure integrity in accordance with the expectations of the legal entity/minister acting on behalf of the owner.

The characteristic features of ethical governance based on integrity

State-owned business organisations have a significant role in the national economy. The value of their assets and the number of their employees are substantial, and the significance of their social role is shown, among others, by the fact that the ten million Hungarian citizens use their (public) services on a daily basis, and directly or indirectly pay significant amounts – in the form or charges, fees, rates and/or taxes – for them. This alone illustrates the fact that the successful and efficient management of these companies is in elementary public interest and has a substantial impact on the efficiency of the national assets. Safeguarding and increasing their assets and efficient and successful operation bring an enormous responsibility and poses a huge challenge. Each decision made by state-owned business organisations can make

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a difference of billions of forints to the central budget and thus on Hungarian households. For this very reason, thoroughly grounded and prudent companies managing resources on a frugal budget can fundamentally contribute to social welfare and improve the efficiency of and raise the added value in the national economy.

The essence of management with focus on integrity is that the organisation endeavours to implement the common good and formulates its mission and the values to be adopted by each of its employees accordingly. With the establishment of integrity controls, the risk of incorrect employee behaviour jeopardising the service of the common good is reduced to the minimum.

The meaning and essence of integrity can be summed up in a sentence: I am what I am supposed to be and I do what I am supposed to do. For a person this means that he performs his obligations and fulfils his mission in agreement with the values he advocates. At the level of an organisation, this may be put as follows: it does what it has been established for and in a way it is expected to fulfil its mission (Pulay, 2017).

One of the essential preconditions of achieving the objectives set for a "well-governed state" is the manner of establishing and running the institutional system required for the fulfilment of its social role and for providing its services, with the ultimate goal of performing public duties in an efficient, successful and accountable manner, frugally using the available resources. Ultimately, state management fulfils its mission if it serves the common good. State management includes all the planning, organisational, management and control activities required for the establishment and operation of the system of institutions that enable the performance of state functions.

The efficient and successful management of state-owned business organisations is conceivable basically uniformly. The reason is that their duties, the challenges related to their management, and their operating environments are basically identical, and all of them are required to work for the common good, similar types of conflicts of interest arise and challenges are posed to the party exercising ownership rights, the supervisory committee and the managements, and all of them are run in the same social and economic environment. The concept of managing business organisations includes the exercise of all the rights and performance of all the obligations directly by the party exercising ownership rights or indirectly by the body authorised by it (typically the supervisory body), on the one hand, and the management, managing director or managing body (board of directors) in charge of the state-owned company, on the other.

In terms of content, the management of state-owned business organisations includes the determination of characteristic features for the objectives of the goods and services these companies intend to provide (strategic objectives), the specification of operating conditions and performance requirements, the selection of the members of the management and of the supervisory committee, organisational and workflow management, the evaluation and control of achievements and operation, and the decisions adopted as a result or affecting the managers in person. According to the nature of management, the owner may exercise ownership rights over the companies in its ownership directly or may transfer them. In both solutions a super-

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visory committee may be set up for auditing the company's operation on behalf of the owner.

A company's efficiency, social use and performance of public duties primarily depend on its managers, in other words, on the combination of their knowledge, expertise, responsibility and willingness to go that extra mile. The primary expectation from the managers of state-owned companies is compliance with the rules. In addition, a manager should prepare for quick changes in the environment, including numerous challenges, and for the fact that legislation can only be adjusted subsequently, with a delay. Consequently, innovative capacity, risk management, change management and the ability to facilitate organisational learning are increasing expectations from state-owned business organisations. This means that today, managers have roles far beyond static management merely required to ensure lawful operation.

The innovative capacity of public-sector companies means the extent to which they are capable of establishing and applying new or significantly renewed services, communication methods, procedures or organisational methods. The management has an important role in shaping the innovation capacity through the configuration of work organisation solutions (Makó and Illésy, 2017).

Risk management is a system that consists of the means and methods of governance, including the elements of risk identification, analysis, classification, tracking and, if required, the mitigation of exposure to risk (Domokos et al., 2017). The establishment and operation of the risk management procedure in adjustment to the characteristics and objectives of the organisation is the responsibility of the manager of the organisation. Change management is a series of carefully considered and previously planned activities to facilitate the achievement of both individual and organisational changes, and in the expected results (Farkas, 2017). Responsibility for managing changes and for planning lies with the top management. Organisational learning is the efficient transformation of the knowledge and competence obtained by the members of the organisation into an organisational capability, their becoming shared knowledge and integration into the memory of the organisation (Makó and Illésy, 2017). Knowledge management, which implements organisational learning, has an outstanding significance for the competitiveness of organisations, as based on an analysis of its activity, procedures and risks; this includes improvement in the operation of its organisation and in its results in the framework of change management.

The State Audit Office bases its audits on the Fundamental Law, and judges the performance of the manager of the organisation that uses public funds and public assets primarily based on his enforcement of lawfulness, efficiency and expedience. In order to determine the requirements that may be set for public sector management, the baseline was the elaboration of proposals for the quality of management on the basis of the experiences obtained during the audit of state-owned business organisations. Since October 2016 it has been decreed that the managers of public service institutions are in charge of the creation of an internal control system suitable for enforcing ethical values and integrity. The integrity approach focuses on the prevention of corruption, and thus the organisation's executives have increased responsibility, as

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it is presumed that with the help of corruption risk analyses, the executive reveals and raises awareness of the corruption risks jeopardising the organisation in its management. The other characteristic feature of the integrity approach is its emphasis on the significance of manifesting and following positive values. This can be done, among others, through a strategy, a mission statement and/or a code of conduct setting values, and through the management's example.

Based on the audit experiences obtained by the State Audit Office, in sum it can be assumed that irrespective of whether they perform public duties or not, in order to adopt a state management approach, state-owned business organisations need to serve the common good. Its implementation is conceivable in an ethical management system elaborated in a state management approach based on a strategic principle, focussed on values and capable of preserving, and moreover, reinforcing the organisation's advocated values during adjustment to changes. Setting up an organisational framework that ensures lawful and efficient operation without profligacy is first and foremost the responsibility of the top management of state-owned business organisations.

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Dimensions in Hungarian State Companies – in an Historical and International Perspective

Summary

The Hungarian economy has been bearing the mark of disadvantage in development due to a late state organisation (at the end of the 10th century) and late rise of the middle classes (second half of the 19th century). The process was made really "vibrant" after the relatively rapid spread of market relations that followed the termination of the feudal production method and social order in the middle of the 19th century, the losses of World Wars I and II and then the nationalisations corresponding to the spirit of the age in Eastern Europe. Between 1947 and the 1980's, state ownership predominated, and then after four decades, the entire system was nearly completely knocked down: this meant the privatisation of collectively owned assets, including radical changes in companies' ownership and management positions. After laying the foundations of the new public finance regime adopted in 2010, the government's regulatory, control and business management achieved its full potential. However, the "time travel" made in this study and overarching more than one and a half centuries also sheds light on the fact that capitalism was built and rebuilt, and to an even greater extent, private ownership was torn down with the state's active participation, and moreover, with its inevitable intervention, which is another unique feature of Central and Eastern Europe, and more specifically Hungary. This study discusses the successive relays (periods) in the mentioned one and a half centuries, with special focus on the procedures that took place in direct state (proprietary) and indirect regulation, in order to provide a scholarly background to the state's current involvement, particularly the prioritisation of companies in community ownership. Consequently, this

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lends relevance to outlining the 19th-century building of capitalism, market socialism and the 21st-century proactive, state-managed economic policy in Hungary,[1] and especially to discussing the logic of the operation of companies that can be considered as the fundamental aggregates of production and to tackle the economic policy governing corporate management.

Journal of Economic Literature (JEL) codes: B5, D00, E00, F15, G01, H6, N00, P2
Keywords: economic management, corporate management, Austro-Hungarian Monarchy, socialist planned economy, market socialism, neoliberal transition to a market economy, proactive state model, Hungary, European Union

Introduction

The economic involvement of the state was a basic prerequisite of launching the development of capitalisation in the Eastern and Central European region.[2] In agreement with the spirit of the time, in the first half of the 19th century, Friedrich List was of the opinion that the German economic area should close the gap by improvement in transportation and support to the industry, with the state acting as a patron, similarly to the developments of Hungarian capitalism after 1867, which was implemented with the state's effective involvement. The neoclassical economists of the second half of the 19th century raised the necessity of state intervention and its method (anew), although its justification and depth remain matters of debate to date. In the position taken by Hanke (1987) and Storr (2001), in a purely private economy deprived of the state, national and community considerations are impaired. On the other hand, excessive government ownership has numerous risks (primarily due to the insufficient enforcement of efficiency and of the ownership approach on a systemic level, which may result in abandoning development projects and allowing the use of obsolete technologies (Megginson and Netter, 2003; Savas, 1987), as we could experience in the planned economy regime. Megginson (2005) is of the opinion that if strategically significant companies have an irresponsible management, the inevitable demand for (repeated) rescues becomes constant. A series of Hungarian and international examples evidence that neither the excessive withdrawal of the state nor the state's excessive sprawl on the economic participants is appropriate. However, there are situations like the one that evolved in the years after the outbreak of the global economic crisis, or gap-closing trajectories, when the means available for economy orientation are indispensable. Based on these, the elaboration of an optimum economy administration and ownership structure is a complex task.

If the Hungarian economic policy, including asset management policy, followed in the past one hundred and fifty years is depicted as being in constant gap-closing due to its considerable lag, the massive economic influence by the state is justifiable, and can entail the expansion of the national wealth (by purchase) and support to compa-

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nies by the means available in the state budget. In other words, with the exception of the soviet type planned economy, the government's intention to influence the Hungarian economy, which was lagging in development or in the state of a crisis, during the past one and a half centuries, was not improper.

A few considerations relating to the age of the Austro-Hungarian Monarchy with regard to the history of theories about the state's policy on assets and corporations

Transition from a society of a feudal hierarchy[3] to a constitutional monarchy and from the feudal production to a market economy started in Hungary with the adoption of the April 1848 statutes,[4] and then after the compromise made with the Habsburg Empire in 1867,[5] it strengthened and resulted in the launching of the capitalist method of production for the most part built on industrial companies. The state helped the start and further operation of companies established on the territory of the Kingdom of Hungary by placing orders from them, providing a favourable economic policy regulatory environment and a statutory background to ensure this background. The most outstanding example of state involvement was the state's support of railway construction, but additional forms of support to the industry, subsidies and government purchases also played an important part. A common customs border was established for the entire territory of the Monarchy,[6] and this ensured protection of the domestic market for all who lived in this dualistic state formation, including protection for Hungarian food industrial products. The government of the time acted as a go-between to encourage the inflow of foreign direct investment. In more specific terms, the state had plants and factories of its own in iron- and steel-making, machine manufacture, silk manufacturing, metals mining, salt mining and the tobacco industry, employing in excess of 50,000 people on the aggregate already in 1900, or 18 per cent of the total number of industrial workers at the time.[7] Raw iron and steel-making had the highest significance, as the products were used mainly in railway construction and the manufacture of agricultural machines. The Hungarian state took over 10 blast furnaces and 18 refinery sites from the Austrian state treasury.[8] The state also had shares in private companies, primarily in those that had run into bankruptcy or needed to be saved (e.g. the Testory Metal and Lamp Factory). The Finance Minister was in charge of the management of state-owned assets, which was administered through the Directorate of State Goods. After World War II, Marxist history writing strongly criticised the dualistic state formation, and especially the "factories owned by the treasury" as a corporate form. Lajos Leopold called the capitalist production method implemented on the territory of the Kingdom of Hungary "false capitalism" or "simulated capitalism" (Leopold, 1917, pp. 97, 131). Based on Marx's propositions, Endre Nagy considered the social character antagonistic to the private capitalist form, and as such, he thought that it represented termination of the capitalist method of production within the limits of the capitalist mode of production (Nagy, 1977). Capital, which is based

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on the social method of production, requires the concentration of the instruments of production and of workforce, and in this case it is directly manifest as social capital, in contrast to private capital, and its companies are all social companies, in contrast to private businesses. As a result, within the capitalist mode of production, a state-owned company also eliminated private capital, similarly to a joint stock company; however, their points of departure are different: the latter is based on a private capital formation, while the transformation of a treasury company is essentially a breakdown of the feudalist mode of production. In respect of the development of the individual companies, Marxist authors did not make a clear distinction between treasury ownership and social nature, and rather they presumed a contradictory coexistence between the various momentums of the treasury and the social nature.[9] In addition, following the logic of Engels's theory of feudal nationalisation, Endre Nagy, who was one of the main representatives of Hungarian Marxist historiography considered state-owned factories as means to salvaging the power of the agricultural and feudal social layer to the next social order.

In contrast to Marxist historiography, it can be established that the political consolidation had a beneficial impact on the development of Hungary. The situation that followed the liberation of serfs[10] acted as an economy boosting factor for the political and economic élites alike, and made the creation of the conditions for capitalist development inevitable.[11] "The basic principle of the official economic policy remained liberalism all the time. However, the situation of the national economy and the difficulties of development necessarily required the increasingly direct intervention of the state. This was also admitted by the advocates of liberal economic policy (Katus, 2009, p. 151). Moreover, László Katus also ascertains that "right after the Compromise, the state undertook a direct role in building a modern infrastructure. Private railway companies were supported by state interest guarantees and shipping companies by annual subsidiaries" (Katus, 2009, p. 152). Government bonds were issued for the establishment of railways and sewers (1867, Art. 13). Act 44 of 1881 on the tax benefits granted to the Hungarian industry provided government allowances to the factories "equipped in accordance with the current technical development" if they "manufacture goods that have not been made in Hungary so far" and any other factory existing or to be established if they manufacture industrial products listed in the act. In 1872, guilds were abolished by law in Hungary, thus paving the way for the establishment of modern business organisations. After 1875, in accordance with the German example a statutory regulation allowed the establishment of general partnerships, limited partnerships and joint stock companies.[12] These state actions had a key role in the commencement of capitalist development in Hungary, but due to the late start and undercapitalisation, all this was possible in the form of a government-controlled capitalism, in a system including the state as the establisher of corporations, while also supporting p private companies and placing orders to them. In this respect there was no significant shift between the two World Wars, and in addition, state involvement increased, especially through government purchases from private companies, among others, as a result of the Győr armament programme.[13] In order to

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provide a proper grounding for the assessment of the economic history, a brief mention should be made of the fact that the Kingdom of Hungary entered the war on the side of the central powers, and being a defeated party, after the 1920 Peace Dictate, it lost two-thirds of its territory, population and other economic resources. Its territories were annexed to the neighbouring countries and newly established countries that had fought on the side of the Entente, what is more, even the Austrian part of the former Austro-Hungarian Monarchy was given Hungarian land. This unfair peace treaty, in effect to this very date, urged the political leadership and moreover, every social layer, between the two World Wars to take revenge, and the economic administration was subordinated to this intent.[14] In World War II, Hungary was defeated once again, all the results of the consolidation between the two World Wars were lost, the country lay in ruins, and as from the spring of 1945, it came under uninterrupted soviet communist influence backed by the permanent presence of the soviet occupying forces up unto the change of regime.[15]

Asset Management Policy in the Planned Economy – The Soft Budgetary Limit

Between 1945 and 1949 the entire privately owned Hungarian industry, including companies, mines and banks, were nationalised, and the established collective property served the purposes of the planned economy according to the guidelines, and what is more, requirements of the "plan-statutes". As Tamás Sárközy discussed it, the 1959 Civil Code codified a system with state holding considered as the primary property or public holding, while the secondary social property was the collective (kolkhoz) type co-operative property (Sárközy, 1991, pp. 11–12). In addition, the state holding was internally uniform and undivided, and the state-owned corporations set up as sub-holdings created in the so-called institutional type of property, only managed and "operationally" administered the state assets under the leadership of a director appointed from above. In this structure, the private ownership of the means of production were extremely limited; "capitalist" private ownership of an entrepreneurial type was prohibited, and consumer goods, which were extremely scarce due to the low standard of living, constituted personal property, acknowledged as a socialist form of ownership in addition to social (state and cooperative) property.

In the planned economy system, the national economic plans set the expected performances in a breakdown of companies, and assigned all the input the companies were allowed and obliged to manage, from human resources through raw materials and bank loans to state subsidies. The operation of socialist companies was permeated by a voluntarist approach, especially in the first decade of building socialism, when little attention was paid to initiatives and financial interests whether on the level of corporations or of employees. However, the new economic policy approach that appeared in 1955–1956,[16] and especially the New Economic Mechanism announced in 1967 and started on 1 January 1968, brought forward-looking changes in the management of state companies. The new direction, called "methodical market regulation"

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mitigated regulatory limitations and enforced price and cost relations in an increased extent. Moreover, it paid higher attention to corporate and employee incentives. In Hungary an experiment started with the increased enforcement of market elements, especially in the management of large companies. Nevertheless, due to efforts at restoration, especially waves of pressure by the Soviet Communist Party and the Hungarian retrograde forces, market socialism failed to take place in Hungary, as the predominance of the planned economy and of state ownership prevented the evolution of genuine market conditions.

However, the peculiar Hungarian company management practice, which had remained in fragments up to the change of regime, differed from that of any other COMECON member. Separately accounted units and business partnerships were allowed to be established within state companies, and the opportunity was given to take out certain units of state companies on rent (this was called "gebin" in Hungarian), especially in catering and the service sector. All these generated a more efficient management of companies' assets and a more intense interest and increase in incomes by the employee-lessees. Despite halt and moderation after the successful initial years, the Hungarian market socialism became a model, and nevertheless improved the performance of the national economy through improvement in the efficiency of state asset management. Hungarian companies became more cost-sensitive, responded more to solvent demand on the market, despite numerous opposing forces of paternalist system elements cut back its speed and prevented its fulfilment, e.g. the "Bucharest price principle"[17], or the economic management under party control, and most importantly, the unnatural maintenance of the planning system, the economic basis of socialism. The very first heavy blow on planned economy and on the regulated conditions was a steep rise in the prices of hydrocarbon products (and especially mineral oil) at the beginning of the 1970's, which made loss-making in the operation of the highly energy-consuming Hungarian industrial companies irreversible, as they were unable to shift the additional expenditures incurred as a result of rising raw material prices to the market. Thus loss-making business management became systemic, bridging losses became characteristic of the system, and – through exchange rate losses and debt services that could no longer be earned by operation – borrowing from abroad to maintain the paternalism of the socialist state caused the collapse of the system by the end of the 1980's. Naturally, at the final point, the system-specific features of the regime included the impossibility of state company operation and the serial application of the soft budgetary limit, as defined by János Kornai, as a means of (temporarily) fending off such an untenable operation (Kornai, 2014, p. 383, reference on pp. 15–17). Considering its impacts, Kornai considered the syndromes of the soft budgetary limit as an unhealthy phenomenon, as they predispose companies to engage in frivolous spending, in other words, they do not need to be afraid of gross financial problems, because the rescue will provide for their survival despite overspending and loss-making. Secondly, the soft budgetary limit syndrome reduces decision-makers' price and cost sensitivity, because a company that can be confident of being rescued will certainly pay less attention to cost management. Thirdly, still quoting János Kor-

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nai, the soft budgetary limit syndrome rearranges the perceived perspectives and the focus of attention and activity for the organisations demanding rescue or support. This means that less attention is paid to the improvement of the original purpose of the given organisation, and more attention is paid to building good relations with any potential rescuer, and both separately and in the aggregate, these effects deteriorate the efficiency of operation. Moreover, Kornai notes that the soft budgetary limit syndrome has a disruptive impact on social morals, as non-paying debtors are saved, and so the other companies will not make great efforts at fulfilling their obligations and at improving the conditions of reasonable and economical business management either. Kornai analysed the soft budgetary limit syndrome mainly in corporations, while this study exposes its macro-economic connotations.

In addition to the pampering effects of the soft budgetary limit applied to the companies of the planned economy (actually meaning regular rescues), beyond János Kornai's opinion,[18] it is equally important to highlight the responsibility of the state, i.e. economic management. Situations causing the mass bankruptcy of companies result from the state's economic policy, and thus the loss-making corporate behaviour is mainly a consequence and a manifestation of the incorrect state management on a micro-economic level, and if it becomes general, it may make macro-economic operation impossible, as had happened and essentially caused the collapse of the planned economy by the end of the 1980's, including the bankruptcy of several hundreds of state companies. This is to say that the administration of the socialist planned economy spread the application of the soft budgetary limit to the entire corporate sector, thus disintegrating its own responsibility towards these companies, and this resulted in the bankruptcy of the majority of companies due to "non-optimum" and "imprudent" state-controlled economic management. The economic conditions of transition to a market economy also suffered from the phenomenon called soft budgetary limit. Masses of companies and banks that had been taken into private ownership, and moreover, due to irresponsible foreign exchange lending and lenient state supervision, also local governments and households became insolvent and were rescued from the state budget, which had been strengthened in the meantime. Thus the rescue of the individual units in the sub-system of corporations and even public finances (e.g. community local governments[19]) did not exclusively (fundamentally) relate to the previous incorrect business management of those rescued, but also to the insufficiently circumspect management, regulation and control performed by the central government authorities managing, regulating and controlling them. Obviously, the companies and local governments indulging in overspending and disregarding cost management were responsible, but corporate and institutional organisations are embedded in a national economy, and as such, they are in a subordinated position and follow rules. If their management by the state is insufficiently prudent, the regulatory system hinders optimum business management, and the methodology of state control and the powers granted to the controlling authority are insufficient, the unit waiting for a rescue should not be solely blamed for its bankruptcy and sinking into a state that requires rescue. Ultimately, when a state rescues its bankrupt company or, among

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market economic conditions, privately owned corporate or banking entities operating in public administration, in fact, it rescues itself, as the operation of corporate organisations provides the basis of the state. In other words, the rescuer consolidates the consequences of the unfavourable economic climate and environment created by the state itself. János Kornai recommended dispensing with the practice called soft budgetary limit, but actually this would only indirectly trigger the bankruptcy of companies, as ultimately the broader managing and regulatory environment of the companies would go bankrupt, whether in a planned or in a market economy. There was hardly any deterrent or disincentive for companies heading towards bankruptcy, as the environment of their operation was shaped by the state, especially in the Soviet and post-Soviet region.

After the rescue, when, in an optimum case, the bankruptcy of the rescued company is resolved, the state management and control and, not in the least, the corporate management are responsible for enforcing the accounting principle of going concern, for creating the conditions of sustainable management and for carrying on operation accordingly (Lentner, 2013; Zéman and Lentner, 2018).

If the companies operating in the planned economy and the initial (market-oriented) enterprises organised around them (separately accounted units, economic partnerships and leased corporate units) were allowed to achieve their full purpose, they could have provided a sound base for the decomposition of the socialist planned economy without a major crisis. The New Economic Mechanism, which focussed on endogenous factors, could have spilled over to a social market economy with companies retaining their original forms, perhaps broken down to clearly delimited units, which could have been given into employee ownership. Instead, the state budget, which had been gradually running short of resources, corporate managements incapable of innovation, the employees, who had grown inert in the course of several decades, limitation of the efforts made at the full enforcement of financial interests, and most importantly, the absence of capital gradually changed the direction of the economy and shifted it to foreign direct investment and the resettlement of foreign companies in Hungary.

Asset policy and corporate conditions during the transition to a market economy (between the 1980's and 2010)[20]

According to the research by Éva Voszka, already the analyses of Western Europe in the 1980's called the attention to the fact that in large private companies, where ownership is separate from management, control and incentives encounter the same problems at public property does, and therefore in the case of companies facing privatisation efficiency improvement may fall below the expectations (Voszka, 2018, p. 141). In other words, Voszka thinks that the interconnectedness of politics and the economy is not exclusively characteristic of state-owned companies: private companies may also influence central decision, while state purchases and subsidies create

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heavy dependence. Even after 30 to 40 years this assumption remains applicable, especially evidenced by the recent bribery scandals performed in order to win certain public procurement tenders by private companies, but also by demanding the refund of state subsidies granted in return for support to political campaigns, and by obtaining state purchases through means that suggest abuse. Due to the general nature of the system and of human behaviour, the management, control and ultimately efficiency problems encountered in the case of companies operating in the framework of a planned economy remained characteristic during the transition to a market economy, although more moderately than during the period of the planned economy, because private ownership has a more powerful and direct interest than collective ownership. Based on all this, the privatisation of state assets, launched in the late 1980's, and mainly its theoretical grounding should be received with reservations, in other words, giving the majority and the most valuable part of the national wealth into private hands did not solve the problems. However, similarly to the other countries of the post-Soviet region, privatisation in Hungary was built on the axiom that "the state is not a good owner".[21] The failure of the decades that followed the change of regime sophisticated the general legitimacy of this assumption; however, the companies that continued operation in national ownership also have numerous efficiency-related difficulties.

During transition to a market economy, the state continued to generate budget deficit and government debt, while being incapable of creating incentive conditions for the entire circle of companies in private ownership (including international companies and businesses in Hungarian hands), and moreover, public finances repeatedly ran into increasing operating problems. It can also be evidenced for Hungary that inappropriate economic management and the "general" spread of disinterest at the level of state companies, insufficient motivation – whether of the management or of employees – cut back corporate efficiency. On this basis, the acquisition of corporate property by purchases, whether for resident or non-resident owners, did not contribute significantly to improvement in corporate operation – mainly due to the habits ingrained under the conditions sustained for decades – and a fundamentally new situation was not created. In addition to this base-dependence, the rudimentary market conditions did not encourage competition and generally failed to trigger higher performances in the post-Soviet region. "Without a legal framework of property rights, or commercial institutions such as functioning banks or stock exchanges, without convertible currencies, or even a culture of market exchange, the process of privatisation did not prove an immediate panacea for the structural problems of the economies of these countries as some western advisers enthusiastically promised" (Clarke and Pitelis, 1993, p. 12). As a predominant characteristics also in the Hungarian market economy, through their privatisation or their greenfield investments, well-capitalised foreign companies abounding in know-how created islands of ample innovation, efficiency and profits, however, these isolated circles failed to expand to national parameters, rather they remained secluded and only boosted the total national economy in a limited extent. Although they triggered a favourable propelling

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effect, on minor enterprises operating in their respective regions and respective profiles, mainly in domestic ownership, but this also cemented the dependence of SMEs.

All that said about the circumstances, a sophisticated picture can be given of privatisation in Hungary and the conditions of companies remaining in national (or Hungarian private) ownership. Especially in respect of their efficiency, as it should be noted that the government's economic policy required international companies to pay taxes only far below their tax payment capacities. What is more, in general they were granted resettlement and investment support they could use for further improving their competitive edge, mainly against Hungarian small and medium-sized enterprises. This is to say, a genuine (universal) market economy has never been established in Hungary. In this evolving market space, the most striking example of market competition was seen on the level of public utility companies. The privatisation of public utility companies, which were technically obsolete but organised on a territorial basis and thus had a secure clientele, started as early as the middle of the 1990's. The nature of their services and their geographical dislocation also earned them a monopoly position, and these should have been reflected in the privatisation price paid, but they were sold at a loss. The new owners could expect a secure return on their developments, and this was topped by the government guaranteeing an 8-percent return on assets for them in the privatisation contracts. The amount determined by this method was guaranteed by the state if it was not raised from the payments made by the clients, participating in the transactions as a surety. The enforcement of such a powerful state support prevents the purely market-based assessment of the efficiency and profitability of even foreign-owned public utility companies on the basis of traditional market calculations.

The dependence of transition to a market economy on planned economy as its base, the inherited poor work ethic and the burdensome regulatory environment were especially traceable in the management of state companies, but also affected private businesses. János Kornai calls this process the feed-through of the elements of the socialist system (Kornai, 2012, XV–XVI, XIX, XX–XXVIII). He mentions the effects of values inherited from socialism, bubbles retaining an economy of shortages, and the survival of the soft budgetary limit syndrome. In Kornai's position, wherever state ownership predominates and goods or services are provided to the consumer or user free of charge, the economy of shortages necessarily appears. This applies even more to the market of state healthcare and educational services. After all, in these fields the economy of surpluses, characteristic of capitalism, has not evolved, instead the economy of shortages remained. Calling the quoted proposition into question, we assume that the Central and Eastern European population cannot yet afford to pay the "marketised prices" of the private healthcare and educational sectors. For this reason, the operation of the traditional state-owned service providers is perhaps justified, and provides a higher security of supply for the wider masses than the one a private sector could offer.

However, pushing the complete state sector into the background caused significant tensions at public utility service providers. Households encountered increasing difficulties in paying the ever rising priced set by the public utility service provider

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companies privatised in the 1990's, and a significant amount of debt was accumulated. True, the services provided by service providers improved significantly. During privatisation, the state's assumption was that a private company could operate e.g. a district heating, a water supply or an electricity service provider more efficiently than the state or local governments. Assuming the Hungarian state's permanently tight financial situation, a new and highly capitalised foreign owner was expected to be able to spend more on technical developments. An interesting thing about the companies given ground in the privatisation of Hungarian energy and public utility sectors is that most of them came from continental Europe (Germany and France). Moreover, from countries where the public utility and energy sectors are preponderantly in national ownership. Another interesting thing is that a significant part of the Hungarian public utility companies were purchased by German and French local government-owned public utility companies. This fact contradicts Péter Mihályi's assumption that the state is a bad owner. Perhaps, in Hungary the state was a bad owner, or rather a frivolous owner, but this is not true everywhere in the world. The genuine remedy the large number of companies and public utilities that went bankrupt during Hungary's transition to a market economy is not the direct application of a soft budgetary limit (repeated rescues), rather, an efficient economic policy securing the sustainable operation of these companies and optimised to Hungarian conditions. But the Hungarian state management was incapable of this.

The decentralisation of other kinds of (classical) public services – for example state and local government administration, and giving the companies performing public services from national ownership into private hands, and thus a shift to profit orientation in these companies according to the underlying philosophy of company management, implemented the DPM paradigm[22] of the New Public Management, the neoliberal economic theory of the state. For two decades the Hungarian state's economic management operated along these guidelines, in close correlation with the principles of the Washington Consensus, prevailing since the 1970's, and with the Copenhagen Criteria favoured by the European Union, as compliance with the Maastricht Criteria were hoped with their help. Overall, the role of the state was gradually decreased, and within that scope, the economic philosophy of moderating its regulatory and control functions was enforced when the Hungarian State Property Agency and the local governments sold the public utility companies in their ownership, which had been organised on a geographical and supply basis. Subsequently, they only had very slight control and regulatory authority over the internal business management of these companies. After all, due to corporate independence and to the "overemphasised" sanctity of private ownership, after privatisation the state could barely influence and did not have much insight into the procedure of setting consumer prices and the procedure of accounting cost items. In addition, as the privatisation contracts were concluded in an exigency of the seller state, they also provided very little opportunity for any further state or authority control over sales prices as well as further operation. There were hardly any example for such provisions in privatisation contracts, and perhaps even the intent was missing.

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Due to the primacy of profit considerations in the business management of the public utility companies obtained by the new owners, payment tensions increased on the consumer side. Based on all these, one of the key elements among the criteria of state management and state operation, revised in 2010, was the reversal of the decentralisation processes that took place in public finances. In other words, the state centralised the general government (including both the central and the local) budgets. The most important example for this was seen in the field of local governments' debt management, financing and the performance of their duties. Another key action in centralisation was the takeover of private pension funds' assets into government coordination. In addition to centralisation, taking public utility companies into national ownership (through purchases) was another reasonable solution in order to have a say in setting the prices that significantly affect the housing conditions of the population. Once the state became an owner, and also through its reinforced regulatory powers, it could influence service charges. Thus, by enforcement of price regulation, the public utility companies repossessed into national ownership reduced the service charges. Instead of the priority of profit, service of the public good was given a key role in their operation, and especially in their regulatory environment.[23] The previous DPM paradigm of the obsolete NPM system was thus replaced in state operation by a new Weberian and French étatist state model, the CPNG[24] philosophy of the state's active economy influencing activity. The duty of the state and its controlling authorities is to constantly supervise the efficiency of the business management triggered by regulation and to monitor the operation of public utility companies. Then the State Audit Office was required to fulfil the majority of the duties related to making comprehensive proposals (Domokos et al., 2016, pp. 178–198).[25] The absurdity of the previous situation is well illustrated by the fact that up to 2011 the State Audit Office had not been authorised to audit public utility service provider companies in local government ownership. In other cases, due to regulatory deficiencies, the fact-finding audits performed by the State Audit Office were improperly utilised and failed to entail consequences condemning the transgressor and extorting normalisation of the situation.

Returning to the 1990's: in the case of companies given into private hands during privatisation, the paid sales prices have been the matter of debate to date. Undoubtedly, the majority of state companies put up for sale was characterised by an obsolete technical level and narrow market opportunities. The exigency of the seller state was manifest in the resources that were insufficient for the continuation of operation or even for survival, and in the absence of any concept whatsoever in state management. Bianka Parragh highlights that the first "spontaneous privatisation" started already in 1989 without the formulation of a public privatisation strategy. Numerous highly significant questions of the property transfer remained unanswered, there was no act on privatisation, there were no rules for inviting tenders, proposals or quotes, and asset valuation was also unregulated, thus corporate self-governments had a broad opportunity to move assets.[26] Theoretically, the price of a company put up for sale is determined by its equity and its market prosperity. However, György Matolcsy found that

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impairment was basically unrelated to company privatisation; rather it was caused by the aggregate impacts of high inflation, import liberalisation and the exchange rate policy (Matolcsy, 1991, pp. 227–229). Árpád Kovács and Gusztáv Báger think that such a rapid depreciation of companies would also have taken place without privatisation (Kovács and Báger, 2004, p. 25). Based on all this, it can be concluded that the privatisation of these companies was an involuntary solution among the given suffocating macro-economic conditions, which at least created the opportunity for additional operation by the new owners. Giving these companies into private hands were often characterised by circumstances that raise the suspicion of criminal offences.[27] After twenty five years, as a result of a proactive state operation, today the circumstances of business management seem to be returning to normal, and the problems encountered during transition have been resolved.

After all, if we seek to know the efficiency of the assets that provided the Hungarian economy's technical base and were "operated" in a corporate framework, or in other words, the total corporate efficiency achieved by privatisation, a depressing picture is obtained. In an analysis by Péter Mihályi (a neoliberal advocate of "unlimited" privatisation), between 1989 and 2009, the average rate of GDP growth (resulting for the most part from corporate performance) was 1.1 per cent (Mihályi, 2010, p. 51). According to Mihályi, this value is dramatically low, but it represents a change in the trend in comparison to the 3.6 per cent characteristic of the period between 1968 and 1989. In the first two decades after the change of regime, while the number of the population dropped by only 3.6 per cent, the number of active wage earners dropped by 15.4 per cent from 5.2 million to 4.4 million. It should be added and should not be forgotten that at the beginning of the change of regime, when corporate management was changed to a new mode (forced by deteriorating economic conditions and as a result of privatisation), 1.5 million industrial and agricultural jobs had been terminated up to 1995 and an intention to reintegrate this huge mass of unemployed into the labour market was only shown after 2010, when the opportunity was created by a proactive (once again) state-managed economic policy.[28]

György Matolcsy related the privatisation procedure to the debt portfolio that put a heavy pressure on the country and to the resulting compulsion. "Despite the fact that we were given help for a spill-over and launched the sale of state assets, primarily to foreign investors, we did not escape the debt trap. From approximately USD 21 billion in 1990, by the end of 1995 the gross debt to the rest of the world had increased to about USD 32 billion" (Matolcsy, 1998, p. 25). It follows from Matolcsy's argumentation that the re-organised technical base that had been given, for the most part, to private hands, mainly to foreigners, was incapable of releasing Hungary – with the help of the state's economic management – from the grave debt crisis that had evolved by the end of the 1980's, and moreover, as privatisation gradually spread, the crisis deepened. Indirectly, this gives a depressing picture of the performance of market economy (mostly already in private ownership). This means that Péter Mihályi's "inherent" concept that the state is a bad owner can be received with even higher reservations. Naturally, the state may not be the best owner, but it is, or was in the

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past, far worse in leadership and economy management, i.e. it has a limited capacity to create an optimum economic policy for companies. In a historical retrospect, this was the case both in the period of the planned economy and in the decades of transition to a market economy. Companies are basically not to be blamed for corporate failures, whether made in the period of the planned economy or during transition to a market economy, as they were caused by incorrect economic policies, which put the companies owned by the state or sold to private owners into chronic loss-making. The state mitigates its unsolid economy influencing, regulatory and controlling role by rescuing (through the soft budgetary limit facility) corporations, from time to time, as illustrated by numerous examples since the restart of proactive state operation (after the 2010 change of government and economic philosophy), to resolve the problems that had been accumulated in the previous decade. After all, in summary, the raw, neoliberal Hungarian market economy practice that followed the planned economy can be represented in a single sentence or the title of one of my previous studies: *Is the Hungarian market economy a genuinely higher-level economic model than the planned economy system modified by market elements?* (Lentner, 2010, pp. 11–13). I could not give an affirmative response to this question in my analysis presented at a plenary session at the Pázmány Péter Catholic University in 2010.

A road to the present – or a summary[29]

In relation to the "completion" of transition to a market economy and the regulation of a new, proactive state operation practice, Tamás Sárközy thinks that when redefining ownership conditions, the government has directly taken (naturally, based on authorisation by the electorate) the right of economic constitutionality (Sárközy, 2014, pp. 285–286). Professor Sárközy argues that economic constitutionality includes the direct or indirect determination of a country's economic system. In 1989–1990, following the German example, Hungary's economic system was defined as a social market economy in the Hungarian constitution. However, this definition was left out of the Fundamental Law that set the framework (among others) to the post-2010 proactive economic policy practice, in other words, the economic system is not defined, and moreover, the discussion of the system of ownership is also very low-key. It does not discuss the ratio of public assets to private assets, and ultimately (indirectly) this provides a general public authorisation for the government to control and determine the desired processes. Moreover, to continue along Sárközy's train of thoughts, our economic system should be a market economy based on specifically Hungarian features but also compliant with the basic economic and political principles recorded in the Treaty of Rome establishing the European Union. In other words it is based on private ownership, i.e. it is built on the market competition of autonomous market participants. Consequently, it is self-regulating but – in order to mitigate the past discrepancies – it is complete with state regulation that is stronger than in the past decades. This ensured fair procedure, good faith, equitableness and co-operation between the various economic participants, and integrates the social element, including

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the corporate social responsibility of large corporations, in market competition. Our economic system should be based on an ownership structure based on private property as a fundamental element, completed by public property (owned by the state, local government or public body). However, the fulfilment of these requirements rules out the kind of state capitalism as applied in most successor states of the Soviet Union, but it is in agreement with the obligations undertaken vis-a-vis the European Union in the relevant international treaties.[30]

Simultaneously with this abstract legal definition, it should be emphasised that the Article 38 of the new Fundamental Law clearly points out that the requirements of retaining and protecting the national wealth and of the responsible management of national assets are specified in a cardinal law. The Fundamental Law also provides that a cardinal law should specify the scope of the state's exclusive ownership and exclusive economic activity, as well as the limits to and conditions of the alienation of national assets given priority for considerations related to the national economy. The purpose of act on national assets (Act CXCVI of 2011) is, in agreement with the Fundamental Law, to define, on the highest level of legislation, the general principles of protecting national assets constituting the primary infrastructure for the performance of public duties by the state and by local governments, and of managing these assets. The purpose of the Fundamental Law and the act about national assets is to enforce the principle of division of public duties performed by the state and by local governments when assets are allocated for the performance of a given duty from central ownership to local government ownership, or if the particular duty is assigned to the state, from local government ownership to state ownership. The act stipulates that the primary purpose of national assets is the performance of public duties, and defines the concept of "public duty" in general terms, with due consideration to the meaning of the terms "public duties" and "public services" given in other statutory regulations. Thus the act on national assets was drafted with the aim to enforce the goods declared by the Fundamental Law to constitute the ownership of the state and of local governments as national assets. The cardinal act, on the other hand, defines the use of national assets in public interest and for the purpose of public needs, and requires the retention of national values in order to secure coverage for the needs of future generations. In order to fulfil all these goals, the transparent and responsible management of national assets are specified as requirements. It follows from these statutory definitions that the public utility companies given into state and local government ownership must serve the public good instead of seeking profit. The State Audit Office's audits, proprietary control, inspections by the authorities and the committed work of the corporate management are meant to serve the efficiency of their corporate management. In addition to disciplined budgetary (financial) procedures, the state makes efforts at achieving its objectives set in the Fundamental Law more directly and operatively.

Therefore it is essential that 2011 was a watershed in the management of national assets. While the previously effective Act CVI of 2007 provided that state holdings had already been pulled down during the previous two decades, institutional and mass

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privatisation had been closed. Thus the conditions had been created for making a coherent statutory regulation of the remaining state property, which was "still very significant" in 2007. As "it is disproportionate to public duties," the purpose is to "reduce the currently excessive amount of state-owned assets". In other words, the previous political leadership thought that assets should only remain in state ownership over the long term if it is justified by retention of the value of the asset, the nature of the asset or an overriding economic policy interest or consideration.

A comparison of the 2007 and 2011 acts on national assets reveals an essential difference: the 2011 statutory regulation sets the goal of increasing national assets, and thus to perform the widest possible scope of public services in the interest of the public good, with the "implementing" organisational units set up for the satisfaction of public needs at the highest possible standard. The new approach expands the scope of public duties and intends to improve its quality, by expansion of the circle of companies in national ownership and improvement of their efficiency.

Summary

To a great extent, a particular country's asset management and corporate policy are determined by its development trajectory, geopolitical location and dimension, and its history. The state cannot create an efficient asset management (including the state's involvement as an owner and the strength of its regulation in respect of the companies) on the assumption of dependence on a base; it is only possible with consideration to the capacities, realistic endowments and demands of the society and the economic participants. This is evidenced by the events of Hungarian asset management policy in the past one and a half centuries.

The mass privatisation launched in the 1980's was similarly harmful, primarily because it caused financial and social damages, similarly to the forcible nationalisation performed after 1945 with reference to economic reason. Both distorted the conduct of businesses: the nationalised companies and their employees interests were reduced, while companies during the transition to a market economy, with the exception of a few international corporations, were never brought into a competitive position. Moreover, a large number of the former state companies went bankrupt as a result of the incorrect approach to the economic policy role of the state. The market economy environment re-shaped since 2010 is characterised by state control, similarly to the period of the Austro-Hungarian Monarchy, when the state assisted in the "preparation" of companies for market competition and for coping with the market requirements. The goal, just as in the period of the Monarchy, is the diversity of company sizes, and the state provides a supportive economic policy environment for the achievement of this goal.

Catching up is, *mutatis mutandis,* always a matter of closing the gap to a more developed entity. But an analysis of contemporary England and its lessons provide an appropriate benchmark for the arguments in favour of the necessity of state influence on the economy in Hungary. In *The Wealth of Nations,* Adam Smith argues in favour

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of an "invisible hand", or the invisible state, in a period when England had already become the most developed state of the world. However in one of his earlier works (entitled *Inquiry into the Nature and Causes of the Wealth of Nations*), he determined the tasks of the state, and of the ruler who managed the state, in a positive sense. These include the protection of society, the obligation to operate the administration of justice and running public utilities and public institutions. In order to be able to meet these expectations, the state needs to be strong. These are the developments currently in progress in the post-Soviet region, especially in Hungary In other words, the state must create the framework conditions of asset management policy and corporate operation, and when required, it must reconsider and restart the procedure, just as after the feudal mode of production or in the period that followed the world economic crisis after the millennium entailing a budget weakening.

Notes

1 It is important to note that due to constraints on length, this sketch only provides limited academic information, however, the book entitled: *A magyar állampénzügyek fejlődéstörténete a dualizmus korától napjainkig. Nyugattól keletre, Kelettől nyugatra* [The evolution of public finances in Hungary from 1867 to our day. East from West, West from Asia] (L'Harmattan Publishers), published early in the summer of 2019 offers ample data. This work is available in English (under the title *East of Europe, West of Asia)* since the beginning of 2020 and in Chinese and French since the spring of 2020. The apposite subtitle East of Europe, West of Asia refers to the unfortunate "inbetween" character of the Hungarian economic policy, interposed in the middle of Europe, not merely in a geographical sense of the word.

2 Catching up, *mutatis mutandis,* is always a matter of closing the gap to a more developed entity.

3 The Kingdom of Hungary, torn into three as a result of the Ottoman Empire's conquest, was under the constant pressure of uninterrupted wars, and then from the 17th century, after the Turks had been thrown back, subjugation to the Habsburg Empire had an unfavourable impact on the country's economic development. The fact that the Habsburg Empire, including the Kingdom of Hungary, was left out of the world's new economic trends (e. g. from the economic expansion resulting from the discovery of America) considerably limited its positions and economic standard, and the empire gradually degraded into a medium power. Its social conditions were characterised by a late rise of the middle classes and by inherited serfs, an institution that evolved everywhere east of the River Elbe in the 16th and 17th century, and achieved its full purpose in Hungary in the 18th century. Its evolution was closely related to the reduction, termination or absence of institutions and relations based on goods, which considerably slowed economic growth in the Eastern and Central European region, as the conservation of the feudal conditions prevented the financial fulfilment of the most important element of the economy: man, while the other important factor of production, namely, land was not negotiable (it could not be sold or mortgaged). Inherited serfdom essentially means that serfs were inherited like goods and were not allowed to move from the land they toiled (they were "earthbound"), in other words, the ownership rights of the serf and the land belonged to the landlord and his successors. This also included serfs not obtained by the landlord but inherited from his forefathers. The use of this term spread for the most part on the basis of F. Engels's works.

4 At the beginning of the 19th century, the idea of economic and political independence came to the foreground. This period is called the Age of Reforms, however, in the wake of the largest European capitals, by the spring of 1848 this had evolved into a revolution and then an armed war of independence, which was bloodily put down at the end of the summer of 1849 by the army of the Russian Empire, which hastened to the assistance of the Austrian emperor and heavily outnumbered the Hungarian rebels. The statutes adopted in April 1848 (voted for by the very last National Assembly of the nobility), terminated

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the nobility's tax exemption and the taxes and duties payable and services provided to landlords by serfs free of charge, and eliminated serfdom.

[5] Initially, the two decades that followed the 1848–1849 War od Independence up to 1867 only saw retaliations by the Austrians and passive resistance by the Hungarian nation. Following the Austrian example, a "Prussian" kind of tax administration was adopted, which created the basis of public finances. Although at that time the nation contemplated it belligerently (refusal to pay taxes was high), subsequently it benefitted from the system. The Habsburg Empire, which repeatedly lost wars on various European battlefields and suffered from its shrinking political influence, and the Hungarian society, wishing to develop, were driven towards a compromise, which finally took place in 1867 on the basis of mutual interests.

[6] One of the most important element of the economic compromise concluded with the Habsburg Empire (or the "Austrian Emperor") in 1867 was the commons customs border, which protected the producers of the empire, as a kind of a protectionist instrument.

[7] Source of data: Berend and Ránki, 1972, p. 79.

[8] Source of data: Sándor, 1954, p. 201.

[9] Based on Marx, 1909 and Nagy, 1977.

[10] Act IX of 1848 abolished services provided to landlords free of charge and the administration of justice by squires and Act XIII of 1848 terminated the obligation of tithing.

[11] Mention should be made within this framework of Act XV of 1848, which abolished the ban on selling the inherited estates of noblemen, allowing the sale and mortgaging of property, and thus facilitating the movement of capital.

[12] Act XXXVII of 1875 on commerce and trade.

[13] This was an army development programme with a budget of one billion pengő, with a term of five years set by the Darányi Government.

[14] The Peace Treaty of Trianon and its consequences are detailed by historian Béla Makkai (Makkai, 2019).

[15] The Yalta Conference declared Hungary to belong to the area within the control of the Soviet Union, similarly to other, surrounding Eastern and Central European countries, before the end of the war.

[16] Easing the framework of the bigotric and rules-based soviet type Hungarian planned economy started in 1955. In 1956, first in the soviet-controlled area after World War II, armed combat broke out in Hungary. Although vastly more numerous soviet troops stifled the 1956 Revolution and War of Independence, the same normative soviest economic policy could no longer be enforced in the People's Republic of Hungary. One of the consequences of the implementation of the 1968 reform gained Hungary the reputation of the "most cheerful barrack" in the Easter block. Initially, improvement in the standard of life was financed from a more efficient enforcement of financial interests, and later on, after the (unfortunate) moderation of the former, from foreign loans and borrowing. By the end of the 1980's, the economy of the Hungarian People's Republic, which was "operated" from western loans, went bankrupt economically and politically.

[17] The Hungarian industry, which was compelled to import energy, received mineral oil within the framework of COMECON, mainly from the Soviet Union, for a price based on the average world market price of the previous five years. Although this was a discount, primarily after the outbreak of the 1973 world market oil price, this delayed effect pampered the Hungarian economy, made it energy-wasting and deteriorated its efficiency, and consequently it increasingly slipped back in the world market competition. As a simultaneous problem, as a result of curbing financial interests from the 1970's employee motivation, discipline and performance dropped. As the institution of socialism, and simultaneously, both employee and corporate interests were cut back, so the Hungarian economy's dependence on external loans increased. Instead of more efficient production, the standard of living was improved by increasingly intensive borrowing.

[18] Appreciating the school-forming work of János Kornai, the best known Hungarian economist, mention should be made of the fact that Kornai considered the application the soft budgetary limit and feed-through of this phenomenon as a flaw not only of socialism but also of the two decades of transition to a market economy, and especially of the proactive state model applied after 2010. These problems are also

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tackled below, however, it is important to point out right here that the flawed economic policy, which did not match either the endowments and requirements of the productive resources or the production and social conditions, were "created" from top to bottom, and moreover, imported (whether from the soviet planned economy or from the Anglo-Saxon neoliberalism), including the economic practice ("only") forced on companies (and did not evolve at that level), was the principal cause of mass losses. Thus arising from the peculiar features of the system, it was the elimination of the "optimum" market during the socialist planned economic system and the application of coarse market rules during transition to a market economy that triggered the bankruptcy of masses of companies and banks. In these cases the rescue of companies and banks (after all this) was a "moral obligation", as the state made efforts at preventing the wide spread of bankruptcies and society's sinking into anarchy.

[19] For more details about the state consolidation of Hungarian local governments that went bankrupt in the framework of a neoliberal market economy operation (and the application of the soft budgetary limit), see Lentner, 2014.

[20] Transition from the socialist planned economy into a rude market economy started as early as the end of the 1980's, during the planned economy "managed" by the Hungarian Socialist Party. However, this was a forced procedure. The participants of the system were helpless and had no concept, but they endeavoured to save their power, and so they allowed spontaneous privatisation, in other words, the acquisition of assets and property by those affiliated to the system. Moreover, at state companies the management discipline completely eroded. In such an economic policy practice of "turning the bull loose", abuses were made in masses. The commencement of the market economy was not an ethical procedure at all. Simultaneously, sanctions were mitigated and moreover, due to the absence of preparedness by the law enforcement agencies, most of the mismatches and anomalies became blurred and faded away. The political changes that resulted in a multi-party system were brought about by the 1990 general elections, however, the situation did not improve, at least initially, with the adoption of a raw and "rootless" neoliberal market economy in Hungary. With the change of regime, the "good" part of the old system (government planning, coordination and control) were also discarded, but an efficient new system (including the quick decomposition of state ownership and the moderation of regulation and control) was not set up.

[21] In the publications by Péter Mihályi, this is a repeated assumption about the start of the change of regime. See, for example: Mihályi, 2010 (quote from page 5).

[22] Decentralization, Privatization, Management.

[23] In fact, the "mandatory reductions in utility bills" started during the "period" when most of the public utility service providers were in private hands. For further details of this process, see Lentner, 2015.

[24] Centralization, Nationalization and Public Good. For further details see a CNPG model, see Lentner, 2017.

[25] The authors give account of the operation of public utility companies, which is, for the most part, not cost efficient and does not comply with the relevant statutes, including the Accounting Act. The fact-finding activity performed by SAO, and according to the report of the auditors, the restoration of compliance and the continuation of operation with the approach expected of a careful owner may release additional reserves at public utility companies and may lay the basis of further reductions in prices and charges.

[26] Based on Bianka Parragh's position, the act on business organisations, which entered into force in 1989 and the act on transformation, also effective sing 1989 (Act XIII of 1989) gave corporate self-governments ample room for manoeuvre. See Parragh, 2014.

[27] Mihály Tóth, a specialist of this topic, thinks that a small fraction of the criminal offences can be related to the privatisation performed at the time (Tóth, 1995). This is due to the fact that the law enforcement agencies were unprepared and the cases were complex, and these made the recognition of non-compliance more difficult.

[28] Based on the competitiveness research conducted by Attila Chikán and his colleagues (Chikán et al., 2019), gave a dismal view of the period between 1995 and 2018.

[29] For more details on the operation of the post-2010 proactive state model in the economic space, see the works of György Matolcsy, László Domokos and Árpád Kovács.

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[30] At the same time, in relation to the "regularities" and sustainability of the "illiberal" economic policy practice, László Csaba expresses his doubts (Csaba, 2019), while Péter Mihályi and Iván Szelényi assign low value to the role of the layer of businessmen, dependent on economic policy (EU funds) and on actual politics, in the effective productive sectors and think that over the longer term they will be pushed to the background (Mihályi and Szelényi, 2019). It is, however, a fact that Hungary's economic positions improved considerably after the 2010 change of government.

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Dániel Molnár and Gábor Regős

The Change of Government Debt Management in the Visegrád Countries

Summary

Management of government debt in Hungary is a particularly important task, as the country has a relatively high level of debt above 70 per cent of GDP, despite its declining trend in recent years. The same indicator is lower in the other Visegrád countries, in Czechia, Poland and Slovakia, it is between 32 and 49 per cent. Since 2010, the Hungarian Government Debt Management Agency has also placed considerable emphasis on making public debt financing more secure and has achieved significant results. In terms of managing public debt, three types of risk factors are distinguished and are called 'original sins' in the economic literature. The first one is indebtedness in foreign currency, the second one is short-term indebtedness, and the third one is indebtedness to foreigner investors. This study examines the effects of these three risk factors from a theoretical point of view. The evaluation of these risk aspects between 2010 and 2018 in Hungary is also presented in comparison to Czechia, Poland and Slovakia. The results obtained suggest that at present Hungary and Slovakia are in a better position than directly after the crisis in two parameters, and Czechia has improved in one, while Poland has increased its risk exposure in all the three criteria.

Journal of Economic Literature (JEL) codes: E44, F34, H12, H63, H74
Keywords: government debt, original sin

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Introduction

Professional discourse on public debt is mostly about its size relative to GDP, and this is the only debt indicator even in the Maastricht criteria of euro adoption. However, the indebtedness of a country and the stability of its debt are defined by many other factors as well: the composition of the debt (foreign currency or domestic currency), its maturity structure, and the actors (domestic or foreign, household or financial institutions) holding it. A combination of all these influence public debt and the government's room for easing in a turbulent period. In this paper the evolution of the current structure of Hungarian government debt is tracked down from the 2007–2008 crisis and compared to the other Visegrád countries (Czechia, Poland and Slovakia).

After a presentation of the evolution of public debt in the surveyed countries, developments in the main structural indicators between 2010 and 2018 are described on the basis of the "original sin" concept, coined and elaborated by Eichengreen and Hausmann (1999) and Eichengreen et al. (2002). This is to assess the extent the countries of the Visegrád Group are prepared for a possible future crisis and the adverse effects of a low level of preparedness on debt.

Developments in government debt and interests

The high level of government debt has an effect on the country's growth prospects. Reinhart et al. (2012) illustrated that very high government debt, above 90 per cent of GDP, slows economic growth: they measured an average 1.2 per cent point slower growth rate in periods with high indebtedness compared with periods when the debt level was below this rate. Thus, it is worth examining how indebtedness developed in the Central European region. Government debt to GDP changed differently in the various countries of region between 2010 and 2018: in Czechia, it decreased by 4.7 percentage points to 32.7 per cent, in Poland by 4.2 percentage points to 48.9 per cent and in Hungary by 9.4 percentage points to 70.8 per cent. In contrast, in Slovakia, public debt increased from 41.2 to 48.9 per cent per of GDP in the reviewed period. The reason behind Slovakia's growing debt is a looser fiscal stance. The primary deficit (deficit indicator excluding interest income and expense) of the Slovakian budget was on average 1.5 per cent of GDP between 2010 and 2018, while the primary deficit in Poland was 1.3 per cent and in Czechia 0.2 per cent. In contrast, the Hungarian budget, excluding interest payment, had a 0.9 per cent surplus on average between 2010 and 2018, which significantly contributed to a substantial reduction in public debt despite the higher interest burden resulting from higher indebtedness. It was achieved by a fiscal policy discipline and the fact that reduction in the public debt to GDP ratio was made a government priority. It is called "fiscal turn", while in the 8 years before 2010 opposite developments took place: as a result of high budget deficit, the debt ratio rose from 55.3 to 80.2 per cent of GDP in this period.

It is worth noting that before the 2008 crisis, not only the state suffered from excessive indebtedness in Hungary but also companies and households. Similarly to public

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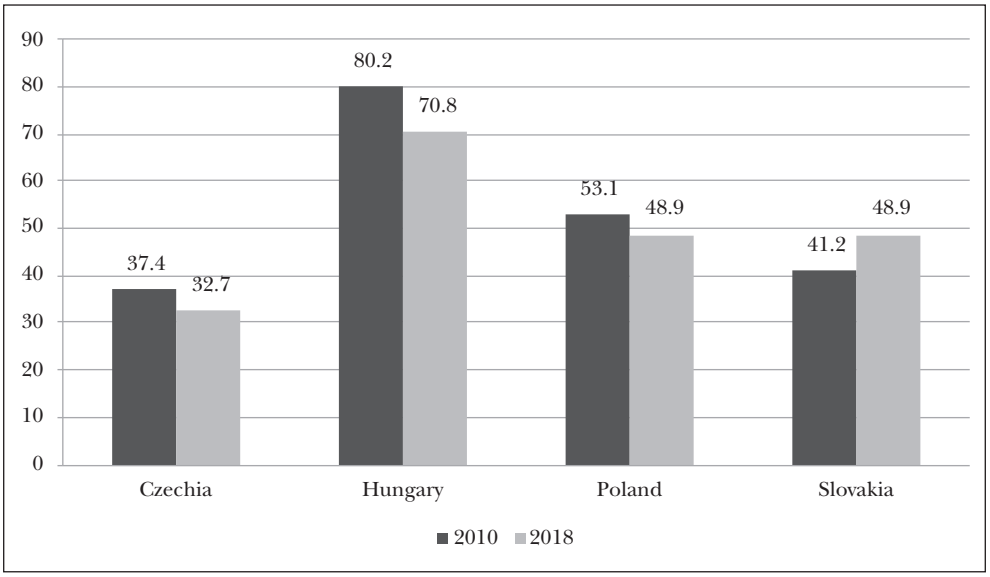
debt, in addition to the volume of borrowing, the structure of the debt portfolio, i.e. the share of foreign currency loans in household lending was significant, as their repayment caused problems after the crisis. As a result of the unfavourable experience in lending, which was restarted to enterprises under various programmes (different phases of the Growth Credit Programme) led by the National Bank of Hungary.

The level of public debt is regulated by the Maastricht criteria, which include the requirements of joining the euro area, also as a general rule applicable to the members of the euro area. IN theory, an EU Member State wishing to join should not have debt exceding 60 per cent of GDP, but in practice, the European Central Bank also accepts continuously decreasing debt. Hungary applies a stricter fiscal rule, also included in the Fundamental Law: as long as the public debt exceeds 50 per cent of GDP, Parliament can only adopt a budget that reduces the government debt relative to GDP. In addition, according to the Stability Act, if both the inflation and real GDP growth exceed 3 per cent, rise of the nominal public debt cannot exceed the difference of the inflation rate and half of the real GDP growth rate recorded in the previous year. The Hungarian regulation is special because it applies not only to planning and approvale but also to implementation (Kovács, 2016).

Chart 1: Government debt to GDP (%)



Source: Eurostat

In addition to the government debt to GDP, it is also important to examine a country's spending on interest each year, as it demonstrates the actual cost of public debt. According to the Eurostat data, in Czechia, the interest paid by the budget fell from 1.3 to 0.8 per cent of GDP between 2010 and 2018. Over the same period, interest expenditures fell from 2.5 to 1.4 per cent of GDP in Poland and from 4.1 to 2.5 per

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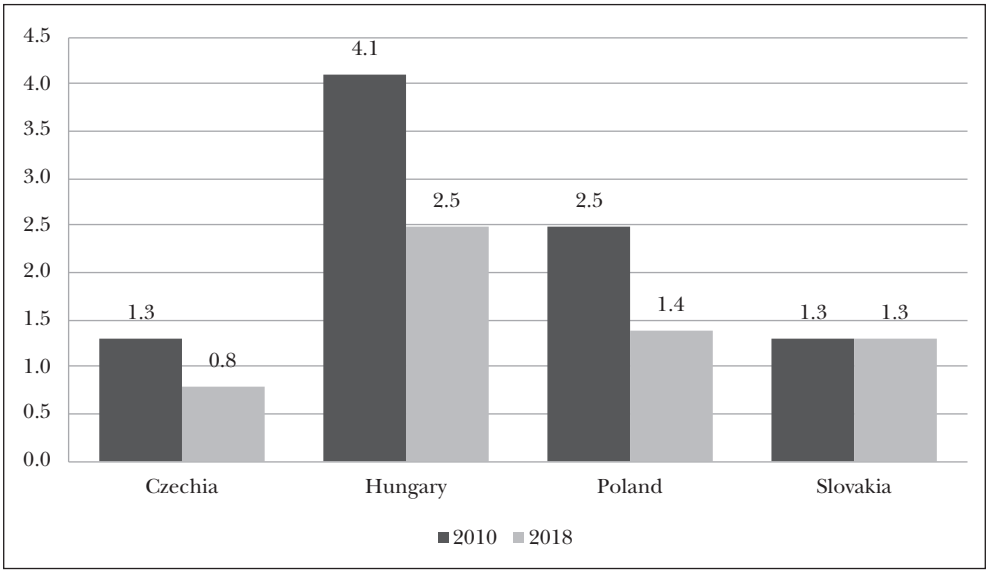
cent in Hungary. In Slovakia, despite increase in public debt, the interest rate to GDP remained unchanged. Reduction in interest is extremely important for governments, as it allows use of the available resources for economy development, increases competitiveness and improves welfare through social benefits.

Chart 2: Interest payment to GDP (%)



Source: Eurostat

Decline in interest in Czechia, Poland and Hungary can also be explained by the low-interest-rate environment, which also explains why the Slovakian interest expenditure did not rise in parallel with the rise in public debt.

In 2010 secondary market yields were the highest in Hungary: on a 1-year maturity yield was 6.5 per cent, while over a 3-year maturity it was around 8 per cent. However, by the end of 2018, yields had declined significantly: on a 1-year maturity, the government was only able to issue bonds at a rate of 0.45 per cent, and 10-year yields had also decreased by more than 5 percentage points during the examined 8-year period. The data are somewhat misleading because due to changes in the international environment, yields had already risen in 2018. Yields were influenced partly by monetary policy between 2010 and 2018. At the end of 2010, the central bank base rate stood at 5.75 per cent, which had dropped to 0.9 per cent by the end of May 2016. However, the National Bank of Hungary influenced yields not only by changing the base rate but also by launching various programmes to reduce them (Lentner, 2018). In addition, the favourable international environment and the improving perception of Hungary also contributed to decline in interest rates. This is clearly visible in the change of 5-year CDS spreads, which is a country-risk indicator: its value was 386.75 basis points in Hungary at the end of 2010, the highest value in

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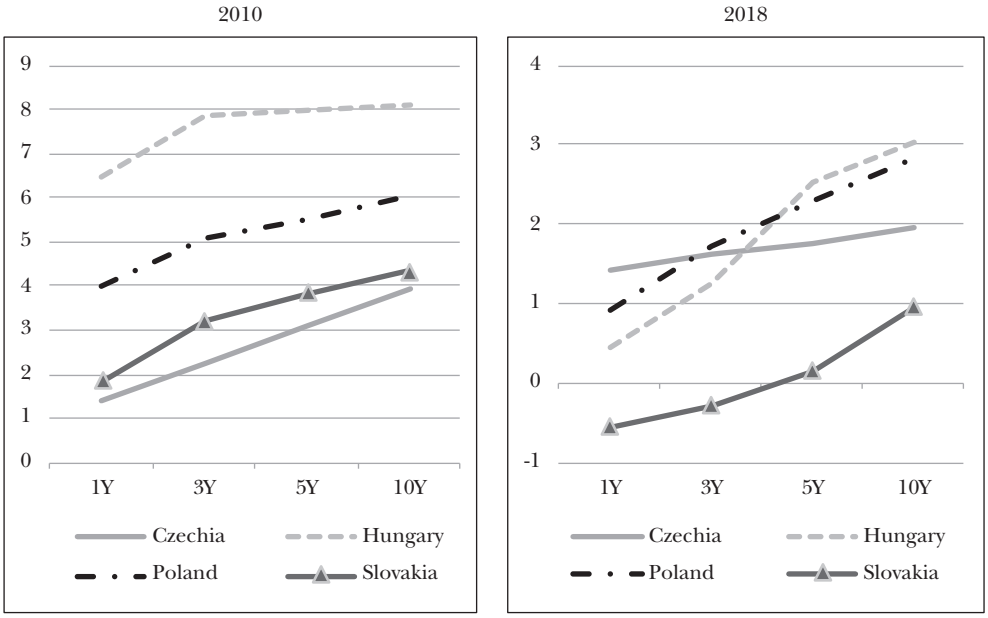
the reviewed four countries, but it had decreased to 88.14 basis points by the end of 2018.

Similar developments have occurred in the case of the other countries in the region. In Poland, the short, 1-year yields fell from 4 per cent to 0.9 per cent, while the long-term 10-year yields fell from 6.1 to 2.8 per cent. Similarly to Hungary, monetary policy also had a significant impact on the yield curve in Poland. At the end of 2010, the base rate of the National Bank of Poland stood at 3.5 per cent, while in 2018 it was only 1.5 per cent. In addition, perception of the Polish economy had improved significantly: the value of the 5-year CDS spread fell from 146 basis points to 67.55 basis points in the period reviewed. However, the 2018 developments had a different impact on the Polish indicators than on Hungarians: yields could decrease further but the CDS spread slightly increased by nearly 12 basis points.

Chart 3: Yield on the last day of the year (%)



Note: For Slovakia, the 5-year reference yield at the end of 2010 is the authors' estimate Source: Reuters Datastream

Yields decreased the least in Czechia during the period under review, as a result of several factors. On the one hand, the Czech yields were the lowest in the region at the end of 2010: 1.4 per cent on one-year maturity and slightly below 4.0 per cent on the ten-year maturity in the secondary market. Thus, there was only a very slight room for the decrease in bond yields up to the end of 2018: it declined to 1.9 per cent on the ten-year maturity, 1.7 per cent on the five-year maturity and it has not changed on the one-year maturity. Another factor that contributed to this was that the Czech National

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Bank's base rate was already at a low 0.75 per cent in 2010. The European Central Bank started a tightening policy in 2018: it increased its 0.05 per cent base rate in two steps to 0.5 per cent in the second half of 2017, and then to 1.75 per cent in 2018. It also had an impact on bond yields because there were negative yields on the five-year maturity in the secondary market in the case of Czech government bonds at the end of 2016. Similarly to Hungary and Poland, the Czech five-year country risk premium also fell during the analysed seven-year period, although slightly: from 91 to 40.86 basis points, the lowest among the Visegrád countries.

While in Slovakia yields were still between 1.8 and 3.8 per cent on the one-year and five-year maturities at the end of 2010, on the three-year maturity they went into the negative at the end of 2018, but at the maturity of five years, yields were also at a minimum 0.15 per cent. The ECB's monetary policy, which had a direct impact on Slovakian yields and an indirect one on the other yields in the region, played a key role in creating negative yields in Slovakia. The ECB's base rate was still 1.0 per cent at the end of 2010, which then gradually decreased to 0 per cent. Besides, the ECB's bond purchase programme had a significant impact on bond yields. From July 2009 the ECB implemented asset purchase programmes, but the Public Sector Purchase Programme (PSPP), the most significant one of all, only started in March 2015. In the PSPP the ECB buys government bonds issued by the Member States of the euro area, as well as bonds issued by acknowledged agencies, regional and local governments, international organisations and multilateral development banks. Within this framework, the central bank bought bonds for more than net EUR 2170 billion at the end of 2018, of which nearly 90 per cent were government bonds issued by Member States. This had a significant impact on yields at the long end of the yield curve. In the case of Slovakia, the European Central Bank had bought Slovakian state bonds for nearly net EUR 11.7 billion in the framework of its asset purchase programme by the end of 2018, which represented 26.5 per cent of the country's public debt in 2018. As the other three Visegrád countries are not members of the euro area, they were only be indirectly affected by the asset purchase programme through the rearrangement of investor portfolios. However, the Slovakian 5-year CDS spread was still the lowest among the Visegrád countries (83 basis points) partly also because of the euro area membership, and then it decreased to 48.58 basis points. Consequently, besides the favourable yield environment, improvement in Slovakia's perception has also contributed to decline in yields.

Consequently, the Visegrád countries could benefit only slightly from the favourable market developments (loose monetary policy and significant improvement in the international perception of the region) to reduce their public debt, and moreover Slovakia was characterised by increasing public debt relative to GDP, despite the unconventional monetary policy of the European Central Bank. In spite of this, countries in the region are in a favourable situation because the debt ratios of Czechia, Poland and Slovakia are considerably below the Maastricht threshold of 60 per cent and the Hungarian indicator is also 9.2 percentage points lower than the EU average.

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The role of foreign currency debt

The literature on debt management contains the concept of the "original sin", which was adopted by Eichengreen and Hausmann (1999), and by Eichengreen et al. (2002). In these papers, the authors considered three cases as original sins.

The first type of original sin is a case when a country is unable to issue bonds in its own currency abroad, and so the country is compelled to issue them in foreign currency. Depending on the share of foreign currency funds, this may cause several adverse effects on the country:

– An open foreign currency position is generated in the country's balance sheet, raising the debt level denominated in domestic currency in the case of severe exchange rate fluctuations or significant depreciations of the domestic currency exchange rate;

– The central bank must pay particular attention to avoid unfavourable exchange rate movements when setting the base rate, and this reduces the effectiveness of the monetary policy;

– The central bank is forced to maintain significantly higher foreign exchange reserves, and this also means higher costs;

– Foreign exchange debt, therefore, limits the central bank in preventing liquidity crises and fulfilling its lender-of-last-resort role;

– High FX debt increases the risk premium and downgrades credit rating;

– The volatility of capital flows increases in the country.

Olivier (2002) confirms Eichengreen's and Hausmann's (1999) assertion and highlights that certain less developed countries are unable to finance their public debt by issuing domestic currency denominated bonds abroad or on a long maturity. Instead, less developed countries finance their public debt in foreign currency, through the issue of government bonds abroad. As a result, they are more vulnerable to financial turbulences. The author undoubtedly blames the lack of credibility of the monetary policy for rising foreign exchange indebtedness. The more credible a monetary policy, the higher the chance to issue long-term government bonds in domestic currency.

Claessens et al. (2007) examined a new aspect of foreign currency indebtedness and used panel data to show that not only the size of the economy but also the extent of the domestic financial system (measured as loans for the private sector and stock market capitalization) also plays a role in the development of bond markets with higher domestic currencies. If such a market emerges, the state is less compelled to issue bonds in foreign currency.

In spite of the above, the argument for indebtedness in foreign currency is mainly that government securities become available to a broader investor base, and this results in lower yields than in indebtedness in domestic currency. In addition, the government and the central bank have access to foreign exchange and there may also be political benefits for their presence in certain foreign markets.

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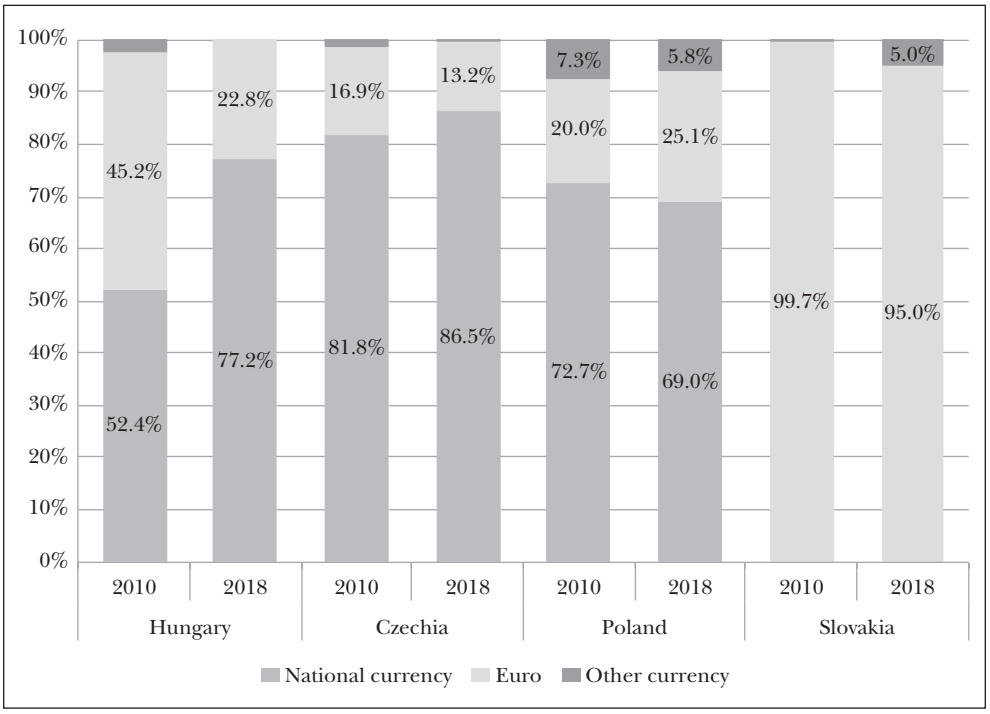
Chart 4: Composition of the Maastricht debt by currency



Source: European Central Bank

The share of the Maastricht debt denominated in foreign currency varied differently in the Visegrád Group. In Czechia, it decreased slightly, from 18.2 to 13.5 per cent, and in Hungary significantly, from 47.6 to 22.8 per cent. In contrast, the ratio of public debt denominated in foreign currency increased from 27.3 to 31.0 per cent. The role of foreign currency in public debt was the lowest in Slovakia in 2010 and in 2018 as well. However, Slovakia's situation is partly different from the other Visegrád countries: as a member of the euro area, the Slovakian central bank does not have the same level of influence on its own currency as the monetary policy-makers of the other three countries, and therefore it has less room to change the size of the debt.

However, it is important to highlight that the above chart about the FX debt by currency is somewhat deceptive because of the European Central Bank's methodology. For example, in Hungary, only 42.3 per cent of foreign currency debt was denominated in euro at the end of 2018, based on data from the Government Debt Management Agency. However, the debt manager performs swap operations to convert the total cash flow (capital and interest liabilities) of the issued debt denominated into euro, and thus the debt only runs the forint-to-euro exchange rate risk.[1] In addition to the euro, the Hungarian state also issued government securities in dollar, Japanese yen and Chinese yuan, the latter two on the local markets (Samurai and Panda bonds). The 2017 Panda bond issue was extremely important for Hungary: as a result, the

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Hungarian State became the first foreign issuer to have yuan bonds issued both in the internal (Panda) and in the external (Hong Kong) market, and the transaction was part of the "One Belt, One Road" Initiative of the Government of China. The Polish public debt manager executes swap operations similarly to Hungary, although not for its total foreign currency debt. In 2017, 78.3 per cent of the Polish foreign currency debt, including swap operations, was denominated in euros, 12.9 per cent in dollars, 5.5 per cent in Swiss francs and 3.3 per cent in Japanese yen. The Czech public debt manager only ran the euro-to-koruna risk.

As a conclusion it can be established that while public debt exposure to the first original sin has significantly decreased in Hungary, has reduced slightly in Czechia, and has increased in Poland. Slovakia is not exposed to the first original sin in the classical sense of the term, due to its membership in the euro area. But it is important to note that exposure of the debt to foreign currency is a high risk in terms of finances, and it is not an optimum strategy for debt management bodies to fully terminate this kind of debt, as it has its advantages, and with swap transactions the risk can be reduced significantly.

Maturity of the government debt

According to Eichengreen and Hausmann (1999) and Eichengreen et al. (2002), the second type of original sin is to be indebted in the short-term. The problem arises when a country is unable to finance its long-term debt with fixed interest rates, so the risk of renewing funding can be high. Thus an increase in the remaining maturity of a debt is welcome because it reduces the vulnerability of the debt issued in domestic currency.

Stein (2012) specifically emphasizes that in the case of significant or predominantly short-term financing, individual actors (bank intermediaries) underestimate the social costs of fire sale generated by individual market players. Banks can decide to increase their capital or sell their financial assets in order to improve their solvency. Both lead to a prudent operation on a micro-economic level, but if banks choose the latter massively, the prices of financial instruments may fall drastically, which leads to systemic risks. A similar situation evolves when certain countries are primarily indebted in the short term and underestimate the importance of liquidity constraints and interest rates/yields increase when government bonds are renewed.

In contrast, Greenwood et al. (2015) point out that governments can also pursue macro-prudential policies through the management of public debt. If the state is indebted in the short term, it displaces the private sector's short-term liabilities and directs them towards longer maturities. According to the authors, the government should be indebted in the short term as long as the social costs of short-term indebtedness fall short of the private sector's money generation costs. In other words, the state should be indebted in the short term until it has a comparative advantage over the private sector in issuing risk-free financial instruments. Among the costs of short-term indebtedness, the authors highlight the fluctuation of taxes. Angeletos (2002) points

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out that a change in the tax system, in any case, reduces social welfare, and thus the government must always strive to ensure a stable tax system. This is only possible if the change in the debt perfectly compensates the changes in budget expenditure and in the tax base (given that the present value of taxes is equal to the sum of the present value of expenditures and debt service). In the case of short-term indebtedness, the government has to react to the fluctuations in the budget balance by raising taxes (and increasing debt in order to smooth taxation), but if it is indebted in the long term, the market value of bonds decreases during a crisis, resulting in profits for the state, thus compensating the rising expenditures and declining tax revenues.

Broner et al. (2013) analyse the reasons for the fact that emerging countries (EMEs) primarily issue short-term bonds as opposed to long-term financing. They find that this is mainly due to the fact that short-term financing is cheaper than long-term financing. During a crisis, the interest rate/yield difference between short- and long-term bonds (term premium) increases. This shifts the government securities portfolio even further towards short-term financing and shorter average maturity. In addition, Missale and Blanchard (1991) argue that in economies with high public debt the government is forced to reduce the maturity in order to maintain its credibility and ensure investors that it is not its goal to vanish public debt through increased inflation.

However, it is important to draw attention to the duality of maturity too. The long maturity is favourable during a crisis because rising interest rates appear only delayed in yields. Thus, the interest on the budget will only increase delayed, which means that budget resources can be used to alleviate the symptoms of the crisis. In contrast, if the economy has a long maturity at the start of a prosperity cycle then the resources are needed for paying the yields of government securities issued earlier in a crisis period (in a higher interest environment), and for repurchasing them before they expire. The optimum strategy is to increase the average maturity of the public debt as much as possible during the prosperity, and when the economy slows down and, if the market environment allows, issuing only in the shorter term.

Several indicators are available in the literature to measure maturity. Three are worth highlighting: the average time to maturity (ATM), the average time to re-fixing (ATR), and the duration. All the three indicators measure the maturity of public debt but taking into account different types of risk (Mohai, 2018). The average time to maturity is the weighted average of the remaining maturity in the government debt portfolio, thus showing the risk of renewing public debt. In contrast, the ATR takes into account that floating rate instruments may be repriced several times during maturity. Therefore, the indicator shows, in the case of fixed rate government bonds, the average of the remaining maturity, and the average remaining maturity until the next interest rate re-fixing for floating rate securities. Thus, the ATR primarily shows the interest rate risk of public debt, i.e. the time horizon of a potential rise in interest rate within the portfolio. Duration differs between the ATR and the ATM in several repects: it is based on market value instead of the face value and takes into account the payable interest due to maturity. However, due to the latter, it responds primarily

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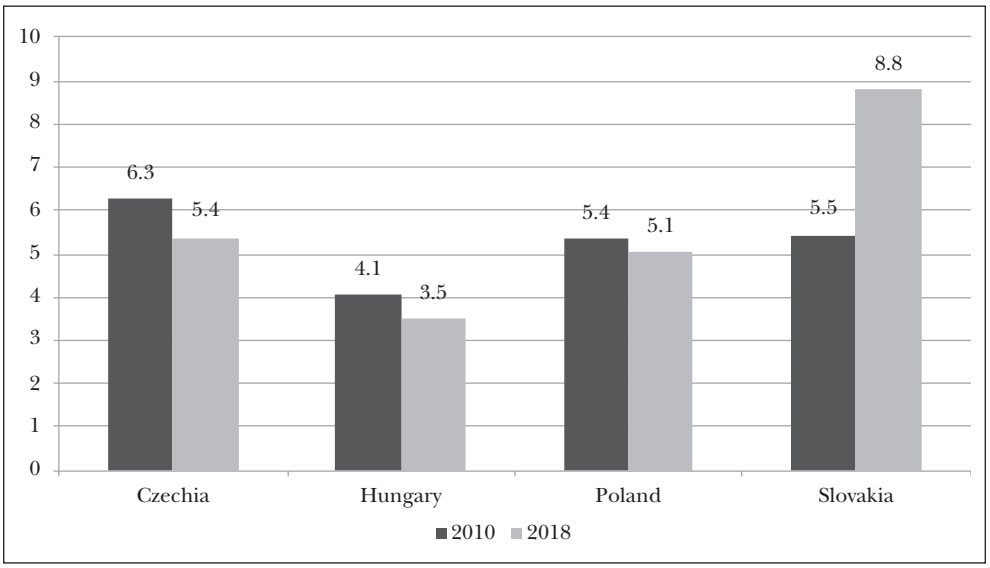
to changes in the market environment, which does not fundamentally affect public debt management and is therefore mainly used by investors. Nevertheless, several government debt managers use this indicator for setting benchmarks. Up to 2019 the Hungarian government debt manager used duration as a benchmark, but from this year it has switched to the use of the ATR, and the Polish and Czech government debt managers also include both the ATR and the ATM in their objectives. On the other hand, the Slovakian debt manager sets a target for the ratio of bonds maturing within 1 and 5 years for the refinancing risk. Similarly, in the case of repricing risk, they primarily look is at the proportion of bonds repriced within 1 and 5 years, while the duration is the secondary indicator.

Chart 5: Developments in the average time to maturity, ATM (year)



Note: October data for Hungary and June data for Poland in 2018
Source: Czech Ministry of Finance, Hungarian Government Debt Management Agency, Polish Ministry of Finance, ARDAL

The average remaining maturity decreased in three of the four countries: in the greatest extent in Czechia, by 0.9 years to 5.4 years, as against the target set by the public debt manager in the financing plan, being 6 years in 2018. The value of the ATM decreased in Hungary to a lesser extent by 0.6 years to 3.5 years. In Poland, data also show a decreasing trend, but it is important to note that in contrast to Czechia, in Poland the value of the ATM is still above the benchmark set by the government debt manager (minimum 4 years for domestic and 5 years for foreign public debt). Notwithstanding the above, the three countries were more exposed to the risk of renewal in 2018 than in 2010. By contrast, the average remaining maturity of the government debt portfolio rose significantly from 5.5 years to 8.8 years in Slovakia.

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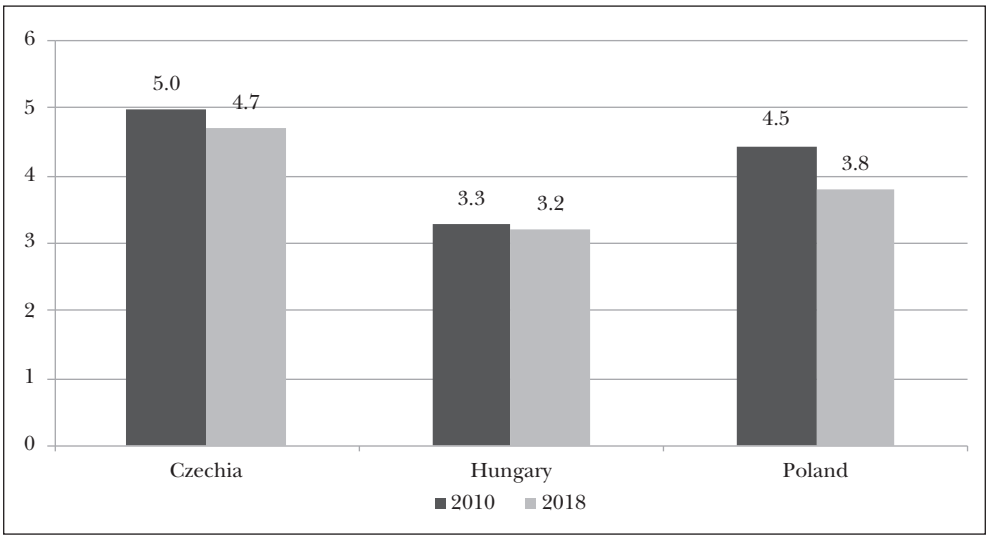
Chart 6: Developments in the average time to re-fixing, ATR (year)



Note: October data for Hungary and June data for Poland in 2018
Source: Czech Ministry of Finance, Polish Ministry of Finance, Mohai, 2018

A similar picture emerges for the ATR: the Czech indicator declined from 5.0 to 4.7 years, exceeding the 4-year target set by the government debt manager. The value of the Hungarian indicator decreased from 3.3 to 3.2 years, while the Polish indicator fell from 4.5 to 3.8 years.[2] In other words, the interest rate sensitivity of public debt portfolios increased slightly during 8 years under review in the three countries. However, the Slovakian government debt manager does not provide data on the ATR. This is mainly due to the fact that the government debt it manages is fully fixed, i.e. the repricing of floating rate bonds in Slovakia is not a risk when interest rates increasing.

It is worth noting the role of variable interest rates in other countries as it shows the difference between the ATM and the ATR. Only the European Central Bank's data series are available about this difference, but they fail to show the public debt managed by government debt managers, with the exception of the Maastricht public debt. Besides, in the database, the breakdown into fixed and variable interest rates applies only to government debts with a maturity of over one year.

The role of floating rate government securities is marginal in the region. Between 2010 and 2018, there was a slight decrease in Slovakia, while in Czechia the role of floating interest stagnated within the Maastricht public debt: in both economies, around 10 per cent of the government debt with maturity of over 1 year had floating interest rates. In contrast, in Hungary and Poland, the role of floating rate government securities increased significantly, by more than 10 percentage points, and as of 2018 more than one-fifth of long-term Polish debt had floating interest rates.

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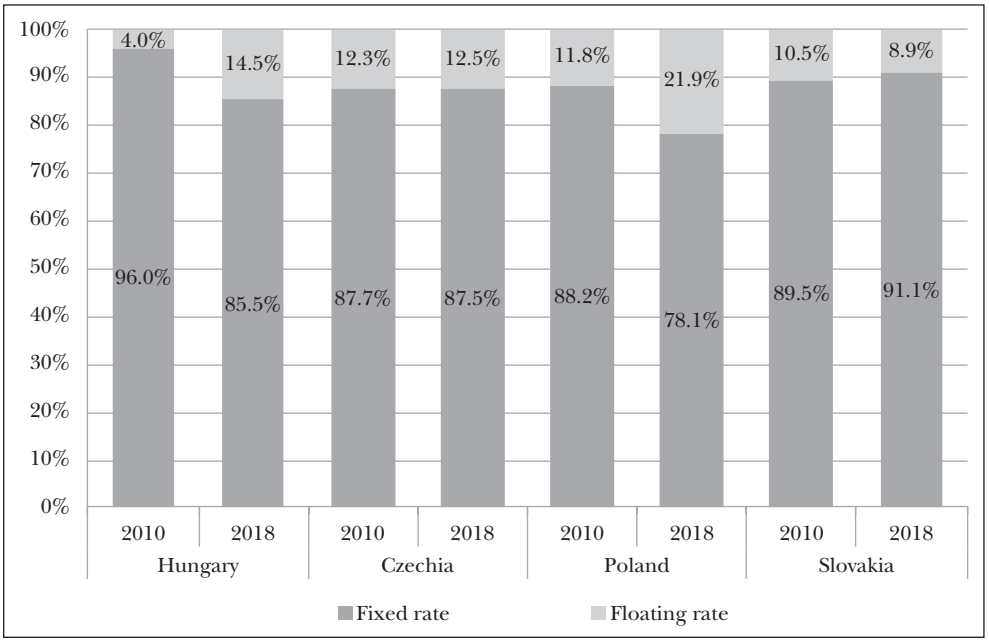
Chart 7: Long-term government debt (over 1 year) by interest type



Source: European Central Bank

Government debt by holder

For public debt management the ownership structure, i.e. whether the issued public debt is held by domestic or foreign actors, is also important. This is related to the third type of original sin, when a significant part of debt denominated in domestic currency is held by foreigners. In the domestic currency portfolio of foreigners the activity may be quite volatile, which can significantly outperform the behaviour changes of domestic market participants. This may affect the country in particular during a crisis. Yields can suddenly rise and sales by foreigners on the domestic secondary market can cause significant financing difficulties. In contrast, if a significant portion of government debt is held by residents then the interest paid by the state remains within the country and no capital outflow occurs as a result of interest payments.

In addition, Panizza (2008) emphasizes that companies in emerging countries often do not have access to the international capital market, and so the state acts as an intermediary either by providing guarantees or by issuing the amount needed. In addition, widening the domestic investor base may reduce risks, so the efforts made by decision-makers to this end should be supported but they should make significant compromises. Most of the emerging countries are unable to be indebted in the internal market over long maturities at an acceptable interest rate. The Polish data give a good illustration: at the end of 2017, the average remaining maturity of domestic Polish debt was 4.49 years, while that of foreign debt was 6.46 years.

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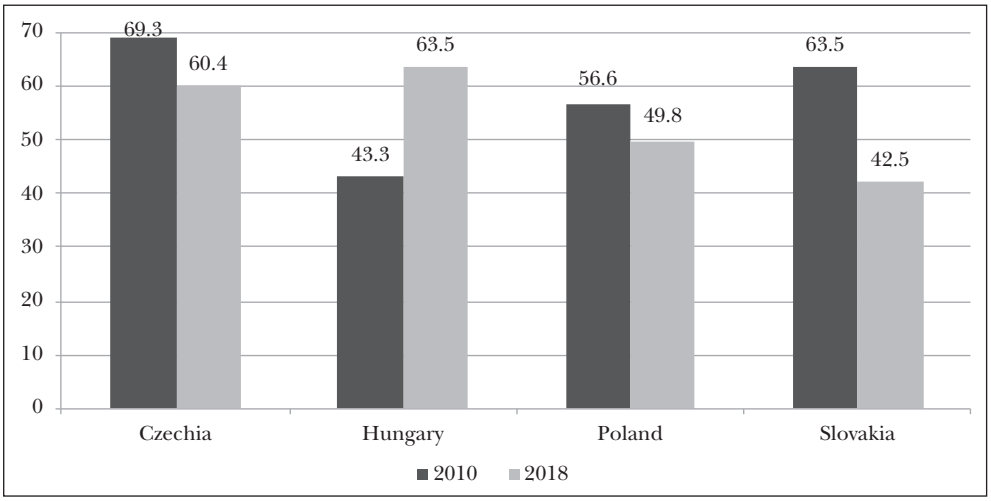
According to Panizza (2008), the presence of capital control may play a role in the success of internal indebtedness but the literature has various results in this regard. In addition, the author highlights the size of the internal market in terms of the success of internal indebtedness, but a wider circle of investors may cause problems if they are not well informed. Attracting foreign investors to the domestic market may have unfavourable effects on the volatility of capital flows and can lead to financial instability. Panizza emphasizes that despite the fact that indebtedness in the domestic market is more expensive, governments should use this form as the creation of the internal market can generate significant positive externalities.

A well-functioning domestic government security market can also contribute to the development of domestic financial markets, by increasing savings and investments. As government bonds are marketable instruments, they are suitable for trading in interbank markets, which improves banks' liquidity and thus reduces the need for monetary policy intervention. Besides, interest rates on government securities can also serve as benchmarks for financial actors to issue bonds that help the corporate bond market development. In addition, government bonds offer investors an alternative against foreign investment which can reduce capital flows and result in a return on savings, deepening the financial system (Abbas and Christensen, 2010).

Additional risks for domestic indebtedness in the domestic market include the crowding out effect. By issuing government securities domestically, governments absorb some of the savings that could be also used by the private sector, thereby reducing investment and slowing economic growth. However, this is only a problem in countries without an extensive financial system and with private sector players having no access to international capital markets. Besides high and safe yields, the banking sector is less motivated to finance risky projects, which can reduce investment activity.

Chart 8: Government debt held by residents (% of debt)



Source: European Central Bank

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According to the data of the European Central Bank, the ratio of foreigners was the highest in the Hungarian Maastricht debt among the Visegrád countries in 2010: the Hungarian state paid interest rates to abroad after more than half of its debt. By 2018, this had radically changed: domestic residents hold the majority of the public debt, and thus, they have the most important role in financing public debt. The other Visegrád countries have experienced opposite developments: the ratio of public debt held by domestic residents has decreased. As a result, in 2018 foreign ownership is in majority in Poland and Slovakia and the share of domestic investors have fallen by 8.9 percentage points in the Czech Republic too, but the 60.4 per cent ratio of Czechs is still considered high in the region.

In addition to the ratio of domestic to foreign ownership, the composition of investors (fund managers, banks, the central bank, households) holding government securities in the given country is also important. In Hungary, one of the key factors in the transformation of public debt management in recent years has been the encouragement of households' participation. There are two arguments for increasing this participation. Firstly, people are less sensitive to changes in the market environment, so it is unlikely that in a turbulent period they will decide to get rid of the government securities, which means a stable investor group for the government. Secondly, the budget pays interest to the population after government bonds, some of which is returned to the budget through consumption, in the form of taxes. The disadvantage is primarily higher cost: a sales network needs to be maintained by the public debt manager and the public should be familiarised with the bonds. In addition, the interest rates must be higher than those offered for institutional investors in order to make the individual schemes attractive.

The chart below shows changes in the role of the households in financing public debt. According to the European Central Bank's data, the share of the non-financial sector in government debt is marginal in Czechia, Poland and Slovakia. Slovakia does not offer government bond schemes to households, and although such government securities used to available in Czechia, they were withdrawn at the end of 2014. On the basis of the financing plans at that time, the Czech public debt manager continued to take into account household investors, however, in order to reduce the cost of sales they wanted to solve the sale directly by avoiding financial intermediaries. Since 2016 the public debt manager has no longer been counting on this segment due to declining public debt and interests.

In Poland households, foundations and social organizations can buy various government securities with maturity between 3 months and 10 years, at a nominal value of 100 zloty, through the PKO Bank Polski network. The role of the sector in the total debt remains low, although slightly increased since 2010. By contrast, in Hungary, the role of the non-financial sector increased significantly between 2010 and 2018. In 2010, the share of the sector was close to that of other Visegrád countries. However, by 2018 more than one-fifth of the total debt had been concentrated in the hands of non-financial players. In Hungary, growth in government securities held by households can be attributed to several factors. Firstly, various types of

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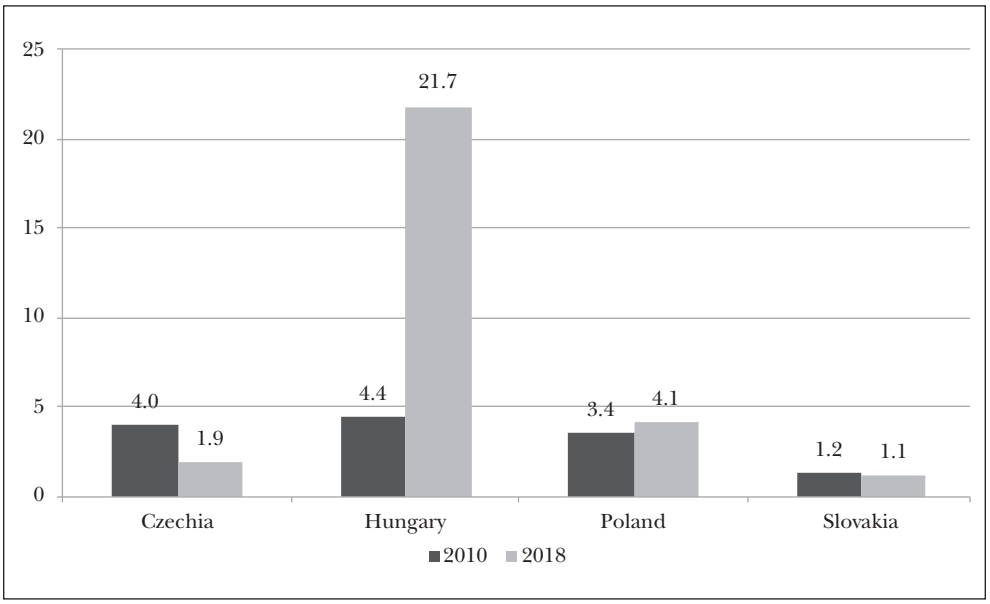
Chart 9: Government debt held by the non-financial sector (% of debt)



Source: European Central Bank

schemes (maturity, interest rate) are available for household investors, so it can be an attractive investment opportunity for individuals with diverse savings preferences. Secondly, the yields of the bonds are significantly higher than those of bank deposits, so they are very attractive for those who want to save, and are also widely known through the notable marketing activities of the Government Debt Management Agency.

According to the calculations of Kicsák (2016), the change in the Hungarian ownership structure, i.e. the growth relative to household government securities was not accompanied by an increase in budget expenditures, as higher interest rates were offset by rising tax revenues and lower market yields due to lower supply. Besides, the portfolio reorganization has reduced Hungary's external debt and thus its vulnerability.

In summary, among the countries of the region in Czechia, Poland and Slovakia, exposure to the third original sin increased between 2010 and 2018. In the case of the latter two, foreign owners had the majority of government debt. In contrast, domestic financing has become a core strategy in Hungary: with the involvement of household investors, government decision-makers have succeeded in getting foreign funding into the minority in public debt. However, the government is planning further advances: in the next 5 years in order to fully replace foreign financing, efforts are made at doubling the stock of household government securities (Kuti and Koroknai, 2019).

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Summary

In recent years significant changes have taken place in sovereign debt in the countries of the Visegrád Group. Due to the low-interest environment and to the more favourable international perception of the region, interest on public debt has significantly decreased in the V4. However, in Czechia and Poland, the government debt relative to GDP decreased only marginally, while in Slovakia it rose even further between 2010 and 2018. Hungary's public debt declined most (almost 10 percentage points) between 2010 and 2018, but it still remains the highest among the four countries. In Hungary, the reduction of the government debt to GDP ratio was primarily driven by the disciplined fiscal policy of the government, which was also supported by the low-interest-rate environment created by the National Bank of Hungary. The latter was made possible by the money surplus in the international financial markets. However, preparedness for a potential crisis is only partially reflected in GDP-proportionate public debt, it is also influenced by other factors of public debt. In recent years, Hungary has also taken steps to financing public debt in a more secure way.

This paper has shown changes in the structure of public debt in the Visegrád countries in respect of the original sins defined by Eichengreen and Hausmann (1999) and Eichengreen et al. (2002). The role of foreign currency debt, i.e. the first original sin, has declined significantly in Hungary and slightly in Czechia, so these two countries are in a better position than in 2010. In Poland, on the other hand, the role of foreign currency debt has slightly increased along with the exposure to the exchange rate risk, while in Slovakia nearly the total national debt is denominated in the domestic currency, namely the euro.

The literature considers indebtedness in the short term as the second type of original sin. There were unfavourable developments in the two analysed indicators, the average time to maturity and the average time to re-fixing. In Czechia, Hungary and Poland, the maturity of public debt have decreased, while in Slovakia it has increased significantly. In other words, the Visegrád countries were more exposed at the end of 2018 to the risk of renewal and interest rate than in 2010.

The third original sin is indebtedness to foreign investors. In this respect, only Hungary managed to secure a more favourable position during the reviewed 8 years, primarily due to the encouragement of household participation. In Slovakia and Poland, however, opposite developments have taken place: majority domestic ownership recorded back in 2010 has been replaced by foreign majority, and the role of non-residents has also increased significantly in Czechia.

In summary, the Visegrád countries have achieved mixed performance with regard to the three original sins: Hungary and Slovakia are in a better position than directly after the crisis in two respects and Czechia in one respect, while Poland has deteriorated in all three. However, the extent to which the countries in the region will be affected by the expected next crisis and the extent to which public debt is crisis-proof, remain a matter of concern.

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Notes

[1] The European Central Bank shows the composition of government debt taking into account FX swap operations.

[2] The Polish public debt manager only sets an ATR benchmark (2.8–3.8 years) for domestic public debt, which was achieved in June 2018 (3.24 years).

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Róbert Tóth, Krisztina Szük, Boglárka Szijártó and Krisztina Sisa

The Role of Modern Day Education and Qualified Workforce in Improving Corporate and National Economic Competitiveness

Summary

To boost economy, it is essential to enhance the research and development performance of secondary and tertiary educational institutions, which can contribute to increased performance in the whole profit and non-profit sphere. This can in turn help improve national economic performance (GDP). In our view, it is also worth examining education and competitiveness at the regional level. With a view to achieving strategic objectives aimed at boosting Hungarian economic performance, special attention must be paid to improving research and development regionally in the future. Competitiveness of the national economy can be viewed as the synthesis of regional competitiveness. There is a need for the reinvention of the whole structure, as well as the structural, methodological and financing background of vocational training, the adaptation of international best practices, not only for the sake of convergence in underdeveloped areas and regions lagging behind, but also for improving the competitiveness of the national economy. Looking at Hungary's innovation system, it can

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be concluded that based on the indicators used by the WEF the country is behind the EU average. Corporate innovation capacity is poor; the majority of businesses still base their production on cheap labour and cannot or will not innovate. However, in order to become a knowledge-based society in the future, Hungary needs increased investment (financial investment and a paradigm shift) in the areas of education and innovation.

Journal of Economic Literature (JEL) codes: I23, D8, O3, O33, R11
Keywords: competitiveness, growth, education, healthcare, training, corporate growth

Introduction

Today most developing and developed countries view knowledge-based society as an important means of economic development, which, however, can only be achieved by greater and consolidated public commitment, the creation of a solid macro-economic basis (a fiscal, monetary, growth and in the future competitiveness turnaround), to ensure a more dynamic and sustainable growth path (Kolozsi et al., 2017; Lentner, 2015). In the 21st century, besides raw materials, technique and technology, as well as data and information are the major economic drives, which require continuously updated knowledge and skills to be used and utilised. Alongside life-long learning, education also has a vital role in acquiring this knowledge, given that one of its aims is transmitting learning skills. Teaching these skills is not only needed in primary, secondary and tertiary education, but also in vocational training. Technological developments in the rapidly changing economic and business environment highlight the importance of knowledge, learning skills and abilities on every level of the economy and society (national economy, company, social/local community, individual). The basic interests and goals of economic and social actors differ. While from the point of view of the entire national economy the advantages of the knowledge-based society led economy are, for example GDP growth, secure and growing tax revenues, promoting and maintaining full employment; at the corporate level it means business stability, profitability, and efficiency. On the individual level knowledge is manifest in a different form, for example, a competitive salary, secure livelihood or higher standard of living. From the perspective of the national economy knowledge has a significant effect on competitiveness, and economic growth as innovation always has a strong presence in a knowledge-based society. In Hungary the early phases of innovation, research and development are characteristic, however, the next step has to be taken, creating a prototype, as well as developing and strengthening the forthcoming phases. At the individual, the employee's level, there is coherence and synergy between knowledge and wages. Skilled professionals can easily find a job, realise competitive wages which help them improve their living standard – they use more products and/or services – thus indirectly pay more taxes (PIT, VAT, etc.) and generate further demand in the

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economy (multiplier effect). Knowledge and unemployment are in an inversely proportional relationship. The more knowledge and experience an employee has, the better position they are in the labour market (and lower the chances of them ending up unemployed). This is beneficial for the national economy for more than one reason. Firstly, the unemployment rate and the related state transfer is lower. Secondly, there is an increase in the number of skilled workers having a stable (fixed) income, and thereby increasing tax revenues. The world-famous American competitiveness researcher economist M. Porter says, "The better a country's innovation capabilities and higher its level of general knowledge, the higher chances it has for a successful competitive economy. Chances, however, can become the reality only in the possession of appropriate state development policies. In their absence knowledge and skills remain unused and may even deteriorate." According to László Parragh, the president of the Hungarian Chamber of Commerce and Industry (HCCI) only those economies of the world have been able to improve successfully and present economic miracles which could link knowledge and economic development. The HCCI president mentioned the German, Japanese, South Korean and Finnish economies as good examples, adding that Hungary also needs to focus on knowledge-based economy, the further restructuring of the education to better adjust it to the needs of the economy (Parragh, 2017). This is also stressed by Bod (2018), according to whom strengthening innovation and education can improve Hungary's competitive position. As he sees it, continuous attention needs to be paid to improving education and skills development, since these determine economic performance as well.

It is worth noting that the Central Bank of Hungary (MNB) also calls for a stable, up-to-date and strong education system with a view to domestic economic competitiveness development (Matolcsy, 2016). The MNB has taken active part in all this, and is trying to use all the means at its disposal in support of achieving a knowledge-based economy as soon as possible. The reason why the MNB is so actively involved can be explained by how they view national economic competitiveness. In the MNB's view the competitive operation of the national economy not only requires macro-financial and real economic stability, but also the availability of high standard education and healthcare, among others. Based on these, a well-functioning and predictable business environment can be created, investment and innovation may be promoted, which through the appreciation of the skilled workforce can eventually lead to increased productivity and permanent economic and social convergence. This idea was also confirmed and elaborated by Lentner (2007), whose study clearly showed that alongside a stable environment for public finances, modern education and healthy highly skilled workforce are also prerequisites for national economic competitiveness. Training today means much more than it did 20 years ago. According to Lentner, in developed market economies education-training is less likely to end with acquiring the first degree. Continuing technical and economic progress makes it necessary to take part in several different forms of training, periodic further training, as well as professional changes due to the continual transformation of the economic structure. Lentner (2007) makes a link, inter alia, between economic development and growth and the standard of education

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and healthcare. He reveals that whenever the level of education and healthcare is appropriate in a country, it has a positive effect on economic growth; however, the opposite is also true: if the economic growth in a country is adequate, there is an increased possibility that the government will allocate higher financial sources for the education and healthcare systems. From another angle, Csath (2018) also highlights that the level of the education system influences the competitiveness of a country, that is, there is a close link between competitiveness and the standard of education. In his opinion, it can be explained by the fact that competitiveness is highly dependent on new value creation in a given country. New value creation, on the other hand, is also influenced by the existence of an appropriate number of professionals needed for greater added value creation. In addition to the above, Csath (2019) says that a healthy population is a matter of national interest, as the economy can only be successfully operated with the help of such people on a permanent basis. It is clearly visible that this viewpoint is close to professor Lentner's way of thinking detailed above.

Parragh also stresses the importance of knowledge, and in his understanding "the day after tomorrow is about knowledge." According to the HCCI President, this calls for high standard tertiary education, in the development of which the market has to be consulted, and this requires restructuring of the training system in a number of areas. This is all in progress today, hopefully with future results that can be translated into numbers. Nevertheless, he also points out that, one of the biggest challenges the present education faces is to prepare youngsters for the future – unpredictable – situation of the labour market, which is getting harder and harder to forecast due to increased progress.

The above ideas show that one of the basic criteria for competitiveness is human capital, assets. This is confirmed by the results of the MNB publication of its competitiveness workshop. According to the Competitiveness Mirror (2019) publication, Hungary's greatest asset is its available skilled human resource, which is the key to the survival and successful convergence of the country. In answer to this idea the Ministry for Innovation and Technology worked out (2019) the mid-term strategy 'VET 4.0 – for the renewal of VET and Adult Education (AE),' the policy answer to the challenges of the 4th Industrial Revolution, with the major aim of educating future professionals who can support efficient production and service creating higher added value, and are in possession of adequate knowledge to meet the needs of the current market. It is also worth mentioning Zéman's idea (2019), who stresses the future importance of the dynamic and inductive relationship of the sciences, education and best practices trio, which will only operate well, if their connectedness and functional efficiency are improved.

Investment in education and vocational training is fully returned since

– corporate innovation capability and willingness are improved,

– companies create higher value-added products and services,

– corporate productivity and efficiency increase,

– businesses are more likely to appear on the international market (integrate into global value chains).

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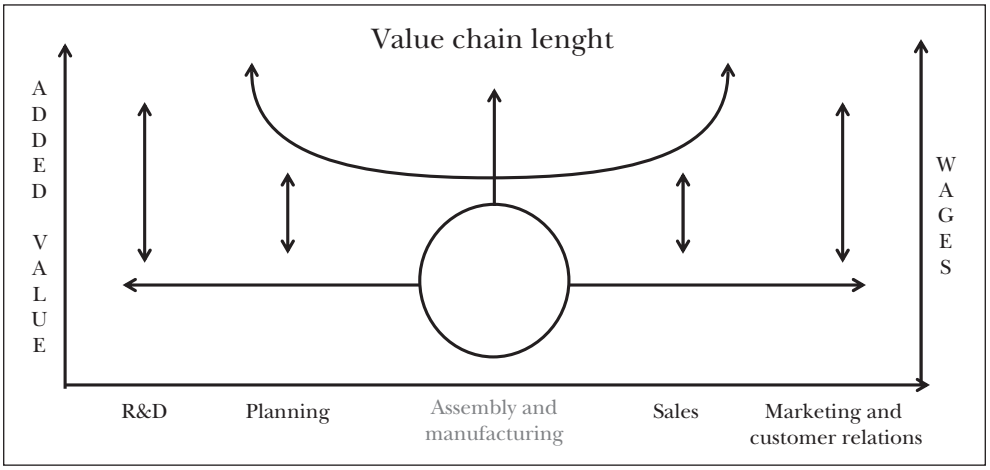
Based on the above, education clearly improves competitiveness, which indirectly brings about increased tax revenues.

The role of education in increasing competitveness

One of the most important factors of economic growth and increased corporate competitiveness is human capital, which affects economy through the number and the skill level of the workforce alike. To improve competitiveness, increasing employment rate is not enough tough, it requires the expansion of workplaces that generate higher added value, which is difficult to achieve without the existence of knowledge-based society. This all means that businesses that are capable of generating higher added value need highly skilled workforce. The link between added value and wages is demonstrated by the value chain below (Chart 1). Hungary, at present, instead of generating added value, is still at the stage of building on assembly and manufacturing. Increasing productivity and efficiency, however, calls for opening towards innovative activities.

Chart 1: Added value and wages



Source: Presentation of Csath, M., 56th Economists Roaming Conference

Investment in education and vocational training become manifest in economy with differing intensity. While public education expenditure is recovered in the long run on the national economy level, adult training and further training (can) even yield short-term results.

The Europe 2020 strategy announced the EU's employment and growth strategy for this decade (2010–2020), with objectives relating to areas of employment, research and development, energy management, education and fight against poverty and social exclusion (Kőrösi, 2012). In terms of education there is a special emphasis on drop-out rate, on optimising the number of students in tertiary education. The

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strategy aims at lowering the rete of early school leavers below 10%, and increasing the rate of higher education qualifications of the 30–34 year-old EU population to minimum 40% (European Commission, 2010).

In accordance with the education objectives and financing opportunities Hungary has already taken steps towards change in the tertiary education sector. At the end of 2014 the Gear Shift in Higher Education strategy for restructuring tertiary education was adopted. The Government's aim is to develop a future performance-oriented higher education, in which institutions have clearly defined educational profiles that help them provide high quality education in their specific educational area. This may help create competition among institutions to concentrate on improving knowledge quality and standard. Creating such an institutional network contributes to improving the competitiveness position of disadvantaged regions. There is a focus on reducing drop-out rates, increasing pushing motivation among students, skills and abilities development, and meeting labour market needs with the fundamental aim of transferring knowledge that enables graduates to find effective and efficient employment in both the domestic and foreign job market. The main objective of the concept is to create a high quality tertiary education network of optimal size and composition: the development of knowledge-based society, which is capable of efficiently reacting to the social and economic-cultural challenges in Hungary and abroad (Kormany.hu, 2014).

After reviewing the concept, based on the experience and the lessons learned from the 2014–2016 period, a strategy including more exacted objectives and interventions was adopted. The Gear Shift in Higher Education 2.0 was accompanied by an Action Plan for the 2016–2020 period. The strategy set the 2030 deadline for transforming higher education, with a view to developing future educational programmes in which student abilities are appropriately differentiated and which focuses on both student and teacher performance enhancement. To create the basis for quality education, teachers' attitudes, both professionally and in terms of methodology need development. In the restructured institutional system each institution is specialised, has a distinct educational profile and there is space for both cooperation and healthy competition among institutions. Thus unused capacities would cease to exist and by reallocating resources there could be more emphasis on research initiatives. The parallel functioning and operation of research and development with education activities can contribute, on the student level, to increased attraction of international students, while on the instructor level, to improved social and economic competitiveness (Kormany.hu, 2016).

A possible means of strengthening the link between the education and the economic sector is the creation (preferably on the higher education level) of Knowledge Centres which are focused on economic (market) demands. These knowledge centres may also become key actors in domestic RD&I activity. Research, development and innovation activities are funded by both the state and the private sector. However, it can be clearly stated that the domestic private sector is in lack of appropriate amounts of capital power, which decidedly hinders domestic SME actors in the acute market com-

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petition. Added value generated by RD&I activity is evidently a decisive competition factor today. Looking at the research and development investments of the national economy in the past 15 years, it is concluded that in Hungary the R&D-to-GDP ratio reached 1% in 2009, and it has been on the increase ever since, reaching its (1.49%) record level in 2018 (HCSO). It shows that the state has acknowledged the importance of RD&I in competitiveness. However, Hungary is still among the medium-performing countries in terms of innovation. Industries already involved in global value-chains – such as the pharmaceutical industry, the ICT sector and vehicle production –, as well as research and development companies with international relations significantly strengthen domestic innovation performance. Nevertheless, the RD&I performance of the majority of domestic businesses is well below the performance of their counterparts in more developed countries. Naturally, RD&I is closely linked with higher education and investment in this sector. Unfortunately, in Hungary this situation is far from shiny: recent investment in R&D in tertiary education could only conserve the current situation. Oftentimes this sector is characterised by divestment. It has to be highlighted that countries that prioritise tertiary education quality improvement and RD&I activity support in this area, are in a much favourable position in both IMD and WEF rankings. There are encouraging signs though showing that Hungarian tertiary education institutions are starting to take to partnerships with businesses. This is also indicated by the fact that institutions and companies cooperate in more and more areas, which can be mutually advantageous and students may also benefit.

The success of research and development activities is not only measurable in terms of increased investment. Without an appropriate level of education, which provides the conditions for research and development from the human resource side, the expansion of R&D activities is inconceivable. High quality human capital training and improvement contributes to national productivity. The standards of education and healthcare play a decisive role in developing competitiveness (Lentner, 2007). Therefore, alongside focusing on economic growth, attention must be paid to social welfare. To evaluate and monitor these, the OECD developed an indicator system, including key indicators that are indispensable for well-being (Mizobuchi, 2014). The Better Life Index maps and measures well-being on the basis of 11 indicators. Besides income, it includes community, education, civic engagement and health factors as well (Durand, 2015). A speciality of the concept is that there is no objective or absolute ranking among the participating countries, as the countries themselves determine several parameters. Hungary is below the OECD average in terms of education, subjective well-being, social relations and health.

Going back to education, the role of higher education institutions is also significant as by providing information to the community about the intellectual value created by them, as well as by its economic utilisation institutions contribute to regional social and economic growth. Changes over the past two decades have markedly influenced the regional structure of higher education. Besides its social role, tertiary education also has a decisive role in economy. Several studies reflect on the significance of higher education in rural areas. Higher education institutions in a region contribute

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to its strength and development. The educational spectrum and training structure provided by universities are integral parts of regional development and renewal opportunities (Rechnitzer, 2009; Sisa et al., 2018a).

The Hungarian higher education has undergone several transformations; the higher education reform has finished: both the financing system and the institutional background have been restructured. There is observable commitment to create a performance and quality-oriented increasingly more internationalised Hungarian higher education system which supports value creation, has the ability to react to global and social trends of the world, and takes into consideration the generational characteristics and attitudes of the participants of higher education (Sisa et al., 2018b). Tertiary institutions, besides their educational and research activities, play a major role in the socio-economic development of a nation and providing its intellectual capital. Among the multiple functions of higher education in Hungary, supporting social mobility has to be emphasised which needs to be provided in the disadvantaged regions as well.

Higher education plays a considerable role in the less developed regions of the country, where there is a demand for both social mobility and economic development. Consequently, it is the task of higher education to create a segment in its institutional system that is dedicated to local prosperity. Specific institutions need to take into account and adapt to regional labour market needs when they develop their educational programmes. Practice-oriented training has to be the first and foremost objective, to provide youngsters with the basics for their future career path. To boost economy, tertiary institutions need high research and development performance, which contributes to the development of the entrepreneur sphere and eventually to GDP growth.

As we see it, adjusted to the strategic guidelines defined for higher education, the secondary level vocational education system should also be rethought. A good starting point could be - talking Winarno (2019) as an example – increased SME-actor involvement in vocational training, with mapping SME-sector labour needs as the first step. The aim is to create an integrated model which builds on vocational training (education) – business cooperation. The key elements of the integrated cooperation model are: product (service), production (service provision), human resources, management, marketing, financial system, the elements of value creation and the foundation of a sustainable training centre (Winarno et al., 2019). Small and medium enterprises have a vital role in economic growth and improved competitiveness; therefore the role of entrepreneurship education is unquestionable (Imreh-Tóth, 2014).

Knowledge, competences, skills are all driving forces of economy on all the levels (employee, employer) of the national economy. Skilled (and well-paid) workers are more efficient in a given working environment when they have an overview of the work processes at the company and also when they can use the given technology better; thus by using their expertise they efficiently support companies that create the appropriate working environment for them. Moreover, good working conditions and competitive wages lower employee turnover, shortening the initial training period, when in a period of intensive turnover businesses are burdened with the continual training of newcomers. A stable highly qualified workforce works efficiently, generates

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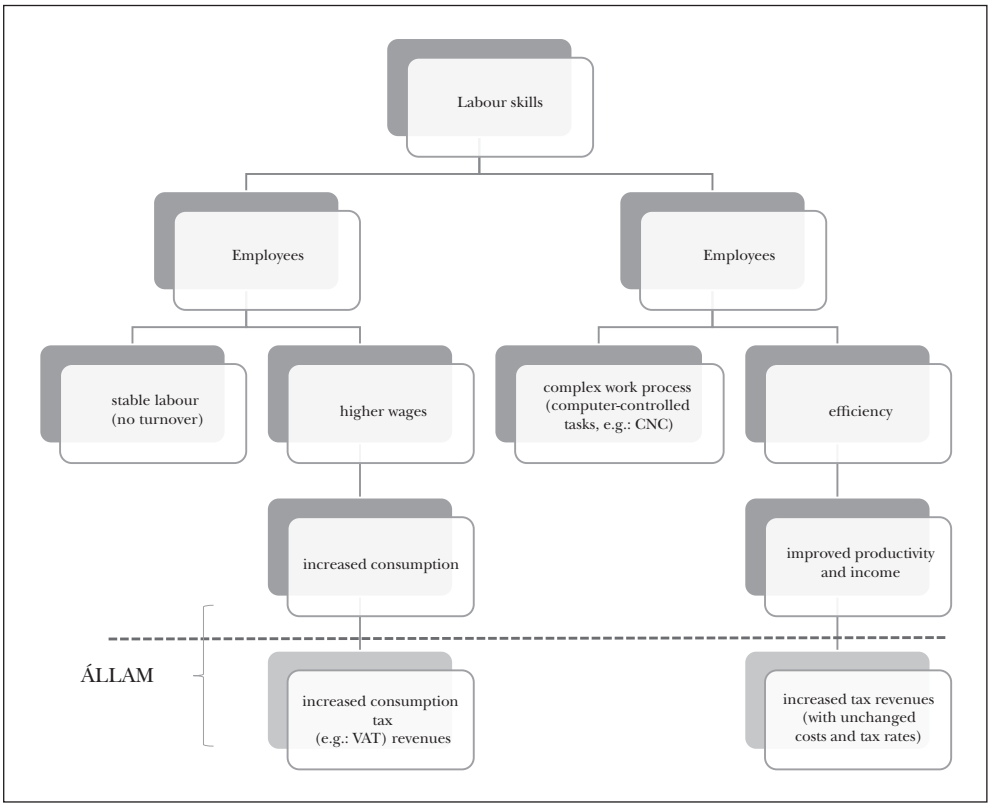
higher added value for the business, thus improves corporate profitability. Higher work efficiency lowers per capita labour costs – and with the same corporate cost structure and tax regulations –, increases profit before tax and corporate tax payable. Highly skilled workforce – under favourable labour market conditions and due to the effect of the increasing minimum wage – realises competitive wages which improves their living standard. This, in turn, raises the demand for certain products and services, which indirectly increases VAT revenues. The Chart 2 gives a summary of the above process.

Chart 2: Advantages of skilled labour



Source: Authors' own compilation

Domestic and international outlook

Human capital has a major effect on economic growth and improved corporate competitiveness; firstly, by means of quantitative change (staff increase), secondly, by means of quality change (higher skills). The MNB publication Growth Report (2018) shows – analysing 2010–2017 EU data – that employment rate increase and per capita GDP changes have a positive relationship. In Hungary rates for the 15–74 year-old

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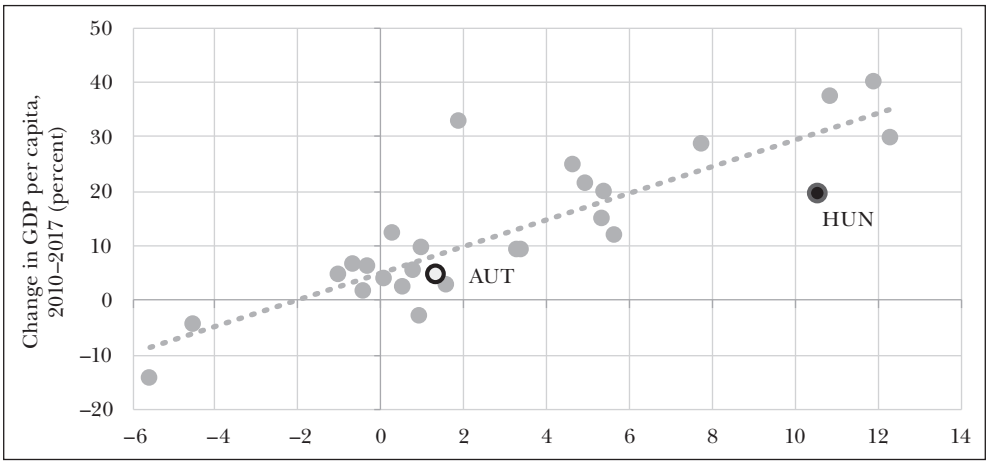
population increased by 10% point; thus per capita GDP grew almost by 20% by 2017. The Chart 3 shows employment and per capita GDP changes in EU countries.

Chart 3: Employment rate and per capita GDP growth rate in EU countries, 2010–2017



Source: MNB, 2018

The *strong labour demand* of the past few years *originates in* government measures taken in previous years to increase employment. Consequently employment rate increase resulted in about 20% per capita GDP growth, while demographic changes had a negative influence on the indicator. Given that due to demographic changes the labour force is continuously shrinking – and also because of labour shortages in the sector and improved productivity efficiency –, increasing employment in itself is not enough to maintain competitiveness. It is indispensable that certain work processes are rationalised and digitised, for which skilled labour must be provided. This requires training and vocational training even in the short term. The current education and (vocational) training system calls for development, updating and fine-tuning.

The Chart 4 clearly shows the positive effect of improved employment on per capita GDP growth.

The reduced pace of employment growth rate is also shown in the report on the 2018 labour market by the Hungarian Central Statistical Office published in April 2019. Data show that in 2018 the number of employed persons kept increasing, amounting to 4,469 thousand employed, a 1.1% increase, about 50 thousand employed, compared to the previous year. Although both 2018 and 2019 show positive employment growth, the pace of growth slowed down despite having significant shortages in the labour market. Increased labour demand – supported by constant conscious government measures – redirected a part of previous public sector employees into this market segment. In addition, the significant scale of pay rises in recent

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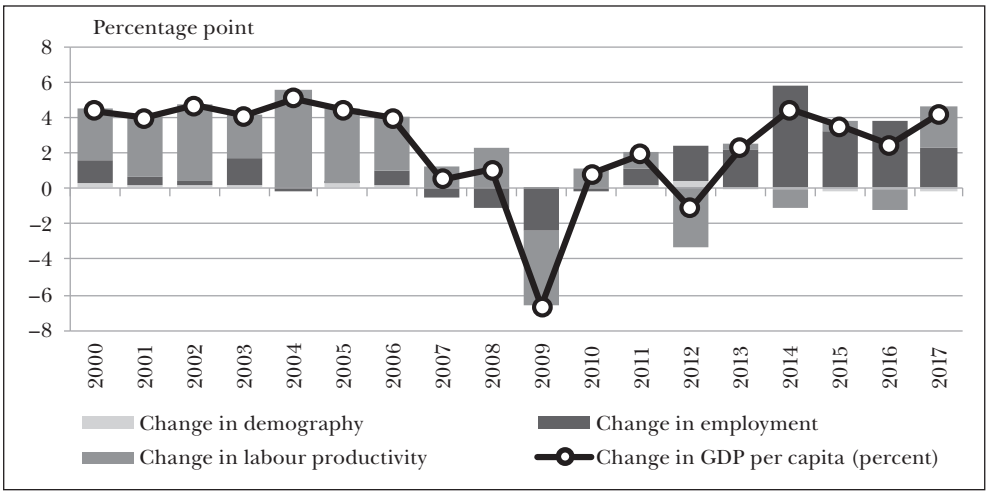
Chart 4: Labour market factors in domestic per capita GDP growth



Source: MNB, 2018

years also contributed to stopping the increase in the number of workers seeking employment abroad. To sum up, Hungary is nearing full employment. This means that businesses need to restructure their labour capacities and employment to be able to meet increased market demands and increase productivity. This can only be achieved by automatisation (digitisation) and by employing and training (more) highly skilled labour.

Own research

Domestic and international practice shows that companies that provide employees with personalised training programmes fitted to their jobs, are more effective and efficient in their everyday operation. As evident from the previous sections, it can be stated that in today's turbulent world education and training are vital in the development of the individual and the company alike. Based on all these, a targeted survey was conducted among businesses *(both SME-sector and large companies)* for the 2016–2018 period, which looked into training opportunities provided by employers, their results and the lessons learned, and their effect on corporate productivity, efficiency and business operation.

The company training questionnaire examined whether companies supported or are going to support employee training it the past and forthcoming 3 years, respectively, in what form, and what the motivation for supporting further training was. Additionally, it was examined how entrepreneurs view the supported trainings, how these relate to corporate operation (profit, growth, etc.), and what role they play in employee retention.

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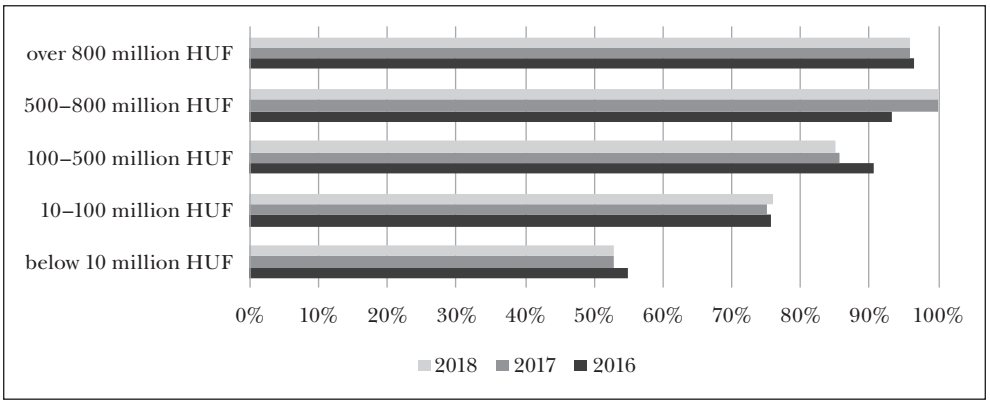
Corporate training

This section presents the results of those companies which stated in the survey that they supported or are going to support professional employee development and training it the past and forthcoming 3 years, respectively. 86% of respondent companies supported employee development and training, which confirms that businesses find it more and more important to provide employee training opportunities. 46% of these businesses have practical training places related to dual training.

Next, the distribution of companies supporting employee training according to the number of staff, revenue and region were examined. While in businesses employing 1–9 workers willingness to support employee training is 63%, large companies show significantly higher results. It can be concluded that as the number of staff increases, so does the number of companies that support employee training and professional development.

Looking at staff number and revenue categories, it can also be established that with their growth training support exponentially grows, too. Based on the results it can be said that there is only one outstanding result, that is, significant difference among the categories: in the smallest category for both number of staff and revenue. Basically this is caused by smaller company size, narrower and less complex scope of activities, and more simple organisational structure. (The smallest businesses support employee development the least.) Smaller companies are characterised by less precise separation of functions, simpler management structure and less complex or digitised work processes, thus there is lower demand for training. At the same time, in the next staff and revenue category (10–49 workers and above 100 M HUF revenue) companies need to develop a more complex organisational structure, where decision-making, organisational tasks and work processes are clearly separated; therefore they require specialised knowledge and skills at their disposal at all times – hence training is of importance.

Chart 5: Distribution of businesses supporting employee training according to revenue



Source: HCCI own compilation (N: 213)

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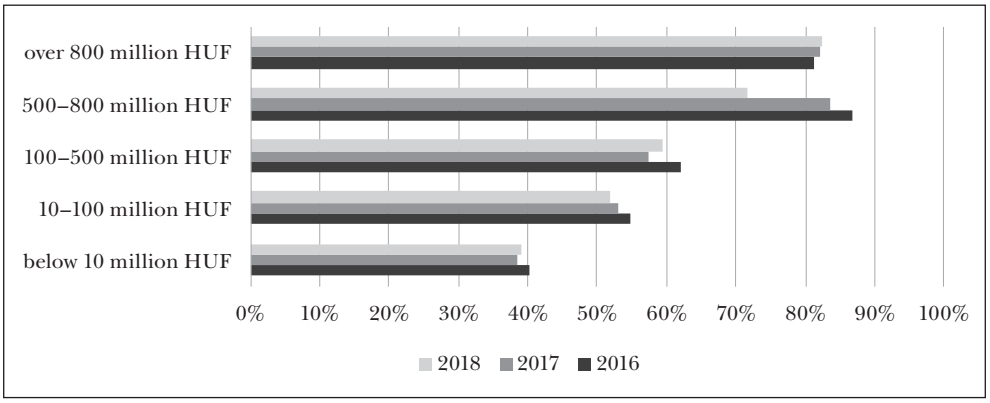
Characteristics of supported trainings

In the previous section those companies were presented that support employee training. This part analyses the major characteristics of supported trainings (level and type, content, motivation for training, initiators, aims and forms of training). The analysis of employer supported trainings draws a distinction based on training level, content and form. The next chapters detail these categories.

Level of supported training

The level of training refers to (1) own internal training, (2) state-recognised trainings in the National Vocational Qualification Register (NVQR) and/or other supported trainings outside the NVQR, and (3) higher education. In terms of training level, in the past 3 years 81% of participating companies supported state-recognised trainings in the NVQR and other supported trainings outside the NVQR, 71% supported internal professional trainings, whereas 51% supported higher educational training (college/university). Training levels were examined in connection with company size (number of staff) to see different training type preferences for different sizes. In this respect, a high percentage of companies with smaller than 50 and larger than 100 staff supported NVQR training, while companies with 50-100 staff preferred internal training, but they supported NVQR trainings as well. Higher educational programmes (college/university) were mostly preferred by companies having more than 250 workers; however, for this size – similarly to other company sizes – NVQR trainings were still prevalent.

Chart 6: Distribution of NVQR and other supported trainings outside the NVQR based on company revenues (%)



Source: HCCI own calculation (N: 213)

Besides NVQR trainings higher education support is also significant, therefore, we also looked at the revenue factor for this training type. In the examined period two revenue categories show greater change in supporting employees' college and/

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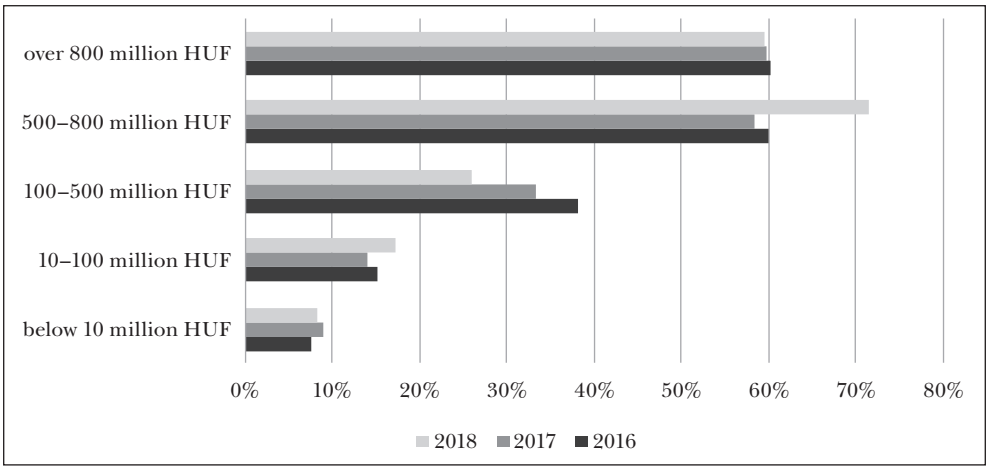
or university education. Support for this type of education has significantly grown in companies with 500–800 million HUF revenue, while in companies with 100–500 million HUF revenue, support for this type of education has decreased (Chart 7).

Chart 7: Distribution of higher education training support based on company revenue (%)



Source: HCCI own calculation (N: 213)

Supporting higher educational programmes is justified by the complexity of corporate processes, the higher standard of professional knowledge requirements and the development of a knowledge-based competitiveness model. Larger companies are more likely to have a human resource strategy, which helps long-term planning for individual workers, and provides them with future prospects that motivate participation in longer educational programmes.

Content and direction of supported training

Based on training content we created 5 categories as follows: (1) language trainings, (2) digital competences, (3) compulsory professional training (e.g.: certified accountant training), (4) non-compulsory professional training, retraining (5) organisational development (marketing, strategy, etc.).

It is important to remark that non-compulsory training serves as an umbrella term for all trainings that were initiated individually by businesses, that is, not out of compliance with legal obligations. Within the non-compulsory professional training category, a few important areas were highlighted, such as digital competences development, organisational development and language trainings. This area has the highest value (63%), which indicates that those training types are prioritised which help improve corporate development, efficiency and effectiveness.

Apart from compulsory and non-compulsory professional trainings the participant companies prefer language trainings followed by organisational development cours-

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es. Digital competences development, however, takes the last place among supported trainings. The low ranking of digital competences development shows that businesses are not aware that today digital competences are needed to secure their market position, profitability and stability, partly through digital development of operations, and partly through professional development of employees using these tools and systems.

The cliché "Whoever is left out, is left behind," is often heard these days. Raising corporate awareness in this respect could be taken up by the government, with a more efficient involvement from the chamber system. In the survey companies were asked how secondary vocational training and tertiary education is linked to the professional development of employees: whether they develop their existing skills or support acquiring new knowledge different from their earlier expertise. Based on the results, supported and provided employee trainings further develop existing skills acquired in secondary or higher educational programmes, which indicates that deepening existing knowledge is preferred by companies.

This enables employees to acquire in-depth knowledge in a certain professional area complementing existing knowledge with new, which then will be integrated into their everyday operation.

Aims of supported trainings

The survey set up 9 aim categories as follows: (1) digitalisation, (2) installation, safe and efficient use of new tools, (3) new software introduction, (4) new hiring, (5) old employee with new duties, (6) promotion of employee self-fulfilment (employee retention), (7) updating knowledge on regulatory environment, (8) compliance with legal obligations, (9) compliance with safety and/or environmental standards.

Taking a look at the aims of supported employee trainings, it can be concluded that the most important aim is employee retention, which is followed by compliance with safety and/or environmental standards, and updating knowledge on regulatory environment (see Chart 8). It is a surprising finding that the least important motivation for supporting employee trainings is digital competences development (digitisation).

One of the major aims of supporting employee training is employee retention. This underlines responsible leadership and management decisions that in today's tense labour market situation seek to lower turnover rate and retain existing workforce in the long run. It is perceivable that businesses are becoming more and more aware in this respect. Besides employee retention, compliance with safety and/or environmental standards and compliance with legal obligations are also stressed showing that companies pay special attention to legal compliance. Based on the results, businesses ranked digital competence development least often as the aim of employee trainings.

This reflects the fact that businesses are not fully aware that today is the age of digital revolution (4th industrial revolution), and, if they fail to incorporate/apply available digital developments, they are bound to be left behind. It is a clear conclusion that there is a huge untapped potential in digitisation.

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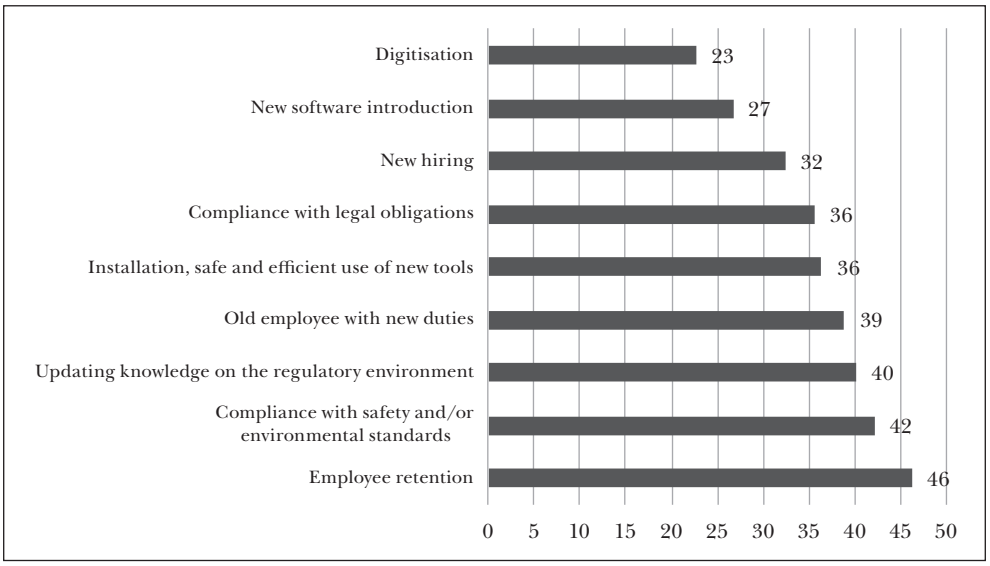
Chart 8: Distribution of supported employee trainings based on motivation (%)



Source: HCCI own compilation (N: 185)

The aim of supported trainings has a considerable effect on willingness to support trainings; therefore the aims were examined from another angle, based on company size (staff number). Characteristically, micro businesses employing 1–9 workers marked compliance with legal obligations as their sole and foremost objective. While employee retention is an important aim of supported trainings for small companies, smaller medium enterprises (50–99 staff) find new hiring related training the most important. For large companies updating knowledge on regulatory environment is seen as the primary training aim. Smaller businesses dominantly concentrate on one aim, whereas larger companies determine much more and more diverse aims which they regard equally important. On this basis it can be stated that while legal compliance takes up a great deal of energy in smaller businesses, large companies, in the possession of up-to-date regulatory knowledge, have ample capacity to exploit opportunities, sooner and to a greater extent.

For medium enterprises introduction of new tools, new hires and employee retention all indicate an intention to strengthen their market position. Training preferences of medium-sized companies definitely reflect their purpose of growth.

Training costs

The study also examined to what extent companies gave support for employee professional development in the last 3 years. In order to achieve comparability and receive detailed results, a scale was developed, which helped companies identify the volume of their training costs. The scale includes the following value categories:

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– below 50,000 HUF
– 50,001–300,000 HUF
– 300,001–500,000 HUF
– 500,001–1 million HUF
– 1–3 million HUF
– 3–5 million HUF
– 5–10 million HUF
– over 10 million HUF

Data analysis shows that in the given period companies increased their employee training expenditure. Another positive point is that the rate of companies supporting employee development with the least amount – that is less than 50,000 HUF – continuously decreased. It has to be noted that the largest improvement is related to the 1–3 million HUF and over 10 million HUF value categories. In the examined period training cost per employee shows a marked increase. In addition, considering the form of training support, time off work for studies, and covering all or a part of the training costs were typical. The above data clearly confirm that companies invest more and more in employee development and besides financial subsidies they support employees with providing time off work for studies. It also has to be mentioned that more than 50% of participant companies stated that they had not applied for/received any external aid or subsidy for supported employee training costs. Taking all of these into account it may be concluded that businesses invest increasingly more in employee development from their own resources. In summary, companies are aware of the importance of training in corporate performance and more of them invest increasingly more in this area.

The effect of corporate trainings on pay rise

From the employee's point of view, besides self-fulfilment, the possibility of pay rise is also a motivating factor. For this reason, *pay rise* following the successful completion of a training was also examined in connection with the *form of training* (external training company and/or internal training), and also compared to the *type of training* (internal training, NVQR or other supported trainings, higher education). Overall, it was found that 60% of participant employers rewarded their employees with a pay rise after they have successfully completed their studies.

Comparing the types of training to the rate of pay rise, it is visible that in the case of company-independent and blended trainings employee wages increased at a higher rate than following the completion of "only" internal training courses. Pay rise following training completion showed the highest rate (65%) in those companies where blended (external training company and internal training) forms were used. The lowest rate of pay rise was characteristic of companies that only offered internal training. The prospect of pay rise following successful training completion is not only dependent on the form of training, but also on the type of supported training. The following was found in terms of the connection between training type and pay rise: 81%

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of companies supported NVQR or other supported trainings, 71% supported their own internal professional training, while 51% supported higher education (college/university) training programmes. Companies mainly prefer shorter duration trainings rather than longer, occasionally 3–5 year-long, higher educational programmes.

The possible reasons for this could be that the company operation requires employees taking part in short and more targeted training, or, if an employee with higher skills is needed, they prefer hiring new adequately qualified employees instead of enrolling existing workforce. It also has to be noted that in several companies there is a perceivable lack of consciously designed human resources strategy, which could help them choose the most fitting form of training for a certain job, employee or task.

The rate of companies rewarding their employees with a pay rise following the successful completion of a training does not differ greatly based on the type of training. While for internal trainings 61% of companies reported employee pay rise, in companies supporting "only" NVQR trainings, the rate was 62%. Respective data for higher education was 67%. Based on data analysis it is favourable that pay rise is present for all training types. This shows that companies acknowledge employees' knowledge expansion financially as well.

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Béla Makkai

Chopping Hungary Up by the 1920 Peace Dictate of Trianon

Causes, Events and Consequences

Summary
The regime that emerged with the peace treaties concluded after World War I chopped up the Kingdom of Hungary and rewarded its neighbours, helping them to establish themselves on the basis of the principle of national self-determination, by giving them two-thirds of Hungary's areas and one-third of its Hungarian-speaking population. During the settlement that followed World War II, the great powers repeatedly forced this shocking decision upon Hungarians drifted to the losing side. This essay sums up the causes and events of this difficult-to-survive historical traumatism and its adverse impacts on the Central European region, in retrospect after more than a century.

Keywords: Kingdom of Hungary, Austro-Hungarian Monarchy, Peace Treaty of Trianon, Little Entente, protection of ethnic minorities, nationalities, homogeneous nation state, integration, autonomy

Causes of disintegration

At the very end of the 9th century, the nomadic Hungarian tribes arriving from the east converted to Christianity and founded a state, which then successfully repelled attacks by both Byzantine and German imperial conquerors organised under various names. St Stephen's kingdom was considered as a potent, medium-sized power, with an independent status symbolised by a closed crown granted by the Pope in 1000.

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The House of Árpád established family relationships with the most powerful dynasties of Europe. Only the 1241 Mongol Invasion caused a severe loss of blood to this rich country having an effective fighting force. That year marked the commencement of immigration by foreign nationalities in larger numbers. Without an exception, all of them found home in the country. The Ottomans conquest reached the southern borders of the country, and thus Christianity, at the end of the 14th century. However, supported by the Black Army and the system of double fortresses, the well-organised Renaissance state of King Matthias I (Matthias Corvinus) firmly defended its borders up to the end of the 15th century.[1] As a result of the internal conflicts that flared up after King Matthias's death, the 1514 peasant rising and especially the battle lost at Mohács in 1526, the country was profoundly shaken. Amidst feuds between various claimants to the throne, the Turkish conquest tore the country into three parts (the Habsburgs, who had been elected kings of Hungary, ruled the north-western, the Turkish occupied the middle, and the Principality of Transylvania organised in dependence of the Turkish, comprised the eastern part). For two hundred years, Hungary's entire territory became a battlefield.

Historians today consider the military defeat suffered from the Turks and its subsequent division into three parts as the "first Trianon" for Hungarians (Pálffy, 2015). The assumption is supported by the facts that from that point in time, the fate of the leading nation in Central Europe was decided abroad (in Vienna, Istanbul and Rome); and the financial, intellectual and moral resources of Hungarians were wasted away by the intentions, political coveting and, especially, desperate combats fought in self-defence. Due to destruction, blood loss and exodus, the central, plains areas of the country were depopulated, while the nationalities (Slovakians, Ruthenians and Romanians) living under the shelter of the semi-circular mountain chain of the Carpathians fringing the country survived uninterrupted wars with lower losses, and showed healthy demographic increase, with southern Slavs and Romanians fleeing from the Turks constantly immigrated to the country. Vienna's conscious settlement policy consummated the redrawing of the country's ethnic map. In addition to increasing the amount of taxes collected and the defence capacity of the empire, its purpose was to bridle the "revolting Hungarians", who frequently rose and organised numerous independence movements in defence of the Hungarian nobility's constitution. As a result of this double procedure, after the expulsion of the Turks (in 1718), Hungarians became a minority in their own country.[2] They could not gain foothold on the re-captured territories, because the Viennese court expelled Hungarians from the most fertile area of the country for 60 (sixty) years, as they considered it their loot. On these territories they settled masses of Catholic Germans they considered "reliable", and granted privileges to Serbians, Croatians and Romanians in the border guard areas. [3] This divisive policy offered an opportunity to the minorities living, thriving and strengthening on the confines to mature and implement their own nation-building objectives (Gulyás, 2012, pp. 217–224).

The late 18th-century national awakening unfolded in the region supported by the ideas of nationalism and literary romanticism. The evolving national identities of the

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"co-nation" Croatians, who previously had an independent state, Slovakians and Serbs were dominated by their proposition of being indigenous in the Carpathian Basin. For this reason they started to mention Hungarians, who arrived from the east, as a "barbarian horde"[4] which tore "peaceful Slavs" into three parts. It was no accident that plans for unification or independence with the leadership or patronage of the only independent Slavic state, the Russian Empire, popped up one after the other in this period.[5] The ethnic intelligentsia endeavoured to support their equivalence with Hungarians by the demographic force of Slavs[6] and – in a Romantic approach – by their noble origin in contrast to Hungarians' claim of Hunnic and Turkic ancestry.[7] As inspiring the doctrines advocated by Jan Kollár and others were for the ethnic minorities in Hungary, so menacing they were for Hungarians (who would learn in 1849 what exactly the Pax Russica meant).

At the turn of the 18th and 19th centuries, the Hungarian gentry, capitalising on their political experiences gained in county administration, launched a public law against the centralisation policy of the Habsburg dynasty, and this struggle intertwined with the economic and social modernisation of the country. The Age of Reforms released enormous intellectual and moral energies. The most influential point in the programme of the political élite was their voluntary waiver of the majority of noblemen's privileges (e.g. tax exemption),contribution to public finances by all was announce and this created a vast basis among the masses for the achievement of national goals. In fact, the ethnic minorities shared an interest with the reformer Hungarians against Vienna's Germanising policy and also looked to them as a model; however, in order to determine their own national characteristics, Hungarians were also used for the perception of an enemy (Sokcsevits, 2004, pp. 131–154). Especially when in 1844, Latin was replaced by Hungarian as the official language of the country. Partly for defence reasons, the ethnic minorities, which had become competitors, sought alliance with the imperial court and this lead to the armed conflicts during the 1848–1949 Hungarian revolution and war of independence, which obtained a civil war character in the case of Romanians and Serbs. Thus, in addition to "Europe's gendarme", tsarist Russia, Hungary's ethnic minorities, drifted to the Viennese reaction, also participated in the crushing of the lawfully elected Hungarian government.

Ten years after the 1848–1849 Hungarian war of independence that ravaged the prestige of the Habsburg Empire, the Monarchy was compelled to give in to the pressure from the French Piedmont alliance. Finally, in 1866, after a defamatory flash defeat, Prussia also turned it out of the German Alliance. Thus, from the power centre of Western Europe, the Habsburgs were ousted to the Eastern European periphery for good. Against all odds, in 1867 the dynasty arrived at a compromise with the Hungarian political élite. Over the long term, the latter had two options: either to agree with the ethnic minorities and transform the country into a federal state,[8] or, capitalising on but not abusing the dire situation of the dynasty after two decades of passive resistance to despotism, to choose the division of power based on parity. Having chosen the latter option, which required less effort and offered more benefits over the short term, the Austro-Hungarian Monarchy was established, as summed up by its firs For-

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eign Minister: "...as a partnership between the German and the Hungarian elements against Panslavism."[9]

Naturally, not everybody was happy with this outcome of the lengthy consultations. The participants of the Vienna Slavic congress professed their belief in a pentapolar federal state. Although the new public law situation reflected the momentary balance of power, it proved to be a complicated and rigid structure,[10] and the peoples of the Danube Valley did not constitute an organic economic and political union. Their intellectual community was even less obvious, as the memory of the many centuries of a common "hungarus" past had already faded considerably. The empire seemed to only be held together by the Catholic masses' loyalty to the dynasty, an army of a million soldiers, the supranational aristocracy, the high priests, and the staff of public administrators, as a framework, completed by the interests of large capitalists, and fear from the two neighbours: the expansive tsarist Russia and Germany, in the progress of organisation to an empire.

The challenges of modernisation resulted in uneven competition for the regions of different levels of development,[11] however, it is obvious that the criticism formulated by the politicians of ethnic minorities against dualism and their frequently voiced slogans about the democratic forms of the division of power and social justice frequently concealed the vulgar motives of obtaining position and financial gain. It follows from this that nationalism, which invigorated western nation sates, had a fragmenting force in the Monarchy. With the intention of creating independent states and in order to change western public opinion, this was the reason why certain southern Slavic and Czech politicians unjustly called Austria-Hungary "the prison of nations" (Makkai, 2012).

The Hungarian political élite, which seemed to have ridden at anchor in 1867, incorrectly sized up their opportunities over the long term. Despite ensuring equal rights (irrespective of mother tongue, nationality and religion) to everyone, following the example of western nation states, they made efforts at insisting on the concept of "a uniform Hungarian political nation". The single exception was the Croatian "co-nation", which had been developing in a commonwealth for eight hundred years, and was granted broad autonomy (Act XXX of 1868). However, vis-a-vis the peoples termed by Otto Bauer as "having no history", Hungarians referred to their state organisation capacity and past sacrifices made in defence of state sovereignty.

This approach is reflected in the act on ethnic minorities, unprecedented in Europe at the time (Act ILIV of 1868). More than half of the members of the drafting committee were ethnic minority experts; however, their proposal for ethnic representation relative to headcount was not included in the legislation. The reason for this was that the freedoms applicable to each single citizen of Hungary were personal rights, in agreement with the zeitgeist of liberalism at the time. However, with a view to their autonomous church organisations and to their societies built on patriarchal large families, the Serbs and Romanians demanded collective rights, and in the unfavourable demographic situation of Hungarians and in the imagined or actual threat of Panslavism, this may have undermined the territorial unity of the state. However, the act genuinely sought to serve peace, and generously provided about the linguis-

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tic and cultural rights of minorities,[12] even though several articles were not put into practice. First and foremost, it provided broad language use rights in culture, public administration and justice at the level of communities and counties, when a particular ethnic minority reached 20 per cent, set as a threshold.

Minority leadership in counties with a majority of an ethnic minority was not implemented, and an enacting order was not drafted to this act. It is also a fact that this period was characterised by liberalism gradually losing ground and its unfavourable impacts were also felt in Hungarian minority policy. However, the responsibility of the radical minority leaders can also be established as they brought forward some exaggerating demands[13] and failed to vote for the act.

Finally, to protest the ethnic minority parties announced a "passivity" policy, although this was not justified by any intent of subordination or rights abuse. When they decided to re-adopt participation in politics during the hot debates of the turn of the century, they already demanded the full implementation of the act. But by that time the Hungarian political élite's readiness to compromise had diminished[14] due to the government's stability, the favourable demographic indicators, the salient improvement in the standard of living[15] and the celebration of the millennial of the Kingdom of Hungary.

As a result of the spectacular economic and social development and long peace, the new generation of politicians were overcome by a kind of complacency. They underestimated the political weight of ethnic minorities, as the latter were represented by a low number of MP's at Parliament, due to the tight suffrage.[16] Similarly to the new movements of agricultural workers and industrial workers, their movements were considered as subversive activities, and mass emigration could not be halted either (e.g. by a targeted policy). The election campaigns, not free from violence; the wasting away of Slovakian cultural institutions, the school close-ups during the Bánffy Government, the Hungarianisation of geographical and personal names, and the setting up of Department III/3 for monitoring ethnic minority politicians and the press all triggered apprehension in Hungary and abroad, as the ethnic minorities brought their legitimate and imagined grievances to international forums. Consequently, the international reputation of Hungarians, who made history in 1848–1849, had spectacularly deteriorated (Jeszenszky, 1986). Especially by renowned foreign publicists (like the British Robert Wiilliam Seton-Watson or Henry Wickham Steed) and writers (e.g. Norwegian poet Bjørnstjerne Bjørnson) became the ringleaders in a smear campaign associated with ethnicity propaganda. Budapest did not take the untrue charge of "brutal" Hungarianisation[17] seriously, and also failed to reckon with the effects of leftist political powers and the criticisms by the influential freemasonry, intended at class war or world improvement caused erosion. This also applies to the criticisms received from the press and Parliament in the other half or the country, made for political reasons, although the Germans that constituted a one-third minority on the opposite side of the empire made similarly tenacious efforts at maintaining their decreasing power as the Hungarians, who had a very narrow absolute majority on this side of the River Leitha (Zöllner, 1984). In Austria, the administrator govern-

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ment, usually relying on Slavic Catholic electorates, also had difficulties in coping with the opposition forged into union by parliamentary obstruction (and sometimes street) fights. The efforts made by young Czechs, who applied radical means after the failed Czech effort at establishing a tripartite state (1871),[18] by Italian irredentist, who knew no compromise, by the tenacious Polish, who wanted to create a state, and the southern Slavic problem that became acute as a result of the 1875–1878 Balkan crisis forced the costly forms of a parallel public administration, which did not serve peace between the nations, and men's general suffrage in 1907. However, despite all these, with the consciousness of being the "masters" of the empire, the Germans, who paid the highest amount of tax, continued to claim the leading posts. Many who lost on decentralisation found the solution in Georg von Schönerer's programme of a large German unification.[19]

Meanwhile, the international relations also deteriorated in the region. In the 1880's and then in the early 1900's, the Monarchy embroiled in lengthy customs warfare with its neighbours: Romania, advocating a "nation unification" strategy, and Serbia. And as in October 1908, without a thorough diplomatic preparation, on the authorisation of the 1878 Berlin Congress, it annexed Bosnia and Herzegovina, in addition to the southern Slavs; it also triggered partial military deployment by the "host" state Turkey and the Slavic protector Russia. Despite Italy being a member of the alliance of central power since 1882, and Romania from 1883, both condemned the unilateral action and increased their irredentist campaigns. It was no accident that the Austro-Hungarian chief of staff, Conrad von Hötzendorf urged a preventive war against their unstable allies on several occasion (for good reason, as during World War both attacked the Monarchy from behind, Zöllner, 1984). The dynastic expansion of the Monarchy also inflamed internal ethnic tensions,[20] and the plans made in the crown prince's surrounding for transforming the Monarchy into a federal state could not mitigate them.[21]

By that time, the best Hungarian politicians had already been aware of the fact that what was at stake was not the illogical territorial expansion, which increased the number of ethnic minorities, but the survival of the Monarchy, including the Kingdom of Hungary. After the scandalous interludes of cutthroat debates on the development of armed forces in the European arms race, on the eve of the war, Count István Tisza, considered to be the most influential statesman of the empire, called for reconciliatory negotiations with the Romanians, Croatians and Slovakians.[22] However, the modest results achieved were already insufficient for winning the élites of the separatist ethnic minorities endeavouring to have independent national states.[23]

Collapse of the Monarchy, including the Kingdom of Hungary

The war that soon set the world ablaze and fundamentally changed the power structure of the region offered an excellent opportunity for the separation of ethnic minorities concentrated on the rims of the empire. In order to expand its resources,

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the entente persuaded the Italian and Romanian governments to betray their allies by holding out the promise of obtaining significant territories.[24] However, the leaders of the Croatian, Serbian and Czech political emigration also joined the competition for the expansion of the national land. They promised saboteur actions in return for weakening the Monarchy's hinterland, and subsequently also held out the prospects of deploying troops. The Yugoslavian Committee established in London in the spring of 1915 conducted a diplomatic campaign for creating a federative common southern Slavic state, while the Czech Committee Abroad, which advocated the union of the Czech and Slovakian nations, started operation a few months later in Paris. The territorial claims of the two organisations, which also competed with each other, stretched far beyond the ethnic borders (Zeidler, 2009, p. 21).

In order to prevent further war adversities Charles IV, who succeeded the elderly Franz Joseph I in 1916, offered a special peace agreement to the Entente in 1917, but the attempt failed. A few days later, however, Russia, which had plunged into a deep social crisis, was replaced by the United States as a belligerent on the Entente's side. With its declaration of war sent on 6 April 1917, it turned the tide, and in his speech delivered on 8 January 1918, President Thomas Woodrow Wilson already revealed the principles of the post-war arrangement. Its 14-point programme still included the maintenance of the Monarchy, but with the autonomy of the peoples under its control.[25] Essentially, England agreed with this. The earliest initiative for the division of the Monarchy was made by Russia. The policy of the Entente Powers only changed, however, when the German Middle Europe plan threatened with materialisation after the signature of the Treaty of Brest-Litovsk, and Berlin indicated the significance of its intentions by placing the allied Monarchy under military custody.[26] France endeavoured to mitigate the threat of a "German Europe" by weakening Germany's allies and laying the foundations of its own system of allies. Parcelling out the Austro-Hungarian Monarchy offered an obvious solution for both. In light of all this, on 7 January 1918 the establishment of an army of the Czechoslovakian migrants in France was ordered. Within barely half a year, its allies followed its example and recognised the Czechoslovakian National Council. (One of the leaders of this body issued the catchword: "Smash Austria-Hungary!") With this they gave a green way to the separatist ethnic minority movements in the Monarchy, as in essence they raised the Czechoslovakian, Southern Slavic and Romanian emigrant political lobbyists to the level of allies. Change in the circumstances was indicated by the fact that US Foreign Secretary Lansing declined the proposal made by the Monarchy's Foreign Ministry for an armistice (on 4 October 1918) on the grounds that it was no longer sufficient to offer autonomy to the ethnic minorities as a basis of peace, as they would already decide their fate independently (Zeidler, 2009, p. 22).

This new diplomatic failure accelerated the appointment of the government of the pacifist and pro-Entente Count Mihály Károlyi in Hungary (which actually took place on 31 October). The quest for peace had significantly damaged the soldiers' heart for combat, and the hinterland was stirring because of the hitches in supply. On 23 October, with Károlyi's leadership the Hungarian National Council was established

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and led the people to a civil war called the Aster Revolution, and as a result, Hungary regained its independence. However, the ethnic minorities also made a move... On 29 October, Croatia decided to break its nearly 800 years of legal bond with the Hungarians. On 30 October the Slovakian National Council announced union with the Czech nation, and on 25 November, the Serbians living in the south of Hungary declared their accession to the Kingdom of Serbia. This was followed by a declaration of union by the Romanians in Hungary on December 1, and one month later the assembly of Transylvanian Saxons also announced their accession to the Kingdom of Romania. These illegitimate forums were given great support after November 1918 from the Serbian, Czech and Romanian armies, which attacked the defenceless country in order to secure as favourable lines of demarcation as possible, not really disturbed by the intentions of the general staff of the Entente, and occupied Hungarian territories (Lipcsey, 2009, pp. 46–47).

Meanwhile, the Károlyi Government made desperate attempts at stabilising the country's precarious external and internal situation, primarily at organising public supply and restoring the operation of legislation. He declared the Republic of Hungary, and having a naive belief in democratic settlement, and also hoping for the legitimation of his government and the halting of the occupying armies, he entered into a humiliating pact with the Balkan military leaders of the Entente. Military considerations hardly justified the Belgrade convention (13 November), as the Padova ceasefire concluded with the collapsing Monarchy had been in effect, and pursuant to this agreement, no foreign army was stationed on the (Zeidler, 2003, pp. 31–32). Seeking the triumphant parties' benevolence, the Hungarian delegation nevertheless accepted an unfavourable occupation plan along the southern border section, and started the withdrawal and disarmament of the several hundred thousand strong Hungarian army, who returned home inordinately, and moreover, they even gave up significant assets to the Entente troops.[27] Nevertheless, these bona fide and irresponsible actions failed to earn higher appreciation for the Károlyi Government among the winners, but made the country militarily vulnerable. Negotiations with the Slovakian and Romanian parties about federative re-organisation failed, similarly to the proposals for territorial autonomies unilaterally offered to the Ruthenian and German minorities, and the late autonomy agreement concluded with the pro-Hungarian representation of Slovaks was even less successful against the Slovakian National Council. The Entente continued to refuse to recognise the Károlyi Government or the Berinkey Government that replaced it, and did not contain the advancing Serbian, Czech and Romanian armies, which obviously intended to give the Paris Peace Conference, convened on 18 January 1919, a foregone conclusion. The Vix Memorandum of 19 March 1919[28] ordered the depleted Hungarian army to give up further areas and thus the country would have been cut to one-third of its territory. These tragic conditions foreshadowed the future borderlines. Recognising the total failure of the pro-Entente policy, the government refused the memorandum and resigned.

Károlyi, in the meantime elected as head of state, asked the social democrats to form a cabinet, and already hoped support from the international labour movement

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and Soviet Russia. In the new cabinet key roles were granted to the representatives of the Communists' Hungarian Party. Especially Béla Kun, the Foreign Commissioner of the Soviet Republic proclaimed after the merger of the two parties, who acted as an ally to the "fraternal" Russia, and proposed negotiations to settle the territorial claims made by the Entente on the basis of Wilson's principle of peoples' self-determination.[29] At that time, the Entente sent general Jan Christiaan Smuts to Budapest, with the intention to have a slightly more favourable line of demarcation accepted. However, with the conditions still unacceptable for any Hungarian government, Paris failed to get through, so to exert pressure; they allowed the Romanian troops to take possession of the eastern half of the country up to the River Tisza. The newly organised Red Army successfully halted the advance of the Romanians launched on 16 April 1919, and within a few days they also repulsed the Czech armed forces even beyond the language boundaries in the north.

But the country's financial and military strength was insufficient was insufficient for permanent success against vastly superior forces. For this reason, as a result of two confrontational telegrams by French head of state and the chairman of the peace conference Georges Clemenceau, the military leadership withdrew from the occupied territories. This withdrawal extorted by a double-edged (threatening and promising) diplomacy demoralised the army and so they could no longer resist the repeated offensive by Romanians, who did not stop at the line of demarcation. On 3 and 4 August, the Romanians occupied Budapest without opposition. The Soviet government did not wait until that date: they resigned on 1 August, and the majority of its members fled abroad. The trade union government taking office was arrested – with Romanian support – by a group organised of political adventurers on 7 August. The country fell apart to six regions under separate controls and chaos set in. In order to conclude the peace treaty as soon as possible, a British diplomate, George Russell Clerk was engaged in Paris to facilitate the formation of a legitimate Hungarian government on condition of the withdrawal of the occupying Romanian troops. As a result of his mission, (after grave atrocities[30]) in November 1919 the Romanian army withdrew from the capital city and from between the Danube and the Tisza. A few days later (on 2 December) the government of Károly Huszár was formed and at last an authorisation was granted from Paris to appear in the presence of the winners at the Peace Conference.

At the Paris Peace Conference

The Hungarian delegation led by Count Albert Apponyi (who had a bad reputation for his pro-German attitude and for his 1907 draft bill in favour of the spread of the national language) arrived in Paris on 7 January. The members included to subsequent prime ministers: Count István Bethlen and Count Pál Teleki, who had both been aware, since Clemenceau's Memorandum (of 13 June 1919) of the fact that they had to expect losing the greater part of the country (Zeidler, 2003, pp. 74–75). However, it was a new development that territories had to be given up for the benefit

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of a "partner state", namely Austria, by redrawing one of the oldest borderlines of Europe (which had been in place for more than a thousand years).[31] Such a mutilation by more two-thirds of the territory and 58 per cent of the population, the drastic reduction of the army and the instructions on the payment of extensive restitutions cast doubts on the self-sustaining capacity of the remaining country. The uninhibited territorial claims by the neighbouring peoples had already been on the table of the expert committees a year earlier. All the three subsequent successor states lodged claims for territories and industrial areas with a majority of Hungarian-speaking population. (Thus the Czechs, the Serbs and the Romanians made attempts at presenting Csallóköz, the coal basin around Pécs, and the eastern rims of the Hungarian Plains, respectively, as if they had a legitimate right to them, e.g. referring to the strategic significance of railways.) The Anglo-Saxon powers, and essentially also Italy, considered the demands of the minor allies legitimate up to the ethnic borders; however, the French position predominated repeatedly in most cases. Passing on responsibility to the defeated parties and ransoming them for the damages and losses caused were in the common internal policy interest and endeavours of the victorious powers, however, obtaining influence over the Central European regions was mostly coveted by French diplomacy. This was certainly due to their "holy hatred" of Germans[32] ever since the 1871 annexation of (mainly German-inhabited) Alsace and Lorraine. Thus, France was perhaps the most interested in weakening Germany and limiting the opportunities of revenge. This included the prevention of Germany from finding strong allies for any possible retort. This was the reason for dividing the Monarchy and the Ottoman Empire, for taking additional areas from Bulgaria and imposing substantial restitution penalties on all of them. On the other hand, Poland, Czechoslovakia, Romania and Yugoslavia were meant to have a role in halting the spread of Soviet Russia and bolshevism. Thus, to oblige six allies by granting them territories and financial goods (through restitution) and by imposing a serious punishment on a single country seemed to be a reasonable solution

The peace conditions received on 15 January surpassed the worst expectations of the Hungarian delegation. Therefore it was highly apposite from them to present a professional memorandum to the experts of the conference right upon their arrival in order to somewhat offset the frequently grossly cooked data lines and propagandistic argumentations of ethnic minorities (the authenticity of which was subsequently doubted by the decision-makers themselves). The Hungarian position was worded by Count Albert Apponyi, who was an excellent speaker (Szarka, 1998, pp. 285–297). Next day in his speech delivered in French with English and Italian summaries before the Supreme Council (including heads of government and ambassadors), Count Apponyi called the document unsuitable for securing equitable and permanent peace and unacceptable. He complained that the decision made by the right of the winner was disproportionate to Hungary's war efforts. Of all losing parties, a country that had not been completely independent and was not granted the opportunity to represent its position and participate in drafting the peace was afflicted by the worst mutilation of its territory. He criticised the violation of the principle of ethnicity[33] because

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nearly five million Hungarians and Germans were thrown at the mercy of the successor states. Already the mass redundancies of Hungarian teachers and administrators evidenced political discrimination. As the method of decision-making most compliant with principle of self-determination the speaker proposed referendum concluded in a controlled framework.[34] He also made reference to the advantages implied in the country's exceptional geographical unity, which justify integrated control and management. Finally, he gave a flash of the exposure to the spirit of revenge if a forcible settlement was made, and the security risks related to the oppression of minorities (Szarka, 1998, pp. 285–297). Apponyi's stately argumentation had an impact on Prime Minister Nitti of Italy. The head of the British government Lloyd George showed interest in the data evidencing the Hungarian claims, and in response, the chief Hungarian negotiator presented the audience with the so-called Red Map by geographer Pál Teleki, displaying the scale data of the 1910 consensus. Its novelty was that mountain and barren lands were marked white, and thus it gave a graphical portray of the predominance of Hungarians in the spatial structure of the Carpathian Basin. Based on what they saw and on the documentation submitted several days earlier, the British delegation, supported by Italy, motioned for the renegotiation of the borderlines and certain economic issues. As a result of the rigid French position and vehement opposition by the minor allies, finally they stuck to the original conditions, despite the truckload of evidence added by the Hungarian delegation to its various modifying motions richly supported by maps and statistics. However, this thorough and professional documentation that gained appreciation was only sufficient for a little more lenient financial conditions and textual corrections not affecting the essence. This text was received by the delegation on 5 May with the accompanying letter by the new French Prime Minister Millerand, providing the border-setting committees' option for making proposals on the modification of any border section they might consider unjust (however, in contrast to the increased expectations of the Hungarian public, this provision only applied to setting village borders, Zeidler, 2009, pp. 37–39).

The Hungarian peace delegation considered the authentication of the document unsupportable and they resigned. However, due to its predicament, the Hungarian government was not in a position to refuse signature. This fifteen-minute diplomatic act took place in the large Trianon Palace on 4 June, with two minor public administrators, the Minister for Public Welfare and the Minister of Labour, and the ambassador plenipotentiary signing the peace document on behalf of Hungary. At 10 o'clock on the day of signature, life stopped in the remnants of Hungary: public institutions and entertainment facilities closed, traffic stopped, flags were let fly at half mast, the bells tolled and the air-raid sirens gave a hoot. The entire society was in mourning.

Effects of the peace dictate

The ruthless interests of great powers imposed disproportionately grave peace conditions on Hungarians, who received the peace dictate with astonishment and shock. They had every reason to do so. Hungary (excluding Croatia) lost 67 per cent of its

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territory.[35] The victorious powers increased the territories of six neighbouring countries by chopping up Hungary, creating a peculiar situation: this is the only country in Europe that borders itself, as depicted in the map below (Chart 1).[36] The country's population reduced from 18,264,533 to 7,615,117 (Vizi, 2016, pp. 9–10). One of three inhabitants in the areas torn away was a Hungarian, and one-third of these Hungarians lived in blocks, right next to the new borders, making ethnic majorities. Underlying these drastic decisions there was undoubtedly a kind of anti-Hungarian sentiment, among experts as well as among the highest circles of decision-makers. However, Miklós Zeidler gives conclusive examples of the fact that these prejudices could only be enforced to the extent allowed by the current power interests (Zeidler, 2009, pp. 30–31).[37]

Chart 1: Country parts annexed after the Peace Treaty of Trianon

Naturally, the peace-makers expected the fact that Hungarians would not easily resign to such an extent of mutilation, and so they made efforts at making military retort impossible for them. Similarly to the other defeated countries, Hungary was required to drastically reduce its army. Mercenary troops of maximum 35,000 people were only

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Table 1: Size and population ratios of the annexed areas

The "beneficiary" country	**Area of the granted territory (km²)**	**Population of the annexed territory (person)**	**Percentage ratio of the Hungarian population (%)**
Czechoslovakia	61,633	3,517,568	30.3
Romania	103,093	5,257,476	31.6
Kingdom of Serbia, Croatia and Slovenia	20,551 (and Croatia: 42,541)	1,509,295 (in Croatia: 2,621,954)	30.3 (in Croatia: 4.0)
Austria	4,020	291,618	8.9
Italy	21	49,806	13.0
Poland	589	23,662	1.0
Total annexed:	189,907 (including Croatia: **232,448**)	10649416 (including Croatia: **13,271,370**)	

Source: Edited by the author

allowed for policing and border control, all modern arms (tanks, navigation and aviation fleets) were liquidated and all weapons were confiscated. Setting up a general staff and the conventional forms of military administration and mobilisation were prohibited. Concerning ammunition, only the topping up of any used stocks were allowed. The peace document went into minute details concerning post-war reparations, however, the financial chapter only required the blocking of public revenues as coverage for the subsequently established 200 million crowns payable as indemnity and occupation costs. Chapters XI and XII regulated the conditions of railway and waterway transport (despite the fact that the Romanian army had "rescued" the overwhelming majority of the railway transport equipment from the country well in advance[38]). The peace treaty regulated Hungary's economic, political and diplomatic ties with the great powers, the successor states and the newly established League of Nations, including citizenship and property.

The treaties concluded near Paris undoubtedly reduced the number of vulnerable ethnic minorities on the continent, but each of the states established on the ruins of the Monarchy still remained multi-ethnic (e.g. in Czechoslovakia there were more Germans living than Slovakians). In order to offset this doubtful outcome, the victorious powers set up a system of treaties for the protection of minorities, however, they did not apply even to the losing large powers, and a significant part of the successor states (including Hungary's neighbours) endeavoured, by every means, to escape the fulfilment of their obligations. Equal treatment of the minority population in the annexed areas could have been a token for the long-term sustenance of these treaties. However, the successor stated made efforts at keeping the obtained areas under their control "forever" by the creation of homogeneous nation states (i.e. by brutal assimilation and settlement policies). The operation of international minority protection forums also contributed to this, as they adopted doubtful decisions, in only a fragment

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of the disputes, and rarely if ever to the benefit of the complainant minorities (Romsics, 1998, pp. 204–213, 227).

The peace treaties concluded near Paris caused serious disruptions in the economic processes of the region. This risk was indicated in 1919 by the renowned economist J. M. Keynes, who participated in the peace conference as an expert (Keynes, 1920). The manufacturing excess capacity due to the gross shortage of raw materials and the cutting off of territories caused a difficult-to-handle problem in the operation of the Hungarian economy. More than 400,000 Hungarians chased away or fled from the successor states had to be taken care of. For years they led a hand-to-mouth existence in railway carriages and emergency homes (Csóti, 2002). Certain flourishing city centres and regions suddenly became withering rim areas (Kovács, 1990). The secluded and autarchistic economic policies of the successor states terminated the previous free movement of labour and capital and the smooth division of work that had evolved between the various economic regions over the centuries, and this had adverse impacts on the entire Carpathian Basin that have been felt to this very date.

Therefore the peace forged along rude power interests was destined to be short-lived. Bitter disappointment and indignation overpowered the entire society. Protecting demonstrations and memorial services were held one after the other. All political trends in the Hungarian society urged a review of this punitive settlement. Differences concerned at most the extent of territorial claims. The government made efforts at keeping this psychosis, also incited by irredentist social organisations, on track,[39] and also capitalising on it according to its political intentions (partly to mitigate class conflicts and partly to support revisionist external policy).

Later on, numerous former decision-makers admitted the legitimacy of Hungarian revisionist demands. Nevertheless, the international supporting campaign organised by the press guru Lord Rothermere at the end of the 1920's failed despite the fact that in contrast to the Hungarian government's previous rigid position, instead of the restauration of the full territorial unity of the country, he only encouraged equitable political borders up to the language borders (Romsics, 2003, pp. 238–239). However, the large powers refused to support a correction compliant with the principle of self-determination, as that would have been tantamount to admitting their previous fallacies. The affected successor states formed a military and political alliance (Little Entente)[40] to combine forces to prevent the loss of their estates obtain. Their neighbourhood and minority policies were shaped in the spirit of the psychological pattern "I am angry with you because I have hurt you". Thus the opportunities of a compromise in revising the peace narrowed for good. The failure of this peace that did not serve reconciliation in Europe but laid the basis for a military revenge instead was also indicated by Germany's subsequent aggressive tactics. Despite the best efforts of the allies, by the 1930's the Third Empire had developed into an economic and military power that could afford the annexation of Austria and the Sudetenland, and then together with the fascist Italy, which was found the increase in its territories insufficient, it was authorised to decide territorial disputes with the Czechoslovakian and then the Romanian successor states. Due to the lenient conduct of the western large powers, in 1938 the German-Italian

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arbitration awarded the southern part of today's Slovakia, predominantly inhabited by Hungarians to Hungary.[41] This was followed by the re-annexation of Subcarpathia, populated by relatively less Hungarians, but the restoration of the border was of primary strategic significance due to the historical alliance with Poland.[42]

In the summer of 1940, following unsuccessful Hungarian–Romanian negotiations, both parties agreed to arbitration by large powers. This time Northern Transylvania and the Hungarian-populated Sekler Land were re-annexed to Hungary (pursuant to the second Vienna decision).[43] In April 1941, Bácska, Drávaszög and Muraköz were re-annexed in the south.[44] However, the Germans cynically capitalised the territorial disputes between the countries of the region in their war against the Soviet Union: they urged the competing parties to make increasing concessions, or otherwise they would take with actions that served the benefit of the other party.

Involuntarily driven to another war due to the revision, Hungary had to share the fate of the defeated once again. The propaganda spread by the successor states stigmatised Hungarians as collectively guilty, despite the fact that all of the neighbouring countries entered the war in alliance with the Germans. As a retort for border changes, in the endgame of the war, the damages to and discriminative treatment of the institutions, church and cultural communities of Hungarian minorities led to gross atrocities (ethnic cleansing). The Hungarian community was intimidated by the retaliatory actions performed by the Maniu Guards in Romania (Gábor, 2016, pp. 104–105), and by the murder at least 20,000 listed civilians in Yugoslavia (Arday, 2002, pp. 145–146). In Czechoslovakia, considered to be democratic, masses of people were deprived of their citizenship, tens of thousands were deported and a hundred thousand people were resettled and their assets were confiscated to create a homogeneous nation state. This time the Anglo-Saxon large powers considered a correction of the borders along the Trianon line but close to the ethnic boundaries, and the experts (including Russians) even kept a plan for an independent Transylvania on the agenda, and still, the armistice agreement enforced the 1920 borders. At its meeting held in September 1945, the only correction the Council of Foreign Ministers considered possible was a minor one along the Hungarian–Romanian border. But Soviet Commissar Molotov firmly rejected the proposal. Nevertheless, the Hungarian peace delegation made an effort at getting through a correction by 22,000 sq km, in a zone that was once exclusively inhabited by Hungarians but had become partly Romanian-populated due to resettling, but it was not granted diplomatic support. It was refused despite the fact that the proposal, based on the principle of mutuality, could have created a situation in which nearly as many Romanians would have come under Hungarian control as the number of Hungarians stuck in Romania. Although this arrangement and political practice was not too principled but efficient in practice, and if generally applied, it would have ceased Hungary's unilateral vulnerability to blackmail, and reciprocity could have pressed the successor states to apply more temperance in their minority policies. However, instead of equitableness and balancing, once again "large powers' rationale" predominated in the decision-making process. The 1947 Peace Treaty of Paris reflects directing disputes towards the least resistance. It cynically turned a blind

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eye to collaboration between the Romanians, Slovakians, Croatians and Slovenians and hit Hungary by upholding the territorial provisions of the 1920 peace dictate. The difference is that the United Nations, which replaced the League of Nations, did not elaborate a minority protection system similar to the one adopted after World War I. With this, they encouraged Hungary's neighbours, repeatedly declared to be "nation states", to successfully complete the homogenisation of their multi-ethnic countries, and sent neighbourhood to a repeated low.[45] The Hungarians living on the other side of the border were given as hostages of this policy, and similarly to Germans, they were about to face even greater ordeal.

As an unfortunate outcome of the decades that have passed since then is a reduction in the headcount of Hungarians to one-third in the Carpathian Basin, while the neighbouring peoples have nearly doubled, including the assimilation gain (Kocsis and Tátrai, 2015, p. 34).

Trianon's aftermath

In the historical memory and identity of Hungarians, made a scapegoat, plundered and humiliated, the shock caused by Trianon and its indirect consequences have caused permanent distortions. Not even the change of regime could find a remedy for this schizophrenic and undeserving situation. After several aborted attempts, a consistent programme was elaborated for the unification of the nation across borders during the various Fidesz-led governments (e.g. Hungarian ID card, preference act, and then the adoption of double citizenship, Vizi, 2016, pp. 203–235). In order to educate the generations that have been made completely indifferent and to improve social cohesion, the Day of National Togetherness has been adopted at schools (on the day of singing the Treaty of Trianon). The parent state has also undertaken a significant role in the maintenance and improvement of Hungarian communities and institutions beyond the borders. In addition to appearing as a patron (e.g. as a supporter of autonomy), in neighbourhood policy it makes genuine efforts at reconciliation with the host nations through maintaining and strengthening good neighbourly relations. These efforts are also supported financially and morally by the European Union in the framework of regional co-operations. Although the elimination of distortions imprinted in the self-image as a collective failure and the resolution of grievances mutually suffered by the neighbours during the centuries of coexistence may require decades, the question is worth asking today, on the hundredth anniversary of the Treaty of Trianon: Will loyal citizenship of minorities and the generous policies of majority nations securing national development create harmony based on agreement and reasonable co-operation in the Central Danube Valley?[46]

Despite the existing prejudices and mutual suspicion, it can be established as a matter of fact that the Hungarians living beyond the borders have always acted in a constructive manner in spite of all kinds of subordination and limitation of rights. They did not take any irredentist or rogue action (and neither did the parent state) when Czechoslovakia, the Soviet Union and Yugoslavia disintegrated. During the change of

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regime, they advocated and worked on democratic transformation, whether in opposition or in government. They did not use any of the radical or violent methods available in both the western and the eastern repertoire of ethnic minority struggles, quite the contrary. Thus Hungarians do not represent any security risk in the region, rather more, they can be considered as a stabilising factor already because of the double affiliation of separated Hungarians, as the knowledge of several regional languages, cultures and mentalities is a peculiar value. Based on these criteria, we have good reason to hope that – in the shared interest of the challenges posed by globalisation and in the spirit of respect and mutual concessions – Hungarians and non-Hungarians will create a common future that brings peaceful increase in the Carpathian Basin.

Notes

1 This included significant parts of today's Czechia, Austria, Croatia, Bosnia-Herzegovina, Serbia and Romania.

2 During the reign of King Matthias I, 74 per cent of the country's population may have belonged to the Hungarian ethnicity (or 66.1 per cent, if Croatia is included). By 1790 this ratio had dropped to 31.5 per cent (Kocsis and Tátrai, 2015, pp. 6–7).

3 Settlers were granted exemption from taxes for five years, freedom of movement, and construction timber and sawing seeds free of charge (Kollega Tarsoly, 2011, pp. 33–34).

4 Hungarians' settlement in Croatia was simply called "Mongol invasion" in the press published in Croatian.

5 In 1804, Serbian Stevan Stratimirović, archbishop of Karlovci sent a draft to Tsar Alexander I, motioning for the liberation of Serbia and the annexation of Southern Hungary, partly inhabited by Serbs, under the leadership of a dukes of the Romanovs (Gyetvai, 2015, pp. 62–63).

6 In 1910 they made the relative majority of the empire (46.6%), while in a narrower perspective, in the Kingdom of Hungary they shared 25.8 per cent.

7 Slovakians entertained the concept of the Great Moravian Empire, a vassal to the Franks; Croatians clung to their Illirian origins before the Romans, and Romanians to the Dacian heritage, also considering themselves as heirs of the Roman culture. Before long, they put forward bellicose programmes, including the Daco-Roman continuity theory. In 1838 the Greater Romania unification programme, also targeting the detachment of Transylvania, was born in Walachia, a region under Turkish and Russian rule at the time.

8 An effort made at this included the "peace pact" concluded by Lajos Kossuth, number one leader of the Hungarian war of independence with the leaders of the Romanians. During the decades he spent in emigration, he arrived at the idea of the Danube Confederation, an alternative offering longer-term benefits than the dualist solution for the peoples of the region.

9 Quote from Friedrich Beus (Vadász, 1998, p. 233). Meanwhile, the aggregate ratio of Slavic peoples (46.6%) still exceeded the joint ratio of the two leading nations (43.5%) even in 1910 (Pándi, 1995, p. 184).

10 One parliament and one government operated in Vienna and another one in Budapest; foreign, defence and military affairs and finances that served as a coverage for the previous were under the control of common ministers, however, instead of a superior imperial parliament, they only reported to so-called delegations of 60 persons each, and ultimately to the emperor. This structure also included numerous dysfunctions and remnants from feudalism.

11 In 1913, per capita DGP was 435 crowns in Hungary and 304 crowns in Croatia. In the Austrian and German provinces it was 790 crowns, in the Czech provinces it was 630 crowns, in the coastal provinces it was 450, in Carniola and Dalmatia it was 300, and in Galicia and Bukovina it was 255 crowns (Katus, 2012, p. 473).

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[12] Broad language use rights were ensured in culture, public administration and justice at the level of communities and counties. The authentic translation and publication of statutes in the languages of the ethnic minorities were ensured, and any of these languages could be used for records made at municipalities. Courts were allowed to communicate with the communities, congregations and associations in their own languages. The language of village and church administration and school education could be freely chosen, and Hungarian was mandatory only in contacts with the government. The act also ordered the establishment of minority departments in education wherever the ratio of ethnic minorities so required. At the same time, ethnic minority citizens and associations of ethnic minorities were allowed to establish tertiary educational institutions according to their own requirements and from their own funds (Katus, 2012, pp. 347–350).

[13] The Serbian and Romanian critiques of the act demanded the inclusion of the establishment that ethnic minorities were state-creating constituents and demanded that the official language of municipalities should be the (local) language. In Transylvania Romanians demanded a Romanian "voivode", a Romanian minister in the government and a Romanian department in every ministry, speeches made in Romanian in Parliament, a separate university and a separate Romanian army (Katus, 2012, pp. 592–594).

[14] Although these decades saw the drafting of numerous relevant liberal acts, e.g. about compromise with the Croatians, and about the Greek Catholic faith, which vested broad religious autonomy rights in Serbian, Romanian and Ruthenian ethnicities, or the acts about the separation of the church and state, and about the full emancipation of the Jewish people, drafted subsequent as a result of efforts made in the field of ecclesiastical law.

[15] During the fifty years of the Monarchy, GDP increased by 2.7 per cent per annum in Hungary, and this was equal to the German growth rate. In other words, in contemporary Europe, only Sweden and Denmark developed faster (Katus, 2012, p. 472).

[16] The series of Hungarian millennial celebrations were held in 1896 in the illusion that the Medieval large power would revive, and this rendered the realistic assessment of the historical role and contribution of the admitted ethnic minorities impossible. This was exactly why the latter faced the event with stern indifference, while considering themselves as state constituting factors, and made their citizen loyalty conditional upon the government's concessions.

[17] Undoubtedly, Hungarians' demographic increase significantly exceeded that of ethnic minorities. This had three components: the high reproductive rate of Hungarians (mainly due to the more favourable mortality rate), the human capital lost to emigration, which mainly afflicted the ethnic minorities living on the outer rims of weaker carrying capacities in the country, and the gain from (mainly spontaneous) assimilation (Jewish, Slovakian and German) on areas of mixed population, which had resulted in a slight absolute majority (54.4%) by 1910. However, "violent assimilation" is not evidenced by the fact that barely more than 23 per cent of the ethnic minorities living in Hungary spoke Hungarian, the official language of the country.

[18] Part of the political élite supported the Czech efforts at transforming the dualistic Monarchy into a tripolar one by raising the 3 developed Czech provinces among the peers, however, there were concerns that the Polish, the Italians etc. would then come up with similar claims. Soon, a trialistic political trend based on a Croatian–Serbian(–Slovenian) ethnic background gained ground among the Croatians (Zöllner, 1984).

[19] However, the so-called Anschluss would only be carried out by Hitler's Germany in 1938.

[20] Due to the failure of the unification of Great Croatia, Croatia was looking for a way out in a Yugoslavian cooperation, while Hungarians deplored that the two provinces were governed by the common Finance Ministry, despite the fact that Franz Joseph I announced the annexation of the province on the legal basis that Hungarian kings ruled the area in the Middle Ages.

[21] Turning the western part of the empire into a federal state was only declared by the new emperor and king Charles IV on 16 October 1918, but within a few days the empire split up into national regions.

[22] It was István Tisza who opposed joining the war after the Sarajevo assassination, saying that even if won, it would result in an increase in the Slavic and Romanian population, which in turn would represent an even more threat to the territorial integrity of the state.

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[23] The leading Romanian ethnic minority politician, Ioan Slavici's following words shed light on the irreversibility of the separatist intentions: "Do not believe that you can win us by smartness or kindness. We do not want the Hungarian government to treat the Romanian people well, we would rather like them to oppress them as cruelly as possible. Because we are not seeking agreement, in the interest of our future, we need strife" (Raffay, 2015, p. 56).

[24] They agreed with the Italians in London on 26 April 1915 about giving up South Tyrol, the Istrian Peninsula and part of Dalmatia; and then with the Romanians in Bucharest on 17 August 1916 about the annexation of Transylvania and other areas mostly inhabited by Hungarians, up to nearly the River Tisza.

[25] He recommended the adjustment of the border along ethnic boundaries to the benefit of Italy, and urging the restoration of Poland, he also questioned the political borders of the Monarchy, although at that time not yet its raison d'être (Pándi, 1995, p. 280).

[26] Friedrich Naumann's Mitteleuropa Plan was born in 1915, and outlined an enormous area under German economic influence between Scandinavia and the areas leading to the Caucasus. Dependence of the peoples of the region on Germans was also reflected in the draft (Zöllner, 1984).

[27] The commander-in-chief of the Balkan front was not authorised to mark out lines of demarcation cutting deeply into areas inhabited by Hungarians, and he did not comply with the agreement he himself dictated. On the other hand, Károlyi satisfied all his demands. Applying a bad tactic, he also confined the troops of the victorious commander Mackensen of the German army returning from the lower stretches of the Danube (although they could have been extremely useful in repulsing the Romanian troops that broke into the country; Nagy, 2019).

[28] Lieutenant-colonel Ferdinand Vix was the Entente's liaison officer in Budapest (Zeidler, 2003, pp. 69–71).

[29] Letter by Béla Kun to the Paris Peace Conference, dated 24 March 1921 (Zeidler, 2003, pp. 71–72).

[30] In the course of "pacification" grave atrocities were made (647 persons lost their lives in other than combat operations), and requisition and damage amounted to 9 billion golden crowns. The robbery of the art treasures of the Hungarian National Museum was only thwarted by General Bandholtz's forceful response (Lipcsey, 2009, p. 104).

[31] The expression "thousand years old borderline" also applies to the north-western Czech and eastern–south-eastern Romanian border sections.

[32] French Prime Minister Léon Gambetta: "Republicans should closely unite in the idea that objection by law and justice will be a revenge on violence and dishonesty" (Vadász, 1998, p. 119).

[33] This assumption is supported by the fact that an area of 103,000 sq km were cut out for Romania, making reference to less than 3 million Romanians living in Hungary (including 2 million ethnic minorities), while only 93,000 sq km were left for 7.3 million Hungarians.

[34] The Czech head of state Tomáš Garrigue Masaryk, who had the reputation of being an exemplary democrat, cautioned against holding regional referendums, since he was confident that in this case the newly established Czechoslovakia would lose not only the purely Hungarian Csallóköz, but even the Slovakian-speaking population would decide to return (Popély, 2010, pp. 190–191).

[35] The only territorial correction took place in 1921 by a referendum at the western border, which resulted in the re-annexation of Sopron and its surroundings to Hungary.

[36] This number changed to eight on the signature of the 1947 Treaty of Paris and then after the disintegration of Czechoslovakia, Yugoslavia and the Soviet Union (Austria, Slovakia, Poland, Ukraine, Romania, Serbia, Croatia and Slovenia), and Italy was excluded from among the "beneficiary" countries when the seaport Fiume (currently: Rijeka) was annexed to Croatia. (Subcarpathia was included in Czechoslovakia between 1920 and 1939, in Hungary between 1939 and 1944, in the Soviet Union up to 1991, and it is in Ukraine today.)

[37] This assumption of his is also evidenced by the fact that in 1912, while President Wilson of the United States, a country that did not even ratify the peace treaty concluded near Paris, was governor of New Jersey, he made the scandalous statement that the immigration of Hungarians should be prevented as their intellectual level fell short even the abilities of Chinese coolies. In Hungarian public opinion it was incorrectly ingrained that the Trianon borders resulted from relentless anti-Hungarian sentiments. Without denying

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the existence of anti-Hungarian sentiments, a British diplomat saw the causes of merciless border setting in the fact that expert work was performed by separate committees, and exaggerated claims were made in each border section "in order to have enough to give concessions from". However, the Hungarian party was not granted the opportunity to participate in the preparatory work, and in the last stage of the exhausting work dragged for months, no strength and sufficient attention had been left for the substantial discussion of the meticulous and professional documentation handed over by the Hungarian peace delegation upon their arrival, and for the collation of the various proposals made by special committees, thus the decision-makers approved them without any amendment Cartledge, 2010, pp. 81–94).

[38] According to the 23 October 1919 report of the Clerk mission, the Romanians plundered the occupied territories, depriving them of the means of transport to the extent that fuel and food supply became practically impossible. Up to their withdrawal, they had robbed 39,395 draft horses, 1,302 locomotives and 34,160 rail carriages (Lipcsey, 2009, pp. 91, 111).

[39] E.g. in May 1921, Foreign Minister Miklós Bánffy requested the government to subject irredentist organisations to increased control as they jeopardised foreign policy interests (Zeidler, 2009, p. 107).

[40] About cooperation between the successor states between 1921 and 1938, see Ádám, 1989.

[41] Pursuant to the first Vienna decision dated 2 November 1938, 11,927 sq km were re-annexed with 1,060,000 inhabitants, 84 per cent of whom declared to be Hungarian (Romsics, 2003, p. 246; Zeidler, 2003, pp. 315–316).

[42] Approximately a hundred thousand soldiers and civilians could escape (and leave for the west) with Hungarian help thanks to the recapture in March 1939 from Poland grip of the Germans and the Soviets. The majority of the inhabitants in the area occupying 12 thousand sq km were Ruthenians, but Prime Minister Pál Teleki intended to grant them territorial autonomy. He submitted a draft act, however, under the war conditions, it did not enter into force (Romsics, 2003, pp. 246–247).

[43] The decision effective from 30 August 1940 re-annexed a territory of 43,000 sq km to Hungary. According to the 1941 consensus, 52 per cent of the population was Hungarian, 38 per cent was Romanian and 10 per cent was German (Romsics, 2003, p. 248; Zeidler, 2003, pp. 317–318).

[44] The area of 11,500 sq km was populated by 1,030,000 people. 39 per cent of its population claimed to speak Hungarian, 19 per cent German, and 16 per cent Serbian as their mother tongues. Banat, mainly inhabited by Germans, was brought under German control (Romsics, 2003, p. 251).

[45] Their means included the confiscation of assets, the limitation of linguistic and cultural rights, the collective deprivation of rights (Beneš Decrees), deportation and even genocide (e.g. in the winter of 1944–1945 in Yugoslavia). Not even Csallóköz and Szekler Land, still populated by an overwhelming majority of Hungarians, have been granted autonomy.

[46] A telling illustration of such distortions is the drop of the ratio of suicides from 0.0293 to 0.0236 within just a single year in Hungary. Such a reduction was unprecedented anywhere else in Europe at the time (Romsics, 2003, p. 248).

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Gábor Máthé

Post-Modern Rule of Law

Summary
In this paper the classical rule of law, born in the 19th century, is compared to the current post-modern rule of law through the opinion of the author and of the relevant international experts. The paper focuses on nation states' sovereignty, the settlement of jurisprudential problems between the European Union and its Member States, the elimination of anomalies in the post-modern rule of law, as an ultimate guarantee, the constitutional courts of nation states and the Conference of European Constitutional Courts.

Keywords: nation state's sovereignty, postmodern rule of law, postmodern rule of law, the constitutional court of nation states, Conference of European Constitutional Courts

Classical Rule of State in the 19th Century

Balance in the first half of the past two hundred years was based on the principles of military alliance, settled territorial arrangements and cooperation between the three founders of the Holy Alliance: Tsar Alexander I of Russia, Emperor of Austria and King of Hungary Francis I, and King Frederick William III of Prussia. In the history of Europe the initiatives taken by great powers were accompanied by illustrious congresses. Among them, of paramount significance was the 19th-century Congress of Vienna, as it successfully managed international crises up to 1914 (Harmat, 2015). The simultaneous enforcement of the three requirements was the token of the continent's success. Legitimacy, or in other words, the exercise of power through inheritance or elections, and then the alliance of stated in equilibrium was the criterion, and ulti-

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mately, responsibility for the future always predominated in conflict resolution. In the first one hundred years after the congress, a new order evolved. Legitimacy was proclaimed in opposition to the ideas of the French Revolution, and primarily monarchic and dynastic solidarity were manifest in this restoration going against the revolution. Moreover, this power was Christian: it was built in an alliance between the throne and the altar, and could finally remain continental (Máthé, 2015a).

However, once it was realised that the interests had changed, by the 1860's the alliance began to gradually incorporate the power policy principles built on fundamentally new ideas, and first and foremost it recognised the need to create the rule of law.

The two basic pillars of the rule of law is freedom and the sacredness of property: and in the triad of state, society and the individual person, it is an essential requirement that institutions are established to control the exercise of power. The early concept of the rule of law was a summary of the desires cherished by political liberalism: the ruler's subjection to positive law, the submission of state activity to law, and the prevention of using the formal opportunities inherent in legislation and execution for unlawful intervention in citizens' fundamental rights.

In the state that evolved, a compromise was made to the benefit of a formal state. According to the Viennese professor Ogris, the nature of the rule of law secures the integrity of law and order and not its content. The essence of the state is that through law it determines and unalterably ensures the trajectory and limits of its own operation, and the breathing room for its citizens. As he put it, directly, in its capacity as a state, the state should not reach beyond the scope of law in implementing moral ideas. It became clear that the retention of the elbowroom for certain legal titles, legal protection and judges has a stabilising and financially beneficial effect. Thus, politicians' interest became focussed on the results to be achieved, and formal legal protection became a central issue especially in the field of state administrative affairs. In Werner Ogris's witty wording: The idea of the rule of law drifted apart from the theory of the state and vigorously jumped over to administrative law and the academic discipline of public administration (Ogris, 2010, p. 23). This is because the crucial question was the enforcement of rights in practice. In response to this the compulsion of control over public administration was born, aptly expressed in Otto Mayer's opinion that the rule of law is the state of a well-organised public administrative law. Consequently, in 1896, the priority institution of legal protection, the Administrative Court, was also established in Hungary, and thus the citizens' protection against the unlawful measures taken by the state was manifest in a specific form. This was subsequently completed by other corner-stones like the division of power, the independence of judges and the system of fundamental rights, in place for several generations now. Submission of the classical power triad to law was ensured by great legislations: in addition to our commercial act, proposals that represented outstanding achievements in the codification of private law, the code of civil procedure, and the masterpiece of criminal law, the criminal code named Csemegi Code after its maker, which served several generations of lawyers in dealing with the facts.

The dual monarchy that evolved in Eastern and Central Europe in the 19th century comprised two independent countries: Austria and Hungary. They had com-

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mon affairs and joint organisations to handle them. As a multi-cultural entity that had an incredible geographical diversity, the Monarchy put the principles of the Holy Alliance into practice, successfully established the full range of the institutions required for the division of power and created the codes carrying European legal values (Sári, 1995; Máthé, 2015b). In a characterisation of the Monarchy, it is important to highlight that the system of law had priority and the economy unfolded within this framework. Basically due to its social motivation, between 1870 and 1914 the economy operating with the predominance of local markets resulted in a new, bourgeois lifestyle. The economy of the dualist Monarchy may be a notable example, as the budgetary ratio of pragmatic affairs was 70:30, and after a few changes, for the last time in 1908 it reached 63.6 to 36.4 to the detriment of the countries under the imperial council (Balogh, 2007). Consequently, the Hungarian sovereign benefited from economic efficiency. In the assessment of Eisenmann, a French historian, with the 1867 Compromise, Hungary was granted half of all the rights for a third of the costs, and obtained two-thirds of the influence in the Monarchy (Eisenmann, 1904).

Fredric Jameson, a significant contemporary US thinker, provided a highly pertinent assessment of the Monarchy in a postmodern cultural frame of mind. Among others, this is important because in our time theories are only created about the conditions of opportunities in our period, and they merely include lists of changes and transformations. Jameson endeavours to change by thinking of something in a historical perspective in an age when the method of understanding the present from the past has already been forgotten. "...the Austro-Hungarian Empire was in any way a nightmare. On the contrary, besides being the last of the old archaic empires, it was also the first multinational and multi-ethnic state: comfortably inefficient when compared with Prussia, humane and tolerant when juxtaposed with the czars; finally not a bad arrangement at all, and an intriguing model in our own postnational period, still riven by nationalisms" (Jameson, 1991, p. 316).

The postmodern rule of law in our days

The procedure of implementing the basic principles of the rule of law has never been seamless: either in the period of establishment or today. It is important to note that the rule-of-law model is far from being a closed system, and as such it needs to be constantly developed. Nothing guarantees that its achievements will last forever. This is well illustrated by the European Union in the 21st century. This is because the Member States struggle helplessly in the grip of the common and the individual systems of political institutions, as the situation has been characterised by the former President of the European Parliament, adding that in Europe, sovereignty is based on the separation of powers: we have a government Parliament can decide against, and an independent judiciary that controls compliance with the law.

At the beginning of the 20th century the Treaty of Versailles that closed World War I, upset the territorial order and destabilized Central Europe. After World War III, with the Yalta Conference and the subsequent Treaty f Paris, Europe set out on

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the way to becoming Transatlantic and gradually losing its global political influence. Then the Treaty of Malta, signed on 2 December 1989, reintegrated Central and Eastern Europe and represented a completely new standard of quality, as these areas were required to return to the political and economic relations laid down in the 20th-century Roman Treaties in the spirit of the Washington Consensus, mediated by the USA.

In a world that had become unipolar, the integration of Central and Eastern Europe departed even more from the previous established principles. The order of elements included in the Washington Consensus, namely, privatisation, deregulation and commercial liberalisation, was implemented on the basis of the scenario created by the international finance. The reason was that the creators of the programme failed to distinguish the various dimensions of statehood and the ways they relate to economic development. Privatisation resulted in enormous asymmetries and the state was supposed to correct them. Milton Friedman, the most excellent representative of free-market economics, aptly noted that the tenet has been proven: legal order is probably more essential than privatisation (Gecsényi and Máthé, 2009, pp. 16–18).

The correlations between these international processes are described by academician and professor of economics, Dr. Béla Kádár in a highly edifying assessment. His clear establishment of the facts is self-explanatory: "The international climate in which Europe's destiny was shaped by powers outside Europe for half a century evolved in the wake of two self-destructive world wars of the 20th century (and Europe's civil war): in Yalta, according to Soviet, and in Malta, in December 1989, according to American interests. The conditions and duties of the change of regime were determined from outside. This was a fundamental factor that shaped the elbowroom,... however, in this conceptual determination, closing the gap by granting financial support to the countries of Central Europe was not a strategic goal."

Although in the 1990's "the IMF was given the control panel to set the latitude in the economic transformation of the former socialist countries,... however, the IMF considered the content of the Washington Congress as a strategy," emphasised the doyen of Hungarian economics, whose professional stance is undisputed. To put it in another way: "In the absence of external financial support, the IMF therapy was merely a conceptual economic policy limitation of movement" (Kádár, 2018).

In his monography, Jameson gives a highly convincing diagnosis of the current theory of postmodernism: "...one may also wonder, with Adorno, whether 'in our time the commodity has not become its own ideology – that is to say, whether practices have not replaced rationcination (or rationalisation), and in particular whether the practice of consumption has not replaced the resolute taking of a stand and the full-throated endorsement of a political opinion. Here too, then, the media meets the market and joins hands upon the body of an older kind of intellectual culture" (Jameson, 1991, p. 406). A similarly true dramatic assessment claims that "even the nation-state itself has ceased to play a central functional and formal role in a process that has in a new quantum leap of capital prodigiously expanded beyond them, leaving them behind as ruined and archaic remains of earlier stages in the development of this mode of production" (Jameson, 1991, p. 420).

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According to an opinion that has become a firm conviction; the most significant international gap in development is that the compromise cooperation between the developed North and the feebly developed South, comprising the largest part of the world's population, has become unviable. In the globalising world, the asymmetric interdependences between capital exporter and capital importer countries appear to be additional principles. The narrowing of national sovereignty over Hungarian economy, in other words, giving the decisions determining the future structure of the economy into foreign hands leads to the expansion of transnational companies, which implement a global business policy through their strategic cooperation and the transfer of goods, capital and technologies. This globalisation has a harmful effect, as it erodes national sovereignty, and more specifically, state sovereignty, weakens the government's offset of the market preponderance. Thus globalisation re-defines the role of the nation-state as the efficient manager of the national economy (Szentes, 2002).

It should also be admitted that in the age of globalisation it is the governments' accountability rather than the role of the state that decreases. To a major extent, the success of efforts at making the highest possible profit at the lowest cost and without risks in the framework of cooperation with transnational companies depends on a government's policy. However, national economies should still make efforts at ensuring that mutually supportive impacts predominate national development.

Consequences of changes in the spatial structure

In the 1990's, a new concept emerged in social sciences: the supraterritorial space. As a new phenomenon, it indicated that something new had evolved in contrast to the traditional territorial structures of states. The relationship between the economy and law was predominated by the contemporary contractual system of international law, which, however, fit to the classic spatial structure, according to a diagnosis by József Hargitai, a specialist of the history of diplomacy. After World War I, modern international law did not represent a change in the traditional spatial structure of law, moreover, the internal development of international law, or if you please, its becoming international and expansion beyond European culture, did not trigger changes in the spatial structure (Hargitai, 2004).

If a state is not submitted to the legal rule of another state, it is sovereign. However, international law is not include any obligation to maintain sovereignty, thus a state may even waive part or whole of its sovereignty, say by joining a federation. "*Argumento a maiore ad minus* it follows from this that it is allowed to waive the partial elements of sovereignty, and this process actually takes place whenever a contract is concluded to the point where the concept of sovereignty, for example, by accession to the EU, is rendered nearly meaningless" (Hargitai, 2004).

The picture that had evolved by the early 21st century may be summed up as follows: in the system of international law and the universal treaties appearing in it, the state has been caught in the net of obligations that have upset the freedom of international law from values. The expansion of the modern-age tenet that law can also

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arise from alternative sources other than legislation is no accident. This law provides a framework for the world market structure, and broadly detaches itself nation-state or international legislations (Hargitai, 2008). The supporters of the new world order, or the postmodern world, proactively urge these processes, and while states are losing their previous political, legal and economic powers, other participants, acting in parallel and against the state, simultaneously increase their influence. In addition, multinational companies, civil society organisations, initiatives and NGOs also gain enormous influence, and using the globally enforced standards, they generate a peculiar "earthquake". As an example of the application of the so-called transnational law, MC's cross-border organisational structures need to be highlighted, let alone the syndrome characterised by the saying "the world is a global assembly line" with the flow of goods operated between the various branches and subsidiaries of international companies rather than export and import run by nation-states. In addition, as a peculiar development, they only obey regulations aimed at maximising profit within their concerns. In addition, they typically do not operate according to the law of the place of investment. A clear explanation may be given for this distinct emancipation through the fact that these companies realise revenues multiple of nation-state budgets.

The 20th century had an endless supply of modalities in "spatial changes". As an example, remember that in the second half of the last century, the aether was still subject to regional rights, however, today multinational telecommunication companies operate according to different rules. The globalised version of this traditional space is manifest as a virtual space (Internet). This is because the Internet has ruined the legal forms of spatial structure. The cyber space or virtual space is nothing more than the set of transactions, relations and ideas created between people and machinery in a communication net. It turned out that the worldwide web was also a scene for economic activities, and functions as a symbolic market, with the flow of real-life goods and capital. However, the state also discovered the Internet, and wants to use increasingly for the modernisation of public administration. The spread of information technology also had a special impact: a professional élite has evolved that takes action with increasing awareness against governments' restrictive legislation. Making reference primarily to the requirements of human rights, this team is technically well-versed enough in programming to override areas already regulated by law.

In order to conclude this outline description of the postmodern rule of law, an interesting feature is recalled. It is thought-provoking that the traditional forms of justice within the frames of nation-states have failed to prove suitable for the effective enforcement of the legal matters of transnational formations. Thus the enhancement of the role of international arbitration tribunals is no accident. It is conspicuous, however, that among the objectives of multinational empires having the power to organise, the "termination" of the state is not yet on the agenda. For the time being, it seems to be sufficient to change the role of the state according to their interests, after all, they need someone to implement the arbitration awards.

To sum up the above, it can be established that the legislative procedures and structures regulated on the basis of traditional nation-state constitutions (the hier-

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archy of legal sources and the legal system) are gradually falling apart. This allows the conclusion drawn at the end of a succinct and highly expressive study by Preuss (1999): The disempowering of state legislators has been implemented. Well, the deprivation of government legislators of their power reached a peak by the establishment of the European Union through the gradual expansion of the EEC. The EU came into existence by transfer of certain elements of the Member States' sovereignty and based on European values. Actually, sovereignty was the greatest achievement of the European civilisation, and the only framework for a viable democracy, claims Thierry Baudet with aphoristic wisdom. Due to volume constraints, the theoretical questions of the "division of power" between states cannot be discussed here, however, it is recommended by all means that sovereignty and the rule of law are complementary concepts (Máthé, 2014).

Return to the positivisation of law?

In his monography, Professor Helmut Coing highlights general legal positivism. He finds that "...in our age, law is the product of an evolution that from archaic social system to ancient high cultures and finally to the modern-day high cultures of our current social forms. This evolution is primarily manifest in control over the ever increasing complexity. Although law is, on the one hand, supposed to provide security for the prevalent regulatory expectation, on the other, it should leave room for the development of new structures of expectation and thus the evolution of further systems of rules" (Coing, 1996, pp. 87–88). In his opinion of the parallel between the normative and cognitive propositions, speaking of the current legal philosophy discourse, he specifically gives a criticism of Luhmann's (1981) theory. The essence of Luhmann's concept is that although positive law comes into existence and is enforced through decisions, a static world order has no role in its legitimation, in contrast to the foundations laid in the European tradition of classical natural law (Strauss, 1999). Positive law should especially be legitimised by the rules of its creation, the political procedure of the decisions adopted to select such rules. Classical natural law was the reflection of an eternal world order, and the idea of a classical justice presumed an overall perfect order of things that could legitimate law and provided criteria for the distinction between just and unjust, or lawful and unlawful, when legal decisions were made. However, by now it has become clear that under the conditions of our complex modern society, this is ruled out. To ensure "an adequate complexity of law", a "system theoretical interpretation" is required to replace it (Coing, 1996).

In the postmodern world of the 21st century, due, among others, to the above, adherence to the requirements of the rule of law is even more indispensable. The rule of law is an undoubtedly one of the fundamental values with legal security as its guiding principle and law used as a factor of gauging the state. Thus today the rule of law is: *a constitutional state* that regulates the procedure of legislation; *a state regulated by laws* that set limits to individual behaviour, establish government institutions and determine their structure and competence; and *a state that protects law* with the help

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of appropriate institutions that enforce compliance with the laws. Its characteristics also include: submission of the legislator to a constitution; the subjection of judicial power to law; the protection of fundamental rights; the accountability of state organisations for compliance with the statutes; the wording of legal orders and the clarity of promulgations.

In his monography published in 2018, Canadian professor Jordan B. Peterson gives an ingenious characterisation of our age: "The insane and incomprehensible postmodern insistence that [...] Society must be altered, or bias eliminated, until all outcomes are equitable. […] The fact that both of these cannot logically be true, simultaneously, is just ignored (or rationalized away with another appalling post-modern claim: that logic itself – along with the techniques of science – is merely part of an oppressive patriarchal system)" (Peterson, 2018, p. 314). People need principles or otherwise chaos pops its ugly head up. Rules, checks and values. "You must determine where you are going, so that you can bargain for yourself, so that you don't end up resentful... [...] Don't underestimate the power of vision and direction. Define who you are" (Peterson, 2018, p. 63). This instruction also made it clear that we must return to the starting point of natural law and to the positivisation of law.

The reason is that every historical work exists in a one-off form. Law is part of culture, it is bound to objects and primarily provides solutions for problems arising an a social order. Incontestably, economic power and all other kinds of power have a role (or attempt at having a role) in the generation of law. However, the "threads" of culture are strong, and do not tolerate unilateral settlement (Coing, 1996, pp. 163–164). For all these reasons, jurisprudence and its practitioners should have a pivotal role in the solution of the problems causing tension in the EU. Jurisprudence belongs to the humanities. On the one hand, it serves the practical implementation of the system of law, and on the other, it is the discipline of the structures in force. As Edmund Burke has put it in his eloquent assessment: "And first of all, the science of jurisprudence, the pride of the human intellect, which, with all its defects, redundancies, and errors, is the collected reason of ages, combining the principles of original justice with the infinite variety of human concerns..." (Coing, 1996, p. 273).

Controversies in legal literature also characterise our age. As an example of debates on sovereignty, the concept of American researcher Jeremy Rabkin (2004) is highlighted, who agues that the global order must also be based on the sovereignty of states (Máthé, 2013, pp. 160–161). The reason is that these are the unique international factors that unify democratic legitimation through the enforcement capability of statutes. Let alone that, on the basis of unanimous intent, economic areas and regional centres may be established between the individual sovereigns, for instance, in the EU, on areas created by mutual will, within or beyond the borders.

Thus the above may well be the 21st-century priorities in the theory of the state, providing focus for the transformation of the entire organisation and decision-making mechanism of the European Union, based on the common currency and intended to be operated by the core Member States, not in adjustment to globalisation, but to "several world-economies operating at the same time", as Fernand Braudel (2008)

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aptly put it. Within Europe, various regions of shared value may be established. This is because the peculiarities of historical regions coincide with the current economic trends seen in the EU (Szűcs, 1983).

The changing role of the Constitutional Court

The peculiar challenges of a comparison of the European legal system are of paramount significance in both legal and political terms, writes Armin von von Bogdandy, Director of the Max Planck Institute of Heidelberg in the sixth volume of his high-standard *Handbuch Ius Publicum Europaeum,* about constitutional justice. The reason for this special attention is that uniquely in the public law of the European Union, the primary law of the Union, the European Convention on Human Rights and the national laws are interconnected. European public law reconciles this with systems that identify as being based on constitutional rules without blending it into a single legal system. Giving an analysis of the role and practice of constitutional courts and through the conclusions drawn from them, the authors of the volume make it clear that this institution may be the ultimate guarantee for the elimination of the anomalies in the postmodern rule of law (Bogdandy et al., 2016, VII.).

The basis of the European legal system is the area, defined by the laws of the EU Member States, where the regulations of both the Member States and the EU are enforced. This confirms professor Bogdandy's proposition that a complex legal system without a sophisticated set of doctrines usually lacks clarity, predictability and honesty (Máthé, 2017). And when the drafters of the Treaty of the European Union speak of an "area", they mean the full spectrum of interpretations of positive law.

It can be ascertained that constitutional justice is the theoretical basis of comparison within the European legal system, and this role is the pillar of association between constitutional courts. Instead of an interpretation of a clearly designated legal area, the current practice of constitutional courts is far more a kind of "inbuilt" legislative procedure specially focussed on interrelationships. As a result, Bogdandy and his co-authors distinguish five special functions for the constitutional courts operating in the association: interconnection and implementation; translation; legitimation; closing gaps in legal protection and interfacing the law of the European Union and constitutional law. Special significance is attached to closing gaps in legal protection, and more specifically, the role in identity control and in *ultra vires* control, undertaken to protect the system against the EU's organisations exceeding their authorities. This control is pivotal because it deepens and streamlines the elaboration of common European solutions. The Association of Constitutional Courts also contributes greatly to the development of the European legal system by controlling the activities of the Court of Justice of the European Union and the European Court of Human Rights in horizontal cooperation with the courts of the Member States. For this reason, in resolving the problems in the current jurisprudence it can be considered as a forward-looking axiom that European culture and European public law may not be rooted solely in the law of the European Union and in the settled case-law of the European

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Court of Human Rights. This rather requires the creation of a network of the national organisations of jurisdiction (Bogdandy et al., 2016, pp. 8–10).

The authors of the book decline the concept of a standard model for the constitutional courts of the European states, and any effort made at it, and giving an analysis of the test of the Treaty of the European Union, they provide evidence that the equivalence of the Member States' constitutional systems implies the recognition of "diverse mechanisms" that protect the rules-based nature of the constitution (Bogdandy et al., 2016, pp. 13–16). Areference is rightly made to the charter of the Conference of European Constitutional Courts, which assigns the judicial review of constitutionality, judicial independence, the basic principles of the democratic rule of law and the protection of human rights into the competence of the court (Bogdandy et al., 2016, pp. 16–17). Regarding the future of this *sui generis* formation, the excellent experts refer to the quality of argumentation about doctrines in jurisprudence as to a mandatory parable. They find that as a legal guidance, the basic rules-based structure of European public law expects all the stakeholders of the legal system to operate along common knowledge, abilities and values despite the fact that they do not form a homogeneous legal culture. In legal practice and in the theory of law, national interpretations and the content of their doctrines should be examined from the perspective of public law, but there is no need to always endeavour for harmonisation, as there is no general consensus in the jurisprudential and practical local value of the legal acts and configurations included in legal systems In our opinion, the function of comparing constitutional jurisdiction can be classified into the following three types: the verification of a statement; the setting up of a conceptual framework implying a certain statement; and contraposition. As in a pluralistic structure, shared responsibility can only be enforced in the form of a dialogue, a comparative assessment may exist as the building block for the unfolding of common rules-based legislation (Bogdandy et al., 2016, pp. 18–20). This method may, in turn, especially justify the resolution of the legal conflict between the common organisations of the EU and the nation-states as the system of the association of constitutional courts reaches its full potential.

Closing thoughts

The intellectual challenge makes it clear for all of us that legal decisions need to be adopted in professional issues as soon as possible. Let us recall once again the wise ideas of Jordan B. Peterson, as the professor's recommendations bear close consideration: "We must make decisions, here and now, even though the best means and the best goals can never be discerned with certainty. [...] Some reliance on tradition can help us establish our aims. It is reasonable to do what other people have always done, unless we have a very good reason not to. [...] To tell the truth is to bring the most habitable reality into Being. [...] Truth [...] makes nations wealthy and safe. [...] Truth makes the past truly past... [...] Apprehend your personal truth. Communicate it carefully, in an articulate manner, to yourself and others. [...] This will ensure the benevolence of the future, diverging as it might from the certainties of the past" (Peterson, 2018, pp. 221–230).

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Antal Visegrády

On Hungarian Legal Culture

Summary
After the clearing of the nation of legal cultures the author shows the european legal families and legal cultures. After the examination of historical characteristics of hungarian legal cultures he deals with the possibilities and limits of approximation of the EU legal systems and cultures. Finally the paper analysis the impact of EU membership on the hungarian legal cultures.

Keywords: legal cultures, legal families, approximation of EU legal cultures, impact of EU membership

Introduction

It is well-known that between the Middle Ages and the end of the 18th century, the European continent shared a unified law and a single jurisprudence.[1] They were based on the *Corpus Iuris Civilis* and the Corpus Christi Canonici, which were later supplemented by several important legal institutions of territorial rights and customs. These elements constituted the content of the so-called *ius commune*.

However, by the *19th century the term "law" had been used in the sense "the law of the singular a nation state"*. This is to be taken as the root of the problem discussed here, despite the legislative efforts made by the European Community in the past decades towards a unified European law.

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The concept of legal culture and its categories

The relationship of culture and law is characterised by permanent interaction and interdependence.[2] The nature of this relationship could be summed up in two tenets: on the one hand, law is an element of the culture of a society, and on the other hand, there can be no law or legal system unaffected by the culture of the society.

Legal culture, similarly to political culture, is a result of historical development. Political culture can influence or even modify the characteristics of a legal culture (Tarello, 1981). The current state of legal culture is always between tradition and innovation. The development of a legal culture is a long process. It is not simply organic growth – as its task is to preserve the given culture. Having a legal culture is neither insistence upon the given standards, nor change for the sake of change only (Schäffer, 1996).

Legal culture comprises the following: a) written law and "living" (judicial) law; b) institutional infrastructure (judicial system, legal profession); c) the models of legally relevant behaviour (e.g. legal actions); and d) legal consciousness (Visegrády, 2001).

In some respects, legal culture can be divided into two parts: "external" (lay) and "internal" (professional) legal culture (Friedman, 1977, p. 76).

Some even find it apt to talk about *legal "sub-cultures"*. The possible use of the term could be exemplified by the fact that those unwilling to serve in the armed forces are normally found guilty in Northern and South Norway, while acquitted in Western and Central Norway (Podgórecki, 1967).

On a global scale, a possible way of distinction is between *regulative* and *steering* kinds of legal cultures (Kulcsár, 1997, pp. 137–147).

In regulative legal cultures (typically characteristic of the societies of the "Euro-Atlantic" culture), law is accepted as a rule that guides behaviour actually and normatively[3] – but not always to the same extent. In common law systems, for instance, courts have considerably higher prestige than in other countries. Moreover, continental European legal cultures are far from being homogeneous. This is illustrated by two examples: as opposed to German legal culture (traditionally setting high value on law and having sophisticated civil procedures), Dutch legal culture is often characterised by the concept of *beleid,* which means that subjects follow advantageous laws and evade (circumvent) disadvantageous ones at the same time. This might be well illustrated by the fact that until the enactment the Euthanasia Act of 1993 (exceptionally permitting aid to suicide), the Criminal Code had prohibited but the medical institutions had practiced active euthanasia. Besides, the Dutch seek to solve their conflicts out of court.

The legal cultures of the Central Eastern European region could be characterised by a deeply (historically) rooted attitude manifested in faith in legal regulation and excessive expectations concerning legal regulations. This has been accompanied by an inclination to perceive social problems in a certain legal framework. The efficacy of law has also been affected by the fact that (besides overcomplicated legal regulations) the standards of behaviour generated by the actual practice have gained primary significance.

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Families of law in Europe

The national legal systems integrated by the European Union belong to different families of law[4] within the regulative legal culture.

Common law systems

Common law systems can be found on five continents and have three representatives in Europe: English law (practiced in England and Wales); Irish law (which is a kind of "modified" English law); and Scottish law (which has of "mixed" character).[5]

English law is described here as it provides the model for all common law systems. The characteristics features of English law are the following:

a) English law *resisted* the adoption of Roman law during the 15th and 16th centuries (unlike continental legal systems) and followed its own independent way of development.

b) English law is *not codified*: most of its rules are not incorporated in statutes.

c) English law is a *judge-made* law.

d) It follows from the previous feature that the rules of English law are *less abstract and generalised* than the rules of continental legal systems, as they always refer back to a decision made in a particular case.

e) English law is an *open system*. It is based upon a method that allows for answering all sorts of legal questions, but does not contain material legal regulations that are to be applied without respect to the circumstances.

f) Last but not least, as opposed to the Roman-German legal systems, English law has a *historical* character, its development has never been interrupted, it has always maintained its unity. For this reason, one cannot talk about old and new English law; every legal regulation, no matter how old it might be, belongs to the present legal system unless it was repelled by a statute or by custom. Moreover, the older the legal regulation, the higher the prestige it has.

Roman-German (continental) legal systems

The Roman-German legal system was the first family of law in the world. Its history dates back to the distant past. It stems from the law of ancient Rome but its long development has resulted in not only the modification of most of its material and procedural rules, but has also significantly altered its underlying concept of law and legal norms since the times of emperors Augustus and Justinian. Although the legal systems classified into this category are descendants of Roman law, they carry on its development and endeavour to bring its institutions to perfection. They have never been mere copies of Roman law, as many of their elements stem from other sources.

In continental Europe every contemporary legal system falls under this category. It does not mean that Roman-German legal systems are not to be found on other continents. Reaching well beyond the boundaries of the former Roman Empire, it has

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spread to every Latin American country, most of Africa, the countries of the Middle East, Japan and Indonesia. This expansion is explained partly by the influence of colonisation and partly by the advantages associated with the reception of the legal technique of codification generally applied in Roman legal systems in the 19th century.

The characteristic features of the Roman-German legal systems can be summed up as follows:

a) The pillars of these legal systems are the *written sources of law* (statutes, decrees, ordinances). Statutes are primary to other sources of law.

b) Roman-German law is relatively abstract, in other words, the legal rules are not during making a decision on particular cases (with the intention of their application in further cases, like in Anglo-Saxon legal systems), rather, standards determine certain patterns of behaviour irrespective of the specific circumstances of particular cases.

c) Legal "norms," or standards, are characterised by a kind of *optimum generality*: they are not too general (as excessively general standards would impede the application of law) but general enough to be applied to certain type-situations.

d) *The spheres of the creation and the application of law are strictly separated unlike in common law systems.*

e) In these legal systems lawyers' primary task is the interpretation of legal norms. Every possible specification that has been left out of a legal rule automatically opens the way to interpretation. Thus, in Roman-German legal systems, law consists of not only the legal rules enacted by the legislator but also of *"secondary legal rules"* developed in legal practice.

f) The material of law forms an *independent, closed system,* in which – at least in theory – all sorts of questions could or should be answered by way of "interpreting" existing legal rules.

The Roman-German legal systems could be divided into three families of law.

The following European countries that belong to the *family of Roman law*:

1) France (as the "cradle" of this family of law);

2) Belgium, Luxembourg and the Netherlands (which came to touch with French law as a result of French military expansion);

3) Italy, Spain and Portugal (heavily influenced by the German and the Swiss codes, making them representatives of an intermediary type).

The characteristic features of the family of Roman law can be summed up as follows:

a) The code of central significance is the *Code Civil* (1804) in this family of lawe. This code has a clear-cut structure, free of any feudal elements, any "compromises". It leaves almost no room for judicial discretion; its formulations are concise and simple. It is often called the "most *bourgeois*" civil code that laid the foundations for European codification.

The Code Civil is in force in Belgium, in four Italian regions, two Swiss cantons and with some modifications in Baden. Replicas of the Code Napoleon were enacted in the Netherlands (1838), in Sicily (1812), in Parma (1820), in the States of Sar-

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dinia (1837) and in Modena (1842). As an adapted translation of the original, it was instituted in Greece (1841), in the unified Italy (1865) and in Romania (1865). And finally, although not as the exclusive source but as primary inspiration, it influenced the Portuguese (1867) and the Spanish (1889) civil law codification, Just as Louisiana and Quebec in North America.

However, the success of the Code Civil peaked in South America. It was taken over in its original language in Dominica (1825), and later in translation in Bolivia (1831). The creative adaptation of European models (as mediated by French patterns) was first achieved in Chile (1825) that encouraged some countries to follow the lead (Ecuador 1861, Columbia 1873) and others to create their national code based on the Code (Uruguay 1867, Argentina 1869).

In Asia, the Code Civil made an impact on almost the same scale but in a far less homogenous way. Its principles are applied in Japan, and all four French codes were adapted in Turkey. In Egypt, the first codes (1867, 1883) were replicas of the Code Napoleon, the present code (1948) is a developed version based on it (which inspires Syria for adapted reception). The civil codes of Lebanon (1934) and Venezuela (1942) are also of French origin, although both are to be taken as significantly different to it (Varga, 1979, pp. 117–118).

aa) The Code Civil regulates the relationship between the statute and the judge in a rather radical way. Judges are not allowed to interpret the statute "arbitrarily", in matters of legal interpretation they have to turn to the authority of *referé legislative* (established in 1970).

ab) The Code Civil is the code of the "owner". It was based upon the idea of a citizen who makes rational decisions, who is aware of the relevant information and the rules set in law. The Code strives to guarantee the freedom of property and contract as much as possible.

ac) The Code finds a middle way between abstract principles and specific (casuistic) rules. It determined the paradigmatic style for civil law codifications as well as codes on other fields of law for the future.

b) The family of Roman law (unlike Germanic and the common law systems) is characterised by the prevalence of legislature. The influence of Roman law-quite paradoxically because of the early reception of Roman law – is much weaker.

The second family of law within the Roman-German system is the *family of Germanic law*; including law in the following countries:

1) Germany;

2) Austria;

3) Switzerland;

4) The countries of Central Eastern Europe (especially the Czech Republic and Hungary).

As characteristics of this family of law, the following features should be pointed out.

a) With respect to the development of the Germanic family of law, it proved to be a significant factor that, compared to other legal systems, *Roman law* had its *influence felt* rather late (only in the 15th century), but when it did, *it was powerful.*

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b) The code of pivotal significance in this family of law is the *Bürgerliches Gezetzbuch* (BGB, 1900), which is a conservative code (unlike the French *Code Civil*).

The BGB was used in the recodification of Greek civil law (1940), and in the codification of contracts in Poland (1933). It provided the basis for the Brazilian (1916), the Mexican (1928), and the Peruvian (1936) civil codes, (*Codigo Civil*) as well as the codification of civil law in Japan (1898), Siam (1925), China (1929), and Thailand (1962). It also inspired the Italian *Codice Civile* (1942), which is quite remarkable, as the *Codice Civile* of 1865 was formulated in the spirit of French legislation (Varga, 1979, pp. 120–121).

ba) The law set out in the BGB is the law of lawyers; it is characterised by a style that strives for accuracy, subtlety and abstraction. Its addressees are not citizens but primarily lawyers (of course, in the sociological sense of the world). Its institutional schemes and terms are artificial; its language is technical (only professionals can understand its true meanings). As its primary focus is not conciseness but accuracy, the code is often very complicated.

bb) The rules of the code are structured in a specific way that more or less follows the structure of the *Institutions* of emperor Justinian (personal and family law, the objects and types of property, the ways of acquisition of property, etc.).

Many think that the *Austrian Civil Code* (ABGB 1811) represents a kind of balance in between the lawyers' of law of the BGB and the application-oriented law of the Code Civil.

The famous *Swiss Civil Code* (ZGB, 1912) has a distinguished position in the Germanic family of law. The ZGB is "deliberately vague" at certain points to allow the judge to search for the solution that is the most appropriate in the given case. The code is characterised by the extensive use of general clauses that are to be interpreted by the judges in the particular cases.

At last, the Nordic family of law covers the following countries:

1) Denmark;
2) Finland;
3) Iceland;
4) Norway;
5) Sweden.

This family of law can be characterised by the following features.[6]

a) It is often regarded as *a kind of an intermediate version between common law and the Roman-German legal systems.*

It resembles the common law systems as it was hardly influenced by Roman law and the wave of codifications in the age of the Enlightenment (e.g. the comprehensive codification of the civil law has not taken place yet). On the other hand, its similarity to the Roman-German systems can also be pointed out: judges do not have a central role in this system and there is no normative precedent-doctrine.

Nordic countries had lived in relative isolation for a long period. Their legal institutions were influenced by French law in the 19th century, German law at the beginning of the 20th century, and common law (especially the law of the USA) mainly

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after World War II. However, despite all these influences, they have retained their original character.

b) Co-operation between the Scandinavian countries is manifest in their laws as *they make efforts to integrate the content of their legal systems.* An example includes the Scandinavian Sales of Goods Act, passed in every Nordic country (Sweden adopted it in 1905, Denmark in 1906, Norway in 1907 and Iceland in 1922). The act is influenced by both the British Sales of Goods Act (1893) and the German BGB. Co-operation is facilitated by their common legal and linguistic traditions.

c) Last but not least, it should be mentioned that *judges of higher courts and jurists of high authority play an important role in Scandinavian legislatures.*

A glimpse at the discrepancies between the political cultures of the EU Member States suggests, in my opinion, that political culture reveals the subjective side of politics, and – directly or indirectly – to the political consciousness of citizens. The political culture of a society represents the political system internalised in the knowledge, emotions and evaluations of the population. Just as the political system shapes political culture, the latter – as an essential element of the environment – "conditions" the functioning of the political system including the efficacy of the legal system.

The Hungarian Legal Culture

The main historical characteristics of the Hungarian legal culture

Legal cultures in the societies of Eastern and Central Europe have also been mainly regulative in character, although during their history certain features of a steering legal culture also mixed into them. This may be explained by two reasons.

On the one hand, the legal systems of this region had strong regulative features in some respects, for example, with regard to the inclination to litigate, especially in Hungary. In other respects, however, the willingness to evade the law has not simply existed for centuries but has also become an accepted form of behaviour in legal culture.

Although the idea of the rule of law had an impact on royal law-making – as proven by Hungarian legal history –, until the beginning of the 16th century royal law-making practically created legal rules lasting only for the period of the given king's reign.

Until the 16th century neither court judgments nor charters referred to statutes, but to the ancient custom of the country (*antique regni consuetudo*). This circumstance diverted Hungarian legal development – and legal culture – from Western-type legal systems to some extent, and subsequently this repeatedly raised the question of the need for adaptation (Kulcsár, 1997).

In Hungarian legal culture, the social standing of the court and of judges remained ambivalent for a long time. Judicial organisations were only separated from public administration in 1869 and, at the same time, the independence of the judiciary as a principle was laid down in a statute.

On the one hand, the role of judges has never become so significant and prestigious in Hungary as it has, for example, in Anglo-Saxon systems of law. On the other hand,

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the inclination to litigate manifested in Hungarian legal culture indicates the importance of the court as the institution participating in the resolution of legal disputes.

In the socialist era, unrestricted legislation became a dominant feature, the number of bureaucratic type legal instruments of symbolic and technical nature increased quickly, and as a result of the above – normativity was pushed to the background. All this led to a significant decrease in the social prestige of law and the legal profession, which was further damaged by artificially generated political show trials serving political purposes.

Hungarian legal culture after the democratic political transformation

1. Written and living (judicial) law

Looking at the historical past we must consider the question whether the changes within institutional and political cultures are a result of continuity or discontinuity. In Hungary the following spheres may be differentiated:

– political institutions: *discontinuity*, a revolutionary new system of government

– legal system: *continuity*.[7]

Within this field, special attention should be paid to a famous decision of the Constitutional Court (1992), which, among other things, laid down clear statements in the scope of what becomes Rule of Law and the legal importance of a change of regime. "The classification of Hungary under the Rule of Law is both a clarification and a program at the same time. The Rule of Law is established when a constitution enters into force truly and unconditionally. In terms of law, a change of regime means and is only possible if it is made compatible with the country's Constitution and, in respect of any newly adopted legislative acts, concordance is maintained in the complete legal system. Not only the provisions of law but also the operation of government organisations should be in strict harmony with the constitution and then the conceptual culture and value scale of the Constitution also should affect the entire society. This is the Rule of Law; this is how a constitution materialises. The achievement of the Rule of Law is a process. The change of regime took place on a legal basis. The principle of legality requires a state run on the basis of the Rule of Law to unconditionally apply the rules of its legal system to itself. The Constitution, which triggered revolutionary changes in politics, and the fundamental statutes were established in compliance with the principles of the former legal system, technically impeccably, and this is the source of their non-appealable, legally binding nature. The former legal system also remained in effect. In terms of force, there is no difference between the law applied before and after the Constitution. The legitimacy of the various systems in the past 50 years is, in this sense, indifferent, and regarding the constitutionality of the provisions of law, this concept makes no sense. Irrespective of the date of its adoption, every statutory regulation must comply with the new Constitution. There is no dichotomy in constitutional review – and there is no double standard. The date of the adoption of a statutory regulation has relevance on to the extent that previous statutes become unconstitutional when a new Constitution came into effect."

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This decision of the Constitutional Court also refers to the importance of changes in the ways of thinking and attitudes within the legal (and therefore political) culture. This democratic political transformation, having taken place by way of a revolutionary act to establish the Rule of Law and on the grounds of legality and continuity, required an enormous amount of legislation. The emphasis in legislation shifted towards the apex of the hierarchy of the sources of law, this is how more than one and a half thousand effective acts of Parliament were drafted (the legal regulations currently in force comprise almost six thousand legal instruments) (Fleck, 2010, p. 55).

Since the beginning of the 1990's the number of acts of Parliament has been increasing continuously. Seventy-five per cent of these acts have been passed since 1990; and consequently, the most important level of the legal system has been replaced since transition to democracy. While Parliament passed 104 and 145 acts in 1990 and 2000, respectively, the number of acts passed by Parliament between May 2010 and May 2011 reached 200, including the new Fundamental Law, replacing the Constitution of 1989. A high level of activity also is seen in delegated legislation (legislation by decree). The judges of the Constitutional Court exercise permanent control over legislation.

As far as "living law" (judicial law) is concerned, its most important scene include courts, which do not merely "carry out" codified instructions, but also interpret,[8] apply and thereby necessarily develop all branches of law. Accordingly, "*praetor ius facit inter partes*". Therefore, permanent and uniform practice at courts, the precedent-setting decisions adopted by Curia (supreme court) to secure the uniformity of law, its decisions made in individual cases and its opinions to promote uniform practice may all be considered sources of law. As an example: 46 criminal, 37 administrative and 24 civil precedents were made between 2008 and 2010.[9]

2. The legal profession

Before the adoption of democracy, in Hungary legal profession had been characterised basically by two features: on the one hand, its prestige had decreased and on the other hand, in spite of the four decades of "socialist" – and under its cover: Eastern – influence, they had preserved continuity of traditional Hungarian legal thinking to a significant degree. This latter characteristic proved to be of key importance during the democratic transformation (Kulcsár, 1997, p. 135). After the first elections, Parliament was filled with lawyers, independent intellectuals and philosophers in large numbers.

Attraction to the legal career suddenly rocketed – in line with Hungary's conversion into a democratic state governed by the Rule of Law. Instead of the approximately 4000 people pursuing a traditional career in law at the time of the democratic political transformation, today approximately 15,000 lawyers are active, including 2800 judges, 1729 prosecutors, about 10,000 attorneys and 313 notaries. The previous four law faculties of law have been expanded to nine at various universities. At the beginning of the 1990's there were 3000 law students; today there are more than 18,000. On graduation most of them choose to become attorneys.

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3. Litigation

The inclination to litigate, which had always characterised Hungarian legal culture throughout history, further increased as a matter of course, under the conditions of market economy, and courts had difficulty in coping with the increasing number of cases. While, for example, in 1998 the number of cases filed with local and county courts amounted to 402,884, by 2010 this number had increased to 456,188.

Hungary is closer to the countries of short-term lawsuits, but on average all types of lawsuits take a little more time in Hungary than in Germany (6 months) or in France (4 months). Although Hungary can boast with the second largest judiciary (2800 judges) – in proportion to the population – after Germany, first-instance and second-instance proceedings last one year on average, and at the most overloaded courts the length of proceedings may take as much as two years (e.g. in Pest county) (Pokol, 2003, pp. 46–49).

4. Legal consciousness

Changes in the legal consciousness of the Hungarian population following the democratic political transformation are excellently demonstrated by the main results of the analysis conducted in 1997-98 on a sample of 219 persons (Kormány, 1999).

Among the various branches of law, criminal law was known best and administrative law and procedural law were known the least.

Ninety per cent of the respondents were aware of the fact that the court did not accept unfamiliarity with the relevant legal rules as a legitimate defence. Compared to a survey made in 1965, there was a 15% increase in the number of those who gave correct answers.

A fortunate consequence of Hungary being a democratic state governed by the rule of law is that 30% more people think that it is just to enforce this fundamental principle. In other words, there has been a change in the quality structure of legal consciousness.

Eighty seven per cent of the population involved in the analysis knew that in Hungary acts are passed by Parliament, 10% did not answer the question and 3% gave incorrect answers. At the time of the 1965 survey, only 45% said the legislative body was Parliament. The reason for the remarkable difference also lies in the democratic transition, since the weight and power of Parliament has increased significantly and citizens follow – or may follow – the work of Parliament.

It is regrettable, however, that to the question as to how it is possible – without any preliminary permission – to participate at a public court hearing, the proportion of right answers was altogether 33%. This may be explained by citizens' apathetic attitude to courts and by the fact that confidence in the system of administration of justice has greatly deteriorated in recent years.

Finally, mention should be made of the dichotomy that while three quarters of the 219 respondents recognised the difference between homicide and attempted homi-

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cide, they confused legislation with the administration of justice and they were also unable to distinguish between natural and legal persons.

In view of all this, while the consolidation of our legal culture gives reason for contentment, we should not forget about spreading information about law and should improve legal consciousness.

The impact of membership in the EU on Hungarian legal culture

Two questions arise in relation to legislation and Hungary's membership in the European Union. Firstly: Was Hungarian legal culture prepared for accession in 2004? Secondly: Can Hungary make any favourable contribution to the legal culture of the EU?

The law of the EU does not constitute a "European legal culture", but the product of various European legal cultures.[10] The new "European legal culture" is in the process of evolving, as indicated by the proliferation of technical laws and at the same time, by the increasing unification and vertical plurality of the legal system. One must proceed from the fact that, besides national endeavours, several harmonisation factors have always been present in Hungary's legal development of a thousand years. The main forces behind this harmonisation process have been the similarity of Hungary's economic and social structure to the Western-European pattern, and its efforts to catch up with the European standard of living. In this respect, therefore, legal harmonisation during Hungary's accession to the EU was not the first challenge in Hungarian history.

Since the change of regime, several positive trends have been observed in the development of Hungarian legal culture pointing towards conformity with the European Union. These include the lawful performance of the change of regime and the beneficial influence of the consistent practice of the Constitutional Court on Hungary's legal culture. On the other hand, the approximation of laws plays a significant role in consolidating Hungary's regulative legal culture.

Note that the European Union's legal instruments laid down in the White Paper were harmonised by Hungary already between 1990 and 2003.

The further training of judges and civil servants in languages and European law has started, but obviously, the final solution may be expected of the mass employment of the new generation of university graduates.

However, it must be emphasised that Hungary's integration into the European Union does not exclude the preservation of the specificity of the country's legal culture.

Integration has a double aim. On the one hand, it should guarantee the achievement of some common effects; and on the other hand, guarantees need to be built in the procedures in order to ensure that similar premises have similar results. "All this translated into legal terms means that only those elements of our legal culture can – and in some cases: should – be unified that, due to their *sine qua non* role, are instrumental in the fundamental aims to be achieved by all means" (Varga, 1992, p. 446).

Therefore, in the efforts to make Hungarian legal culture conformant with the European Union's, attention should also be paid to fostering Hungary's existing cul-

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ture. Hungarian legal culture could also make a contribution to the development of European Union legal order if Hungarian legal policy was able to initiate the adoption and utilisation of some of our legal solutions for improving legal institutions still not elaborated in the Community *acquis*. Such a solution might be, for example, the Hungarian Ethnic Minorities Act.

Chances of and limits to the approximation of legal systems in the European Union

As it is well-known, the European Union launched the most comprehensive legal harmonisation programme of all times. It concerns not only the 27 Member States but – as a point of orientation – the member of EFTA and the countries of Central and Eastern Europe as well. The goal of the Union is not some kind of a "unified law" but the co-ordination of the legal regulations of the Member States, the elimination of excessive deviations with preserving the national legal systems to a certain extent.[11]

The advocates of the convergence of the various legal cultures to the EU point to the common history, common values and traditions.[12]

On the other hand, many hold the view that the common law and the continental legal cultures are so different to one another that there can be no approximation between them.[13]

And finally, according to the third view, the above mentioned conceptions take legal cultures in a formal sense. We would rather need a sociological approach that concentrates upon identities. For example, civil law is often a symbol of national identity or a manifestation of national legal culture. This might explain why the Member States are so reluctant to "harmonize" their civil laws. However, the EU set its heart on this harmonisation (Paasilehto, 1999; De Cruz, 1995, p. 99).

The first question concerns the extent the European Union makes use of the institutions of national legal systems. The incorporation of human rights in Community law is mainly due to the German Constitutional Court. As Community law consists mostly of rules of administrative nature, many of its basic principles trace back to the highly developed administrative law of France and Germany. Recently, however, the European Court has also adopted certain principles – mostly procedural ones – from the "natural justice" of English law. This is how the "right to hearing", the "duty of justification", the "right to due process" became part of Community law. The Community law also borrows from the economic laws of other Member States (Kecskés, 2009, p. 128).

Secondly, we have got to talk about the European Court. This is the forum functioning as a kind of "merger" of Anglo-Saxon and continental legal cultures. Comparative law is a permanently used "instrument" in the hands of the European Court (Kecskés, 2009, p. 127).

The amalgamation of the two legal cultures is also manifest in the fact that the European Court (basically) applies the case law method, but its verdicts do not function as precedents.

The next problem to be explicated concerns common law. *In concreto*, there is an ever more obvious trend that the practice of British courts – although the efforts to

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synthesize the Anglo-Saxon and continental legal cultures could also be noticed – assimilates with the American model, where decisions are based upon principles rather than rules (Levitsky, 1994, p. 380).

Finally, we cannot avoid posing the question: Is the Hungarian legal culture mature enough to European integration, or: Can the former contribute to the latter in any respect?

Concluding remarks on the perspectives the ius commune Europaeum

The law of the EU is not a uniform "European legal culture" (Gessner, 1992, pp. 5–18), but the product of various *European legal cultures*. The new "European legal culture" is in the making and is manifest, among others, in the proliferation of technical rules and in the growing unity and vertical plurality of the legal system (Kulcsár, 1997, p. 139). However, the future common law of Europe means much more than growing harmony in different fields and Rules of Law. The "euro-centrism" of European law does not involve that it only relies upon the legal systems of the countries of Western Europe. It is also influenced by the legal institutions of e.g. the USA, Australia and New Zealand. A question of the future is how this complex but homogeneous law can integrate the legal traditions of the countries of Central and Eastern Europe (Burrows, 1996, p. 312).

The key to the future of the *aquis communautaire* is the efficacy of its rules.

It is a complex task to measure this efficacy, and includes – among others – an inquiry into the following factors:

– The way the legislatures of the institutions of the Community reflect the policy of the Community;

– Application of Community law in the Member States;

– Translation of the Community directives into national laws;

– Effectiveness of secondary Community legislatures and national "adoption" in respect to the various systems of public administrative;

– Effectiveness of Community law in respect to the activity of economic and other organisations, or even private persons;

– Legal actions concerning Community law at national courts;

– Enforcement of Community law by national courts.[14]

As far as the perspectives of the approximation of the legal systems are concerned, I join the advocates of the convergence of continental and common law models. Both systems will be modified as judicial law becomes significant besides written law, and statutory law gains strength in relation to case law.

Just as in the past, the European states will undoubtedly follow the same legal principles in the future. European law is rooted in Roman law, the trunk of this tree is the *ius commune*, and its branches that grew in different directions will grow in the same direction as a result of a slow evolution, the unifying will of the European people (Schrage, 1992, p. 407).

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Notes

1 Rousseau was right when he wrote that "Il n'y a plus aujourd' ui de Francais, de Allemands, d'Espagnols, d'Anglais meme, quoi qu'on en dise; il n'e que des Européens.' Rousseau, 1964.

2 See e.g. Mayer, 1903; Fezer, 1986, p. 22.

3 Its main characteristics are individualism and rationalism. See Hoecke and Werrington, 1998, pp. 503–505.

4 See David, 1977; De Cruz, 1995; Zweigert and Kötz, 1996. The description given here of the various families of law in Europe combines the conceptual devices developed by Zweiger, Kötz and R. David. Although Zweigert and Kötz heavily criticised David's analysis, I find it apt to link the two categorisations. Kischel, 2019.

5 See Visegrády, 1999; as to Irish law, see Doolan, 1986; about Scottish legal culture see Watson, 1974.

6 Cf. Kondorosi and Visegrády, 2011, pp. 127–137.

7 Cf. Paczolay, 1993.

8 Cf. Zirk-Sadowski, 2011.ungary

9 Cf. Visegrády (under publication).

10 Cf. e.g. Febbrajo and Sadurski, 2010.

11 Evans, 1998; Cabero, 1989, pp. 177–180; Cartou, 1994, pp. 155–158; Gulmann and Hagel-Sorensen, 1988, pp. 287–297; Lauria, 1992, pp. 172–190; Kecskés, 2009.

12 See e.g. Gerven, 1995, pp. 679–702; Joerges, 1997; De Cruz, 1995, pp. 99.

13 See e.g. Legrand, 1996, pp. 52–81.

14 See Snyder, 1993, pp. 25–27. On the concept of the efficacy of law, its factors and its measure, see Visegrády, 1997.

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Developments in Hungarian Labour and Public Service Legislation during the 2011–2012 Codification and the Subsequent Comprehensive Amendments

Summary

The study deals with the second codification wave similar to and following the first codification period of labor and public service law after the change of regime in 1992-1993, which took place because contrary to the previous left-liberal government policy, a very different, right-wing civilian government came to power in the parliamentary elections of 2010. The article in the previous English volume showed in detail only the employment and public service legislation of 1992-1993, while the second codification of 2011-2012 relating to these two fields of law was only outlined. In this writing we give a more profound critical analysis of the re-codification of employment and public service law in 2012 and the subsequent amendments. Our study covers both individual labor and public service law, as well as employment and public service law relations in both the fields of labor law and public service law.

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Keywords: collective labour law, individual labour law, Labour Code, termination, liability for damages, legal personality, reconciliation of interests, collective bargaining, works council, participation

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Transfer from the previous study

The Development of the Hungarian Labor and Public Service Law After the Regime Change', which was published in the special English issue of the Civic Review of 2018, we described the essential features of the 'real socialist' labor law of the period before the regime change in 1990, which included public service law, too. Subsequently, we addressed in great detail the first codification of employment and public service law after the regime change as a result of which three laws, a labor code, a public servant and a civil servant law were drawn up, where workers for non-official public institutions were uniformly listed as public servants, while workers of institutions operating as an authority were classified as civil servants and the legal relations of case managers and physical workers were registered as employment relationships. This classification did not change in the second codification period of 2011-2012, however, the content of the civil servant's legal relationship was changed several times, most recently in December 2018, when the new Hungarian Labor Code was also significantly modified. The legal institutions of working time and rest time were significantly modified in both the new Hungarian Labor Code and the new Act on Public Servants (Act CXCIX of 2011) and in the latter the rules of leave were also changed to a large extent, which mean both sociological-ergonomic and social law problems. These problems of modifications are discussed in this article and besides we are analyzing the Hungarian Labor Code of 2012 in detail, which – due to reasons of extent – was left out of our previous study.

The second labour law codification in 2012 and its further amendments

In 2008–2009, the world saw the worst financial and economic crisis in eighty years, and it resulted in a rise in unemployment. Already before the crisis, the so-called flexicurity programme appeared in the literature of the employment policy of the EU,[1] which includes the need for flexible and reliable contractual arrangements, lifelong learning, active labour market policies, and the need to create more flexible social security systems both in international and national rules (Tóth, 2017; Jakab, 2017).

This programme launched a debate on the development of labour law, and gave rise to the Green Book (European Commission, 2006). This public debate concerned the achievement of sustainable growth while ensuring more and better jobs in the EU through the development of labour law. The study was published in 2006, and it already covered the challenges of the 21st century, too.

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One of the key objectives in developing the concept of the new Hungarian Labour Code was to incorporate the recommendations of the Green Paper into the internal legal order by creating the conditions for flexible employment while preserving the social security of workers. The new Labour Code, according to the official justification, took account of the international social and economic changes, and moved the labour law legislation mainly toward dispositivity. This gives more scope for agreements between the employer and the employee, on the one hand, and the trade union and the employer, on the other, when formulating the content of the employment relationship and thus, the intervening role of the state is pushed into the background. In general, it can be stated that the legislator's intention was appropriate for managing the consequences of the emerging economic crisis. However, the social partners perceive greater dispositivity as a violation of employees' and collective labour rights.

One of the significant changes to the new Labour Code is that the provisions of the Civil Code (hereinafter: 'Ptk.'), which took effect in 2013, clearly appear in the labour law regulations, and this is particularly apparent in the general provisions (e.g. the novel judgment of the ability to act) and the rules relating to labour law liability.

At first, this solution seems quite correct. However, looking into it more profoundly, this solution in the new Labour Code is problematic, because the employer is the stronger party and the employee is existentially defenceless against him. Therefore, in all such agreements, the will of the employer prevails, and if the employee is unwilling to accept the employer's offer, the employer may take reprisals against him. It is no coincidence that the labour laws of the Francophone and Latin-American states are still full of regulations protecting the social and existential situation of workers, which are governed by separate laws due to the absence of codified labour law similar to the German legal system (Prugberger and Nádas, 2014, pp. 48–50).

For this reason, within the framework of labour law, the legal personality of employees is a focal issue. Indeed, the legislator does not extend the scope of the social and existential protection of labour law, and thus the scope of the labour protection system, to all the activities of workers. A long-term business and agency contract is in many respects similar to an employment or a service relationship, but it does not expand the social and existential protection of labour law to cover the latter, as the stand-alone business position protects long-term entrepreneurs and those engaged in outsourcing. Nowadays, however, new forms of employment have emerged as sources of income, and therefore it is basically a matter of legal policy to decide who the personal scope of labour law covers. At the same time, this legal policy decision results from the pressure of economic and social changes and expectations, which will also become a burning issue in Hungary in the near future with the appearance of numerous atypical services, such as Uber. The question is which of them should be given employee rights to provide them a social and existential safety net.

Employee rights include general and specific employee abilities. A general employee ability is the ability to comply with legal requirements and a specific ability is the ability to fill a particular job. General and specific employee abilites are of particular importance for people with intellectual and psychosocial disabilities and for

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people whose work capacity has changed. That is why there is a broader concept of employee rights, which applies to the employment of people with disabilities. This concept is a combination of environmental and personal factors, as not only does the individual's state of health and ability determine the success of employment, but also the social acceptance of disability, economic and labour market conditions, adult protection regulations, the development and capacity of the educational and training system. If the goal is to integrate more people into the labour market, including people with disabilities, the legislator should adopt a holistic approach and understand that integration is not just a matter of labour law, but of broader employment, rehabilitation, education and adult protection regulation.

In addition, employee rights rapidly change. Developments can be defined in the context of historical, economic and social events. Development include the expansion of labour law to various persons, essentially, rating a relationship as atypical employment, or the denial of such a qualification, i.e. the exclusion of certain workers from the scope of labour law.

The employment conditions prevailing in the economic environment of the 21st century have an impact on the personal scope of labour law, on the legal status of an employee, i.e. who can be regarded as an employee and where the boundaries of dependent work are. Judicial enforcement, legal theoreticians, legislation and collective bargaining have all played a role in expansion in Europe. The boundaries of contingent work can be determined in the following ways in European labour law: 1) by the expansion of the concept of the employee, 2) by the creation of a third type (tertium genus) of people who perform work, 3) by the creation of a kind of common right for workers and by the expansion of the different levels of rights to broad categories, and 4) by exclusion. Clearly, workers cannot be treated as a uniform mass. Legal policy responded to this problem by pointing out the necessity of creating an intermediate concept between the employee and the entrepreneur, and to associate it with adequate labour and social protection.

"In labour law, individual self-determination is manifest in the wills of the two subjects of the employment contract or employment relationship, and therefore the determination of the subjects of the obligation is of fundamental importance, i.e. it has become one of the cardinal problems in labour law. The concepts of the employer and the employee correlate with each other'" (Kiss, 2005, p. 104). There is a perception in the legal literature that the distinctive features of labour law are defined through the concept of the employee (labour law is the Sonderrecht of employees) (Kiss, 2005, p. 116). With a view to all this, an employee is a person who carries out work for others. This allows us to distinguish between the employee and the self-employed.[2] This concept focuses on the work, i.e. the ability to work. The capacity to exercise rights has no role in this statement.

According to Article 72 of the former Hungarian Labour Code, a minor of 16 years of age or more and a person with limited legal capacity were allowed to establish employment without the consent of their legal representatives. Based on this, the conditions to becoming an employee included having at least a limited capacity to exercise

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rights and the age, which was in line with the provisions of Act IV of 1959 on the Civil Code. At the same time, there was a conflict between Article 72 of the former Labour Code and Act XXVI of 1998 on the Rights and Equal Opportunities for Persons with Disabilities (hereinafter referred to as 'Fot.'). According to Article 15 and Article 16 of Fot., disabled persons were entitled to integrated employment, so far as possible, and, in the absence thereof, to protected employment.

In the case of integrated employment, the employer is obliged to ensure that the work environment, in particular, the tools and other equipment, must be appropriately modified to the extent necessary for the work, and support can be requested from the central budget for this purpose. In addition, during the recruitment process, the employer is obliged to provide an environment that is equally accessible in all respects, in order to facilitate access to employment for the disabled person. These obligations are imposed on the employer if the vacancy has been announced publicly and the person with a disability has applied for the position by indicating his or her special needs for the job interview and the burden on the employer to provide them is not disproportionate. A burden is disproportionate if the fulfilment of the obligation renders the operation of the employer impossible. If the employment of a disabled person cannot be implemented in this way in the context of integrated employment, his or her right to work must be ensured as much as possible. Employers accredited for the employment of disabled employees and employers engaged in social employment are supported by the central budget as defined by law.

It is clear from the above that the former Labour Code made only allowed for persons with limited capacity to undertake employment. The right to work for people with disabilities was not discussed in the former Labour Code. Only the Fot. regulations included the rules of establishing the general framework for equal treatment in employment and work, while Article 5 of the former Labour Code included the general obligation of equal treatment along with the legal remedies of its violation. This obligation was also transposed to Article 12 of the new Labour Code. Therefore, the employer continues to be obliged to provide an accessible employment environment for disabled persons. The purpose of the amendment was to maintain this obligation during the pre-employment recruitment procedure as well. The specific provisions on equal treatment for persons with disabilities are set out in Act CXXV of 2003 on the Promotion of Equal Opportunities (hereinafter: 'Ebt.'). Before the codification of the new Labour Code, the Fot. and the Ebt. counterbalanced the condition that the employee's right was subject to his or her legal capacity, which was contradictory because, in other cases, driven by needs, it regulated the employment of incapacitated people in a way that their employment contracts should be signed by their legal representatives. However, if the incapacitated person did not have a legal representative, he could not become an employee. This conflict was resolved by the new Labour Code through terminating the conditionality of the employee's right to employment on his or her capacity to exercise rights, and only stipulating in Article 34 that the employee was a natural person who performs work under a contract of employment. By doing so, the new Labour Code classified incapacitated persons as potential employees.

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Besides, with a view to the new Civil Code, the new Labour Code has also included the category of the relative legal capacity with the condition that if a person under guardianship does not have absolutely diminished capacity, he or she can conduct an employment contract without the consent of his or her legal representative within the scope his or her discretionary ability is full and not limited.

Based on all these, work involving personal and economic dependence is one that remains within the scope of labor law. Taking this into account, the new Labor Code included as atypical employment relationships only those from the activities that represent a source of income where there is some form of personal dependence on the employer or the agent, such as in the case of teleworking.

While in the case of the right of employees, the new Labour Code took workers' interests into account to a relatively large extent, this is not the case regarding the settlement of issues concerning the content of the employment relationship. As concerns the two most important areas in the content of the employment relationship, namely, working time, rest periods, leave, on the one hand, and wages and benefits, on the other, within the latter, the new Labour Code has significantly diminished employees' rights. As far as working time is concerned, normal working hours may not exceed 48 hours according to the relevant Directive. The new Labour Code allows the employee to agree with the employer in a separate agreement to undertake overwork, however working time may not exceed 60 hours a week. This commitment may, however, last up to 6 months, but it can be extended. Nevertheless, in Western European labour law, the employee can terminate this commitment at any time. The Hungarian Labour Code does not include such an option. Pursuant to the former Hungarian Labour Code, as a rule of thumb and in accordance with Western European practice, the employee was entitled to additional payment for overwork, and he or she was entitled to leisure time only upon request. In the new Labour Code, however, overwork is compensated by either additional payment or leisure time, depending on the agreement between the employer and the employee. Nevertheless, such an agreement is already governed by the employer's will, as discussed above.

In principle, accounts must be settled with overwork by the end of the following month, although it is possible to compensate it over a longer period of time, called reference period by averaging. This period can be 6 months for ordinary work according to both the Directive on working time, rest time and leave, and the Hungarian Labour Code, and 12 months in the case of seasonal and stand-by work. During this period, flexible working hours must be cancelled out, and if they exceed 40 hours per week on average, on subsequent settlement they must be compensated by payment or leisure time. With authorisation by a sectoral collective agreement, in some Western European states, the reference period can be extended up to 12 months or even more. In Hungary, however, in the framework of a unique comprehensive amendment to the Labour Code performed at the end of December 2018, this period was extended up to 3 years. Although this extension is only allowed on the basis of an agreement between the employer and the employee, the provision on a sectoral collective agreement to mitigate pressure from the employer's side is missing (Prugberger and

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Tóth, 2019). The latter is imperative because the option to extend the working time frame, or in other words, the reference period, to 3 years also includes the possibility that the employer only pays for overtime once in 3 years.

During such a long period of time, there is the employer may even go bankrupt or be liquidated, including the risk of simplified liquidation in the absence of possessions, in which case the employees are not paid for their overwork, and the wage guarantee fund only settles the wages and salaries due to employees from their employers to a limited extent. In addition, although in Hungary the general practice is to use a 4-month working frame as a main rule, several companies have extended it to 6 months by a collective agreement, while the reference period in the EU member states is usually no more than 2-4 weeks (Prugberger and Tóth, 2019).

The term 'shift' means night shift in the EU Directive, applicable to people who regularly work at night and therefore their biorhythm is accustomed accordingly. They receive a lower shift bonus than determined in international labour law and practice. Their shift bonus is usually 15%. This is also used in the Hungarian practice. In the case of work in shifts, 30% is due for night work, similarly to other legislations, due to the greater organisational burden arising from work in weekly changing schedules. Hungary's former labour law also took this into account in the case of afternoon shifts and raised the base salary by 20%. The new Labour Code, however, eliminated the afternoon shift bonus, and introduced a 15% bonus for work between 6 p.m. and 6 a.m., and consequently, those who work during this period are entitled to 15% bonus.[3]

There have also been changes concerning wages and salaries. As a positive change, the minimum wage or salary has been supplemented by the guaranteed minimum wage or salary, which is higher than the minimum wage and applies to those with secondary or higher qualifications. The adverse change, however, is that both the basic wage or salary and the guaranteed wage or salary minimum are determined by the government on its sole discretion, without the involvement and interest reconciliation of social (coalition) partners, and the single parameter taken into account is inflation, and not the consumer basket. As far as the most recent practice is concerned, there seems to be a positive change at first sight: it is provided that in the event of downtime, employers pay must the average wage or salary instead of the statutory basic wage or salary, but with the condition that the lost working time must be worked off subsequently. However, nothing is paid for the subsequent work. And if the employee who was paid an average wage or salary for the downtime wants to terminate his or her employment relationship or if he or she was given a notice by the employer prior to having the possibility to work off his or her downtime, the employer will reclaim the average wage or salary paid to him or her for the downtime.

In both cases, the employer saves payment of the base wage or salary. It is also an unwelcome change that the new Labour Code does not contain any remuneration in-kind, only allows cafeteria, which the government is about to abolish.

Two more labour law institutions need to be mentioned here: the modification of employment relations and the employer's legal succession. Similarly to the German legal system, under the Hungarian Labour Code, employment contracts can be modi-

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fied by mutual agreement as a main rule. However, on a temporary basis, the employer may modify the employment contract by redirecting the employee to another job or workplace within the company, or by secondment to another employer, by posting, and by lending. This is regulated by Article 53 of the Labour Code as "employment by derogation from contractual employment", which also stipulates that all these forms of temporary employment can be applied by the employer only once in a business year for each employee. This regulation is basically more favourable for employees than the corresponding provision in the former Labour Code, which allowed the employer to use each form of temporary employment up to 44 days a year, on condition that total application does not exceed 110 working days per year. However, similarly to the former Labour Code, the current one does not adopt any rule from the Posting Directive, which allows the redirection, secondment or lending of an employee for maximum one year, extendable for maximum another year. It would be a good idea to supplement the Labour Code with such a provision in order to avoid the termination of employment during periods of business slump. This amendment could be linked to the lending of employees abroad, deficiently regulated in the new Labour Code, as the one-year limit to extension is not included.[4] The rules regulating modification in the employment contract in the case of the employer's succession have not changed in comparison to the former Labour Code and are in compliance with the regulations of Directive 2001/23 (EC) on Succession and the Reasonable Interests of Employees.

The new Labour Code has amended the rules on the employer's liability for compensation to the employee and partly placed them on new footing. Exemption has been adopted in labour law from civil liability, with focus on the foreseeability clause, which may result in the employer's partial exemption from compensation for damage if it was unforeseeable at the time of the injury. Another rule also allows the limitation of the employer's liability by introducing the "control circle" instead of the "operating circle". The former is a much broader and an objective category, and according to the essence of the regulation, the employer is exempt from the liability if the damage was caused by circumstances beyond its control. In contrast, the Labour Code of 1992 regulated the employer's liability for damages – especially in the case of a work injury – on the basis of the analogy of dangerous operational liability, where considerably less room was given for exemption than in the new Labour Code, where being out of control and the absence of foreseeability make it easier for the employer to be exempted from the liability. Stricter liability based the analogy of dangerous operational liability and the possibility of exemption would be more appropriate, since the operation of a plant is the employer's risk. This is also based on the fact that the profits made from the operating activities also belong to the employer. Therefore, any effort on the part of the employer to share the risk of operating the plant with employees is unfounded. Besides, this new rule is also discriminatory to employees. Indeed, if e.g. an explosion occurs due to operation and people other than employees are injured, the employer is liable towards them under more stringent rules of hazardous operational liability, whereas in the case of employees – as we have already stated – the employer may be exempted more easily

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(Prugberger, 2014, pp. 145–150). It is no coincidence that, in order to overcome this inconsistency, the judicial practice applies the regulations of the new Labour Code recalibrated for the former rules pursuant to the instructions of the Curia (Sipka, 2015, Chapter V).

Regulations on the employee's liability to the employer have been changed to a lesser extent, and these changes have been implemented at the employee's expense (Prugberger, 2014, pp. 150–157). The introduction of the concept of civil liability in labour law is appropriate and it is also correct that within the concept, the various forms of fault affecting the reduction of the amount of compensation are distinguished. However, the rule is unreasonably burdensome for the employee according to which if the employee causes damage to the employer with more than average gross negligence, he/she may theocratic ally be held liable for the whole damage. In such cases Western European legislations also reduce the amount of compensation. When reducing compensation, it would be necessary to take into account not only increase in the risk due to the employees' several hours of monotonous repetitive workflow (Eörsi, 1961, p. 16; Nagy, 1964, pp. 15–16), but also the fact that in the case of in-plant work, the employer may prevent or mitigate the adverse effects of the damage by work supervision (Deli, 2013).

The system of legal consequences of the unlawful termination of employment has also undergone a major transformation. One of the changes is that the employee can only demand the restitution of employment if the termination was grossly unlawful, i.e. in five cases (Gyulavári, 2015, p. 227). In the case of unlawful termination, the employee, in contrast to the regulations of most of the old EU Member States, may only claim compensation but not restitution, representing considerably less compensation than before (Prugberger, 2012).

The employee may claim income missed in the case of damages, but the amount of compensation is limited: it should not exceed the amount of payment for a 12-month period of absence. The new rules have taken over the provision of the Civil Code relating to mitigation of damages, according to which the employee is obliged to look in a new job after the termination of employment and he or she must also prove it at court. In the old Member States, on the other hand, the employer is obliged to pay full compensation of the employee in addition to restitution. Moreover, in the case of the unlawful termination of employment by an employer in several Northern European states, adopted from the law of the United Kingdom, the employee is entitled to a base flat-rate compensation (basic anwart) ex-lege, and if the employee's damage is larger than that amount, he or she can also claim compensation (compensationsanwart) in excess of the amount of the base compensation. In this case, however, the burden of proof is on the employee (Prugberger, 2012).

As a new chapter, data management was added to the most recent amendment to the Labour Code. This amendment is justified in 2016 by the Council and the European Parliament on the adoption of Regulation 2016/679 (EC) of the European Parliament and of the Council on the protection of individuals with regard to the

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processing of personal data and on the free movement of such data (hereinafter: 'GDPR'). The Regulation seeks to achieve full legal alignment, so that the rules applicable horizontally (in general, for all data management legal relationships) in the areas of its scope are applicable directly and in Hungarian law.

As a general rule in the context of data management, the purpose and legal basis of data management should be indicated. According to the Labour Code the purpose of data management is the processing of personal data that is essential for the establishment, fulfilment, termination or enforcement of an employment relationship. Although the Labour Code does not specify the legal basis, there are three possible legal bases for data management at the workplace. The consent of the data subject, legal authorisation and data management based on the legitimate interest of the employer. The opinion of the Data Protection Working Team[5] is that the voluntary nature of contribution is uninterpretable in employment relations, and therefore in labour law this legal basis can only be invoked exceptionally.

A new provision seeks to promote privacy. If the employer provides the employee with a computer to work, only the data related to the employment relationship are allowed to be inspected. However, in general, the Labour Code stipulates that the employee may only use such devices for work.

An important change concerning collective agreements in the field of labour relations is that the law restricts the parties' collective bargaining to the slightest extent. The new act has significantly changed the rules for the conclusion of a collective agreement, so the collective agreement can already be concluded by the trade union with membership amounting to 10% of the people employed by the employer. This rule is absolutely antidemocratic, because if there is no other trade union at the company, the minority can force its own will on the majority of the employees, to whose detriment the employer may collaborate with the trade union signing the collective agreement. Previously, winning the works councils' elections was the benchmark for the contracting ability of a trade union.

It is legally unfounded that works councils precede trade unions in the new Labour Code. In this respect, the Labour Code follows the US solution, where employers prefer to negotiate directly with employees and enter into "win-win" agreements than with trade unions that are considerably stronger in advocacy.

Recently, works council formations have appeared in some states in the USA, but they only have the right to express opinions and consult, and they do not have the same co-decision right as in most Western European states (Hennsler and Roman, 2003, pp. 557–558). Probably this model has contributed to the reduction of works councils' co-decision rights in the new Hungarian Labour Code and has made it formal.

As concerns the right of interest reconciliation and the ability of the social partners to enter into a tripartite collective agreement with the state have been altered completely. Act XCIII of 2011 completely modified the National Labour Council and the National Interest Reconciliation Council. The National Labour Council has been extended to a National Economic and Social Council and has been fully transformed into a consultative institution with no authority to conclude national

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general collective agreements. Therefore, only sectoral and territorial reconciliation exist with the participation of the sectoral dialogue committees and as a result, there is a sectoral collective agreement. Unacceptably, as stated above, corporate collective bargaining has been altered in such a way that a trade union with only 10% representation can conclude a collective agreement on its own with the corporate management with an effect on employees who did not join the trade union.[6] According to the minister's argumentation, the legislator hopes that these changes will significantly increase activity by interest representations in shaping employment, while at the same time limit unjustified state interference and restrict it to the use of market-conform solutions. In the meantime, however, the legislator exposes employees to employers.

Amendments affecting government officials following the enactment of the Act on Public Service and the Act on Civil Service

The re-classification of government officials by Act LII of 2016 only due to a different wage or salary chart was abolished by Act CXXV of 2018 and the uniform status of government official was restored. It was also discussed that Chapter XVIII of the same Act, through the adoption of a general 4-month working timeframe – allowed an increase in the daily working hours to 12 hours for several weeks and to 60 hours per week for several weeks, which are already 9 hours per day and 45 hours per week as against the regulation in effect in 2015. In addition, government officials' basic leave was reduced from the earlier 25 days to 20 days per annum. In addition to what has already been emphasised in our previous essay, these violate the provisions of Act XXV of 2003 on Equal Treatment. In spite of the fact that officials under the new Act – by positive discrimination – were entitled to higher pays than other employees in administrative positions, a kind of runaway is experienced partly to retirement, and partly to the business sectors.

The reason for this is that the national guaranteed minimum wage has increased the salaries paid by the government and private officials subject to other public service law and public servants, thus the difference is no longer significant. This is the reason for civil servants' attempts at setting their foot on such more lax areas and leaving government service (Mélypataki, 2017, p. 370).

Notes

1 See Commission Communication on developing Common Principles of Flexicurity: COM (2007) 359. The aim of flexicurity is to ensure that all EU citizens enjoy a high level of employment security, i.e. they have the opportunity to find employment in every phase of their life until retirement and have favourable employment prospects in a rapidly changing economy. Flexicurity also aims to help both employers and employees to benefit from globalisation.

2 About the freedom of self-employment as a fundamental right see Kiss, 2006, pp. 285–290. In this study the text of the doctoral dissertation was taken as a basis. See also: Kiss, 2005, p. 116.

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[3] Article 141 of Act I of 2012 (Labour Code). Note that the concept of this shift bonus and the exact period when it is due should have been regulated under Article 89 2) 46 (Concepts) in Chapter XI of the Labour Code.

[4] For a more critical analysis of this area of law, see Prugberger, 2018, p. 25–27.

[5] An independent European advisory body on data protection and privacy issues.

[6] For more criticism of this see Prugberger and Rácz, 2017, pp. 191–192, 195.

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Civic Review, Vol. 15, Special Issue, 2019, 264–288, DOI: 10.24307/psz.2020.0215

András Giday and Szilvia Szegő

Double Coverage for the Pension Scheme – Pensions Require Both Children and Wages

Summary
The authors have elaborated a model to correct the false demographic message of the current pension scheme, as the latter suggests that a stable pension scheme can be maintained without having children. In this model, parents are entitled to a pension supplement for their jobholder children. In order to finance this scheme, an appropriated child-to-parent pension fund is proposed: a specified part of jobholder children's tax payments are contributed to it, and when their parents reach the specified age, their pensions are supplemented from this fund. Following the income and outflow of payments by the various generations, the proposed pension fund would thus create a kind of a generational finance within public finances. With the adoption of the child-to-parent pension element, the generational approach becomes part of both family budgets and public finances. The expression "child-to-parent" lends a symbolic power to the particular amounts, as it suggests that children represent a coverage value. According to our calculations, already the partial enforcement of the generational budget approach we propose will result in a 3 to 4 percentage point economic growth in the next few decades.

Journal of Economic Literature (JEL) codes: J11, J13, H55, H75
Keywords: pension scheme, public finances, parenting, pension reform, demographic risks, child-to-parent pension scheme, child-to-parent pension fund

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Method

Due to constraints on length, we have dispensed with the discussion of other concepts about recognising parenting in pension.[1] Three methodological novelties of this study should be highlighted:

– One of them is its vectored approach (demographic curves, labour market line, parenting trajectories etc.)

– The other is the financial application of this vectored approach, i.e. a vectored financial balance sheet is given as an example.

– And the third one is a re-orientation proposal applied to the specific features of a country based on the theoretical results, simultaneously with monitoring family and public finance balance sheet correlations.

The expected impacts of the proposal are estimated on a 30-year horizon, for Hungary. In our calculations, the headcount in the cohorts of the interactive population pyramid published by the Central Statistical Office of Hungary and included on the payment side were multiplied by the employment rate and reduced by 6-8 per cent for people employed in Western Europe. In respect of reduction in the number of working age people, the data published by *The 2018 Aeging Report* on Hungary were taken into account (EC, 2018).

On the payment side the number of people above the age of 65 was determined on the basis of the interactive population pyramid published by the Central Statistical Office of Hungary. Then the number of women who had children was calculated[2] and the number of men who had children but the mother had died was estimated. This was followed by the application of a 0.85 per cent multiplier to our estimate, as we presumed 15 per cent of the children of the number of people older than 65 not paying any contribution (because they have left for Western Europe, do not have jobs or have died). Thus the expected number of children providing child-to-parent supplement (up to 2050) was obtained. In the first few years, parents would receive an allowance of HUF 20,000 for 1.9 million children, and the number would only reduce slightly, below 1.8 million, after 20 to 25 years.

Introduction

Highly civilised societies are suffering from a severe demographic imbalance. Due to the mode of action followed by developments for several decades, the absence of a demographic balance remained unrecognised for a long time. The outstanding population growth called baby boom after World War II and then the significant number of children born to those born during the baby boom increased this hiddenness. For a considerable time, this double population boom provided input for the layer of jobholders. Economies were granted additional resources "free of charge", and moreover, due to savings in the pension scheme, in addition to the labour market, these resources also appeared in public revenues through pension contributions. In the bubble of these processes, hardly any attention was paid to the demographists and

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economists who noticed deterioration in population growth and the fact that the total fertility rate had systematically dropped below the reproduction requirement of the population also in Hungary. In the period of excess resources a warning of population decrease sounded like Cassandra's prediction. The professional circles taunted and shut them out. Enjoying the positive resources, many thought that a balanced pension scheme was also possible even if the number of children decreased. The absence of a replacement in the labour market by a new generation when they leave the active age was not perceived as a problem.

Family – business – state: generational trajectories and trajectory periods

Previously, public thinking was predominated by an exclusively financial approach. It was rightly emphasised that while in the active age, a generation should provide for its own existence after retirement. However, one consideration was completely bypassed: namely that the coverage for the amount saved for the years of retirement should also be ensured. In other words, money only has purchasing power if there are goods to purchase. Therefore, if a skilled generation suitable for production grows up and enters the labour market. The world of virtual money blurred the correlation that the pension scheme is unsustainable without children.

What happened at the level of families? As we know, in most European countries parenting remains considerably below the reproduction requirement. These are facts that show the actual number of children born. This is an important indicator. However, it is also important to look beyond the indicators. This is what an OECD study did: it compared the intended number of children and the number of children actually born to mothers between 24 and 49 years of age. This test revealed a significant difference between the intended number of children and the number of actually born children. This is conspicuous because these statements were not dim future concepts, they were made by people who were actual parents, and so the intended number was based on experience. In their case the intended number of children should have been close to implementation, however, this was not what happened. The OECD study considered it as an important warning that the desired number of children is considerably below the actual number of children suggests that childbearing (starting a family) is hampered in OECD countries.

The diagram shows the intended and the actual number or children, and the significant difference between the two (Chart 1).

As demonstrated in the chart, even on the average of the European Union, the desired number of children exceeds the reproduction requirement (the latter is above 2, and in this respect, Hungary is ranked the upscale sixth among the presented 27 countries). Thus on the level aspirations, demographic behaviour does not yet suggest population decrease. But the number of actually undertaken children does. This suggests that compulsive obstacles take place and prevent the birth of the desired number of children. One of the authors of this study, Szilvia Szegő, pointed out one

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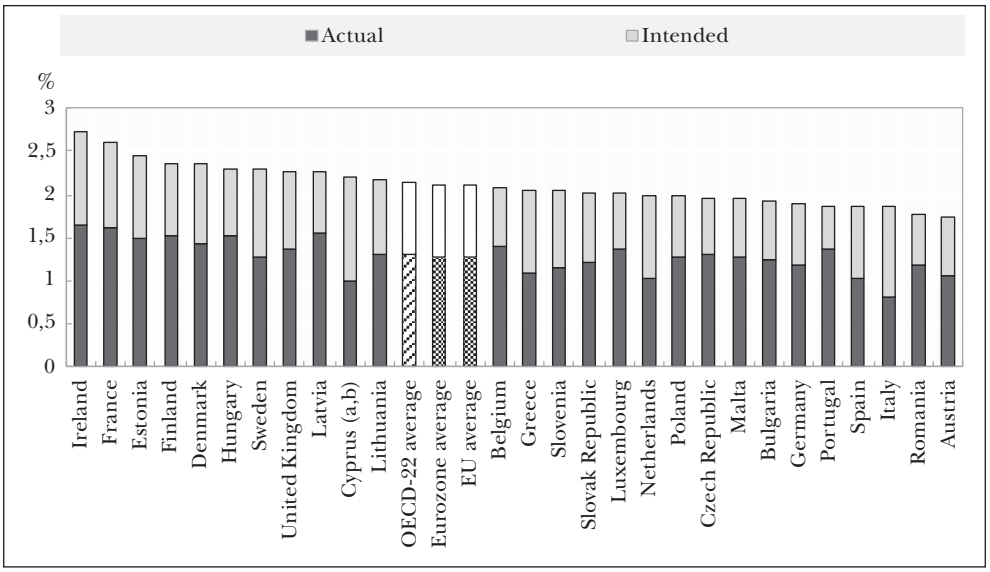
Chart 1: Mean ultimately intended family size, 2011. Mean average actual and intended number of children, women (25-39)



a) Footnote by Turkey: The information in this document with reference to « Cyprus » relates to the southern part of the Island. There is no single authority representing both Turkish and Greek Cypriot people on the Island. Turkey recognizes the Turkish Republic of Northern Cyprus (TRNC). Until a lasting and equitable solution is found within the context of United Nations, Turkey shall preserve its position concerning the "Cyprus issue";

b) Footnote by all the European Union Member States of the OECD and the European Commission: The Republic of Cyprus is recognized by all members of the United Nations with the exception of Turkey. The information in this document relates to the area under the effective control of the Government of the Republic of Cyprus.

Sources: Eurobarometer 2011: Fertility and Social Climate

of such obstacles in several of her essays (Szegő, 2002, pp. 59–83; Szegő, 2004). With the help of analyses revealing the various labour markets and parenting trajectories, she demonstrated that a kind of a "solution" for conflicts between the different trajectories is that a number of the intended children are not born. The time schedule of childbearing is also distorted. The first child is delayed, and childbearing is finished "early" in comparison to the course of life of a person with several children.

Thus parents' childbearing period has significantly reduced within the courses of their lives. Due to the shorter childbearing period, a lower number of parents will have a shorter time on his trajectory to have children. One would conclude that as a complementary event, the time spent at work will then be longer. But this is not what happens. Actually, it is the reverse. In practice, similarly to the childbearing period, the time spent at work also becomes shorter. The jobholding period also starts late and ends early. It follows from this that the two trajectories do not adapt to each other;

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rather they compete for each other's periods.[3] This situation is rendered even more difficult by an increase in the period of parenting. For this reason, parents are compelled to expect a long course of parenting as a result of childbearing.

A serious paradox follows from all these. A relatively long and – if schooling is included – more expensive parenting period is established while the parents' employment becomes increasingly unfavourable as they grow older. The income available for the late education of their children may decrease.[4] We have come to the conclusion *that despite increase in the life expectancy, the periods of childbearing and jobholding are on the decline, while the period required for raising children until they start work has increased considerably.* As an inevitable outcome, a significant number of the intended children will not be born, unless adjustment is made.

Although there are significant experiments towards family-friendly businesses, companies' responsiveness to their employees' family obligations remains rather low. The childbearing age, especially in the case of women, is an *ab ovo* disadvantage.

A problem that is even more serious than the conflict between family versus business trajectories is that companies fail to consider the employee's entire course of life. Companies do not finance human walks of life; they only take account of and calculate with the human period spent with them. As GDP, the recognised performance is produced by the company, this approach is not only characteristic of companies, but also of the society. For a long time it may seem that the performance of the economy is independent of the number of children families undertake to have. It was thus fair to assume almost as a matter of fact that for a long time pension was considered to be independent from childbearing. When it became clear that the demographic structure of the population deteriorated at a rate that was hardly rectifiable during the next generation, emphasis was placed on long-term thinking. While the one-time advocates of the Cassandra prophecies were not allowed to speak up, when a significant deterioration in the demographic resources became inevitable, suddenly it became trendy to deal with the worsening composition of the population. It was made a research topic and – with ample support from the World Bank and other rich institutions – all of a sudden the pension reform thought started to spread. Proposals were made one after the other about the reform of the pension scheme. These recommendations revealed many things, but unfortunately, they failed to tackle one important factor: the fact that pension payment required children, to put it simply, and moreover, jobholder children.

The pension reform proposals seemed to reveal that the failure of the so-call pay-as-you-go scheme, gaining ground after World War II caused the drying up of the resources for the pension scheme. The pay-as-you-go system was contrasted to the proposed full funding scheme. Instead of the current employee wages and the amount contributed by them to public finances, a fully funded resource should be allocated to pensions. In simplistic terms this meant that the pension scheme had to be included in the capital investment system, and savings were managed as investment functioning as competitive capital. In other words, in this approach pensions are based on the capital gain on pension contributions. The investment time horizon needed to be at

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least 40 to 45 years, i.e. the entire time spent in work – and this was less highlighted. Over such a long time period, risks already include developments in the demographic resources. And this exceeds the risk management period of capital investments by a period comprising several generations. When the demographic problem kicked in, the attention was again drawn to state assets.

In an analysis of companies and families we have got to the state. Although pension reforms had been granted huge amounts of support and ideological orientation through state contribution, they actually wanted to oust the state from the resources of the pension scheme, while implicitly shifting the generation-related risks to the state. The latter is the risk we are currently facing. They intended to re-channel the amounts saved by generations to a private capital flow scheme. In this approach, the new generation is also "absorbed" the population in the same way as companies can take up the available workforce. Unfortunately, the research underlying these reforms failed to study the correlations included in generational relations, for example the ultimate party to assume the demographic risks. By now it has become clear that the demographic crisis that has evolved cannot be solved by the "marketization" of generational savings. The problems of demographic imbalance and the resulting pension security issues necessarily rose to the level of the level of the state.

This article is not supposed to analyse the two different kinds of pension schemes, we merely wished to outline the approach that failed to include the need to relay between generations, at least to the extent of raising the problem, in the efforts made at a reform. In Hungary, deterioration in the structure of the population will remain unstoppable for a long time, as any correction can improve the structure of the population in about 20 to 30 years. It is already clear that the former population peaks we could enjoy have kicked back in the pension scheme. The children of the populous generation of the 1950's will soon retire. *To date they have functioned as a kind of a "free" demographic resource, but soon they will cause a deficit in economic growth and in the pension scheme.* This will also have its impact felt in public finances. Those who have increased public revenues due to their relatively high numbers (in times when high unemployment counteracted it) will soon retire and increase the number of pensioners. (This situation is further exacerbated by the complex effect of work abroad, which reduces labour supply.)

In addition to children, the pension scheme requires wages

By now it has become clear that the previous approach that children are not needed for the pension scheme needs to be changed urgently. But even more is needed. Children can only provide coverage for the pension scheme if their performance is sufficient for this. This means that in addition to the number of children, the number and wages of employees are also important if we endeavour to have a financially balanced pension scheme. The pension payments relative to the low level of average wages have been adjusted in recent years in Hungary. For example, in 2018 the net

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average wages increased by 11 per cent, and this had a favourable impact on income from pension contributions. However, it should also be taken into consideration that the predictable increase in the average wages is still insufficient to offset the reduction in the number of employees to take place within a few years. No matter how high the average wage may be, if the age composition of the population deteriorates and an increasing number of pensioners must be supported by a decreasing number of employees.

Due to the ageing population, within a few years the pension scheme will face a severe problem in Hungary. Between 2018 and 2037, the number of people between 23 and 64 will drop by three times as many as the increase in the number of those in the retirement age. These drastic effects will be felt in the generational composition in no more than the next 20 years. For this reason it is crucial to find a quick solution to cover *the payable pensions by an appropriate amount of wages* in the period ahead of us.

Pension scheme adjustment may not rely solely on childbearing, as the expected amount of earnings in the times to come is a similarly important issue. However, the question raised this way leads back to the demographic correlations. There is no more waiting. We need actions to encourage having the desired two children per family.

Pension requires double coverage: pension contribution and children

The pension scheme is covered by contribution payments (whether social contributions or other kinds of pension savings) and by demographic coverage, in other words, the replacement of the retiring generation by their children. The current pension scheme unduly depreciates the role of children in actual pension payments. Approximately one to two per cent of the total amount of the pension serves to recognise that the pensioners had made significant efforts for the child-to-parent coverage of pensions. Those who raise children invest in the demographic security of the pension scheme. Recognition of the investors in the pension scheme – by a kind of a child-to-parent element – would acknowledge this performance and would appreciate having children. Instead of containing childbearing, this new element in the pension scheme would recognise it.

As a historical heritage, women shoulder considerably higher burden by undertaking parenting than men, and this is especially spectacular in women's labour market trajectory. Their lower average wage is partly due to this. Thus in the form of a pension contribution, they have less pension coverage than men. In order to lay the demographic basis of the current pension scheme we need to correct these distortions. A more realistic reflection of the value proportions between childbearing and employment in the pension scheme would have an important moral message.

For the acknowledgement of parenting in the pension we have elaborated a possible child-to-parent pension scheme built in the current scheme. Without changing the current pay-as-you-go scheme, we only propose to add a supplementary pension

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element to move the message inherent in the pension scheme in a more positive direction: to show that pensions do depend on the performance of children born and raised to work.

The principle of family reciprocity – in a child-to-parent pension scheme

The pension scheme essentially does not acknowledge the significant amounts spent by families on raising children (it only pays 1 to 2 per cent for the children), despite the fact that raising children demands significant financial expenditure and household duties. Seeking a solution, we prepared a family budget applied to Hungarian conditions. This clearly revealed that – including both work and financial costs – raising two children required parents at least amount of money equal to the amount of contribution they pay to the pension funds that secure their generation's pension during the years they work.[5] The size of parenting burdens is also shown by the fact that parents who undertake to raise two children immediately consume 30 per cent less than childless couples under otherwise equal conditions.

In essence, our current pension scheme dispenses with the principle of reciprocity. In other words, they consider their pension and the future of their generation independent of whether or not they have children. It is all mental. If families think along these lines, they will act accordingly. This is a typical regulatory failure. In order to remedy this failure, the model has been built to allow families realised the correlation between the pension scheme and having children. In this model, this is the purpose of paying a child-to-parent pension supplement in consideration for their investment made into children. *The investor parents should also share in the yield earned by a jobholder child.*

Currently, parenting is more penalised than acknowledged in the pension scheme. The small amount that appears in the pension under the title of parenting is insufficient for even the minimum compensation, despite the fact that these people have given up a lot for their children. This is to say the current pension scheme is not only unjust but also sends a false message. Part of the message is that parenting is not worth, and the other part is that the state is able to devise a future image without considering the number of children born and raised, including employment in the domestic market. For a long time it was thought that a country's performance can develop independently of the way the generations follow their ascendants. The flawed messages have had severe consequences: deterioration in the demographic structure of the population and weakening the foundation of the demographic pyramid.

In order to alter the false message of the pension scheme, we have elaborated a system that would provide a perceptible pension supplement to parents for their children. The parents would have a share in the proposed pension supplement in proportion to their respective contribution (60 per cent by the mother and 40 per cent by the father). The term "supplement" is used in order to emphasise that the intention is not the change the current, practically pay-as-you-go scheme. We do not wish to reduce the pension payable to childless people. We recommend the recognition

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of having children in the parents' pension by an amount of money that gives weight to the child in the pension if expressed in forint. The symbolic significance of the child-to-parent pension element is even more important than the amounts involved: it calls a spade a spade, i.e. this pension element sends the message that *pension payment requires children.* (It is important to note at this point that in the proposed amount, both the load-bearing capacity of the central budget and the expected favourable labour market effects had to be taken into account. This is explained by the fact that in contrast to distorting messages, demographic messages offer parents the option of making an expected more favourable decision.)

The amount of the child-to-parent pension we have elaborated would increase to about 12 per cent of the total paid old-age pension from the current approximately 1 or 2 per cent. At the level of the families affected, the proposed amount would represent *a rise of about 15 per cent relative to the average pension up to the end of the parents' lives.* This is already an equitable amount, and would have a favourable impact on the approach that has caused the break off of the pension scheme from generational relations and has pushed the principle of reciprocity into the background.

Pension in the family budget

Our proposal puts the above considerations into practice: after the age of 65, retired parents would be paid child-to-parent pension in the amount of HUF 20,000 per month per every jobholder child or offspring in addition to their regular pension. This amount would increase the two parents' aggregate pension (calculated on average) by nearly 15 per cent (if they have to children): by nearly 20 per cent for the mother and 10 per cent for the father. This difference would in part adjust the unfair underrating of women in their average pension. The pension paid to a parent for any reason would be 30 per cent higher.

As an important consideration, the supplementary pension element should assimilate into the values already accepted in the pension scheme: the simultaneous enforcement of performance and solidarity. In this case this meant that the supplement paid for children was not made proportionate to pensions. This would not have made any sense as this supplement is not compensation. In our proposal we do not intend to radically change the current values manifest in the pension scheme. We only wanted to emphasise the principle that children are also required for pension. For the purposes of sending a message of this principle, we selected a pension supplement that is big enough in size to represent genuine value compared to the current minimum amounts. Thus the amount of the proposed pension supplement basically intends to transmit a message about values to the society, the family and to individuals alike. We also considered it important to have a pension supplement that was manageable at the level of public finances and that did not undermine the efforts made at maintaining balance in public finances.

Another important consideration included the requirement that the basis of the pension supplement should be the child's performance. This is because the genera-

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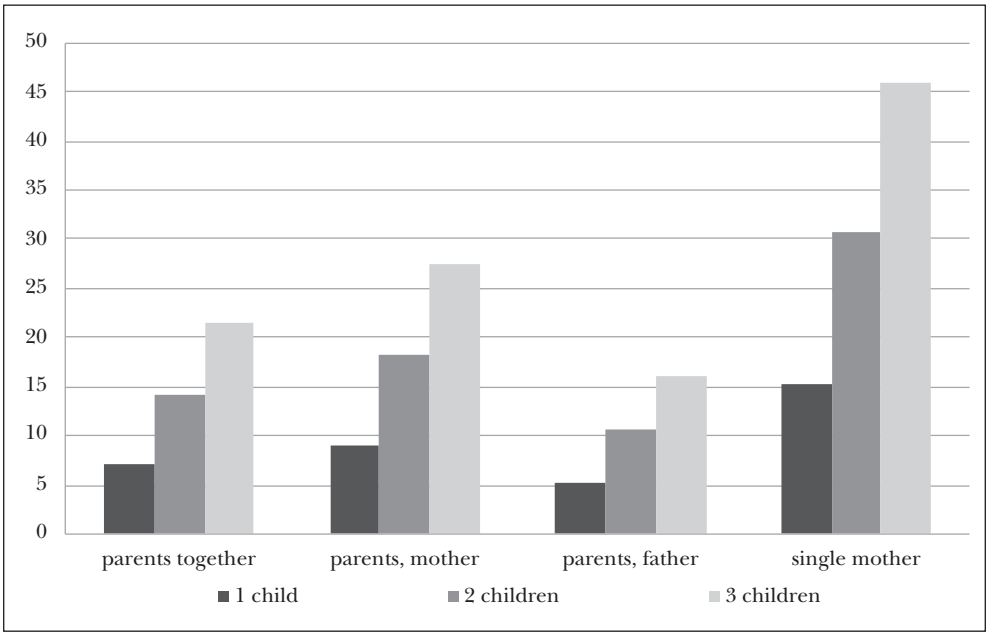
tional reciprocity is not limited to the birth of a child. On retirement, parents need genuine performance. Resources are needed for supplementing pensions. And this resource comprises the payments made by jobholder children, thus a part of their earnings, to the central budget. Thus our proposal significantly differs from those that recommend the payment of additional pension simply on the basis of the number of children.

Our principle was to manage demographic considerations in agreement with the financial procedures. In other words, in our model it is not the child or offspring, but the social contributions paid by them that provide a legal basis for a child-to-parent pension. For this reason, a part of the taxes payable by children would be earmarked for payment to the parents at a later date. In addition to the number of children, parents would also be entitled to supplementary pension on the basis of the child-to-parent pension fund maintained by these children. Such a child-to-parent pension would be established from (a part of) the taxes payable by children and the fund would be used as coverage for pension payments to parents.

The recommended amount – i.e. HUF 20,000 per month per child – would increase the pension payable to retired mothers by a considerable amount, to adjust the current unjust undervalued average pension paid to women. The following chart depicts the amounts parents could have access to according to the number of jobholding children and family status.[6]

Chart 2: Additional income (to the average pension) including the child-to-parent pension supplement, in a breakdown by the number of children and family status, %



Source: Authors' own calculations based on HCSO, 2018

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If the parents' pension depends on the offspring's performance, this also means that *pension is included in the family budget.* Part of a jobholder offspring would be returned to the parents. The value of wage would be appreciated by the family, as it would become income that can be used at a later date.

Thus, in addition to the above, our proposal also has another business management innovation: *the family budget becomes a public matter,* and thus the individual work trajectory (or career) would also be managed as part of the family budget and would be discussed. Later on, we will endeavour to enforce this approach in public finances. Developments in the family budget and the events affecting the various generations at the level of the family would become important considerations in public finances. The reason is that they would have financial consequences in the model we propose.

Coexisting generations in public finances – the new child-to-parent pension fund model

With the child-to-parent pension fund, pension is included in the family budget. A matter of principle, namely that pension requires children, is put into practice. For adult, jobholder children it would thus be made obvious that, through a new, state-administered pension fund, part of their wage would increase their parents' pension. Below is a discussion of public finances. At the level of the state, we also endeavour to enforce the principle of coverage by the next generation, complete with a model of generational finances. We made efforts at the elaboration of a financial scheme suitable for monitoring whether or not a next generation replaces those who retire from work. For this reason, we endeavoured to set up, within the budget, a scheme that monitors the financial relations between the coexisting generations at any given time. To this end, we recommended the setting up of an appropriated child-to-parent pension fund, which collects payments from the affected age-groups of jobholder children, and pays pension supplements to the relevant age-groups of the parents.

Thus, just as in a family, *the coexisting generations work and contribute to the fund,* and just as in a family, *the coexisting generations are paid pension supplement from the fund.* In this case, the social organisation of the budget is not the family but the state institution of coexisting generations and the fund appropriated from public finances that transacts payments and withdrawals. Thus the proposed pension fund is a system capable of monitoring the "household" of generations through the collection and outflow of liquid assets in the pension scheme. The amount of payments depends on the headcount and average payment of the working generation, and on the transfers made from the, while the amount of disbursements depend on the headcount and performance of the generation of the retirement age. The HUF amounts display whether the contributors' performance (the number of the contributing generation of children and the amount of payments they deposit in the state budget) satisfies the pension requirement by the beneficiary generation of such payments vis-a-vis the proposed budgetary pension fund.

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We followed this logic in the child-to-parent pension fund we proposed. This fund would operate in close relation to but separately from the state budget.

By the establishment of a child-to-parent pension fund, we intend to modify the previous approach, which focussed on the fiscal balance and failed to monitor the effects of demographic resources in the budget. Thus during the period of the baby boom, a demographic surplus appeared as temporary additional resources, and it did not predict that over time, decrease in the number of children would cause a shortage of demographic resources in the central budget. *Thus in addition to the pension scheme, the deficiencies of the demographic approach also caused a problem in the system of public finances.* Generation fluctuations disappear in the fiscal system broken down into years and year lines. For this reason we consider it important to apply a financial structure suitable for monitoring funds flows between generations. The scheme we propose, i.e. the child-to-parent pension fund may be suitable.

The question arises when and how to adopt such a system. Obviously, the sources of payments will be the children's contributions paid to the state. It follows from this that for a long time resources are generated but they may only be used, i.e. paid after a period comprising several generations. The question is the matching of the incoming and outflowing funds in time and amount. The absence of a pension fund previously appropriated in the budget for retired parents should also be considered as granted. If we want to adopt an equitable pension supplement also for these people, we need to look for stop-gap measures. This is the reason why we apply a basic scheme launched in the form of payments, and disbursements are made only after the entitlement has been obtained. Furthermore, we apply a stop-gap scheme to pay the current generation of pensioners, as no such pension fund has been set up for them. As the latter scheme is short of funds, the basic scheme has been compiled in a way that its excess funds (the subsequent disbursements) should cover the pension supplements disbursed under the stop-gap scheme.

The basis scheme of the proposed appropriation is the following. Part of the contributions paid by young people to the state budget would be transferred to the appropriated child-to-parent pension fund in the first 4 years of their employment. The contribution would only be deducted and transferred from HUF 225,000 of the child's wage, and transfers from any amount above that would be made to the usual state budget. This cap was set in an amount to allow sufficient funds for the parents' pension supplement. This amount (HUF 1,300,000 per annum) approximately corresponds to the disbursements parents would receive after the age of 65 – on average for about 15 years – as a supplement for their jobholding children. As an important consideration, payments should be made in time, i.e. children should pay the four-year payment into the pension fund by the age of 25-28 (depending on qualifications).

Thus in the structure of this pension fund, as an important criterion, in addition to the number of children, parents would also be entitled to supplementary pension from the social contributions on the basis of a child-to-parent pension fund maintained by these children. The assets side of the pension fund includes the payments

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made by the jobholding children or other offspring, while the liabilities side comprises the pension supplements due to parents after their children.

The amounts accounted in the assets and liabilities sides of the pension fund would clearly show the changes that took place in the succession of the generations. Such a fund would also show if, for example, during permanent and mass unemployment, the topping up of pensions by the next generation is lost.

Thus in our proposal the successive generations are interlinked in the financial balance and the performances displayed in their respective employment. For this reason in the proposed pension fund, any demographic shortage and underemployment as well as the resultant budget deficit (or the opposite, which may arise from a demographic surplus resource) could be monitored. Through establishing a child-to-parent fund, the logic of the financial balance would get closer to the logic of social institutions, including families, the latter term meaning the "large family" of the successive and coexisting generations and their generational household under the government's umbrella.

The specific facility of the child-to-parent pension fund – or the model of generational public finances

The proposed basic scheme is the following. Withdrawals from HUF 225,000 of the monthly earnings of an employed child would be transferred to the child-to-parent pension fund. This would add up to HUF 1,300,000 per annum. This is performed for the first 4 years of the child's career, but up to the age of maximum 25 (or 28 if in tertiary education). This contribution would only be paid for 4 years, and then terminated. (HUF 5 million is collected in 4 years, and this amount is sufficient for paying HUF 20,000 per month to mothers and partly fathers above the age of 65 for the rest of their lives.)

Management of the transitional period was also important in this proposal. This is because we consider it equitable to pay an allowance to currently retired parents for their children. Obviously, at the moment there is no appropriated resource in the central budget for such a contribution. For this reason, the resources are naturally insufficient for the payments to be made from the pension fund. This situation could be improved if the first 4 years following commencement are considered as margining.[7] In other words, during this period transfers would not only be made to the state pension fund of this scheme from the wages of young people newly entering the labour market but all employees younger than 42. After four years, they would no longer contribute to the facility. Subsequently, only those contributors would remain in the scheme who had been unable to pay the required amount within 4 years. They would be given two additional years for making the required payments. Then these contributors would also leave the system. In the period after the initial four years, payments by those who leave the scheme would be uninterrupted because the new entrants to the labour market would continue paying the contributions.

Thus the parents of people below 42 could only be paid pension supplements from the fifth year after the commencement of the facility, i.e. from 2025 in our pro-

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posal, provided that they are entitled. Initially, the number of beneficiaries will be low, as parents need to reach the retirement age.

Thus in the first few years after the commencement of the scheme, payments made by large masses of people below 42 would be transferred to the pension fund, while nobody would be entitled to receive pension supplement for four years. Subsequently, for a time their number will remain low. Thus the pension fund would increase by more than HUF 2600 billion per annum, and this surplus would serve as coverage for the subsequent payments to be made by the pension fund.

Under this facility, these funds would be transferred from the general liabilities of the state to payables to pensioners in consideration of their children, covered by the working generations.

Thus the first four years of the child-to-parent pension fund can be considered as a basic margining period. This is why the following chart shows outstanding amounts among the revenues of the pension fund. Then payment starts, and the revenues raised by the pension fund will be sufficient for fulfilling them up to 2042, when a deficit of HUF 60 to 120 billion evolves between annual incoming and outflowing funds. This is the point where the financial scheme devised by us evidences that it is capable of mapping demographic developments, because the mentioned deficit is caused by deterioration in the demographic composition. In other words, from the fact that the number of children decreases in comparison to the parents' generation at any time, i.e. the elderly generation is not replaced. Instead of demonstrating the frequently emphasised absence of discipline in the state budget, this deficit reveals that irrespectively of financial discipline in public finances, a deficit develops in the budget if the population decreases.

This clearly reveals that *demography, or population developments, and more specifically, the composition of the population, are significant factors in the country's economic growth* or, in an opposite case, in its decrease.

The Chart 3 depicts the proposed supplementary pension facility with payments and revenues in the age-group below 42.

The deficit shown in the chart after 2042–2045 can already be considered as a demographic structural deficit. This suggests that the child-to-parent pension fund is not merely a financing facility of numerous similar options; but it is a facility of a generation's financial management. In other words, in this case the calculated and depicted accounting deficit also highlights the economic demographic deficit of pensions.

Reclassification between generations in public finances – covered by the pension fund

The above is a discussion of payments made by people below 42 and developments in the headcount of the beneficiaries of pension supplement as well as their effects. The situation is different in the case of people older than 42, as the majority of their parents have already retired. An equitable solution should be sought for providing them access to a pension supplement for the children they have raised. An equitable

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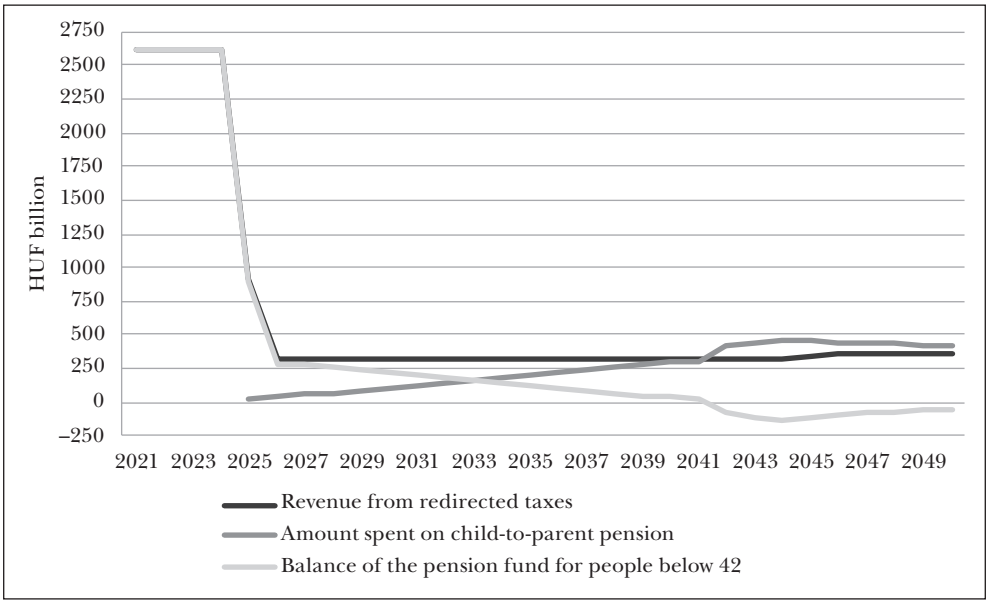
Chart 3: Revenue, expenditure and balance of the pension fund, 2021–2051, people below 42



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

solution should especially be sought for elderly women, because they raised several children while simultaneously working, and therefore their pensions are considerably less than men's. An equitable pension scheme would acknowledge their performance after their employed children.

For this reason, we have also elaborated a facility meeting the above principles. The principle underlying this solution is also the securing of parents' entitlement to a child-to-parent pension by a 4-year employment in Hungary.

– As a fundamental requirement, people above 42 would be required to have worked at least 6 years in Hungary between 2010 and 2020. In this case the parents would be automatically paid the HUF 20,000 pension supplement due to them for their children. If this is not fulfilled, they should also evidence 4 years of employment within 6 years.

– People above 51 should prove to have worked for 12 years since 1988 or 6 years between 2010 and 2020. If these criteria are met, the parents are automatically paid the HUF 20,000 due to them.

– People above 60 should also be expected a similar performance for entitlement to the pension supplement. It is emphasised that in each case, provided that the conditions are met, the child-to-parent pension supplement would automatically be due to the parents.

Where will the money come from? We have not raised any funds. (No more than 4 to 5 per cent will pay subsequently.) It follows as a matter of fact that a significantly higher amount can be collected from people below 42, as shown above, exactly in

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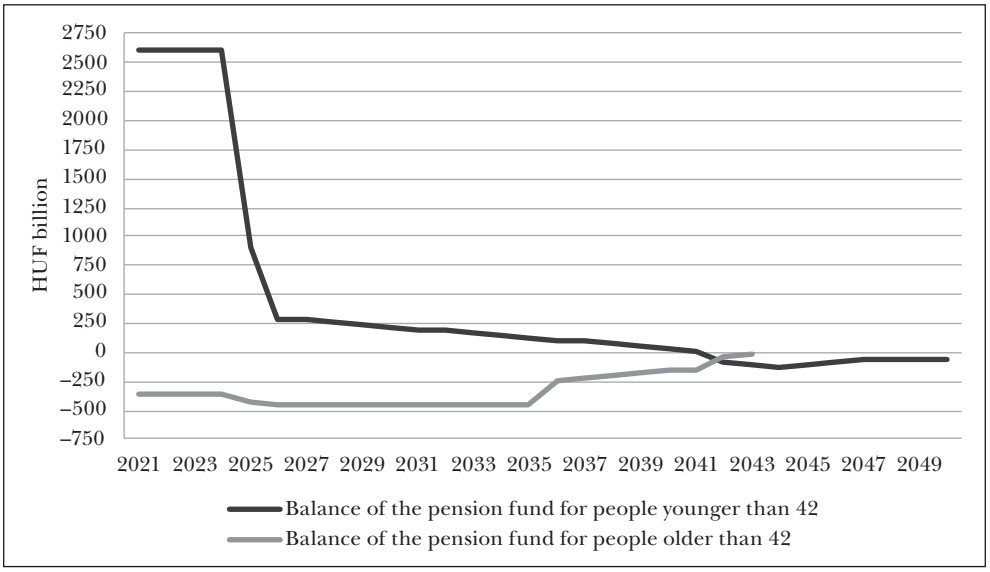
the same years when deficit is to be expected in the case of people above 42. This allows for the option of a kind of reclassification between generations. In this case, this would mean that in the case of people above 42 the state, acting as an institution of generational solidarity, would undertake payment of the pension supplement to the current pensioners. Resources for these payments would be raised by borrowing the money deposited by people below 42 in the child-to-parent pension fund. This is essentially required up to 2045, because by that time this retired age group will not share in pension any more. On the other hand, by that time the pension fund of the currently 42-year-old will start making deficit, and so the redemption of the loan will come handy. It is also emphasised that the child-to-parent fund lends the money collected from payments by people below 42 with the intention to be repaid at a later date, in other words, it expects the state to hedge this amount. In 25 years this amounts to HUF 7.7 thousand billion. At that point things change. After this point in time, the pension fund does not lend any more, but it is repaid the loan it has granted. (Right on time because within 25 to 30 years, the parents of the generation currently below 42 will also require an amount of about HUF 350 billion for the monthly HUF 20,000 pension supplement.)

The Chart 4 depicts the option of generation reclassification, based on the difference between the annual incomes and outflows.

Chart 4: Annual pension fund balances for people below and above 42



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

The chart clearly shows the point when the pension fund having a surplus turns into the negative, and the other fund does not generate deficit any longer. It is also clearly visible that the surplus generated from the payments made by people below 42

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to the pension fund provides coverage for the state to take a loan in the form of domestic bonds for paying the uncovered pension supplements. This means that a kind of solidarity cross-financing can be established by various lending techniques between the two generations within the central budget.

Once the transitional period is over, the scheme's stable financing is ensured by young people's payments. As employment is nearly complete, the overwhelming majority of employees below 25 is expected to spend the first 4 years after commencement with work, and consequently, from the 5th year, no more reclassification would be needed from the taxes on their incomes into the child-to-parent fund. This would result in a drop of the number of payers to the level where each time the taxes on the incomes of a group of 20-25 years old people, i.e. a generation of 4 birth years, are reclassified. This comprises about 250,000 people year by year.[8]

When the HUF 5 million has been collected as a result of payments made during 4 years of employment, young people no longer contribute to the pension fund (say, at the age of 25) through the central budget. However, he or she is replaced by a new entrant, a 19 or 20-year-old person starting on a career.

For this reason, the child-to-parent pension fund is not merely a financing facility among numerous other similar options, rather, it is a facility that highlights the financial deficit incurred in pensions, calculated according to accounting rules and caused by demographic factors. However, after a few years, the number of people employed, and consequently, the amount available for financing pensions, will suddenly decrease.

Effects on public finances

Running internal funds through internal bonds

Since at the start of the scheme payments into the fund would amount to 15 or 20 times the amount required for disbursements, it is advisable to allow the lending of the money left in the fund after disbursement to the parents for the purposes of financing the usual expenses incurred in public finances (e.g. the budget, the pension fund, the health fund etc.). This could be done, among others, by purchasing the internal fiscal bond (e.g. on the last day of each months, the amount available on the fund's account would be spent on this). Pension supplements would be financed from the child-to-parent fund. After these amounts have been paid, internal fiscal bonds would be purchased from the amount left in the fund (e.g. on the last day of every month). Only the child-to-parent fund would be allowed to purchase internal fiscal bonds. (Whether or not a real interest rate should also be imposed in addition to indexation for inflation, what maturity should be set for it and if it should be renewable remain open questions.)

The chart compares the high-amount surplus accumulated over the years from the payments made by people below 42 and the simultaneously generated deficits. The following chart gives a good illustration of the options available for using these resources

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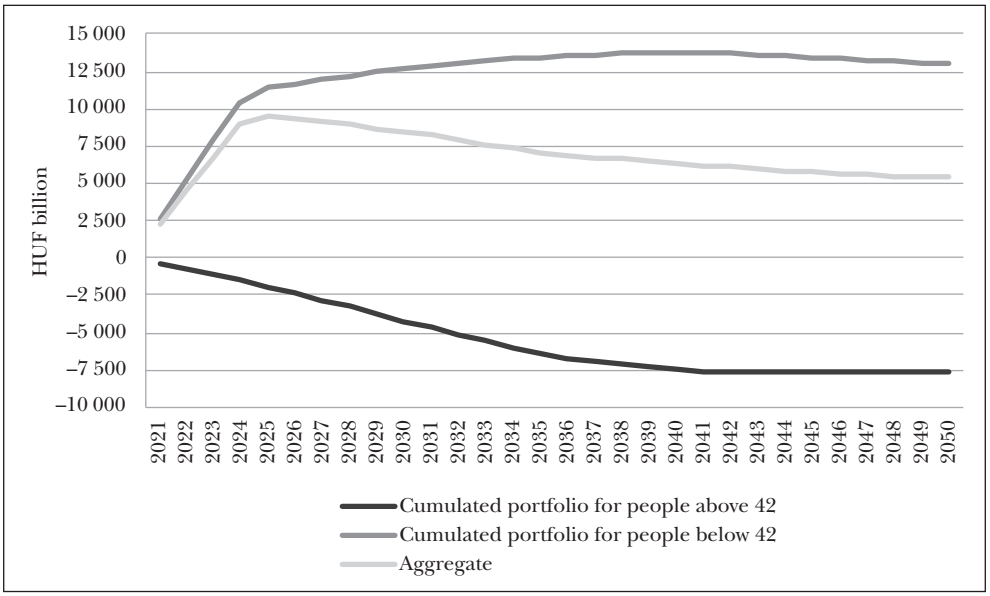
in the internal budget. While annual surplus amounts and deficits are compared in the previous chart, this one shows the limits of growth for the accumulated surpluses and accumulated deficits, and the point in time when their direction changes.

Chart 5: Cumulated annual pension fund balances



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

The chart reveals that while the pension fund surplus increases to HUF 13,000 billion, the government will have a deficit in the amount of HUF 7.7 billion from uncovered payments. This means that actually, such accumulated amounts should be expected when a financing facility is set up between the two pension funds. The government could issue bonds for this accumulated deficit and the child-to-parent pension fund could purchase such bonds.

A decision on the reclassification into the child-to-parent fund would be adopted annually, in accordance with the usual fiscal administration procedure, simultaneously with a decision on the amount of pension supplement payable next year and on the amount of internal bonds to be purchased by the fund.

Maastricht Criteria

Reclassification into the child-to-parent pension fund would remain a transaction within public finances. Thus only the child-to-parent allowance (HUF 20,000 per month per working child) would be included in the Maastricht deficit. The deficit caused would be reduced by the increased amount of taxes due to higher consumption resulting from the additional pension disbursements. The higher employment

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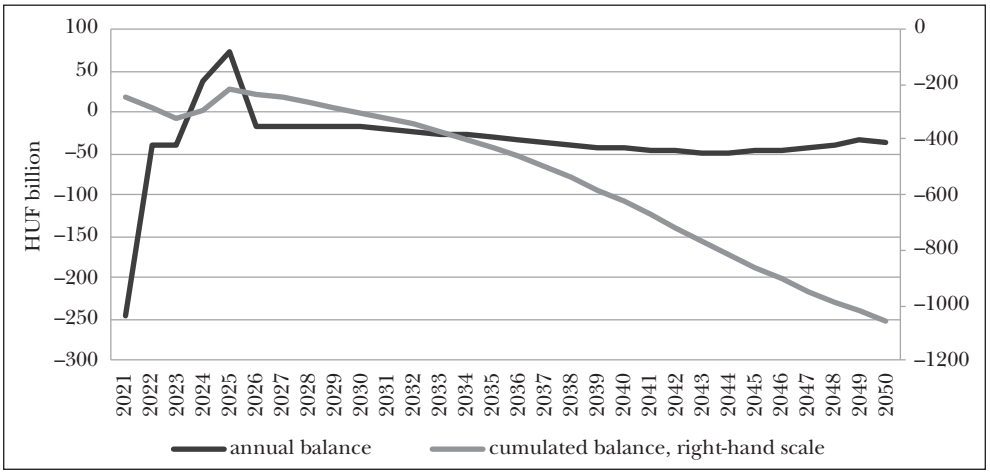
triggered by this model would also increase state revenues. A comparison of expenses and incomes caused by the proposed scheme discloses the actual public finance deficit, shown in the following chart.

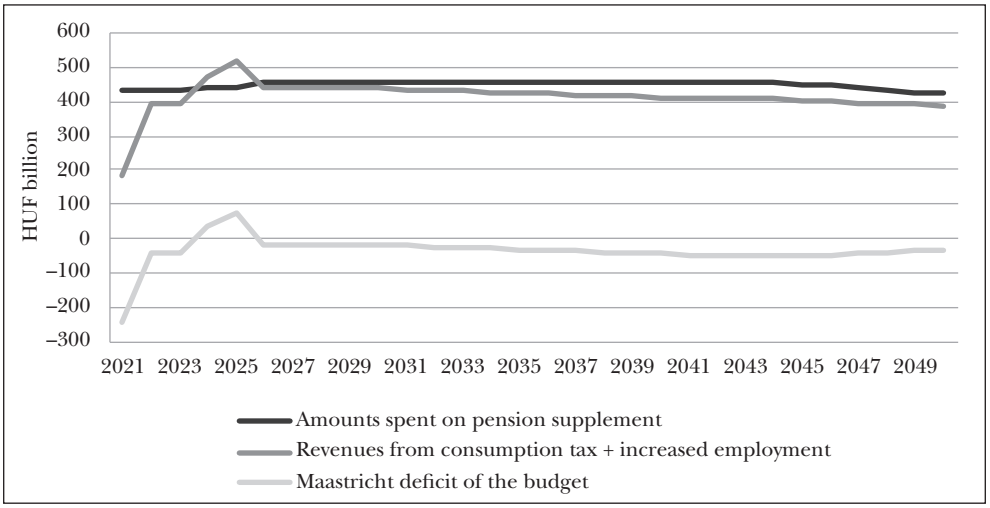
Chart 6: Expected government deficit, incl. the child-to-parent pension element, annual and accumulated Maastricht balance



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

Developments in the child-to-parent pension fund and the details of their effects on public finances are depicted in a single chart.

Chart 7: Impacts of the child-to-parent pension on the government deficit according to the Maastricht criteria



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

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It is clear from the chart that the ultimate total (supplemented) net government deficit is only significant in the first year – approximately HUF 200 billion,[9] and then as a result of the proposed scheme, the deficit does not increase by more than HUF 20-40 billion per annum. The net amount includes the funds repaid to the state, primarily the increased amount of taxes due to consumption.

The obvious fiscal burden is, however, mitigated by the approach that the proposed model considers childbearing an investment that will subsequently reduce the demographic deficit. This also supports the actual birth of the number of intended children, since it makes obvious for everyone that an investment is made into his or her family's future. In our opinion, the proposed child-to-parent pension element also improves the accounting of the pension scheme, not in the lease due to the fund financing technique that also takes account of resources. Similarly important is the approximation of accounting and social values.

Expected effects on employment and on economic growth

The proposed child-to-parent pension model includes pensions in two of the country's important budgets: it will be integrated in family budgets and simultaneously also into the pension fund specifically established within the central budget for this purpose. This will give a clear message to young people to come home and undertake employment in Hungary, and will encourage the conversion of public finances according to demographic correlations. The demographic processes could be given higher emphasis in shaping public finances, for example, in predicting employment or in projecting economic growth. Thus the false message currently sent by the pension scheme, namely that the pension scheme can be made independent of parenting and of adult children's performances. The requirement of reciprocity between generations would represent an important value in both family budgets and public finances.

With the termination of the false message sent by the current pension scheme and with the establishment of relay system in the proposed scheme would gradually change the trajectories of families and of public finances: it will be worth both for families and for the central budget to have two children in every family. In such a budget, children are not seen as burdens but as investment; children are not considered as consumption limiting investment, but as an important factor of future economic growth. As a result of these incentives, the potential headwinds of parenting will become a tailwind in the pension scheme: in respect of both the number of children actually allowed to born and children's employment and especially employment in Hungary.

We expected the proposed pension element to increase the amount of family budgets (for the extended family) by EUR 350 per employed child for 4 years. For this reason work in Hungary would become more attractive than work abroad. (However, a minor part of those who return for this specific purpose would presumably return to the West after the 5th year.) Its favourable impact was taken into account through

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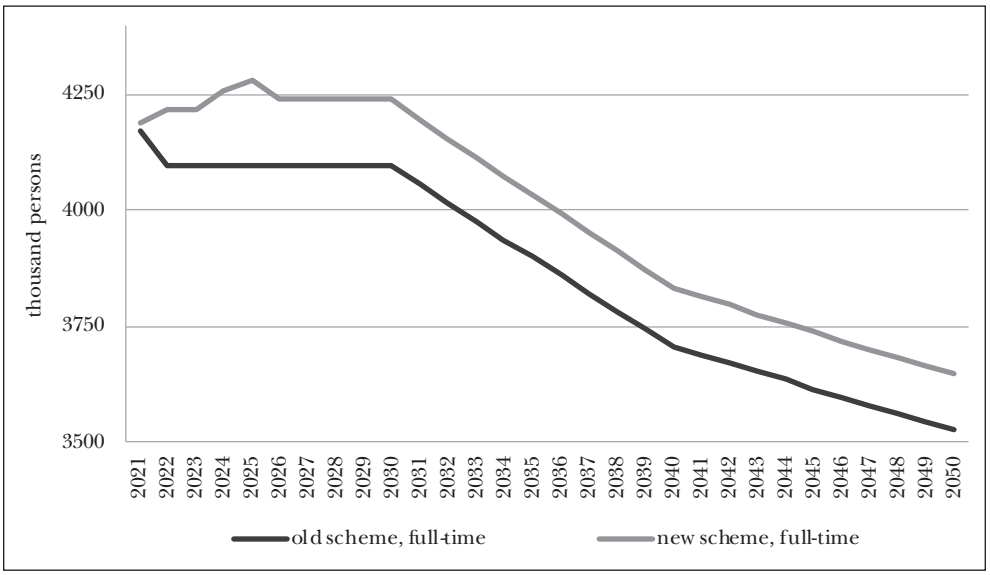
expecting an earlier than the current start of employment for young people. (At the moment young people in Hungary undertake employment at a later date than those in other European countries, and moreover for at least a year they neither work nor study.) This has a particularly favourable impact on skilled workers' employment in Hungary,[10] as it will be less profitable for them to work abroad. Increase in the employment was estimated with a view to the above factors.

Employment needs to be encouraged so much the more as by 2050 the number of employees will have dropped significantly, primarily due to depletion in the population. The reduction will be partially offset by the expected increment in employment. Essentially, this is due to the fact that with the new pension element, pension is partly fed back into the family budget and the requirement of "coverage by children", i.e. balance between the intertwined generation, is displayed in the central budget.

The following chart gives a good illustration of the fact that the number of employees is expected to decrease significantly, by approximately 500,000 in the period ahead of us, representing a 14 percentage point decrease. The adjustment only rectifies this by increasing the number of people employed by about 140,000 on average. In other words, decrease in the number of employed is moderated by this number. Growth in employment will starts slow, but due to the mass effect a spike may take place in the number of those who return to Hungary. Subsequently, the impacts of pension supplement will rather predominate. The unfavourable developments in the number of people employed and our proposal for their correction are shown in the following chart.

Chart 8: Expected developments in employment without (old) and with (new) the child-to-parent pension element



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

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Expected effects on employment[11]

Child-to-parent pension encourages expansion in employment. This will be felt in three respects.

a) In Hungary young people's employment in the period immediately following graduation is relatively low. Mothers are expected to increasingly encourage their children to undertake a job as soon as possible.

b) In the first few years the total wage cost (on the first HUF 225,000 part of their earning) will ultimately go to the child's family. For this reason, an employer's efforts at illegal employment will meet young people's resistance. If a young person has already started on a career, from he or she may be prompted to change shadow economy by legal employment.

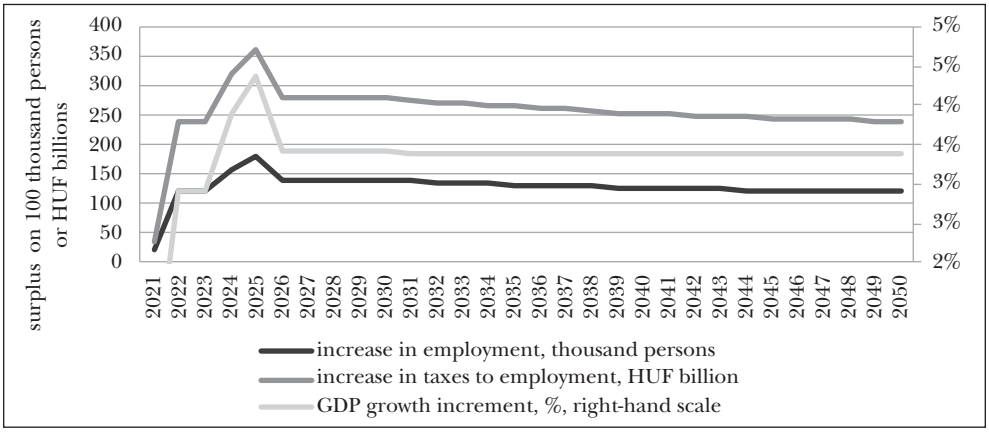
c) According to demographists, the number of people working in Western Europe is expected to grow by 10,000 each year. In contrast, in the proposed scheme mothers will encourage their children to prioritise employment in Hungary instead of western jobs.

According to our estimate, these three factors may increase the number of people employed in Hungary by about 140,000. Of this, number of returning people will be 90,000, and each 25,000 may be due to the other two factors, according to our calculations.

Increase in employment will have a favourable impact on economic growth. According to our calculations, the surplus of economic growth will increase growth by 3.4 percentage points as a result of the new pension element, but in certain years GDP growth may even reach 4 percentage points.

The Chart 9 shows the increase caused in employment, the resultant additional taxes and the growth increment expected in GDP. The chart clearly shows that the proposed model functions smoothly in social terms, and despite a global slowdown in the economy, it can offer a growth surplus.

Chart 9: Impacts of the child-to-parent pension fund on employment and growth



Source: Author's own calculation based on HCSO, 2012; 2018; 2019

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Summary

In addition to improving fairness in the pension scheme, the adoption of a child-to-parent element in the pension is of symbolic significance. It alters the wrong message given by the pension scheme by including the generational approach as an integral part in both family budgets and public finances. To put it simply: it will be financially worth having children. Parents' pension increases by 15 per cent on average due to the partial transfer of the taxes on working children's earnings. This is performed by depositing part of the payments made by working children into the child-to-parent pension fund. With the help of this fund the central budget can also track generational developments. Revenues are raised from payments by the new generation, while expenditures comprise the pension supplement payable to the retired generation who have raised the working children.

With the adoption of the child-to-parent pension element, the generational approach becomes part of both family budgets and public finances. In this scheme, the value of an offspring is not only to bring home bacon but also to mediate a moral code: that of reciprocity between generations. The expression "child-to-parent" lends a symbolic power to the particular amounts, as it suggests that children represent a coverage value. Already a small amount can become a factor that shapes the functioning of public finances. This has a double effect. On the one hand the gap between the number of intended children and actually born children may decrease considerably, and on the other, it will be more worth undertaking a job within the country. All this will have a positive impact on the headcount of employees in the country already in the near future (the number of employees is expected to increase by 140,000) and thus also on economic growth. According to our calculations, already the partial enforcement of the generational budget approach we propose will result in a 3 to 4 percentage point economic growth in the next few decades.

Notes

1 The referenced literature provides partial information of these.

2 The 2011 census data were used for this purpose.

3 A detailed analysis of these procedures is given in the above-referenced works by Szilvia Szegő.

4 South Korean analyses explain the low number of children exactly by expensive schooling. Parents wish to raise one child with an appropriately high schooling until adulthood. This is ruled out in the case of two children. This correlation has become a strict regulator in parenting.

5 See the studies by Giday and Szegő included in the references.

6 In the first few year, parents are expected to receive an allowance of HUF 20,000 for 1.9 million children. Naturally, depending on the number of years spent by the child at work (the relevant rules are not detailed here). It should also be emphasised that the word "child" does not denote the age but the family relationship in this study.

7 If the 4-year period starts in 2021, the period would comprise the years 2021–2024.

8 Except the 5th year, considered as a year of transition, when the headcount would still be 320,000 people due to subsequent return to Hungary or to 2 to 4 months of temporary job seeking. A new fund should also be established for this purpose in the state budget.

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[9] This outstanding increment is due to the fact that the additional income realised from increased employment (people returning from abroad) is only partly offset by expenditures.

[10] Suppose a Hungarian skilled worker earns HUF 495,000 (EUR 1600) in Germany, because he would only earn HUF 270,000 gross (HUF 180,000 net) in Hungary. If the scheme proposed by us is launched, nearly HUF 110,00 would be contributed to the child-to-parent fund, and subsequently to his parents, of the monthly HUF 225,000 payment made to the state on his monthly employment. If the family meeting is convened, it is easy to calculate that although an employee can earns HUF 495,000 net per month abroad between 2021 and 2021, however, if employed in Hungary, the extended family earns HUF 290,000 per month. If the net amount earned abroad is reduced by the EUR 300 spent on housing and the HUF 240,000 per annum spent on returning to Hungary 5 or 6 times a year, no more than HUF 375,000 is left from the wage earned abroad. This is merely HUF 100,00 more than the HUF 290,000 the employee's family can get in Hungary. However, most of this HUF 100,000 would be used up by higher prices and commuting would also take 10 to 12 days from the life to such an employee. Thus at the mother's urging, the skilled worker in the example finally decides in favour of the more convenient employment in Hungary, and returns to German soil only after 4 years. True, during these 4 years, he would miss the EUR 350 savings he is used to, but in exchange the family will save nearly the same amount – although not collected in the pillow-case but on the appropriated sub-account of the child-to-parent fund.

[11] Numerous studies discuss the more pronounced role of mothers and mothers' culture in income effects and in the labour market successes of children. This explain why we consider mothers' role important in the timing and method of young people's commencement of employment.

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József Banyár

The Problems Underlying the Pension Scheme and Low Birth Rates Can Only Be Resolved Together – A Complex Proposal for Linking Pensions to Parenting

Summary

This study provides a brief outline of a pension scheme based on human capital, an idea that stems from understanding that pay-as-you-go (PAYG) pension schemes should be based on the recognition of parenting, as they distribute the yield of investments into human capital. The fact that this is not the case explains the numerous problems inherent the scheme. Similarly to a Ponzi scheme, the promises and options offered by the pension scheme are increasingly divergent: promises are becoming increasingly inflated, while options are diminishing. The system outlined below would resolve these problems. Parenting and the pension scheme are intrinsically interrelated: the former can only be made economically profitable through the latter, as evidenced by the prevailing method applied throughout most of global history, which was only made redundant in modern times.

Journal of Economic Literature (JEL) codes: H55, J11, J18

Keywords: pay-as-you-go pension scheme, human capital, capitalised pension scheme, pension reform

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Introduction

In Hungary – and generally in the developed parts of the world – the increasing difficulty in sustaining state pay-as-you-go (PAYG) pension schemes (Bajkó et. al., 2015; Berki et al., 2016; Oksanen, 2003; Varga, 2014) and the failure of total fertility rates (TFR), which have been low for several decades, to reproduce the population are among the most serious economic and social problems. Although it is clear that the former correlates with the latter (because the emergence of new generations of contribution payers in adequate numbers, i.e. a significantly higher TFR than the current rate is essential for sustaining the pension scheme, otherwise a balance can only be achieved by a substantial increase in the retirement age – see Németh et al., 2019), many are unaware of a reverse correlation: the essentially flawed state pay-as-you-go pension scheme is (one of) the cause(s) for low fertility (although this aspect has been discussed by several authors, e.g. Mészáros, 2005; Gál, 2003).

The pay-as-you-go pension scheme, introduced by President Roosevelt at the turn of the 1930s and 1940s, and then underpinned in 1958 by Samuelson by an "official ideology" (Samuelson, 1958), is based on flawed theoretical foundations, as I have pointed out in several of my studies (Banyár, 2014a; 2016; 2017; 2019b; 2019c). The essence of the problem with the pay-as-you-go pension scheme is that the benefits of population growth are distributed without regard to the persons who have made the efforts to achieve the results, and hence an adequate level of contribution payment capacity is not encouraged. Due to the incorrect distribution principle (entitlement based on contribution payment history), the asset and liability sides of the system diverge just as in Ponzi schemes (Banyár, 2019a). Moreover, in the absence of awareness of the need for investment into the human capital that forms the basis of the system, the investment falls short of the needs, as manifest in the low TFR.

The need to incorporate the recognition of human capital investment in the system was realised by Pál Demény as early as 1987 (Demény, 1987), although he offered an oversimplified, incomplete solution to the problem. Several authors have shared his approach (see publications of Kovács (ed.), 2012; Giday and Szegő, 2018), and some have attempted to provide a more comprehensive solution (Botos and Botos, 2011; 2012; Botos, 2018; Banyár et al., 2016), but in these attempts a good diagnosis was followed by a theoretically incoherent proposal for a remedy. Below is an outline of a concept for a pension reform that leads the pay-as-you-go pension scheme back to its theoretical foundation, i.e. investment into the human capital. The result is an automatically balanced pension scheme that is sustainable in the long term, fully recognises the efforts of parenting and encourages parenting.[1] The solution is a genuinely unorthodox concept that – based on experience – may initially shock the reader. It comes as no surprise that so far only Czech authors (Hyzl et al., 2005) have put forward a similar proposal, as the logic of the current pension scheme is so deeply ingrained in people's minds that it is difficult to break through these constraints even for those who understand the problem.

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In this study, it is argued that parenting should not only be the foundation of the pension scheme, but the reverse correlation also applies: the "economics" of parenting is linked to the pension scheme in multiple ways.

It is also important to note – as a cause for optimism – that in its outstanding the competitiveness programme, the National Bank of Hungary (MNB, 2019) correctly recognised that both the pension scheme reform and a demographic change are of key significance in Hungary's competitiveness, and these two factors are closely related, and so the programme proposes recognition of parenting in the pension scheme. As, however, the above-referenced proposal remains sketchy, the following proposal may be referred to the decision-makers.

A brief proposal for a possible human capital (HC) based pension scheme

I propose a gradual replacement of the current PAYG system with the HC system within the time frame of 15–20 years. This could be implemented by transferring everyone below a given age – e.g. people aged 40–45 – to the HC system, while those aged over 60 would remain in the current PAYG system. People of a transition age would be transferred to a mixed system, depending on the scheme they are closer to, based on their age, i.e. their pension would be determined on the basis of partly the former and partly the new principles.

Principles of the new HC system:

– Pension is based exclusively on the investment of human capital in children (based on the hidden, but unrecognised logic of the PAYG system).

– Accordingly, entitlement is not based on contribution payment, however, payment is mandatory. The reason is that contribution does not constitute the payment side, but the return side of the investment; this is how people repay the costs of their own upbringing. Contribution payment is therefore mandatory for everyone (also for people raising children), but it is limited in time (e.g. for 30 years, preferably for the "best" 30 years, i.e. not from the date of entry to the labour market).

– Parenting efforts are mainly, but not exclusively, made by parents. Based on calculations, in Hungary they currently contribute more than 70%, while the remaining 30% is financed by taxpayers through school education, child care allowance, child care benefits etc.[2]

a) For this reason people with no children would also be entitled to a certain amount of pension in proportion to their tax payments. The amount payable per taxpayer is calculated on the basis of the portion of parenting financed from taxes (30%) and the ratio of taxpayers to children.

b) After the retirement age, childless taxpayers should not be paid significantly less pension than those with children, but would receive the same pension from a significantly higher retirement age.

– Childless people would, however, also receive a pension between the standard retirement age (set for people with children) and the increased one (set for childless

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people) based on their savings. The scheme also includes a pension savings account to which everybody makes payments from the time of entry to the labour market. On this account money saved due to the absence of parenting is held. When the person reaches the retirement age, he/she does not yet receive a pension from the HC system, but he/she may start withdrawing amounts from the savings account distributed in time until the increased retirement age (or he may save these amounts), i.e. a childless person may also retire when a person with children retires.

– If someone has a child (whether delivered or adopted), such savings are reduced by half, and after the second child they are reduced to zero. In other words, funds are immediately available for people with children for parenting. This also means that having children for them will also be financially neutral when the child is born; the "investment" will not only be recovered at the time of retirement. Young people will therefore be no longer encouraged to not have (or never have) children (currently this option is financially more advantageous for them).

A scheme based on the above principles has the following advantages:

– The state pension scheme will be sustainable (as opposed to the current state scheme), it will provide incentives (i.e. encouragement of human capital investment into children = having children) that support sustainability. (If, nevertheless, no one wants to have children, no problem is encountered because no pension entitlement arises.) In other words, this system implements integration between the asset and liability side of the state pension system, which is currently lacking, as the present system (globally) is incorrect and theoretically flawed in promising pensions detached from possibilities.

– In contrast to the present system, where not having children is clearly financially advantageous (and profoundly unfair to those having children), this system will be neutral in terms of having or not having children, and fairness is applied universally). A childless person cannot exhaust the amounts saved (at the moment a short-sighted approach is applied) because he/she needs to save. For this reason, people having children immediately earn income for parenting from the amount they are no longer required to save on account of not having children.

– Having children will therefore be based on the reasonable economic premise that its cost will ultimately be borne by the child, i.e. the person who has received from society and from his/her parents the transfers which create the human capital he/she possesses and uses, and this amount can generate significantly higher value, primarily to the benefit of the child. In other words, parenting (in a positive case: population growth) will become self-financing.

It is important to emphasise that only this solution provides both an incentive for parenting at an adequate level and the sustainability of the pension scheme, that is, contrary to public opinion, these two matters closely correlate and demand a combined solution.

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Brief justification for the proposal

Why is it necessary to link having children with the pension scheme?

It has been clear for some time that, although the two questions seem to be detached because they are related to different stages of human life, they are actually closely related. Overall, there are two major groups of pension schemes:

1) State schemes, also called pay-as-you-go schemes, not capitalised by "physical" capital (this is the prevailing pension scheme in Hungary).

2) Various capitalised schemes (pension funds, retirement funds, occupational pension schemes, capitalised state schemes, as historical Bismarck's scheme).

According to the official ideology of the state scheme, as defined by Samuelson in 1958 (which has been consistently cited approvingly), the yields generated by population growth are distributed among the elderly in the form of a "biological interest", i.e. performance and options directly depend on the number of births. If there are no births, no pensions are paid. This dependence is reversed in capitalised schemes: capital accumulated for pensions generates a yield only if it is operated by someone, i.e. a new generation of an adequate number (and quality) of people replaces the old one, otherwise capital is depreciated and will not become pension (although this correlation is often disputed).

A major flaw of the state pension scheme is its original assumption of a constant level of births and a constant supply of "biological interest" to distribute. A negligible, minimum cost of parenting is assumed, with practically no obstacles to having children. Today it is clear that neither assumption is true (although these assumptions had been relevant at a given time): the costs of parenting are on the rise, with the availability of effective and cheap, widely applied contraceptives to everybody.

It follows that it is wrong to assume a constant source of distribution and to ignore amounts each member of society contributes to parenting. The above realisation prompts various proposals and solutions for linking parenting and pensions. These proposals can be divided into three main groups:

1) A portion of pension contributions paid by children should be directly distributed back to their parents (Demény, 1987; Giday and Szegő, 2018; proposal contained in point 330 of the MNB, 2019).

2) Parenting should ALSO be considered a contribution payment, entailing pension entitlement (Botos and Botos, 2011; 2012; Werding, 2014; Banyár et al., 2016).

3) Complex relationship between parenting and pensions (Hyzl et al., 2005; Banyár, 2014a; 2016; 2017; 2019b; 2019c).

This study discusses the latter proposal, demonstrating why the other proposals are deficient and, to a certain extent, theoretically flawed.

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Who should pay the cost of parenting?

The first question to be reasonably asked is: Who should pay the cost of parenting? Such cost used to be low, and today the situation is no different in extremely poor groups of society and in populations in countries on a similar level of development. Children brought up at such low cost, however, do not receive impulses during their childhood that would render them competent for integration in modern work organisations and for performing useful work. (This is one of the main reasons why migrants from poor countries do not offer a solution to the demographic problems of the West. For correlations between migration and the pension scheme, see Banyár, 2014b.) For such children to become competent, they need to be schooled for a long time and to be exposed to a multitude of diverse – and, of course, costly – impulses. These efforts consume vast amounts of money (and time devoted by parents and teachers, which ultimately also translate into money). Who should pay this vast amount of money? Let us consider the logical options.

Should parents pay?

This has been the case for a long time, logically and unproblematically, as children worked on family farms from an early age, i.e. the parenting investment recovered early. Moreover, when the child took over the family farm from his parents, he repaid the cost of parenting by taking care of the elderly parents. This is the case in many developing countries, which is (also) why there are many children there.

Today the situation is different in developed countries: children do not represent any economic benefits for parents, child labour has been banned for a long time (and family farms no longer exist), but the time and cost of education have significantly increased. The main economic benefit of children – their tax and contribution payment capacity – has become a public good (presumably due to the flawed state pension scheme), i.e. people are not repaid such benefits in proportion to their investment. So why bother becoming a parent? The principle, which has proven to work well for millennia and is still advocated by many today, has clearly become outdated.

Should the state pay?

Financing by the state would seem a logical response to the above problem, i.e. taxpayers should raise the money for the cost of bringing up children. This solution has been partly implemented in many countries, as the state finances education almost everywhere, providing parenting benefits or tax benefits in many countries. Under the current policy of the Hungarian state, the share in financing parenting from public funds in being increased (currently it is approximately 30%). A 100% ratio of state financing, however, is infeasible, taking into account the diversity of individual parenting costs, not to mention the fact that this would require considerable

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additional funds compared to the current volume of the pension scheme. As an additional problem, it is not clear as to why the costs of parenting should be distributed among taxpayers, that is, why the cost of national demographic reproduction should be ultimately in proportion to the burden sharing capacity of individual taxpayers, as they do not receive the benefits of parenting to such an extent. Beyond doubt, the most important and ultimate beneficiary of parenting, however, is the child, as – in economic terms – the purpose of parenting is the creation of human capital for the owner (i.e. the grown child) to generate vast amounts of income primarily for himself/herself. It is therefore logical that the cost of parenting should be paid by the grown child.

Paying by the grown child

This is the sole logical response to the problem. Obviously, the child is unable to immediately make repayments. This is only possible when he/she can operate his/her human capital at least on a basic level, i.e. after the completion of education. Therefore the money and time spent on the child is deemed to be a long-term investment made primarily by the parents (or caregivers, whether or not they are the biological parents) and partly by other taxpayers through funding school education, health care etc., including tax transfers and tax benefits provided to parents.

If the child pays for the cost of his/her upbringing (subsequently, when he/she can work and earn income), paying it specifically to those who have made the investment, the problem of parenting not being reasonable on an individual level is resolved by becoming economically reasonable again. Moreover, return on the investment is significantly greater than what the state can provide by increasing benefits in relation to children, i.e. the incentive for parenting would be greater than ever thought possible.

Since the child is able to pay for his/her upbringing only at a later stage in life, when his/her parents have already been retired, practically the only option is repayment in the form of a pension, i.e. the means of the child's repayment of the costs of his/her upbringing would be the payment of a pension contribution, while the pension would constitute the return on the investment of human capital (return of capital and its yields) to the parents (and taxpayers).

Pensions and demography – inseparably correlated

The above method would provide a common solution to the problem of both demography (low birth rates) and pensions (increasing supported-supporter ratio). In essence, relative to the current situation, a vast amount of new funds would be invested in parenting, where a portion of the income of people with no children would be rechannelled to their pensions (through a savings plan) and the pension funds thereby released would be provided to those with children. Since, however, people with children would not be required to participate in the savings plan (because they would also receive a pension through their children), this money would be imme-

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diately available to them when they have children, i.e. childless people would no longer be clearly better off than those with children. (The objective announced by the Prime Minister of Hungary in the middle of 2019, namely that people with children should be better off than people without children, could be achieved by the means described above.)

It is also important to emphasise that in the described solution, parenting and the pension scheme are not linked by some kind of a magic trick, as the two closely correlate, and essentially the two problems can only be resolved together.

Let us examine the reasons for this. Let us assume that it is possible to find independent solutions for the pension scheme and for parenting, as almost everybody believes to be the case today. This would imply the following.

A solution to the pension problem independently from parenting worsens the demographic situation

If the state pension scheme does not reward parenting, the current demographic problem will persist, with increasing decline in the number of children and a deteriorating ratio of supported to supporters. It is therefore necessary to incrementally increase the retirement age, not only by "natural means", i.e. through increasing life expectancy, but also by maintaining the expected value of the time spent in retirement at a constant level. In other words, life expectancy spent in retirement will constantly decline. The spontaneous reaction of stakeholders to this is the spontaneous partial capitalisation of the pension scheme, which they are already encouraged to do by life insurance companies and pension funds. This means that they save an increasing part of their income instead of spending it on consumption. As the most expedient solution, they will supplement such funds with those allocated to their largest unproductive expenditure: parenting, i.e. due to savings, they will increasingly reduce their parenting efforts, as the cost of parenting will continue to increase without any economic benefits (Banyár, 2019a).

The situation is no better if recapitalisation is not implemented spontaneously, but on a mandatory basis, through a recapitalised state scheme, as shown by the attempts made in Hungary between 1998 and 2011. In other words, the (partial) recapitalisation of the pension scheme further deteriorates demography.

The state pension scheme clearly depends on parenting

Let us assume that the state increases support to parenting, and eventually the state covers all the parenting expenditures (in my opinion this is impossible in practice). In this case children can de facto be considered a public good, as their upbringing will actually become the outcome of public effort. The question arises as to whether the current state pension scheme can operate as it is, on the (currently false) premise that the child is a public good?

Clearly it could not operate in its current form because the accumulated pension contribution would only match the number of births and the level of children's

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upbringing. These issues will continue to be unrelated to each other or to the pension contributions of the working-age population paid during working age. In other words, the pension determination principle of the state pension scheme – assuming the dependence of pensions on the level pension contributions – remains incorrect. As a minimum, a rule would need to be adopted about the distribution of the actually paid-up pension contributions (depending on demography) at a certain ratio (e.g. in proportion to contributions). Thus the current pension scheme should be reformed to allow for the aggregate effect of parenting.

The manner of linking the two is crucial. Parenting is NOT contribution payment

If, however, the two areas are devised in a contingent structure, i.e. pensions depend on parenting efforts, it may seem that only individual researching creativity poses an obstacle to linking of the two. The options mentioned at the beginning of this study may arise, like transferring part of the pension contribution to parents or rewarding parenting efforts by recognised them also as contribution payments.

The problem with these concepts is that they consider the state pension scheme as appropriate in the sense that contribution payment creates the entitlement to a pension. This, however, is a conceptual flaw in the current state pension scheme, as contribution payments presently have nothing to do with the amount of pensions payable to future pensioners. The correct approach should be for contribution payment to be the repayment of parenting costs everybody owes to their parents and other taxpayers of society, for which nothing is due in exchange. In other words, contribution payment is not a payment but a repayment in this system, and due to false analogies (it has been compared to funded pension schemes operated by insurers), this fact has not been realised so far. For this reason the severe asset-liability matching problem encountered in the state pension scheme would not be resolved, were this principle maintained unchanged, as put forward by the cited proposals.

Summary and differences compared to other proposals

In summary, the above-described pension scheme simultaneously manages the problems of state pension schemes in developed countries and the demographic problems of these countries, and also implies that the two problems are in fact closely correlated.

In terms of the pension scheme:

– It matches the promises held out ("liabilities") and the assets available in the scheme, and thereby.

– Eliminates implicit government debt underlying the pension scheme (which essentially measures the unsecured promises inherent in the scheme and amounting to approximately 240% of the GDP in Hungary).

– The system will be balanced at all times independently of demographic changes, regardless of whether there are more or less children.

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– As an important advantage, it does not cost anything; in fact, savings can be achieved in contrast to the current situation, as the redefinition of entitlements is based on an undisputable philosophy.

In terms of demography:

– It eliminates the largest financial counter-incentive to having children, i.e. the bad pension scheme under the current scheme.

– It thereby provides a very strong incentive for parenting over the current situation, because in economic terms it becomes an entirely recoverable investment, as opposed to the current situation, when parenting is clearly luxury consumption (from an individual point of view).

– It does so by not costing anything at all; based on a smart policy, parenting will become economically self-financing; the ultimate financer will be the grown up child himself/herself. This is actually the way to achieve the objective announced by the Prime Minister of Hungary, namely that people bringing up children should gain a more advantageous position than those with no children.

There are other simultaneous proposals based on Pál Demény's idea explained in 1987. In summary, these proposals could be termed as "direct transfer solutions", as they essentially aim to enhance the economic appeal of parenting by providing some of the child's contributions (taxes) to the parent after his/her retirement. In principle these proposals are correct, as they are based – similarly to my proposal – on the correct principle that parenting is considered an investment in human capital, the yields of which (or at least a portion thereof) should be returned to those who produce it, i.e. (mainly) to the parents. These proposals, however, have major disadvantages:

– In contrast to the above-described HC scheme, they only promise a partial repayment of parenting efforts.

– Inevitably, direct transfer solutions can only have a support function alongside the existing PAYG pension scheme; they are unable to replace it. This being the case, however,

a) They legitimise a pension scheme built on a flawed principle,

b) They are vulnerable because they are not based on a correct theory. They give the impression that a "good" pension scheme (i.e. the PAYG scheme) is "hacked" by incompatible, random factors (parenting), and therefore major political efforts may be expected to lobby for the withdrawal of this solution if adopted. For this reason its long-term incentivising power will be lost.

– As, in contrast to the HC proposal, they maintain a deficient system, substantial additional budgetary resources are required.

– Again, in contrast to the HC proposal, which aims to immediately change the economic incentive for people in the child-bearing age, direct transfer proposals aim at securing welfare for the current pensioners, i.e. they highly indirectly enhance the motivation to have children (and this is immediately undermined by the legitimate concern about the long-term sustainability of such a scheme).

The above disadvantages also characterise the reform proposals aimed at linking parenting and the pension scheme, which are, however, inconsistent (Botos and Botos, 2011; 2012; Werding, 2014; Banyár et al., 2016).

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Notes

[1] In this regard there are sceptics who claim that although the state's encouragement of having children is not without effect, its impact is moderate. See Sági et al., 2017 and Sági et al., 2018.

[2] Verbal information provided by Iván Róbert Gál as an informal summary of his thorough research in the field.

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Civic Review, Vol. 15, Special Issue, 2019, 301–316, DOI: 10.24307/psz.2020.0217

Tibor Pintér

Economic Determinants of the Natural Fertility Rate with Special Focus on the EU and on Hungary

Summary

The natural fertility rate directly expresses the reproductive capabilities of a country. Typically, the value of this indicator is considerably lower in the economically developed part of the world than in less developed countries. However, in terms of fertility rates, developed countries are not completely homogenous either, at least in an analysis of changes in time series. Through the example of various EU Member States, this study aims to pick the economic and policy factors that may trigger improvement in the fertility rate. Apart from a few countries, it is a common problem in the surveyed states that population growth is insufficient for ensuring reproduction. Paradoxically, population decline and ageing is a problem in those countries and regions of the world where the material, economic and welfare conditions are the most favourable. It is also important to demonstrate globally detectable correlations between fertility rates and the standard of living. The aim of this study is to highlight the specific social and economic indicators with the most beneficial and most adverse impacts on developments in fertility rates. An important finding of the study is that having children is essentially not an economic, much rather a cultural matter that is closely related to the concept of responsibility, and in addition, economic stability or a balanced income distribution may increase the fertility rate. Overall, decrease in the intensity of childbearing can be considered as a legitimate concomitant of societies with advanced economies. In the study references are made to other variables that

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may shift the unfavourable demographic trends in a more favourable direction in the developed world.

Journal of Economic Literature (JEL) codes: J10, J13, F63, I15
Keywords: fertility rate, economic development, social assistance, ageing, income growth

Introduction

This study aims to identify the economic determinants of fertility rate. It is common knowledge that the insufficient number of children usually poses a serious problem exactly in countries with ample economic resources. Childbearing and family support are also emphatic in today's Hungarian public debates. On the one hand, this can be seen as a very welcome development and a sign that the political leadership has realised the increasing challenge this issue poses in the developed world. However, more emphasis should be placed on the cultural, personal and emotional aspects of this problem, and the latter are just as important in a decision to start a family as financial considerations are. Surveys, databases and everyday experience suggest that a clearly positive emotional and ideological motivation underlies every decision to start a family.

Allow me to only point out two correlations to prove that finances will not solve the fertility crisis on a global scale. Based on the relevant 2016 data published by the World Bank, nearly 85 per cent of the world's population live below the average Hungarian's standard of living. In spite of this, in Hungary the fertility rate is considerably below the world average and the natural reproductive value.

Similar data is related to time trends. In 1960, the fertility rate of an average earthling was nearly 5, with approximately 450 USD per capita GDP. In 2016 (56 years later), a fertility rate of 2.44 is coupled with USD 10,200 per capita GDP. This is not to say that a fertility rate of 5 is desirable, but the trend is more than though-provoking.

However, this study does not have such a distressing message. The group of economically highly developed countries, namely the 28 Member States of the European Union, give a more intricate picture.

Theoretical overview and research questions

In its early stages, economics addressed the matters and areas affected by economic developments more naturally. The implementation of an economic system capable of creating the material needs of a decent family life can be considered such an area. Although the current economic system has created extraordinary riches, it does not at all support family life. In this respect this economic system has failed. Naturally, this failure is not a bolt from the blue.

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Following the early economic theories covering a broad horizon, the classical school of economics (hallmarked by Adam Smith) systematically organised the conceptual and methodological toolbox of this academic field (Mueller, 2010). However, this development isolated the representatives of this discipline and encouraged them to specialise. Since then, only theoretical economists working in various specific fields have been dealing with, say, the demographic aspects and demographic sustainability of the economic system. Within this scope, mention must be made of the work of Thomas Robert Malthus, who suggested in his book, originally published in 1798, that the population growth rate and the potential of economic performance should be compared. His conclusion that global population growth would be permanently higher than economic growth was, of course, incorrect. Regardless of this fact, it should be pointed out that massive population growth is not characteristic in areas where one would expect it on the basis of economic performance and the standard of living. The longer the time series, the stronger discrepancies can be found in this research area.

The correlation between a variable considered important in any academic discipline and the population and demographic developments gives rise to the question whether the fertility rate is a suitable indicator as a dependent variable. A review of the relevant literature has shown that in most cases this indicator can indeed be used as a dependent variable in various models (Becker, 1960; Berde and Németh, 2016).

Another important question is whether there is any relation between the level of economic development and the fertility rate. Although GDP and SNA indicators are frequently criticised in economic analyses, in most cases, demographic trends are compared to GDP or an indicator derived from it (Berde and Kuncz, 2017). In an economic historical perspective, there is a definitely adverse correlation between income levels and fertility; and specific fertility-related theories have emerged to explain this phenomenon, but they have been unable to give a satisfactory answer (Jones and Schoonbroodt, 2010).

Another important trend in the economic analysis of fertility, inspired by economic history, includes the efforts made at identifying the level of economic development where the dynamics of fertility breaks and the way demographic development is related to the series of economic transitions. The need to map correlation between economic transition and the fertility rate arises in highly developed regions (Prskawetz and Lindh, 2007), in isolated areas with medium income levels (Mason et al., 2010), and in bigger countries with low development levels (Hussain et al., 2009). The recent serious global economic crisis has also had a controversial impact on the world's most developed regions (Sobotka et al., 2011).

The assessment of a correlation between the demographic developments, economic performance and the standard of living (Berde and Kovács, 2016) is genuinely important in the case of countries that are considered well-developed in a global comparison and have extensive welfare systems and functioning social security systems (Sági et al., 2018), because (as shown in the charts below) the willingness to have children is typically much lower in these regions of the world. In addition, the correlation between the two phenomena is not explicitly highly adverse in this income

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range, but there is a weak positive correlation. In any case, it can be concluded that a sort of alternative value system is built up in the more developed societies in relation to childbirth (Schultz, 1974).

The directions of intervention and the opportunities of fiscal policy and active state involvement also emerge as major research questions in this context (Yang, 2016). Even though there are differences between the various pension systems, it is important to note that the lower number of children and the accompanying phenomenon of ageing are alarming trends that will need to be addressed in the future (Széll, 2010). Both the academic and the political stakeholders need to deal with the available implementation opportunities.

A direct financial correlation can be established between having children, starting a family and the social security system (Giday and Szegő, 2018). Economic growth has a clearly favourable impact on the life expectancy of a country's population but this does not mean that improvement in health is necessary for starting a family (Barro, 2013). Thus, at a later stage, it may be worthwhile to explore the interrelationship between health and economic performance, as well as the correlation between certain civilization diseases and economic performance. It is worth noting that during my other surveys I found a very strong positive correlation between the ratio of population with cancer and economic development, however, the exploration of this correlation falls outside the scope of the present study.

As a special question (for example, in the context of sociological and regional studies), the exploration of the territorial context of fertility may also be important (Varga, 2005). In a country or other territorial unit, it is exactly the younger population willing to start a family who often move to more prosperous areas (Sági and Lentner, 2018). Many of them do not ultimately have the previously planned number of children, precisely because of the newly adopted attitudes. There is a rationale behind research in countries with similar development historical heritage and similar roles in the international division of labour. For this very reason, Farkas (2017) compares the functioning of the family support systems in Poland, the Czech Republic and Slovakia and draws conclusions with respect to the Hungarian system.

It is also worth highlighting the controversial relationship between the labour market participation and qualification of women and fertility rates (Yang, 2000). Accordingly, there is a clearly adverse correlation between women's active participation in the labour market and fertility, however, this correlation is not so clear in the developed parts of the world. In the range below the natural reproductive level, there is a positive correlation between active female participation in the labour market and the willingness to have children. The special theoretical economic categories and variables such as unemployment and its social consequences, including the psychological basis of the attitude towards having children, can also show a correlation with each other (Kucséber, 2011). Thus, a person living in a more developed country may feel that losing a job is a sufficient reason to postpone having children. However, based on the databases, this is more of a sociological and psychological consideration, since globally a higher standard of living clearly reverses the fertility rate.

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In this study efforts are made at demonstrating correlations solely between data and nothing else. Naturally, this presupposes the knowledge of the most important types of empirical methods. The relevant Hungarian literature has also undergone significant development in recent years. The basic tables were compiled and the analyses were conducted primarily on the basis of the work of Molnár (2015). However, a book published by Dusek and Kotosz in 2016 has provided an excellent complementation, especially by a more sophisticated, elaborate interpretation and data collection.

It is worth reviewing the magnitude of differences in economic development and in fertility rates between the large regions of the world. Instead of merely drawing a static cross-section of the present, it is worth including the temporal changes in fertility and economic development over time. Following this, however, focus falls on the EU Member States, where the reliability of statistical systems may be higher and which are in a similar social and economic situation to Hungary. The most important economic determinants of fertility are identified through direct economic, sociological and regional economic variables. Mostly, the regression model analysis and correlation matrixes are used to highlight the main directions and relationships.

Correlation between the financial standard of living and fertility rates in a global perspective

It is important to demonstrate the correlation between the economic standard of living and fertility rate. Despite its known weaknesses, per capita GDP is used to measure the economic standard of living. The first chart gives a summary of GDP per capita and fertility rates in all the countries of the world in a scatter diagram. The number of sample elements is less than the number of countries, because only countries where both data are available for 2016 have been added to the model.

The following chart shows a negative correlation between GDP per capita and the fertility rate. This correlation is not linear, but rather gives an exponential shape.

The Chart 1 gives a static, cross-sectional correlation between the two data in the same calendar year 2016. The correlation coefficient in the chart shows the accuracy of matching the cloud of points containing real data to the hypothetical logarithmic model. According to the additional model calculations performed by the SPSS program, the results of both the logarithmic regression model and the correlation model are significant. The value of the Pearson correlation indicator is –0.488, which gives a negative, but not particularly high correlation between GDP per capita and the fertility rate. It is important to note that in terms of GDP per capita (shown on the horizontal axis to show the extent to which the standard of living defines fertility and the dependence of the latter on the former), the points are characterized by different locations. It is clearly visible that in the case of poorer countries, a higher fertility rate of 3 or more is fairly common, while in richer countries a value higher than 2 or 2.5 is rarely found for the same, and values below 2 are more typical.

In 2016, Niger's fertility rate was the highest at 7.24 (rounded to two decimal places), followed by two other African countries: Somalia and the Democratic Republic of

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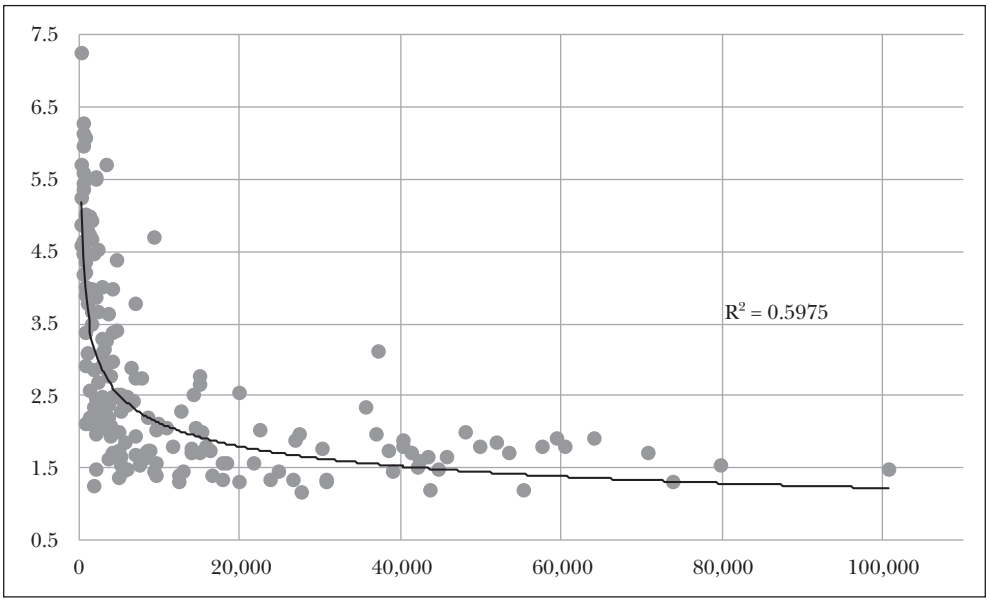
Chart 1: Correlation between fertility rates and GDP per capita in the world's countries, 2016



Source: Based on data from the World Bank

Congo, both with values well over 6. South Korea had the lowest measured value in the world in 2016: 1.117, followed by Singapore and Hong Kong, both with very low indicators around 1.2. Within the group having GDP over 20 000 USD per person, only Guam and Israel have a fertility rate above 2, the latter with a value above 3. This supplement illustrates a higher negative correlation than the indicators, and moreover, the overall population is more concentrated in countries falling in lower income categories, i.e. countries with large populations fall into this income group.

In addition to the analysis of the situation in a given time, a time series analysis is also important. This second model analyses the correlation between the fertility rate and GDP per capita of an average citizen of the world. Chart 2 shows the evolution of these two indicators per annum in the period between 1960 and 2016. The negative correlation between the movements of the two variables is clearly higher.

This chart shows a negative exponential correlation, with the real data almost matching the hypothetical function (R^2=0.9727, a very strong link in a quasi social and economic analysis). The correlation is also high: the rate (Pearson's coefficient) is –0.897. According to SPSS, the correlation is also significant if the value is 1 per cent. Thus it can be stated without any hesitation that the rapid rise in the standard of living seen in the past few decades has adversely affected development in fertility rates. Although the trend of overpopulation continues, the global fertility rate is getting closer to the value of 2. However, the chart suggests that decrease in fertility is slowing, and decline is far from the massive drop seen in the middle of the period. Another important conclusion is that although the term "population explosion" is not directly

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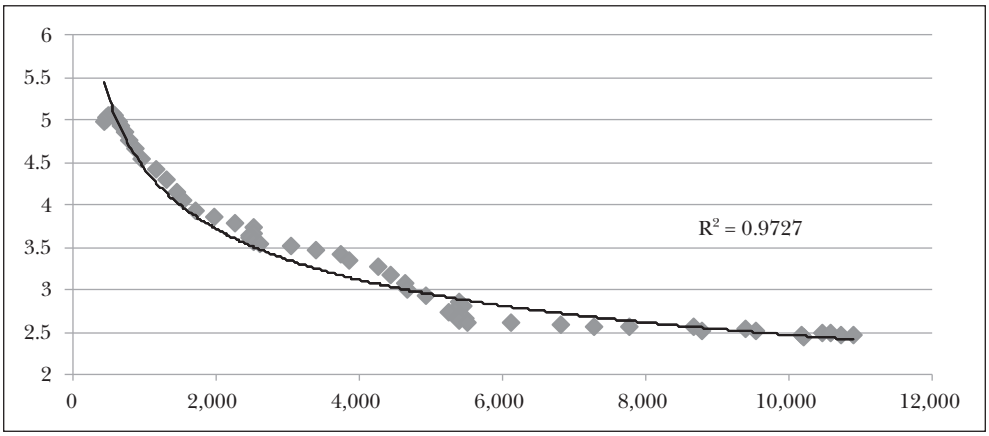
Chart 2: Correlation between fertility rates and GDP per capita, based on average values per person, 1960–2016



Source: Based on data from the World Bank

used to refer to the past few decades, at least in the Western world, it should rather be replaced by "economic explosion" to describe this period, since the average standard of living has increased twenty-fold in 56 years, adjusted for population growth.

Correlation between the fertility rate and its economic determinants in the 28 Member States of the European Union

In terms of global development, it can be concluded that overall, there is a negative correlation between the standard of living and the fertility rate. A stronger negative effect is reflected in the time series, i.e. decline in the fertility rate is clearly associated with improvement in the economic development. However, in addition to a dynamic approach, the static model, which includes the analysis of a single year, showed a lower correlation in a similar direction. In both cases, the correlations were considered significant. In light of this, the result of the model where the scope of observation units was limited to the current 28 Member States of the European Union can be considered rather surprising.

This chapter describes the result of an analysis of the correlation between 19 economic variables and the fertility rate. An effort was made at selecting the variables that have a high level of measurement and include welfare, stability, sociological and territorial (regional economic) criteria. The following variables were included: GDP per capita, ratio of urban population, employment rate, GINI coefficient, ratio of R&D expenditures to GDP in exports, number of hours worked per week, ratio of population living in metropolitan areas, unemployment rate, ratio of internet users within the population, CPI (corruption perception index), Bertelsmann Sustainable Governance Indicators, Happy Planet Index, ratio of domestic loan to GDP, final consumption expenditure to GDP, household consumption to GDP, military expenditure to GDP, ratio of non-performing bank loans, ratio of net public social transfers to GDP.

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Of all the variables, the following table only includes the significant correlation coefficients. Nevertheless, in the explanation, the direction of non-significant variables is also included.

Table 1: Correlation coefficients in the fertility rate and the significant economic variables (mostly 2016)

Included economic variable	**Correlation with the fertility rate**
GDP per capita	0.395*
Employment rate	0.544**
R&D exp 2014	0.455*
Hours worked	–0.442*
Unemployment	–0.394*
Internet users	0.479**
CPI	0.548**
Bertelsmann Sust	0.398*
Bank nonperforming loan	–0.438*

Source: Author's calculation based on data from the World Bank and Eurostat

Based on the above table and on other information, certain conclusions can be drawn about the fertility rate and its economic determinants. The table shows the Pearson correlation coefficients, which indicate the closeness and direction of the correlation per pair. One asterisk indicates that the value of the two-tailed significance is valid within the 5-percent interval, while two asterisks denote validity within 1 per cent, in other words, validity is even higher in the latter range. As none of the values is exceptionally high, it cannot be condfirmed that they are strong economic determinants of the fertility rate.

In an absolute value, the CPI (the corruption perception index) and the employment rate have the highest numerical values. Both show positive correlations. In light of the method of creating these indicators, the conclusion arises that the less corrupt a society is (the value of the indicator increases if corruption is not perceived or less perceived), the more positive shift can be expected in fertility. In addition to the absence of corruption (which may naturally be measured with an excessively normative content), the employment rate of a country has also proved to be decisive (maitaining that neither of the coefficients is particularly high). This can be construed in a way that active participation in the labour market functions as a kind of an existential basis to underpin the willingness to have children. A higher ratio of internet users and a more pronounced presence of R&D-intensive products within exports show a lower but positive correlation. This suggests that the level of scientific/academic development and qualification can indirectly improve fertility rates in the case of a country with a high

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standard of living. Globally, the exact opposite can be seen for these variables; however, limiting our analysis to developed countries reverses the direction of the correlation.

GDP per capita and the Sustainable Governance Indicator of the Bertelsmann Institute show positive correlations of similar strength. Especially the former one is a surprise, given that globally, both in a given year and in the time series, GDP per capita has a clearly negative correlation with fertility. In the 28 Member States of the EU, however, there is a slightly positive correlation between fertility and the standard of living. Consequently, in the case of an EU Member State, fincncial incentives to support having children cannot be considered needless, at least if the fertility rate falls between 1 and 2. This result contradicts the preliminary research expectation that the EU would also have the usual adverse trend.

Only three of all the significant variables show a negative correlation with the fertility rate. These are the number of hours worked, the ratio of non-performing bank loans to the total loans, and the unemployment rate. The more time people spend at work; the lower fertility rate is reported. This seems to be self-evident, however, as the correlation with employment is positive, it is important to draw the attention to the fact that the barrier to childbearing is not employment in itself, but poorly organised, unmanageable work and long working hours. Consequently, flexible working hours and efficient work should be set as immanent objectives in legislation and management. This could further resolve the conflict between work and family.

Despite the fact that, representing a non-characteristic correlation, the indicator of non-performing loans remains below 0.5 in an absolute value, it is still necessary to explain this variable. It suggests that the willingness to have children is reduced by insufficiently covered private-sector loans. This correlation shows similarities to what has already been explained above, namely that existential security is at risk not olny if a person does not have secure employment but also when revenues are insufficient to finance debt payment. Therefore, it is worth considering that support to fertility should be conceptually linked with improving the financial literacy and providing a stable financial system in a country. This is only confirmed by previous analyses not covered in this study, like those related to risk factors (e.g. the EOS risk factor of the World Economic Forum) in certain countries, which have shown that relieving a country from risk factors has a beneficial impact on the fertility path.

Non-significant correlations exhibited the following trends: The ratio of urban population and the ratio of population in metropolitan areas have a very slight positive correlation with fertility. The GINI coefficient shows a low negative correlation with fertility, i.e. unequal income distribution is more likely to discourage having children. The Happy Planet Index has a neutral value (0.052), while the ratio of loans, household and end-user consumption, and military expenditures, and the ratio of net public social transfers to GDP all adversely affect fertility. Thus, the expansion of the social welfare system alone is not a particularly important factor, while consumption has more of an adverse effect. A comparison of the ratio of family support expenditure to GDP (only OECD data are available for OECD countries, so the basic model changes) reveals a very low positive correlation coefficient at 0.06.

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Developments in the fertility rate in Hungary and its economic background

In Hungary the incumbent government places great emphasis on demography. The most recent cornerstone in the relevant policy actions is the 7-point family protection action plan announced in February 2019. The presented fertility rates also justify that the Member States of the European Union, including Hungary, are generally characterised by extremely low fertility rates, and this alone jeopardises the sustainability of the social and economic system. Various concepts, either using external resources or merely by improving the productivity of the internal population, have been set up for solving this crisis and in public discourse the key role of economic policy acions in the provision of a solution is called into question. Although these are not insignificant questions, as they are not strictly economic, they fall outside the scope of this study.

In an analysis of developments in the Hungarian fertility rate, it needs to be noted as a preliminary point that Hungary has also been unable to detach itself from the European trend of declining fertility rates with improvement in the standard of living. This statement is not as simple as it may seem at first sight, because it is only true if the standard of living is expressed in the internationally accepted SNA indicators. In this study GDP per capita is used at purchasing power parity to express welfare. Naturally, certain questions are not addressed at the moment, including: What is the relationship between the two categories if real wages are taken into consideration? What is the relationship if growth financed from indebtedness or foreign capital is distinguished from growth based on internal resources? The experiences of the past few years suggest that people tend to make decisions, among others on having children, more on the basis of such economic parameters perceivable in daily life..

The following chart shows the evolution of the fertility rate of Hungary after 1942. The indicator had clearly decreased from a rate above 2 to a rate below 2 already by 1970, with the lowest rate at 1.23 in 2011, followed by gradual increase in the fertility rate to 1.49 in 2017.

Chart 3 depicts a social and economic historical transition in Hungary from traditional values to a preference for a high standard of living considered worth giving up even demographical sustainability. The above firm political will and the aforementioned claim that a slightly positive correlation is demonstrable between GDP per capita and fertility in countries with a higher standard of living somewhat sophisticates the Hungarian situation.

Béla Tomka writes in his book published in 2016 that in the cross-hairs of Hungarian society and politics Austria has played an important role as a benchmark. Below the Hungarian state of affairs is compared to the Austrian standard of living rather than to the average of the EU (although the latter would show a similar trend). The following chart presents developments in GDP per capita at purchasing power parity and in the fertility rate in Hungary after the change of regime, relative to Austria. Theoretically, this was an important benchmark for the Hungarian society and also the Hungarian political elite. Chart 4 has too vertical axes: the left one measures de-

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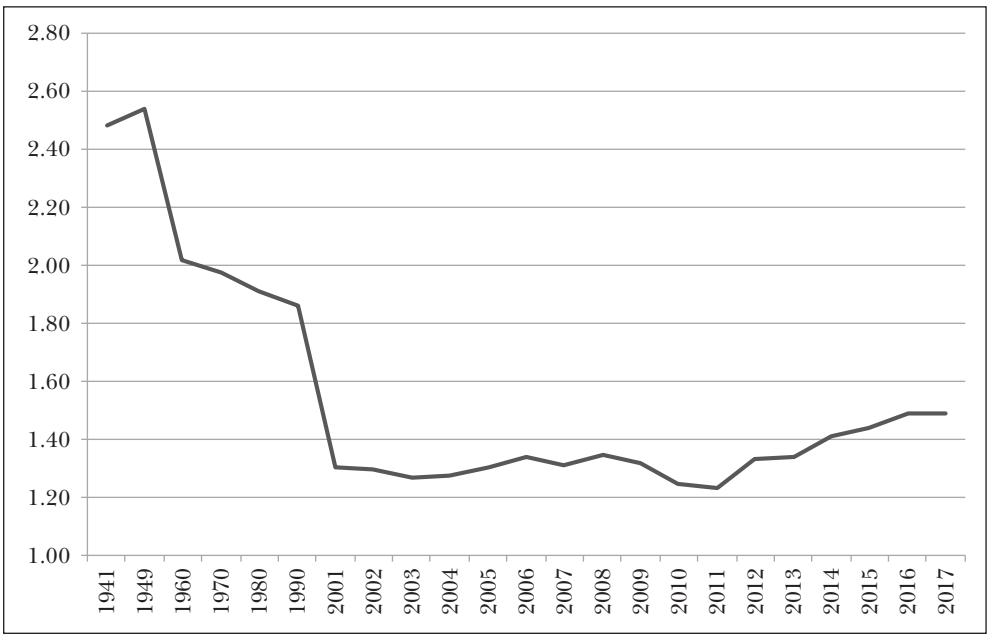
Chart 3: Fertility rates in Hungary, 1941–2017



Source: Central Statistical Office of Hungary

velopments in Hungarian GDP per capita as a percentage of the corresponding Austrian figures, while the right one measures developments in the fertility rate. Only the years between 1991 and 2017 are analysed because the World Bank has only published SNA-indicator statistics for the former socialist countries since 1990.

The chart illustrates that relative to Austria, Hungary now has a higher standard of living than at the beginning of the 1990's. Due to reasons mentioned above, closing the gap is perhaps not readily perceived, and in addition, similarly to the other European countries, there are significant regional differences in convergence. Also note that after 2011 increase in the fertility rate was associated with a catch-up in the standard of livin.

Chart 5 highlights the unclear correlation between the fertility rate and the standard of living. Based on a time-series analysis, the question arises how GDP per capita and fertility rates develop after 1990.

The regression monogenic takes the form of a polynomial chart, and the cloud of points moderately matches the hypothetical regression line. The conclusion drawn from this chart is none different from the previous ones: at the beginning of the period reviewed, the fertility rate decreases in the wake of GDP growth, and then, after a certain point, it increases. In an excessively theoretical field, it may be concluded that having reached a certain per capita GDP, the Hungarian economy has entered ther range of low positive correlation between rise in the standard of living in an economic sense and fertility rate. Departing from the meaning of the model, reference needs to be made to the fact that the transformations that followed the change of

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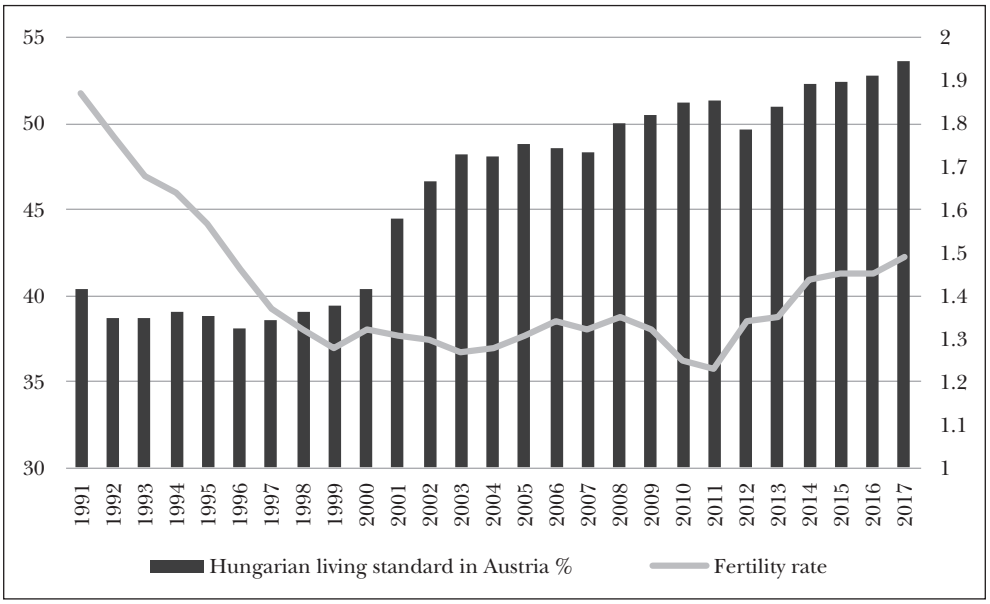
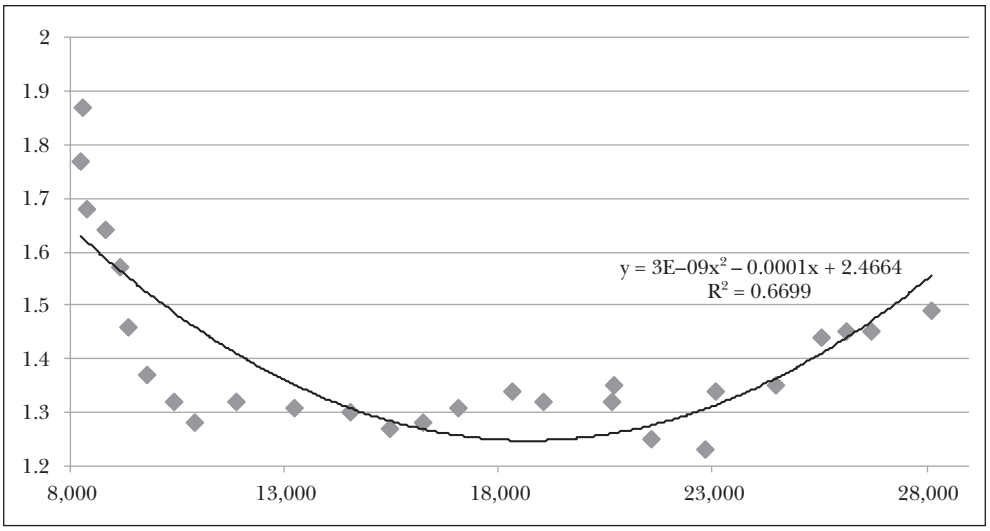
Chart 4: Standard of living in Hungary, as a percentage of the SoL in Austria



Source: Based on the data of Central Statistical Office of Hungary and World Bank

Chart 5: Regression monogenic between the fertility rate and GDP per capita after 1990



Source: Based on data from the Central Statistical Office of Hungary and the World Bank

regime and the shift in social values might also have had a serious impact on demography, and then the experiences gained about the new regime and the altered government policy could shift the demographic trend in a more favourable direction.

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These are evidenced by the findings of a survey conducted among Hungarian university students by Sági et al. (2017). More than a thousand interviewed students clearly expressed favourable opinions on the Hungarian family support system, including financial support and transfers. The overwhelming majority of the respondents considered the fiscal policy incentives beneficial for having children. Another research also pointed out that the family support and home creation aid applied in Hungary is sustainable over the longer term (Tatay et al., 2019).

Table 2: Differences between various NUTS 2 regions in Hungary

Region	2001		2005		2010		2015		2017	
	GDP average%	Live births/1000 residents	GDP average %	Live births/1000 residents	GDP average %	Live births/1000 residents	GDP average %	Live births/1000 residents	GDP average, %	Live births/1000 residents
Central HU.	157.7	9.1	162.4	9.9	165.8	9.8	153.5	9.4	152.9	9.2
Central Trans-danubia	92.5	9.1	94	9.3	86.6	8.7	93.1	9.1	92.3	9
Western Trans-danubia	102.3	8.7	98.9	9	99	8.2	107.9	8.3	105.6	8.5
Southern Trans-danubia	73.2	9.1	69	9.1	67.5	8.2	64.9	8.5	66.3	8.5
Northern HU	65.7	10.1	66.2	9.8	60.1	9.2	66.3	9.9	67.4	10.4
Northern Great Plain	68	10.8	64.4	10.3	63.4	9.1	63.7	10.1	63.5	10.2
Southern Great Plain	73.8	9	68.9	9	64.8	8	71.7	8.6	71.2	8.9

Source: Based on the data of Central Statistical Office of Hungary

Table 2 shows developments in live births per 1000 residents in the 7 NUTS-2 regions in Hungary. As clearly visible, while live births give different rates in different years, the economic sequence of regions shows a stable picture. The Pearson correlation indicator of these 7 regions gives the following data for the years reviewed: –0.4587; 0.1439; 0.5434; –0.1372; –0.283. In addition to the rates, the precursor also changes. In 2001, 2015 and in 2017 we can see a negative correlation between the standard of living and births (in 2001 it is medium), while in 2005 and 2010 this correlation is positive (in 2010 it is medium). Consequently, in certain years the number of births is higher with ssimilarly high welfare indicators, while in others the number of births is higher despite lower standard of living. Although more reliable results are obtained in deeper

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territorial levels, or even on a county level, at present the focus of the number of births is not necessarily at the place where economic indicators would justify.

In a global and a European perspective, Hungary belongs to the group of countries with a positive correlation between the standard of living in the economic sense and the fertility rate. For this reason, it is worth to take policy actions to support the financial aspects of childbearing. This is also confirmed by the recent improvement in the fertility rate in Hungary. Based on model calculations, the Hungarian family support model is sustainable also in terms of public finance. However, the globally negative correlation between the standard of living and the fertility rate, and the spatial processes within Hungary suggest that the factors underlying fertility also include factors beyond the economy (meta-economic factors). Certainly, a cultural and political stance against the concept of humans that can be associated with excessive individualisation may also be instrumental in achieving a more positive trend in this concept (Lentner et al., 2017).

Summary and conclusions

The most important objective of this study is to clarify whether there is a valid correlation between development in the economic sense and the fertility rate. The conclusions drawn from the research findings show a controversial relationship. On the one hand, the fertility rate is high in countries where the standard of living is low, or at least below the average. This negative correlation between the two variables is only confirmed by a rapid decline in the fertility rate since the 1960's, parallel with a reapid rise in average GDP per capita. Thus in a global context, increase in the standard of living results in a decline in fertility. Naturally, it cannot be predicted to what extent the fertility rate will continue to decline, perhaps the trend will slow as it approaches the value 2, or at least this conclusion arises from the analysis of the current path.

However, in the Member States of the European Union the correlation between the standard of living and fertility rate is surprisingly different: at a point the correlation takes a positive direction, although it must be added that the detectable positive correlation is not high. In this group of developed countries, almost without an exception, there is a problem with biological regeneration, i.e. without a positive migration balance, their population declines. Under these conditions, in the context of economic development, the absence of corruption, employment and social and economic openness to novelties, the reviewed data shows a positive correlation with the fertility rate. Accordingly, it may seem justified to support the dynamics of the fertility rate in a country by the corresponding financial incentives. This does not mean that there are no other, more powerful means to achieve this goal but – contrary to the author's expectations – there is some room for manoeuvre for the financial support of the fertility rate: labour market predictability and a household income sufficient to cover the expenses seem to stimulate fertility. However, it should also be pointed out that an analysis over a longer timeframe may be justified, and that this model leaves the overall demographic picture of the 28 EU Member States unchanged. Low fertility is also a major problem in other developed areas from North America to Southeast

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Asia. The question may also arise whether people in developed societies overestimate the economic implications of having children or undertake unnecessarily excessive financial burdens to guarantee their upbringing and careers. This might be a rightful conjecture, and yet it seems that at the current standard of living having children does indeed have serious financial implications. Moreover, in addition to financial needs, requirements related to risk reduction, the stability of the institutional system and the maintenance of a welfare system also arise when it comes to supporting fertility in these countries, including of cours Hungary (although not necessarily by the classical means as the values shown by OECD countries reveal).

The complexity of the issue naturally requires a more complex approach. Sociological and psychological parameters suitable for capturing considerations beyond an individual's life-span, isolated interests and perception of usefulness should also be included in subsequent studies. As John D. Mueller suggests, transcendence and religious belief may be very important factors in supporting fertility (weekly church attendance shows the strongest correlation with fertility in the federal states of the US), and the existence and reinforcement of the positive and modern self-image and identity of a country – and as a higher quality, a nation, may possibly also serve this purpose.

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Zsuzsa Buzás and Damien Sagrillo

The Role of Cultural Heritage in 21st-Century Music Education

Summary
Cultural heritage is an integral part of Hungarian music education. Folk traditions and folk songs are taught in every school, from the capital city to the smallest villages. Thousands of songs were collected by Zoltán Kodály and Béla Bartók, who adopted them in their classical compositions. With this they earned fame for Hungarian folk music and traditions. Zoltán Kodály also composed a series of music reading materials, mainly based on folk songs, which is currently used on all levels of Hungarian music education. Not only the Kodály concept, but the Táncház-method was also selected in the Register of Good Safeguarding Practices of UNESCO Cultural Heritage. In our digital age, the net-generation, unlike the previous student populations, can have different habits, which is the reason why students' music skills were tested with technology-based methods and tools. They are surrounded by popular media; however, the value that folk tradition offers should be inevitable in their education. The findings of our research provides input for the educational system about Hungarian students's music literacy, and their familiarity with its various elements, especially with certain components of their cultural heritage.

Keywords: cultural heritage, digital age, music education, Kodály concept

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Introduction

Music is one of the mainsprings of any culture and behaves in a way almost opposite to language. As language could be an obstacle to understanding a culture, music is about opening up and welcoming people (Mannes, 2011).

The inclusion of cultural heritage in music education has a double role: making traditional folk music accessible for everyone through mainstream education, and developing music skills. Music education also has to deal with historical and contemporary practices and their relative positioning between the extremes of identity and diversity in different regions of Europe within formal, non-formal and informal contexts of music learning (Sagrillo, 2019).

Hungarian music education based on the foundations of Kodály's ideas is well-known worldwide. Zoltán Kodály's music pedagogical method has been successfully applied in many countries of the world and many foreign music teachers and students come to Hungary every year to study it. The success of the Kodály concept is proven by the fact that it was selected for inclusion in the Register of Good Safeguarding Practices of UNESCO Cultural Heritage in 2016, a list of methods that are worthy of international dissemination as good examples to follow.

Cultural heritage of music

In 1989, the United Nations Educational, Scientific and Cultural Organisation (UNESCO) proposed parameters for the items that need to be preserved, and defined "folklore" as "the totality of tradition-based creations of a cultural community, expressed by a group or individuals and recognized as reflecting the expectations of a community in so far as they reflect its cultural and social identity". UNESCO gave recommendations on how to preserve folklore: design inventory systems of intangible cultural heritage, introduce formal and out-of-school curricula to emphasise respect for folklore, and promote scientific research relevant to folklore preservation.

UNESCO initiated the "Intangible Cultural Heritage" programme and the "Living Human Treasures" project in 1993. Specific types of intangible cultural heritage were listed in 2003, oral traditions and expressions, including language as a vehicle of the intangible cultural heritage; performing arts; social practices, rituals and festive events, and traditional craftsmanship (Inawat, 2015). Apart from the Kodály concept, the other Hungarian teaching concept in the UNESCO list of Intangible Cultural Heritage is the Táncház method, a tradition that began in Hungary with focus on teaching folk dance and music (Sagrillo, 2019).

Diversity is the main aspect of cultural heritage on a European level and beyond. The European Music Council claims to foster "in varietate concordia, united in diversity" (motto of the EU) as a main aspect of cultural heritage on a European level. Europeanism is also promoted by the joint preservation of past traditions and cultural values.

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The Kodály concept

The music curricula at schools in Hungary are based on the principles of Zoltán Kodály. Kodály's music pedagogical activity was closely related to his activity as a composer and an ethnomusicologist. The different fields of activity he performed complemented and fertilised one another (Pukánszky, 2005). Kodály's musical educational principles were based on folk music and contribute to the unfolding of a new lifestyle, and they are based on active relationship with music, where the child is in the center (Pethő, 2011).

According to Gruhn (2019), the present situation of music teaching and learning is also characterised by a socially and culturally determined shift from the *objects* of education to its *subjects*, from *content* to *action* and from the orientation on *traditional values of artworks* to an understanding of *music as action in social praxis* that offers the possibility of *participation* rather than calling for factual *knowledge* (Table 1).

Table 1: Schematic confrontation of the core elements of an epistemological paradigm change

UNIVERSAL CONCEPTIONS		**INDIVIDUALIZED CONCEPTIONS**
Consistent philosophy of music education at large that governs all actions based on social consensus about functions and intentions of education.		Orientation on the individual learning process based on students' potential and cognitive development that directs all educational decisions.
homogeneous society		multicultural society
tradition determines **cultural values** relevant to education	**shift** →	globalization determines **musical identity** in Communities of Practice; music as social praxis
education based on contents (objects)		education based on individual potential **(subjects)**
goal: contents and values		goal: **action and participation**
Learner adopted to the CONCEPTION		**Conception adopted to the LEARNER**

Source: Gruhn, 2019

Kodály's vision of musical formation had a broad foundation and envisioned an active and musically literate student. As the folk music of Hungary is one of the country's most important expressions of national identity, his approach pursued the goal of establishing and consolidating national culture as part of Hungarian identity (Gruhn, 2019).

Ittzés (2006) highlighted four principles to define the essence of Kodály's ideas: 1) all children should receive music education; 2) the bases of the music education are the human voice and singing; 3) exposure to music should take place on the basis of the principles of value-orientation guaranteed by the native musical language; and 4) the prerequisite of educating music experts is the acquisition of musical literacy cou-

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pled with the use of relative solmization. The application of the relative sol-fa syllables can serve as a memory aid for reading pitch.

Kodály became interested in relative solmisation sometime in the 1930s, when Sarah Glover's tonic sol-fa system was adapted by John Curwen. Curwen published a number of textbooks and songbooks including *The Standard Course of Lessons on the Tonic Sol-fa Method of Teaching to Sing* (1858). In the 1872 edition of *The Standard Course*, Curwen excluded the staff system of notation from the tonic sol-fa course, relying solely on his own invented notational system in the publication of textbooks, vocal music and even instrumental music. Kodály discovered that relative solmisation could make an excellent tool for achieving his educational goals: music literacy, in the training of school children as it was achieved in Britain in the 1930s.

Teaching experience shows that singing with sol-fa syllables facilitates the rapid and secure development of important musical skills, such as singing, intonation and music reading. Hand signs are often used in connection with sol-fa singing. They give character to each sound, show their spatial relationships, and help to acquire a clear concept of the sounds and the intervals. Hand signs are performed during singing exercises to provide a visual aid.

The role of folk song in music education

Many of Kodály's children's choruses are based on Hungarian folk songs, like the first one from 1925, when Kodály's interest turned towards music education (*Villő / Straw Guy'* and *Túrót eszik a cigány / See the gipsy munching cottage cheese*). Kodály believed that every ethnicity has a suitable body of folk songs for teaching music, so it should be simple to use folk songs in the national core curriculum. However, very few ethnicities have experts like Kodály, who invest in the pedagogical elaboration of their cultural heritage. The composers Zoltán Kodály and Béla Bartók were also collectors of folk songs, and their experiences in the field of ethnomusicology inspired their compositional work. According to Kodály's observations, folk tunes do not only have a single authentic form to be adhered to note by note. The type, which is a certain kind of frame including the structure, is more important than a single variant. The reason for giving an outstanding role to folk songs in Hungarian music education is that a series of important musical phenomena belongs to the basis of musical thinking, and they are the easiest learnt in folk music. Folk songs can be read with text or with sol-fa. Many songs are richly decorated, and at higher levels students need to be taught to read decorations (Chart 1).

Students not only sing folk songs, but also analyse them according to the features of the different styles. They study the fifth answer types of folk songs usually in the pentatonic tone system. Teachers also explain the unfamiliar terms, related to the texts of folk customs, folk costumes and folk instruments. Original sound recordings are used during music lessons, because listening to songs several times can help lead the popular diction and vocal techniques for learning. Students sing songs in bunches, taking care of the topic and the landscape plan, and the songs relate to on

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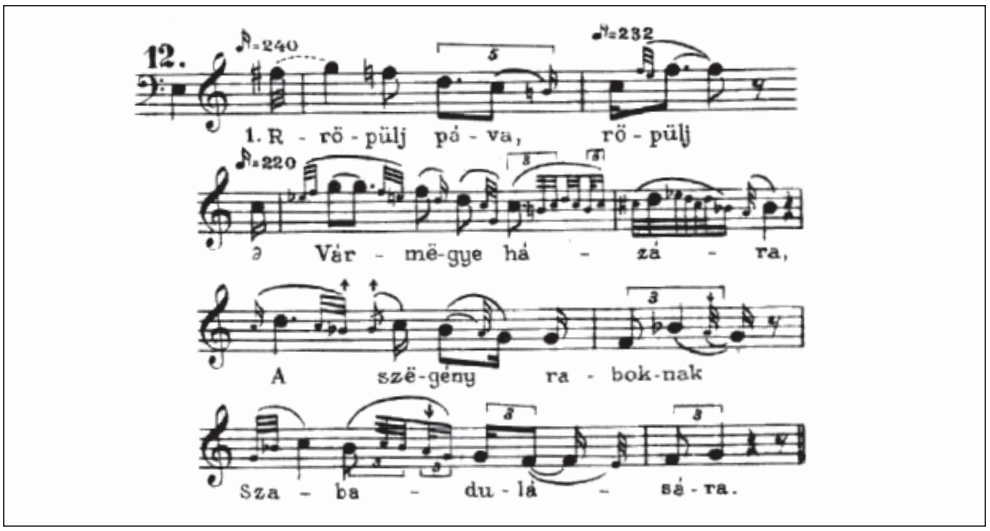
Chart 1: Example of folk song notation



Source: http://systems.zti.hu/br/hu/search/209?inc=r%C3%B6p%C3%BClj+ (accessed 03 March 2020)

another. As a variant of a popular song can teach you more, music teachers can show the students the work by Kodály that includes the particular song. In Hungary, students do not only learn children's songs, but many folk songs and their characteristics to distinguish between old and new-type folk songs. There is usually a descending fifth change in a pentatonic melodic structure in old-type folk songs.

Kodály's singing and reading exercises

As a composer, Kodály characterised his life-work as human voice-centred music. Music education (including the writing of pedagogical pieces) was more important for him than composing larger symphonic works (Ittzés, 2006). He claimed that anyone can learn music reading and writing. In Hungarian music education, solfege lessons are primarily built on the pedagogical compositions of Kodály. These works not only improve music reading and writing, musical memory and intonation, they also introduce students to the common musical activities, to group or choir singing via an invaluable music material. The book entitled *333 Elementary Reading Exercises* (1943), had the original title of *Introduction to Hungarian Folk Music*. The book contains Kodály's own unison melodies from the two-note material or d-r steps to the whole pentatonic scale (l,-d-r-m-s). The tunes are related to Hungarian folk music but show several Western musical characteristics (e.g. periodic structure.) The aim of the booklet is to establish music reading skills via sol-fa notation and the practicing of simple rhythm patterns (Ittzés, 2006).

In *Pentatonic Music* Volumes I-IV, in addition to Hungarian folk music Zoltán Kodály also uses folk tunes from other Finno-Ugric peoples. The four volumes comprise

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a total of 440 pentatonic melodies. The first and the third volume contain a hundred Hungarian and Mari melodies, and the fourth one contains 140 Chuvash folk songs. The second volume of *100 Little Marches* (1947) contains Kodály's own compositions. Elementary-school students can practise by singing or playing the xylophone (or any other available instrument). Music reading exercises are done without lyrics. All of the four booklets are published with sol-fa notation to practice the pentatonic scale in more detail. Kodály's *Biciniae Hungarica* volumes I-IV aim to introduce the reader to two-part singing. The four booklets include 480 biciniae (1947). The first three booklets contain polyphonic arrangements of Hungarian folk songs, and the third volume also presents historical songs. The fourth volume contains 57 Mari and three Finnish folk songs. The *Bicinia Hungarica* present an independent style of Palestrina. Although Kodály claimed that these volumes were not intended for public performance, most biciniae can be performed in concerts. Kodály's two-part reading exercises were published in several series from the 1950s, entitled 77, 66, 55, 44, 33 and 22 two-part practices, respectively, and then his Tricinia was released including 29 three-part singing practices.

Functional music literacy

Music literacy is traditionally defined as an acquired musical knowledge and a skill to translate notation into vocal sound (reading/singing) and sound into notation (notating/writing). Both reading and notating skills are fundamental prerequisites for comprehensive musicianship. However, the term 'literacy' is continually changing and evolving, and we cannot narrow its meaning to this simple definition.

Furthermore, it is important to take into consideration the new ways and forms of communication, the nature and speed of information, and the growing role of technology. Music reading is a highly complex activity on multiple levels, and the acquisition of reading literacy includes learning, using and perfecting a corresponding set of highly interrelated operations, skills and strategies which can and should be improved until adulthood even in the case of highly skilled students (Schnotz and Molnár, 2012).

The term 'functional music literacy' was coined by Jorgensen (1981). It means the minimum level of musical skills which enables students to play an instrument or sing musical materials. Functional reading literacy is generally seen as an enculturation process, where literacy practices at school are designed so that they resemble literacy events, practices, and authentic texts used for specific purposes in real-life contexts, emphasising social interaction and collaborative construction of meaning (Linnakyla, 2007). One of the principal aims of music education is to develop a functional musical literacy through solo or group (choir, chamber, or orchestra) performances. However, music reading achievement is usually weak, only a few music programmes address reading skills beyond the most perfunctory level (Ester, 2010).

As it contains music-reading comprehension, functional music literacy allows students to enjoy music and active music-making through contributing to the development of their musical taste. Through culturally relevant and authentic activities,

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which could partly be in the hands of public schools, it fosters the acquisition of musical reading and musicianship, nurturing the development of musicians, in addition to the development of future audiences.

Digital technology as a tool for preserving cultural heritage in music education

Our students are faced with learning multiple new literacies to succeed in our information-rich world, yet most schools have not caught up with the digital reality that students live in day by day. Lately, more than 30,000 musical applications have appeared on iPad and more than 7000 on android software (Sagrillo, 2016). According to Janols (1990), the new technology has increased students' sense of the basic elements of music. Research into computer-assisted music education started at the end of 1960s in the United States and the United Kingdom. The first computer programs were intended as ear-training exercises (Raynold, 1967).

The use of ICT tools not only improves students' music skills, but at the same time also develops their digital competence. Basic computer skills can also increase students' labour-market opportunities in the future. Although ear-training programs are often used abroad (EarMaster Pro, GnuSolfege etc.), Hungarian music teachers rarely use any kind of ICT tool in solfege lessons (Buzás, 2012).

The rapidly increasing database of the Internet provides resources for teachers as well as students in many cases. Supplementary data for music history, supporting material for ear-training or music analysis, several kinds of software or plug-ins for certain software are always available. Emails can support independent activities, homework or co-operation with, for example, other schools.

Since 2000, Web 2.0 has been characterised by a participatory culture. In this context, users are involved, they interact with the content and collaborate with each other online to create "user-generated content". Culture is produced, consumed and mediated differently thanks to digitisation in general and to the set of new web technologies that facilitate publishing and sharing (Sagrillo, 2016).

In Europe computer-based assessment was first initiated in Luxembourg almost in every field of education. This system was adapted by the OECD PISA 2009 Electronic Reading Assessment (ERA) and OECD PIAAC (Program for International Assessment of Adult Competencies) (Molnár, 2010).

Online testing of students' music literacy skills

Our studies were the first attempts to examine students' music literacy skills with the help of the latest digital technologies. We investigated procedures that encompass a broad spectrum of the components of music literacy based on the Kodály concept. The following research questions are addressed: 1) How reliably does the online music reading instrument assess music literacy skills among music school students? 2) What is the music literacy level of students of the age between 9 and 14? 3) How

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does the music literacy achievement of the students correlate with certain background variables? 4) What is the role of the digital technologies in music students' life?

Participants were tested in the spring of 2017. A total of 204 music school students from five consecutive grades participated in the study. Students were selected from five different music schools, located in Hungarian cities including the capital (Table 2). These students, aged between 9 and 14, have various opportunities to practise music reading in music schools, such as in orchestras and chamber groups, or at solfege classes. All the students learn to play a musical instrument twice a week.

Table 2: Sample for the study

Grade	N	Boys (per cent)	Girls (per cent)
4	41	21	78
5	40	35	65
6	43	40	60
7	38	47	53
8	42	62	38
Total	**204**	**41**	**59**

Source: Edited by the author

The data was recorded on the eDia platform. The advantage of an electronic diagnostic system over paper-based measurements is that the tasks can be made more enjoyable and lifelike due to images, sounds, animations and varied forms of response (selecting, clicking, colouring, moving and rearranging). Participants completed the online music-reading test that consisted of four sub-tests with 55 closed multiple-choice questions. Each appropriate response was awarded one score, with the maximum possible test scores being 55.

The different areas of music-reading skills were covered by the following sub-tests: rhythm reading (including simple meters, symmetrically compound meters, and some rhythm values and patterns), melody reading (including different musical notation systems, the recognition of melodic patterns, such as intervals, scales, triads and musical signs). Melody and rhythm reading with soundtracks were also integrated. To test students' timbre hearing, tasks with certain choir and orchestra compositions were added. Different music reading signs and symbols are taught from the first school years and, in the case of hand signs, even earlier, in the kindergarten.

Findings

In terms of difficulty, the test corresponds to the development level of the grades assessed. The students' achievement was 73 per cent, with a standard deviation of 12.35. According to the results of variance analysis ($F=4.206$, $p=0.007$), significant differences were found between sixth and eighth graders, evidencing that music literacy skills improve in these grades.

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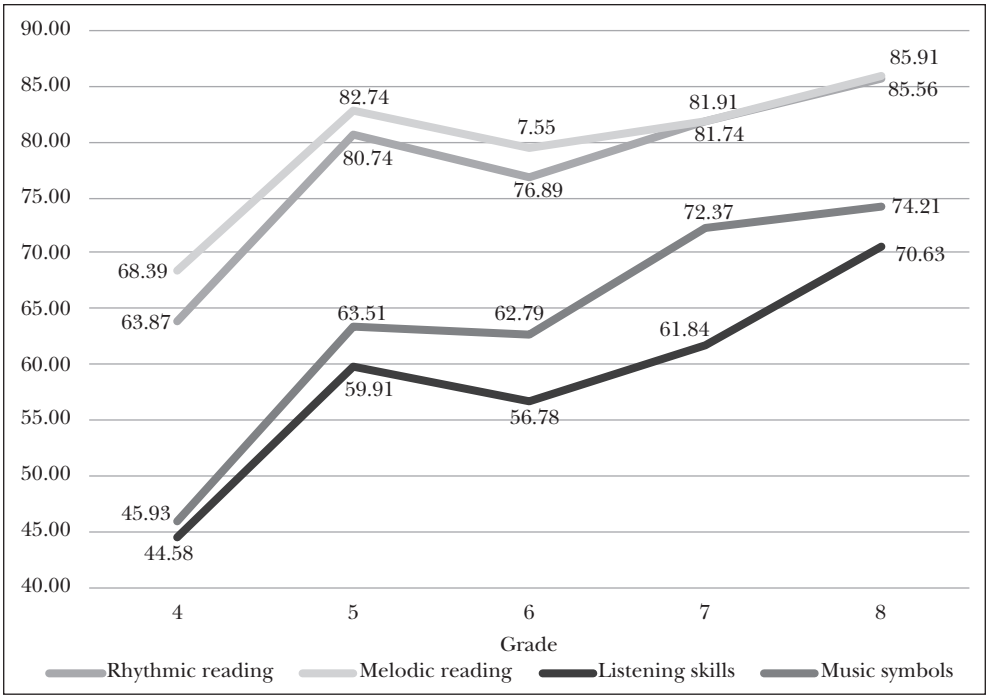
We can observe a higher achievement in rhythm reading than for melody reading. Identifying musical clefs, note names and the perfect intervals proved to be the easiest for students. They had no difficulty with syncopation or recognising a song by its notation. The most difficult task was identifying the 6/8 meter, which is uncommon in Hungarian folk music, so the relative difficulty of identification was in accordance with the assumptions. Finding the four major triads was the second most difficult task in the entire test: 51 per cent of the fifth grader music school students and 45 per cent of the eighth graders identified them. With the use of variance analysis, a significant difference can be demonstrated between the achievements of the fifth, sixth and eighth graders on the task that dealt with a modal scale (F=5.308; p=0.032). Modal scales are typical in Hungarian folk songs. All students gave the correct answer to the task in connection with the perfect fifth interval that is a characteristic of the songs and it was also easy for them to identify the style of a song.

On the other hand, students found it difficult to identify the tonality of a melody. Only 30 per cent of the sixth graders succeeded in identifying the pentatonic scale, while 50 per cent of the seventh graders recognised the tonality. Almost 100 per cent of the eighth graders made the correct choice between the notations after listening to the melody. Recognising the timbre of a mixed choir was one of the easiest tasks: 93 per cent of the eighth graders gave the correct answer (Chart 2).

Chart 2: Descriptive statistics of sub-tests



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The influence of background variables on students' performance

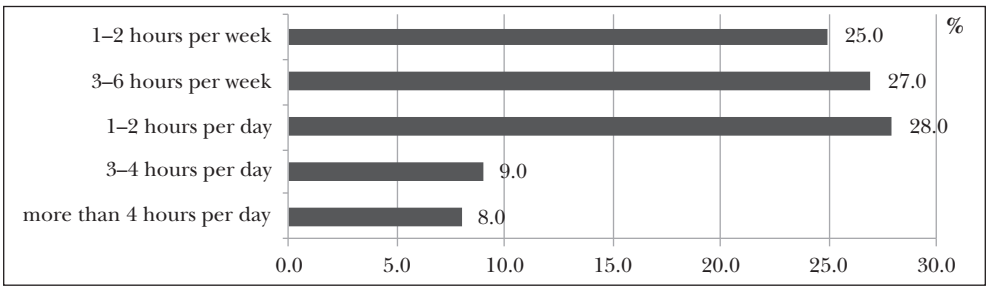
A background questionnaire was also included in the assessment process. The analysis gives a straightforward explanation for the findings of the research, and helps in the interpretation of the context of music education. The majority of the music-school students (43 per cent) found the test to be moderately difficult, whereas 32 per cent of them considered it easy. A weak correlation was found between students' subjective estimation of their own performances and their actual performance in the music reading test ($r=0.214$, $p<0.05$). We found no relationship between the music reading achievement and the parents' educational level. There were no significant differences between boys' and girls' achievements in the sub-tests.

Several studies identify a correlation between students' achievement at school and their motivation. We found correlations between the students' attitude to some activities during solfege classes and their achievement in rhythm reading ($r=0.286$, $p<0.01$) and their attitude to singing ($r=0.237$, $p<0.01$), and between students' achievement and attitude to listening activities ($r=0.245$, $p<0.01$). A positive attitude to singing correlates with music reading achievement ($r=0.305$, $p<0.01$), which accounts for 9.3 per cent of variance in the music reading achievement. It also correlates with the achievement of the rhythm reading sub-test ($r=0.204$, $p<0.05$), the melody reading sub-test ($r=0.274$, $p<0.01$) and with the musical signs and concepts sub-test.

Students' use of digital technology

We were curious about students' use of digital technologies at home in this rapidly developing world. Nowadays, the Internet plays an important role in teaching, research and learning processes, as it is the only and the most powerful tool to provide access to unlimited information. We asked how often students surfed the Internet. 25 per cent reported that they used it 2-3 hours a week, and nearly 30 per cent claimed that they used the Internet 1-2 hours every day. Less than 10 percent of the students reported that they used it more than 4 hours a day (Chart 3).

Chart 3: Amount of time students surf the Internet (%p)



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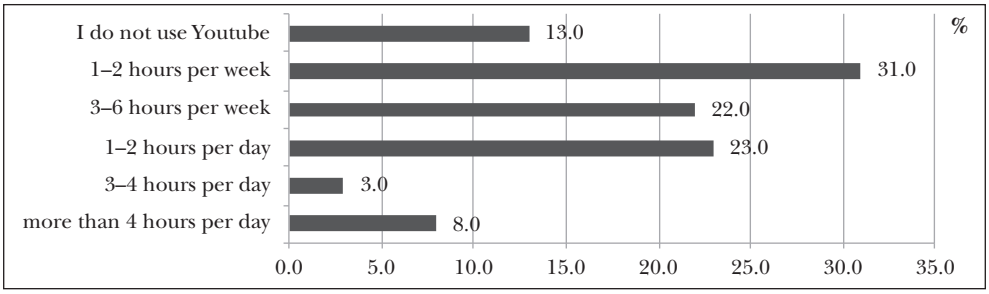
Solfege classes contain various activities, such as music reading, writing or listening to music. In our research, students' experience with YouTube as one of the main online music sources was also examined. Almost 25 per cent of the students use it for 1 or 2 hours a day. However, no significant correlation was found between the use of digital devices and music literacy achievement (Chart 4).

Chart 4: Amount of time spent on YouTube (%p)



Source: Edited by the author

Summary

Music has been part of the cultural heritage since the origins of mankind, not only in an artistic and cultural aspect. In the *Epilogue of Pentatonic Music,* Zoltán Kodály highlighted that learning world music is useful in the study of our ancient music culture. Hungarian folk music draws influences from multiple sources and it has been affected by other peoples' music.

Hungarian music education is based on the Kodály concept. Our online test results revealed that students' music literacy skills are well-developed in the digital age.

According to Kodály: "Hungary is also an integral part of Europe: and as such, it should embrace European traditions. For a country and a people living at the point of impact between East and West, the purpose of life can only be to belong to both, to reconcile any conflict between the two and absorb both to merge them. In this respect, to identify as a Hungarian without a European identity is worthless, and to me, Europeanness without simultaneous Hungarianness is worthless. We should and can learn from the musical culture of all nations. … Isolation and the lack of education will also strip away national characteristics" (Bónis, 1974). According to his concept, every teacher and musical expert has the role to transmit our culture heritage to the next generations.

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László Bartók

Climate Change and the Hungarian Fiscal and Monetary Policy

Summary
In the last months of 2018, every weekend tens of thousands of people demonstrated on the streets in France. The main reason of the demonstrations was the rising petrol prices and its environmental tax that the government wanted to raise according to the 2014 law. The French example shows that in many cases the measures against the climate change can provoke a very deep resistance from a major part of the society; meanwhile the global climate change became a bigger and bigger danger for humanity. In the first part of my publication, I will shortly examine how the climate change became an important issue globally in the last 20 years; and how environmental pollution and the related climate change have become an important research subject in the economy and the answers the scholars gave for these challenges. In the second part I will show the toolkit the fiscal policy disposes to mitigate the climate change, and finally I will examine why and how the monetary policy and the financial system must be involved in the fight against climate change.

Journal of Economic Literature (JEL) codes: Q58, Q55, E52, E62
Keywords: climate change, fiscal policy, monetary policy, green finance

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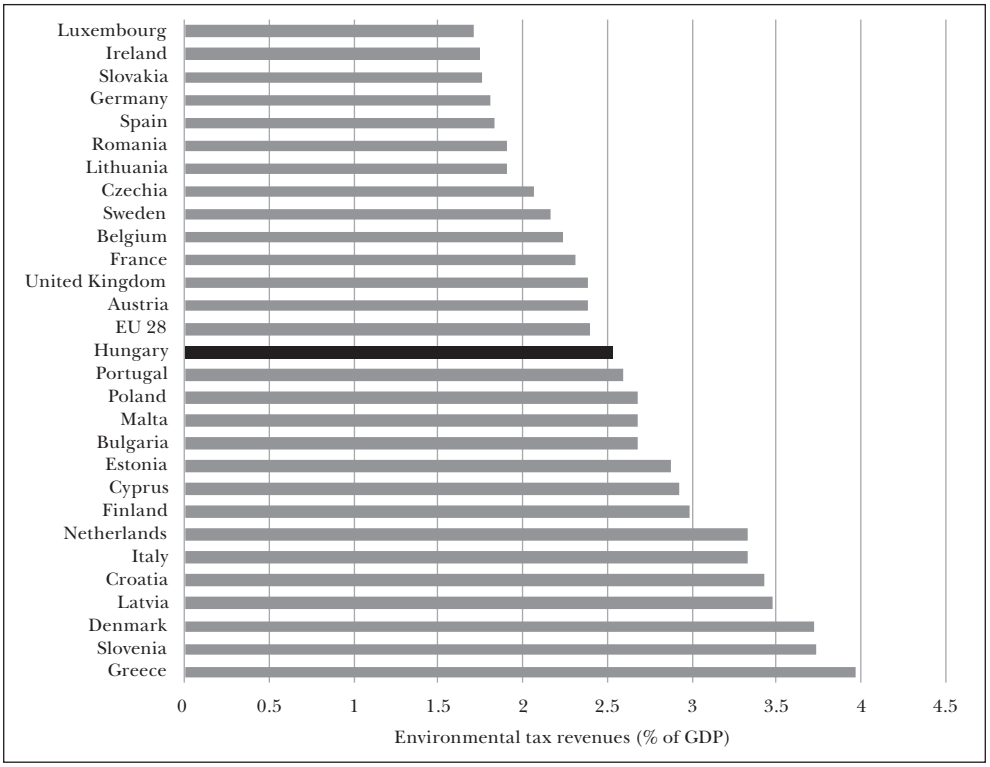
The Hungarian Fiscal Policy and climate change

It was via the environment-related taxes that the Hungarian government, in accordance with the EU legislation, tried to regularize the negative environmental externalities in order to – directly or indirectly – decrease the effect of climate change. The European Commission's relevant country report (2019) included in the *Environmental Implementation Review* gives us a good insight into the importance of environment-related taxes in Hungary. The Commission examines the Hungarian environmental tax system in detail and establishes that "Hungary's revenues from environment-related taxes remain higher than the EU average. Environmental taxes are accounted for 2.53% of GDP in 2017 (EU28 average: 2.4%) and energy taxes for 1.91% of GDP (Chart 1). In the same year, environmental tax revenues were 6.6% of the total revenues from taxes and social security contributions (EU average 5.97%). However, according to the Commission, the consumption taxes remained relatively high (40.2%, 6th in EU28), pointing out the limited potential of shifting taxes from labour to consumption and in particular to environmental ones, therefore the Commission has recommended that Hungary should modify its taxation system" (EC, 2019, p. 26).

Chart 1: Environmental tax revenues as a percentage of GDP (2017)



Source: Eurostat

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In 2009, Sipos (2009) distinguished 17 various environment-related fiscal policy tools, including taxes, tolls, fees and allowances. In addition to environmental pollution and environmental product fees (road tolls, travel cards, energy taxes and gas price subsidies for households), this list also includes taxes which have an indirect effect on climate change, like business taxes and construction taxes. Although most of these taxes, fees, tolls and allowances are still in force, some of them, like the tax break for biofuel, have already been abolished, meanwhile, new tools have also appeared in the past ten years. However, the collection and analysis of the current environment-related fiscal policy tools fall beyond the scope of this publication.

This paper discusses the fiscal policy tools suitable for encouraging the corporate sector to consider environmental aspects in investment decisions. One of the most essential tools is a tax credit for energy efficiency purposes in an investment. Taxpayers can reduce their annual corporate taxes (for the next five years) by a partial amount of the investment cost, if the investment meets the environmental objectives, and if the ultimate energy consumption of the company decreases as a result of the investment. The law endeavours to support small enterprises by enabling them to decrease their corporate taxes by 70%, or 50% and 30% for the medium and big companies, respectively (National Tax and Customs Administration, 2018).

However, corresponding to environment-related taxation, bigger companies can also have another corporate tax allowance in the framework of the development tax credit. If a company makes a minimum of HUF 100 million independent environmental investment, it can claim a tax allowance in the year following the commissioning of the capital investment project (Veress and Bardócz, 2017).

In the field of households, in 2006 the Hungarian government approved a tax policy tool to support the sale of electric cars. The government grants a subsidy (in an amount of HUF 1.5 million) to customers who buy such eco-friendly vehicles. The sales price of the car is decreased by the amount of the subsidy. In addition to this support, customers are also relieved from paying the company car tax, the registration tax and the fee charged for the transfer of ownership.

The National Bank of Hungary and climate change

In February 2019, the National Bank of Hungary (Magyar Nemzeti Bank, MNB) adopted its green policy programme which was, on the one hand, a response of the increasingly serious climate change, and on the other, the central bank realised the importance of green financing and the role of the monetary policy in this field. The purpose of MNB was to provide a far more powerful support to environmental sustainability than currently, through the financial products and services of the domestic system of financial intermediary. In accordance with its statutory mandate, through the Green Finance Programme MNB supports the stability of the financial intermediary system in order to ensure that the financial system promotes sustainable development in the economy and achievement of the government's economic policy objectives.

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Based on the National Energy and Climate Plan of the Hungarian Government, on international experiences, research and the priorities of the central bank, the three pillars of MNB's Green Finance Programme include the following:

1. Green Programme for the Hungarian Financial Sector
2. Social and International Relations
3. Eco-friendly Operation by the Central Bank

Green Programme for the Hungarian Financial Sector

The first pillar includes an ecological and a financial risk analysis. "For MNB, as the financial and monetary authority, one of the most important tasks and responsibilities is to identify the risks involved in climate change (and other ecological anomalies, a megatrend with widespread social and economic implications, for financial institutions and their customers" (National Bank of Hungary, 2009, p. 7). This factor is new within the scope of the financial monetary authority. Accordingly, the central bank and the actors of the financial system are required to observe, analyse and prepare forecasts for the long-term economic and financial effects of climate change.

The first pillar of MNB's Green Programme includes the mobilization and greening of financial services: shifting resources towards the "green" way, and contribution by the financial system to Hungary's sustainable ecological catch-up. MNB intends to encourage the issue of green financial products and sharing the best practices in this field, while also supporting incorporation of ecological and environmental aspects in classical credit products. In addition, MNB wishes to encourage banks and other providers of financial services (for example, insurance companies) to promote and spread green approaches.

Finally, in addition to preparing new green financial instruments, the actors of the financial market also need to change their operation using digital and other types of innovations which can help decrease the ecological footprint of the company. Pursuant to this act, they must set an example for the public and engage them in the combat against climate change. Therefore, MNB supports banks in incorporating ecological considerations in their operational processes (decrease in paper use, the digitalization of basic banking operation, and the creation of Green Bank Awards for the greenest bank of the year etc.)

Social and International Relations

Besides improving the financial system, the National Bank of Hungary tries to build a good social and international network as the second pillar of MNB's Green Finance Programme. Therefore, the monetary authority's objective is to create a good and close relationship with the relevant governmental, academic and social actors. According to MNB, the (financial) education of the next generation is one of the most important factors in building a healthy and effective financial system, thus the central

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bank extensively supports financial education and wants green finance to be the part of financial education at Hungarian universities.

Concerning international relationships, MNB joined the Central Banks and Supervisors Network for Greening the Financial System in January 2019.

The eco-friendly operation of the National Bank of Hungary

Finally, the National Bank of Hungary intends to set an example in green and environmental institutional operation. Therefore, as the third pillar of MNB's Green Financial Programme, it also wants to decrease its own ecological footprint.

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Anita Borzán and Bernadett Szekeres

Accounting Tourism Development Grants in Hungary

Summary
In recent decades demand for and the supply of sustainable tourism related to national parks have increased. Environment-friendly tourism plays an increasingly significant role in the travel habits of the Hungarian population. Hungary has a lot to offer in eco-tourism. Its nature tourism destinations include national parks, on the one hand, and geographical regions, nature parks and geoparks maintained by voluntary civil society organisations. In order to meet the needs of green tourists, centres and nature trails are created and guided tours are organised. Eco-tourism plays an important role in Hungarian tourism and based on the revenues, expenditures and visitor turnovers in natural parks, its importance is increasing in all areas. Support programmes represent vital financial resources in the development of tourism. Several forms of support are available in Hungary to contribute to improvement in different areas. This is a study of the importance, classification and accounting of tourism development grants.

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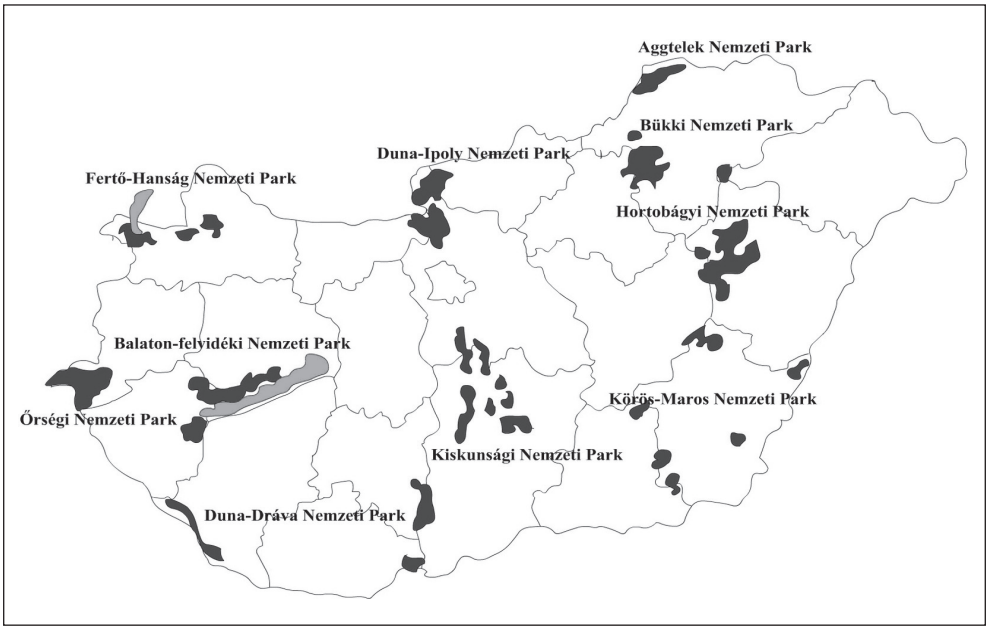
Hungarian Ecotourism in a Nutshell

"Tourism includes, on the one hand, all the movements and activities beyond people's usual routines in life and work, irrespectively of the specific motives, duration and objectives. On the other hand, tourism is also defined as the combination of financial, technical and institutional conditions and services designed to meet the needs related to such movements and activities" (Lengyel, 2004, p. 79). Based on the trends perceptible in tourism, it can be established that demand for sustainable tourism related to protected natural values has increased significantly.

"Ecotourism comprises environmentally responsible travels and visits to relatively undisturbed areas with the aim of enjoying and appreciating their natural and cultural values, sparing them through the mitigation of the impacts of the visit and through the provision of financial and social benefits to the local population" (IUCN, in: Pannon University, 2008, p. 12). Hungary has a lot to offer in ecotourism: national parks, landscape-protection areas (Chart 1), nature parks, geoparks, visitor centres, nature trails and guided tours.

Chart 1: National parks and landscape-protection areas in Hungary



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The international recognition of Hungary's natural values is indicated by the fact that the Hortobágy National Park, the Aggtelek National Park and the Fertő-Hanság Cultural Landscape have all been declared World Heritage Sites. The natural values

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granted the European Diploma of Protected Areas include the Balaton Uplands, the Danube-Ipoly National Park and the Bükk National Park. The European Diploma of Protected Areas is granted by the Council of Europe to areas where outstanding natural, cultural, scientific or aesthetic values are found and excellently managed. The European Diploma of Protected Areas has already been given to the post-volcanic formations of the Tihany Peninsula, the Szénás Mountains as the natural habitat of the Pilis flax, and the Ipolytarnóc Fossils.

A common task in the various areas of ecotourism is raising awareness of the natural values, teaching people to appreciate nature and establishing the conditions of ecotourism. The growing importance of ecotourism is manifest in the increase in visitor turnovers and in incomes. However, this also requires constant improvement, and the areas involved in ecotourism frequently raise the necessary funds from several sources, including grants.

Types and accounting of grants

Following a conceptual overview of tourism, this study presents the diversity of grants. Mention is made of the large number of different areas where grants are available. As a first step in the research, the legislative background in the EU and in Hungary is described to facilitate understanding the types and accounting of the grants.

The regulation of grants in the EU

As the basic principle of the market functioning in the European Union is the freedom of competition, the Member States are only allowed to grant support and thus influence the functioning of the market for specific purposes. The guiding principles regarding the regulation and control of state support to businesses are laid down at the level of the EU. Development funds play a key role in the budget of the European Union. Cohesion policy includes a large part of the European Union's development grants. The European Union determines the development directions of cohesion policy for seven-year programming periods and assigns resources to them. Part of the development costs are distributed through a decentralised decision-making mechanism, i.e. within the Member States' powers, while another part is allocated by the European Commission in a procedure performed in Brussels.

Hungary receives most EU grants from cohesion policy funds, while the amount of resources provided to the country from central EU programmes is low. The basis of strategic planning for the cohesion policy for the period between 2014 and 2020 includes the Europe 2020 strategy, which determines the objectives of the European Union, providing support for the decentralized EU programmes from the below-mentioned five large funds within the European Structural and Investments Funds (ESF) (Chart 2).

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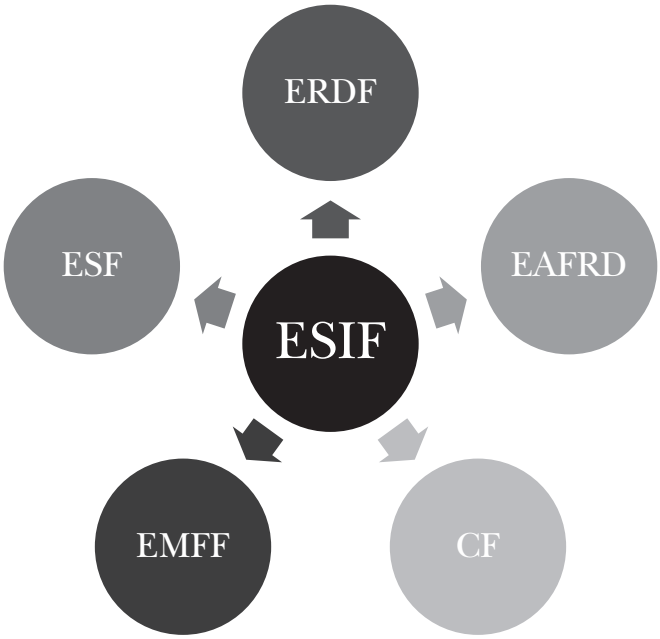
Chart 2: The five large funds of the European Structural and Investment Funds (ESF)



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The implementation of the Europe 2020 strategy is promoted by the above-mentioned funds in the following areas:

– European Regional Development Fund (ERDF): Its primary aim is to ease and reduce inequality among regions and, thereby to strengthen economic and social cohesion. Its main priorities are innovation and research, information and communication technology, support for small and medium-sized enterprises, and a low carbon-dioxide emitting economy.

– European Social Fund (ESF): Its basic principle is improvement in education and employment, including service to people, and its objective is to improve the life for people in multiple difficulties. All the regions can benefit from it. Its main areas comprise promoting mobility, developing employment, raising the level of education and vocational training, fighting poverty and facilitating social inclusion.

– Cohesion Fund (CA): It is primarily aimed at decreasing social and economic inequality between rich and the poorest Member States. Its main fields of application are infrastructure projects and environmental protection.

– European Agricultural Fund for Rural Development (EAFRD): It provides help in managing economic, social and environmental challenges. It has six priorities: knowledge transfer in agriculture and forestry, innovation, support for agriculture technology, competitiveness in agriculture and management of the food supply chain, strengthening and preservation of the ecosystem, and the promotion of resource-

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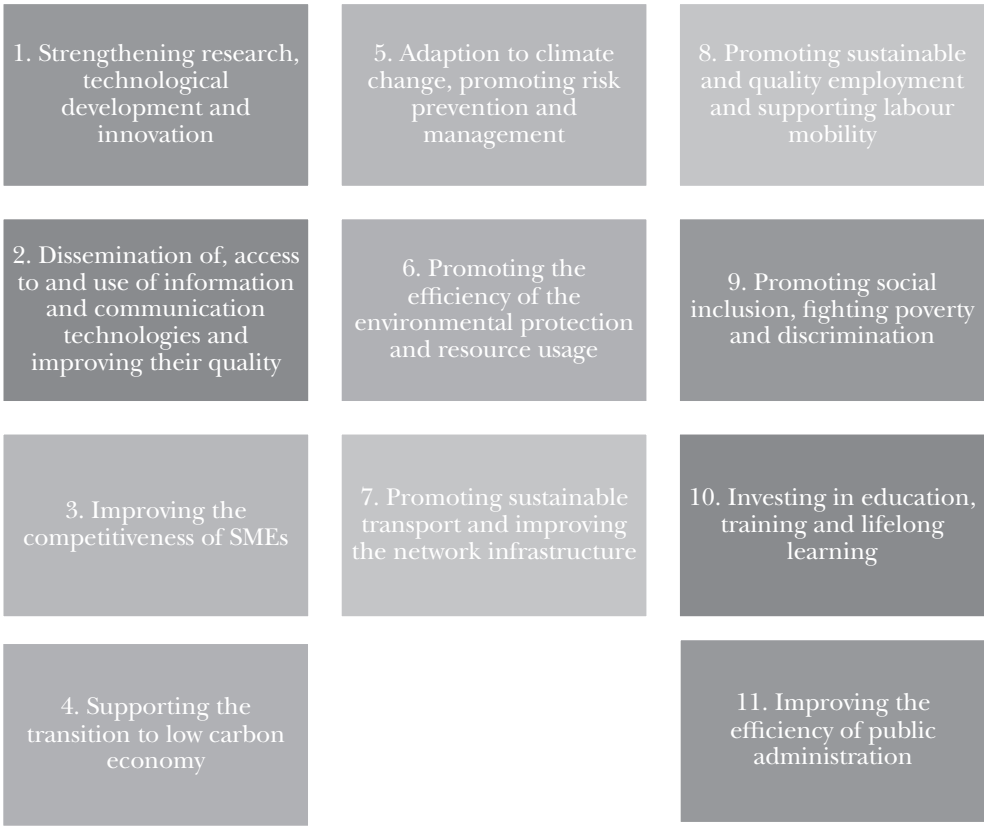
efficiency, low carbon-dioxide emission, social inclusion and the social development of the countryside.

– European Maritime and Fisheries Fund (EMFF): It is engaged in the preservation of fish stock and the management of fishing fleets, and the economic, social and environmental sustainability of fisheries and aquaculture. Its resources are used for sustainable fisheries, the economic risk management of coastal communities and for the establishment of new jobs.

The guidelines of strategic planning in the EU's cohesion policy for the period between 2014 and 2020 are included in the Common Strategic Framework.

The regional policy of the European Union (Chart 3) has 11 thematic objectives for the programming period of 2014–2020. The investments of the European Regional Development Fund support all the 11 objectives, but the main priorities of the investments are set out in sections 1–4. The main priorities of the European Social Fund are objectives 8–11, but it also supports objectives 1–4. The Cohesion Fund supports the objectives 4–7 and objective 11.

Chart 3: The 11 thematic objectives of cohesion policy



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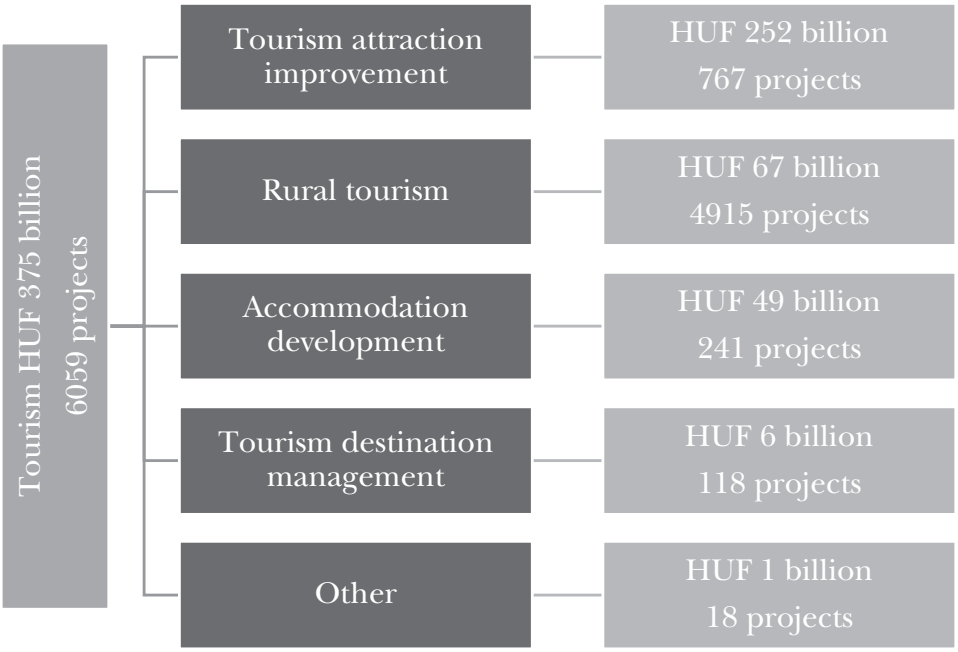
Regulation of grants in Hungary

The development projects performed in Hungary in the European Union's programming period 2014–2020 were named "Széchenyi 2020", in line with the Europe 2020 strategy. Laws and regulations are included in the national regulation concerning the use of the Structural Funds. The Partnership Agreement (PM) is the highest-level planning document for the allocation of Member States' resources in for the period 2014–2020. It sets Hungary's development needs for the period, the objectives of using the cohesion funds, the operational programmes covering each development area and the allocation of the resources.

In the programming period 2007–2013, 6059 tourism projects were carried out using grant worth HUF 375 billion. Of this amount, HUF 308 billion under the Regional Operational Programmes (ROP).

Chart 4: Breakdown of tourism products by payment (2007–2015)



Source: Based on data from KPMG, EMIR and IIER

Table 1 shows tourism attraction developments in a breakdown. The most significant ecotourism projects included the Ecocentre by Lake Tisza and one of the most successful projects in this category, the Zoo in Nyíregyháza.

The overall national development objective of the 2014–2020 programming period is economic growth based on sustainable production with high added value and increasing the employment rate. In order to ensure that developments result in

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Table 1: Breakdown of tourism products based on payments (2007–2015)

Tourism sector	Product	Payment, HUFB
Tourism attraction development	Heritage tourism	115
	Health tourism	49
	Active tourism	49
	Ecotourism	22
	Event tourism	9
	Wine and gastro tourism	7
	Other	1

Source: Based on data from KPMG, EMIR and IIER

significant changes, five key national development (support) priorities are interconnected and cover the entire development policy, including rural development objectives and contributions:

1. Improvement in the competitiveness of economic participants and the intensification of their international presence.
2. Increase in employment (through the economy development, employment, education and social inclusion policies, with a view to regional differences).
3. Increase in energy and resource efficiency.
4. Management of challenges related to social inclusion and demography.
5. Implementation of local and regional development projects facilitating economic growth.

According to our opinion, the grants granted by the EU make a significant contribution to Hungary and serve economic and social inclusion. Within the framework of common priorities, the Member States have room to manoeuvre in allocating the available resources to actions and areas where they are really needed.

Tourism development grants in light of the EU's thematic objectives

Tourism is one of the significant sectors in Hungary's economy, heavily relying on SME's. It is also a priority area in terms of employment. The ratio of people employed in tourism is considerable even in an international comparison, and tourism businesses act as the predominant employers in villages. Consequently, the tourism attraction development projects are important for employment. Tourism plays a key role in the following thematic objectives:

– The third thematic objective, i.e. improvement in the competitiveness of small and medium-sized enterprises, the agriculture, fisheries and aquaculture, requires several projects in tourism, catering and environmental protection services to support the operational programme for fisheries. Consequently, the Hungarian Fisheries Operational Programme can significantly contribute to the local creation of jobs and

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promote tourism, and the role of fishing tourism can increase not only at fishing lakes but also at other natural waters. The fisheries sector represents a small but labour-intensive part in employment in Hungary. However, fisheries can indirectly provide a basis for the growth of employment in tourism and landscape management.

– In terms of the sixth thematic objective – the promotion of efficiency in environmental protection and resource utilisation –, Hungary's world heritage sites are also resources to be protected and developed. The protection, demonstration and utilisation of national parks, certified health resorts and various built secular and ecclesiastical heritage sites represent an essential improvement potential. Familiarity with and visits to heritage sites can be increased by organising them into a network. Cultural values can be found at most settlements in Hungary and their preservation and utilisation can be linked to both urban and rural developments.

– The seventh thematic objective, i.e. promoting sustainable transportation and removing bottlenecks from the main network infrastructure, includes the development of the Danube corridor, and is of special importance due to navigability, tourism and drinking water, making it a priority area also at a macro-regional level.

– The fulfilment of the eighth thematic objective. i.e. supporting sustainable and high-quality employment and worker mobility, primarily requires means to boost economic development: firstly, to strengthen the employment capacity of the SME sector; secondly, to develop labour-intensive economic segments, and thirdly, to build the economy with focus on social needs. The farm coach service programme and other rural tourism development projects have had significant employment impacts on rural development.

In certain operational programmes, the thematic areas eligible for grants from different funds or programmes are identified as thematic areas with particular integration needs. Tourism is such a thematic area, as the different grants that may be granted to it have distinct beneficiaries, policies, methodologies, aims, geographical scopes, supportable activities and project sizes or different dates. As a result, the utilisation, monitoring and evaluation of grants requires careful professional coordination. The following are the support programmes and funds available for tourism development as an area with special integration needs:

– Financing improvement in the Hungarian Fisheries Operational Programme by the European Maritime and Fisheries in the framework of co-financing. The programme supports the diversification of activities of aquaculture enterprises through developing other activities, like transport and fishing tourism. The Economic Development and Innovation Operational Programme supports larger, while the European Agricultural Fund for Rural Development advocates smaller tourism investments.

– The first priority axis of the Territorial and Settlement Development Operational Programme is aimed at the development of the regional economic environment in order to promote employment. The programme links up the achievement of the sixth and the eighth thematic objectives. The essence of a socially and environmentally sustainable tourism development measure is the utilisation and development of local cultural, built and natural heritage sites of regional significance and representing

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tourism attractions, with the aim of creating jobs. The grant can be used for local eco-tourism development, the utilisation of cultural attractions and the development of cycle tracks for tourism.

– As the Rural Development Programme is included in the Common Agricultural Policy, special institutional rules apply. Within the framework of the diversification of agricultural enterprises, tourism can be developed from non-refundable sources. The preservation, maintenance and transmission of the cultural and built heritage and the natural values of rural areas are the engine of the operation of rural communities.

– One of the most important objectives of the Economic Development and Innovation Operational Programme is to increase the employment rate in Hungary. On the one hand, this requires the creation of new jobs, and on the other, there is a need to improve the skills of workers. Further two important objectives of the programme are the focused development of Hungary's innovation capabilities and capacities and of its industry and service sectors. The development of priority attractions based on the heritage development of the programme is realized in connection with thematic objective 6. The support of tourism destination management organisations and tourism marketing and communication activities means one form of enterprise supports under the third thematic objective.

The Economic Development and Innovation Operational Programme supports seven different thematic objectives, covering the areas of Research and Development (R+D), Information Communication Technology (ICT), Small and Medium-Sized Enterprises (SME), the economy with low carbon-dioxide emission, tourism, employment, training and adult and vocational education. The Economic Development and Innovation Operational Programme is supported from Structural Funds, including the European Regional Development Fund and the European Social Fund (Table 2).

Table 2: Distribution of the Operational Programme resources between priority axes

Priority	Name	Thematic objective	Ratio of resources %	Resource, EUR
GINOP 1.	SME	3	18.05	1,581,970,695
GINOP 2.	Research and technology development and innovation	1	19.26	1,687,617,126
GINOP 3.	ICT	2	5.19	454,794,075
GINOP 4.	Energy	4	2.57	225,555,211
GINOP 5.	Employment	8	18.97	1,662,839,216
GINOP 6.	Competitive workforce	10	4.99	437,236,313
GINOP 7.	Tourism	6	4.11	360,532,093
GINOP 8.	Financial tools	1, 2, 3, 4, 8	26.86	2,352,885,426
Total			**100**	**8,763,430,155**

Source: Based on the Economic Development and Innovation Operational Programme

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The seventh priority axis: tourism can be linked to the sixth thematic objective, i.e. the protection and preservation of the environment and the promotion of efficiency in resource utilisation, under the EU2020 aims. In the middle of the priority axis, the protection of cultural and natural resources and the increase of the economic utility can be found.

Areas covered by the seventh priority of the operational programme:

– Network development of cultural and natural heritage sites of national and international importance.

– Development of attractions of international importance which can reach new target groups and can reduce the territorial concentration of tourism.

– The experience-oriented presentation of natural values as tourism attractions is performed with consideration to the load-bearing capacity of the area.

– It is essential to create an independent image, an environment of international standard and supply of the destination at health resorts.

Indicators of the expected outcome:

– Increase in spending by domestic and international tourists from HUF 1,153,109 million (2013) to HUF 1,268,000 million (to 2023) in the less developed region.

– Increase in the expected number of visits at natural and cultural heritage sites and in supported attractions from 352,000 (2013) to 1,660,000 visits/year (to 2023).

Classification of grants, and the accounting of economic events

In Hungary, grants can be classified in many ways (Chart 5), however, in order to explain their accounting, one needs to understand the principle of comparison. According to Section 15 (7) of the Accounting Act, "When defining the profit or loss for a certain period of time, the recognized revenues of the performance in the period concerned of the activities and costs (expenditures) corresponding to such revenues must be taken into account, regardless of their financial settlement" (Act C of 2000 on Accounting).

For accounting, the classification based on the objectives of the grants is relevant because non-refundable grants received for offsetting costs (expenses), non-refundable grants for development objectives and grants to be placed in the capital reserve are recognised differently. The grants received for operating purposes are either support granted for activities not profitable under market conditions or for outsourcing state and local government tasks. Table 3 shows the accounting of grants received for operating purposes.

One of the major problems encountered by accounting experts in recent years has been that costs and expenses were regularly incurred, while successful tenders are typically paid only after completion. Consequently, revenues and expenses are accounted in different financial years. However, the amendment of the Accounting Act reconciled the regulations with the principle of comparability. In the case of post-financing the amount of unpaid grants can also be accrued and deferred against other revenues

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Chart 5: Classification of grants

According to the purpose of the grant

- for operational objective
- development grant
- grant in the form of capital reserves

Based on the financing method

- pre-financing
- post-financing

According to the form of the grant

- paid in cash (in one sum, paid in installments)
- received in the form of an asset
- receivable forgiven

According to the form of financing the grant

- refundable
- non-refundable

Source: Authors' own

Table 3: The accounting of grants granted for activities

Economic event	Debit account	Credit account
Advance on the grant or grant	Liquid assets	Short-term liabilities
Advance transfer	Short-term liabilities	Other revenues
Grants received up to the balance sheet date during the reporting year	Liquid assets	Other revenues
Repayment of grants received in the reporting year	Other revenues	Liquid assets
Repayment of grants received in years preceding the reporting year	Other expenses	Liquid assets
Grants received up to the balance sheet date in the reporting year	Accruals and deferred income	Other revenues
The beneficiary fulfils the conditions and will be granted the grant	Accruals and deferred income	Other revenues

Source: Authors' own

if the entrepreneur is able to prove that it will be able to fulfil the conditions related to grants and it is expected to get the grant. In this case, the entrepreneur must prove that the conditions for accruals and the obligations undertaken in the grant contract have been fully met.

Grants received for development purposes promote long-term business development. In Hungary, post-financing is characteristic in the case of grants received from

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public or other sources. In the case of non-refundable grants granted for development purposes, the principle of comparability is ensured, since revenues can be accounted at the same time as cash flow, which can be deferred as revenue. Deferral is derecognised when the expense is recognised (Table 4).

Table 4: Accounting grants received for development

Economic event	Debit account	Credit account
Grant received for development	Liquid assets	Other revenues
Deferral of grant	Other revenues	Accrued expenses and deferred income
Advance on grant for development	Liquid assets	Short-term liabilities
Reversal of proportional part on approval of settlement	Short-term liabilities	Other revenues
Release of deferral	Passive accruals	Other revenues
Repayment of grants received in the current year	Other revenues	Liquid assets
Repayment of grants received in the years preceding this reporting year	Other expenses	Liquid assets

Source: Own editing

Support granted to the credit of capital reserves affect a relatively narrow circle. Grants received from public appropriations can be recognised in the capital reserve if this is what the grant contract expressly stipulates. These grants must be accounted as equity in the capital reserve simultaneously with the cash flow, and a reserve must be set aside at the time of accounting. These grants cannot be recognised as income. Disbursement of the grant is conditional, the committed reserve must be terminated at the pace and rate the grant is implemented. Grant accounting is detailed in Table 5.

Table 5: Accounting grants in the capital reserve

Economic event	Debit account	Credit account
Grant received for development and to be recognised in the capital reserve	Liquid assets	Capital reserve
Transfer of a conditional grant to the committed reserve	Capital reserve	Committed reserve
Release of the committed reserve on meeting the conditions	Committed reserve	Capital reserve
Reversal of a grant repayable in thie reporting year	Committed reserve	Capital reserve
Repaid development grant	Capital reserve	Liquid assets

Source: Authors' own

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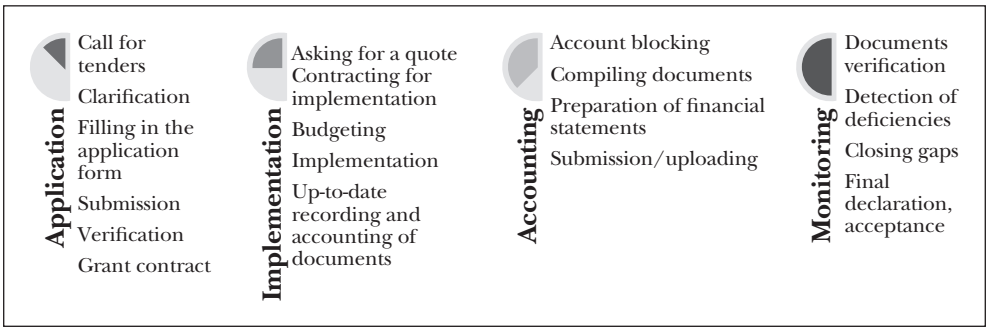
The Administrative Procedures of Grants

For the purposes of the analysed topic, the grant procedure is divided into four main phases. These phases may be managed by separate departments or other organisational units of the enterprise, or by a contracted agency, entrepreneur or other external organisation. They may include official monitoring and authorisation procedures in relation to putting the investment into operation. Chart 6 shows the procedure of tender project management.

Chart 6: Procedures in tender project management



Source: Authors' own

Initially, as step zero, support options should be discovered. In case we opt for a tender, a tender project management is performed.

1. Application: The call for applications must be thoroughly reviewed, each criterion should be considered, making sure that it can be fulfilled within the applicant's capabilities. When the project has been clarified, the application form is filled in, and the application is finalised. As a next step, the board verifies the content of the tender and in most cases there is a possibility to fill in the gaps. If these tasks have been successfully completed, the grant board evaluate and score the application, and if they find everything satisfactory, they approve it. The grant contract is signed after the application and before implementation. In the case of EU funds, the contract is concluded between the managing authority and the applicant, while in the case of national funding, between the granting authority and the applicant.

2. Implementation and project management: The majority of tender invitations require documentation of this phase, specifying form and content. In this phase particular attention must be paid to the requirements set out in the grant contract concerning financial processes. If the project is pre-financed, the collection of the grant amounts must be monitored according to the grant contract. The expected incomes and revenues are reasonably calculated and a financial schedule is compiled to trace and update progress. It is especially important to monitor and verify the compliance of offer requests, orders and the preparation of contracts with suppliers and contractors. The form and content of invoices, certificates of performance, official reports,

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and notes issued during implementation should be correct and in compliance with the contract. They should include the project-related data that allow the clarification of the identity. It is necessary to manage the documentary evidence according to the classification of project elements or in a breakdown by cost groups, and to manage accounts based on the budget of the project and the possible reclassification, and to track booking of the submitted documents. It is an important controlling task to recognise the need for change and modification of frames determined in the budget in time, and to work out a proposal for modification.

3. Accounting phase: In order to support resource utilisation, in this phase a proper accounting and report must be prepared and submitted to the competent or monitoring organisations and to the sponsor. The form and content requirements of the report are determined by the tenderer. In the course of accounting the grants, the summary account must be created in a way to meet both the requirements of the Accounting Act and the needs expected by the sponsor. At the same time, it must be borne in mind that the sponsor's expectations cannot overwrite regulatory requirements. The report may be compiled and submitted via an electronic interface (e.g. in the case of EU financing, the Unified Monitoring Information System, and in case of national financing, the Electronic Tender and Cooperation System) provided by the sponsor, but at the same time a paper-based submission is almost always required, which may include electronic documentation (CD, pen-drive). The submitted invoices must fulfil the formal and content requirements of the grant contract and must be accompanied by the relevant documents (bank statements, ledger statements, payrolls etc.). Most tenders have special rules and many grants involve complicated, over-regulated and over-documented accounting.

4. Assessment phase: Most frequently, an external Intermediate Body, Managing Authority or a Certifying Authority carries out monitoring with the aim to ensure genuineness of the costs reported to the European Commission or to the State, and their compliance with the rules and principles. For the purpose of monitoring, the National Development Agency has published the Interactive Operation Manual, which regulates the monitoring procedure. This first-level procedure based on an itemised verification can (at the very best) justify that the payment claims of the beneficiary are correct, the accounted costs have really been incurred and are satisfactorily supported by accounting and other documents, and meet the formal and content requirements and the objectives and indicators set out in the relevant grant contract. The second-level monitoring may be an on-site audit of the cooperating institution, by the Hungarian Treasury and the Directorate-General for European Aid Audit. The next step can be the final monitoring, carried out before the closure of the operational programme. At this point it is also possible to fill in gaps, and then if everything is found correct, during monitoring, the next steps are the approval of the accounting and the issue of the final or closing declaration.

5. The final phase is project maintenance can be regarded as the closing section, since the Council of the European Union regulates that the projects financed from the European Regional Development Fund (ERDF), European Social Fund (ESF)

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and the Cohesion Fund must be maintained for five, but minimum three years, under the pain of grant repayment, and the beneficiary may be obliged to submit annual project maintenance reports.

Summary

Tourism is one of the most significant sectors and a priority area in the Hungarian development policy. In the EU programming period 2014–2020, tourism development projects can be accomplished in the frame of several operational programmes. EU funs provide possibilities for interactive and experience-oriented projects for visitor centres and nature trails. Grants are available for the renewal of one hundred thousand hectares of habitat, livestock housing and nature conservation site guarding services. Non-refundable grants can be requested for complex tourism development projects in national parks, for attraction improvement and for improvement in conditions of hosting, which can considerably increase the number of visitors. The maintenance of cultural and natural values can be achieved by developing tourism supply based on presenting heritage sites and by increasing tourism revenues.

A large number of grants are widely available in adjustment to topical matters and subject to increasingly specific and accurate legal conditions, while the regulatory and control system is increasingly stricter and more comprehensive. The objectives of the Structural Funds established by the European Union are to improve competitiveness, social and economic cohesion, innovation and information and communication technologies, raise the standards of employment and education, and emphasise the significance of reducing inequality and of sustainable growth. The budget offers the greatest amounts to projects aimed at achieving these goals, while also allowing for environment-friendly options. With a view to these values, in the current programming period eleven thematic objectives have been set in Hungary on the basis of the operational programmes adopted by the European Commission.

In terms of accounting, the recognition of three underlying economic events has been overviewed in this paper. In the case of non-refundable grants for costs and expenses, the cost and expenses incurred and accounted by enterprise reduce the profit, and the amount of the grant can be recognised as other income, not only as in the cash flow account but also if the entrepreneur can prove that he will fulfil the conditions of the grant and it is likely to be granted the support, and thus the principle of comparison is met. In the case of grants received for development objectives, only the amounts actually received can be shown as other revenue. In case of these grants, a problem may arise when the advance granted for the tender is accounted, as until it is finalised, it must be recognised among short-term liabilities. After approval of the accounting of a given implementation stage, the proportional part of the grant must be transferred from short-term liabilities to other revenues. Within the frame of development tenders, enterprises typically generate assets or intangible assets, and the deferred income can be reversed by depreciation. Grants received to the credit of the capital reserve are accounted simultaneously with cash flows and must be transferred

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from the capital reserve to the fixed reserve because these amounts must be repaid if the conditions of the contract are not fulfilled. Contracts specify a monitoring period and when it expires, the fixed reserve can be released and the amount must be reversed to the capital reserve.

In our opinion, there are many opportunities for using grants and they give an opportunity for innovative projects to promote the development of tourism and for reducing the gap. The long-term effects of using grants must be kept in mind as the investment resources included in such grants provide significant financial advantage, but the additional and maintenance costs that are incurred in relation to these investment or development projects must also be considered.

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Judit Sági

Perspectives in Corporate Social Actions and Social and Financial Performance

Summary
The conceptual framework of CSAs in Hungary is evolving in line with the international standards; however, there is a certain delay in conceptualising these actions into a strategic framework in private sector organisations. There seems to be a distinction between for-profit and non-profit stakeholders; the former are characterised by corporate social responsibility initiatives, whilst the latter rely on the sustainability of these initiatives. The author is aware of the fact that these phenomena are likely due to the country being an emerging economy in Europe, and argues that, in a broader context, social actions, if remaining segregated, are insufficient to solve civil society problems. With consideration to social needs (poverty and social inclusion), the arguments for the appropriate targeting and sustainability of CSAs are emphatic, and a shift towards a more strategic concept of social investment is essential. In this perspective, the author argues for the significance of knowledge transfer (i.e. from consultancy partners to civil organisations, or between for-profit organisations) in encouraging networking and increasing the forms of employee community engagement. At the end of the paper, the placing of a project (sign-language distant service to help disabled/deaf persons) into a sustainable and financially sound framework is described.

Journal of Economic Literature (JEL) codes: A13, B55, D64, I31, M14
Keywords: corporate social actions, corporate social responsibility initiatives, social investments

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Introduction

Although not unknown to market participants in Hungary, this topic has been conceptualised in accordance with the international mainstream. There certainly is a gap in the relevant Hungarian literature, and in practice, the forum for corporate social actions is still taking shape: stakeholders no longer have the former links and strategic considerations are still missing from these corporate social actions (hereafter: CSA's). The purpose of this paper is to depict the Hungarian situation for CSAs, with specific focus on stakeholder action.

In this regards, the Hungarian financial authority has a major role in promoting CSAs, among others, in raising financial awareness and training people in financial and business administration. During the implementation of its Pallas Athena Public Thinking Programme, the National Bank of Hungary (Magyar Nemzeti Bank, MNB) set up a strategy to improve financial literacy and financial awareness, and to improve the underlying economic and social knowledge and the related institutional framework and infrastructure. Through its foundations (e.g. Foundation for the Public Good, or Foundation for Financial Awareness), it seeks to play a leading role in the renewal of professional education in economics and finance, and to connect with other institutions and experts while also developing collaboration networks both in and outside Hungary. In MNB's understanding, "corporate social responsibility represents a commitment towards an ethical contribution to sustainable economic growth and the preservation and promotion of cultural and intellectual value, all aimed at improving public satisfaction and the quality of life". In other words, the CSAs of a given institution "comprise voluntary acts aimed at responding to the social and environmental impacts of its operations on a moral basis, thereby contributing to the realisation of goals that serve the interests of the community involved" (National Bank of Hungary, 2014, p. 11).

The author first considers the background of CSAs in Hungary in general, and then the culture of family businesses and the Hungarian context of culture, i.e. the national culture. Bearing in mind the background and the theoretical framework of culture in Hungarian family businesses, the paper then highlights the current practices regarding CSAs in Hungary. Within the scope of this overview, these findings are then discussed and future directions for further research are suggested.

The framework of CSAs in Hungary

The conceptual framework of CSAs has been taking shape in Hungary in line with the international standards. According to the recommendations of the Business Council for Sustainable Development in Hungary, a CEO-led business organisation, the complex interpretation of corporate sustainability encompasses the following (BCSDH, 2013):

– *Strategic approach* – the management of a company should draw up its business strategy with long-term and value-creating economic, environmental and social considerations included, and should provide the resources necessary for implementing such a strategy;

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– *Responsible management* – the executive incentive scheme should include environmental and social goals as well as economic ones;

– *Ethical operations* – the company should operate in a way that respects the law and is ethical (for example, endeavour to be free from corruption and provide fair employment);

– *Respect for human values* – the protection of human life and safety, equality and the right to a healthy environment to be basic values should be taken into consideration when business decisions are made;

– *Environmental responsibility* – the company should be committed to environmental sustainability and should extend this responsibility to the entire supply chain (suppliers, partners and customers);

– *Transparent operations* – information about the company's activities, economic, environmental and social impact and performance should be made available and the company should inform its partners in a regular and credible way;

– *Partnership with stakeholders* – when stakeholders are impacted by its operations, the company should aim to create mutual satisfaction and long-term cooperation and partnerships.

Among the largest companies in Hungary (accounting for 20% of the country's GDP, according to the Business Council for Sustainable Development in Hungary, hereafter "BCSDH"), an increasing number of managers (approx. 80%) consider sustainable development and CSAs in a strategic approach. Good examples are changing product and service portfolios, the creation of shareholder value (Kucséber, 2019), the spread of social responsibility to the entire value chain and donations (Bakó, 2013). The largest improvements have been observed in ethical operations and transparency (Lentner et al., 2017), prompting zero tolerance towards bribery and corruption. The greatest challenges have remained in the government and in responsible management (Kiss, 2018); and there has been a delay in partnership with stakeholders. In the future, the players considered as having a key role in this respect of corporate responsibility are predicted to be the top managers of corporations.[1]

The various concepts of CSAs are reflected in different ways among the market participants in Hungary: in some cases, their actions result in a new business model for Corporate Social Responsibility (Szegedi, 2010), but in most cases they are only about to promote social benefits through donations. There is a certain delay in the conceptualisation of these actions into a strategic framework within private-sector organisations (especially SMEs), which is clear from the ad-hoc and short-term nature of most corporate actions (Hohnen, 2007, Chandler et al., 2017). The author believes that there should be a trend-driven need for CSAs, arising from the strategies of market organisations.

In practice, the challenges rising from the economic circumstances in Hungary contradict the above-mentioned trend-driven need for CSAs. According to the World Economic Forum's Competitiveness Reports, the country is ranked far behind developed ones when business sophistication is (and the macro-economic environment, governmental institutions and labour market efficiency are) considered. The most recent report discussed the most problematic factors in doing business in Hungary,

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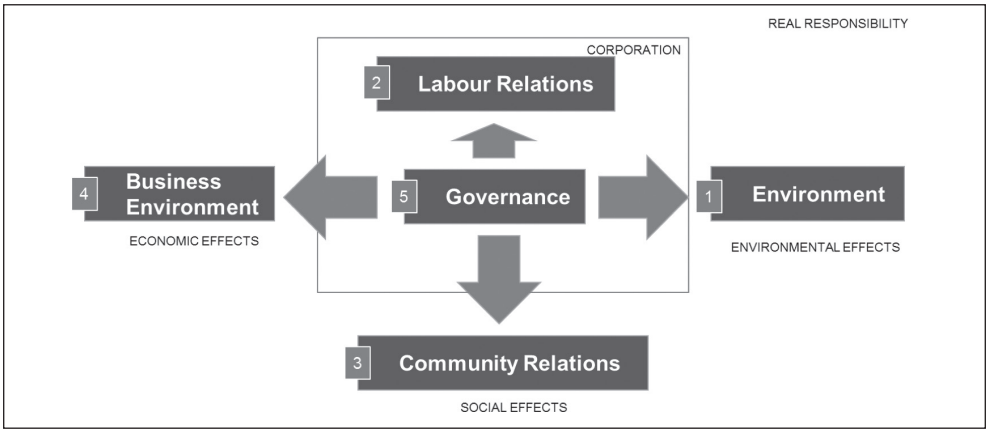
and concluded that political instability, tax rates and tax regulations, inefficient government bureaucracy and corruption are the most significant (WEF, 2014). In an emerging economy the lack of supporting business environment hinders the build-up of a conceptualised CSA strategy, especially when the climate for enterprise does not entertain designs for innovation and business sophistication.

In order to mitigate the risk of failure by CSAs in emerging countries, in 2010 a project called "Enhancing Transparency and Credibility of CSR Practices Through the Establishment of CSR Performance Assessment and Monitoring Systems in New EU Member States" began with the aim to enhance the transparency and credibility of CSR practices. The project successfully laid a basis for country-level CSR measurement and monitoring systems in selected EU member states, including Hungary.

Within this project a handbook was developed as a self-assessment tool of assistance to companies, since they plan to review their CSR policies and reporting practice. It might also be used by civil societies and other stakeholder groups looking for a background to benchmark a company's performance, or by auditors and other corporate advisers on CSR/CSA issues (Dobó and Pintér, 2018). It serves as a *best practice*, since self-assessment may be a mechanism for companies to measure and compare their own performances over time and against peers. Market organisations are able to tailor their approach to verification to fit in the corporate culture, the context, objectives and contents of their CSR strategies and commitments.

The main component of the self-assessment tool is a tailored questionnaire (UNDP, 2010). The questions are classified into five overall categories (Governance, Environment, Labour Relations, Community Relations and Business Environment), and go far beyond the boundaries of an organisation. Each question (indicator) is supplemented by a definition and additional explanations on criteria, documentation, methodology, relevance and practical tips for the users in scoring. In practice, market participants can apply this self-assessment tool with success.[2]

Chart 1: Self-assessment of CSR/CSA



Source: Edited by the author on the basis of UNDP, 2010

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Governance:

– Does the company identify its main economic, social and environmental impacts?

– Does the company have a CSR strategy that defines its commitments to CSR?

– Does the company have designated senior personnel with a clear responsibility for CSR?

– Does the company link corporate responsibility issues to people's performance reviews/appraisals across the company?

– Does the company define key CSR priorities and communicate them throughout the organisation?

Environment:

– Does the company have action plans and programmes to lower its environmental impacts?

– Does the company maintain a monitoring system, measuring the main environmental impacts, especially resource usage and carbon emissions?

– Does the company have a training programme in place to help employees implement its environmental policy and action plan?

– Can the company show a quantifiable reduction in carbon emissions from the previous years?

– Does the company have a recycling programme?

Labour relations:

– Does the company have an action plan regarding labour/human resources and evaluate it on a regular basis?

– Do the employees have official representation in the company?

– Does the company have processes to prevent recurring problems regarding health and safety issues?

– Does the company have plans in place to mitigate the adverse impacts of job reductions?

– Does the company have an effective grievance procedure?

Community relations:

– Does the company have a community engagement action plan?

– Does the company engage in regular dialogue with its stakeholders?

– Does the company actively participate in CSR associations and forums and/or engage with any local NGOs?

– Does the company offer volunteering time, invest in or support any local community initiatives?

– Does the company offer apprenticeship schemes to facilitate skills development within the local community?

Business environment:

– Does the company assess significant suppliers and contractors on human rights, health and safety, anti-corruption and environmental practices?

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– Does the company engage in green procurement practices?

– Does the company have rules and procedures to analyse and counter bribery and corruption practices?

– Does the company have a policy and procedure for making its lobbying efforts transparent?

– Does the company train its staff on ethical supply chain measures and anti-bribery and anti-corruption measures?

As a conclusion, it has become evident that the recommendations made by the international mainstream encourage private sector organisations to formulate their CSA strategies. Although there is a certain delay in this respect, and the business environment is challenging the markets participants, the drive for CSA strategies is clear.

The need for social action

The statistical indicators of poverty and social inclusion published by the Central Statistical Office of Hungary and according to Eurostat evidence need for social actions (Karcagi-Kováts, 2012). The composite indicator of (1) the number of people living in severe material deprivation and (2) the number of people living in households with low work intensity have seriously deteriorated throughout the past years in Hungary. The poverty rate of families with children has remained constant, since children are one of the main target groups of governmental measures designed to reduce poverty. Therefore, the first focus area of governmental interventions is the eradication of poverty and social exclusion.[3] Young unemployed persons and healthcare workers are also included in the thematic focus.

The above-described redistributing function of the government does not contradict the responsibility taken by non-governmental stakeholders in these focal areas (Pintér, 2013; 2018; Pintér and Pintér, 2018). In fact, the extent and timing of private-sector actions is even more substantial in many cases (Carroll, 1983). Participants make investments to reflect social needs, whilst they are not primarily motivated by generating a direct financial return. However, questions remain as to whether CSAs reach the targeted social groups, and solely these ones, with the benefits (Szabó and Pintér, 2015). Within the restrain of imperfect information, the question can be raised: Are social investment budgets spent as wisely as they could be, to generate the greatest possible social return?

The answer goes beyond pure philanthropy, towards a more strategic concept of social investments that involves the stakeholders' engagement and helping to understand the impacts on them by adequate measurements. Completing a social impact assessment can improve the understanding of the social, environmental and economic value that CSA programmes generate. The list of the questionnaire (consisting of 11 themed questions) elaborated by KPMG (2014, pp. 24–25) serves as best practice in this regard.

Within the framework of the corporation's *strategy*, the key questions to be addressed are:

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– What change do you want to create, and what impact do you hope to achieve?

– Why is your business investing in the areas it currently invests in, or plans to invest in?

– Who should benefit from the investments?

– How can progress be measured? What will success look like?

The questions concerning the transparency of social investments via *reporting* are:

– How can you most effectively communicate the story of progress against your objectives?

– Is the data and evidence reported robust and credible?

– What learning can you feed into your ongoing investment strategy, implementation and monitoring processes?

During the *implementation*, the key questions to be addressed are:

– Are all your current investment activities supporting your strategy? If not, can they be redesigned to better align with your objectives?

– Do you have the necessary budget and resources to implement, monitor and evaluate activities?

In the closing phase of *monitoring and evaluation*, the key questions are:

– Are there any existing sources of evidence for progress? For example, existing data on outcomes held by project partners, local government officials or community leaders.

– Are the benefits of your investment realistic? Have you considered the outcomes that could be attributed to other project partners?

Nonetheless, while planning investment into CSAs, certain criteria should be met, for example, those as listed below (KPMG, 2014, p. 15):

– CSAs need to be *supported by effective partnerships* between the market organisation and the community, the non-governmental organisations and the government;

– The social actions must be *sustainable*, originated from the organisation's strategy, and placing emphasis on social impacts;

– Investments into CSAs should be *aligned with business objectives and* local development priorities as well as internal functions that interact with *local stakeholders*;

– *measures* need to be established to quantify the business value of the investment and impact indicators, together with monitoring and evaluation;

– the value generated by the social investment should be *communicated* proactively internally and externally.

One outcome of the social impact assessment can be the build-up of stronger relationships with community stakeholders and project providers (partner organisations). This reflects the importance of an analysis of networking in CSAs.

Current practices in networking and social actions in Hungary

The organisations fostering (formal and informal) networking are described in this section. Among the participants, the Hungarian Business Leaders' Forum (HBLF) is a non-profit association and representative body of local business executives,

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local representatives of international joint ventures and other influential business people in Hungary. It is committed to promoting responsible business practices that benefit business and society, and which help to achieve social, economic and environmentally sustainable development in Hungary. This philosophy serves the interests of the companies, individuals and the society and supports the sustainable development of Hungary through the three pillars of sustainable development: economic, social and environmental well-being for the present and future generations.[4]

Within its aims, the Forum promotes partnerships with members to implement CSR projects and achieve their goals; opportunities for development; and the sharing of best practices and the measurement of results in the business sector. It raises awareness of improved business results in the practice of corporate social responsibility, and their impact on the economy. Furthermore, the Forum advocates sustainable development practices in order to establish healthier and improved conditions for future generations.

Practically, HBLF operates in workgroups; out of which the functions undertaken by the Partnership and Volunteering Workgroup and the Equal Opportunities Workgroup correspond to CSA networking. The former is a cross-sector collaboration (for employee volunteering, donations etc.) among for-profit and non-profit organisations. The latter wishes to draw people's attention to minority issues, especially relating to Romas, to support the equal treatment of all minorities beyond the existing laws and regulations (see also Hungarian Donors' Forum: MAF, 2011).

One of HBLF's initiatives that deserves special mention is the "Give & Gain Day", which is a kind of corporate volunteering day. The idea came from Great Britain, where following the announcement of the British business organisation Business in the Community, thousands of employees carry out various volunteering activities due to the participation of hundreds of companies. The Hungarian event is organised by HBLF, the Hungarian partner of *Business in the Community* in the field of volunteering. On this day, for-profit and non-profit organisations perform useful work for smaller or larger recipient communities. The act of giving carries value not only for the recipient communities but it can also be a lasting experience for the colleagues. The Hungarian experience of corporate volunteering goes to show that such community actions provide a major development force for both the participating individuals and the whole community of associates.

Another organisation that has set the objective of assisting for-profit and non-profit organisation on the road to sustainable development in Hungary is the *KÖVET Association*. KÖVET (literally meaning "delegate", "envoy" or "someone on a mission") promotes environmentally aware business management and preventive environmental solutions to enterprises, and ensures an ongoing exchange of information primarily in the business sector. The organisation acts as a platform to find new ways for industry to reduce its environmental impacts and to promote their use as a basis for a competitive advantage. Their long-term goal is to assist organisations to become sustainable and responsible for society.[5]

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KÖVET is the Hungarian member organisation of the International Network for Environmental Management (INEM), CSR Europe and the Global Footprint Network, through which it is linked to international sustainable business initiatives and projects. KÖVET is an institution that raises awareness and spreads the idea and tools of environmental management and corporate social responsibility.

Another networking organisation in Hungary is the *Centre for Volunteering Association*, which aims at assisting volunteers and their home organisations by providing information, counselling and training, as well as forming the philosophy of volunteering and integrating it into society. The Association has connections both with employees and their employing organisations.

Among its several programmes and initiatives, the Association plays a crucial role through operating a country-wide infrastructure of volunteering that locally coordinates projects, thus helping to meet private persons' willingness to contribute to meeting social needs. Besides this, the Association places emphasis on educating a wide range of people even including primary school pupils and developing their openness to volunteering.[6]

A comparison of these organisations' roles in networking reveals that they interpret the private sector's ability to take part in CSAs and thus respond to social needs in slightly different ways (EC, 2014). HBLF targets profitable corporations and guides them towards best practices in donations and volunteering. KÖVET helps corporations move towards preventive environmental solutions (Tóth, 2009). Finally, the Centre for Volunteering Association is prompting communication between volunteers and those who are in need of volunteers. However, all of these three organisations are committed to long-term sustainability and to the solutions that influence society in the long term.

Lastly, *Pénziránytű Alapítvány* ("Compass for Finance Foundation") was established in Hungary in 2008 with the main purpose of elaborating and implementing programmes for enhancing financial literacy, in cooperation with for-profit and non-profit organisations and governmental authorities as well. Its founders include the Student Loan Centre, the Hungarian Banking Association and the National Bank of Hungary.[7] The mission of Pénziránytű Alapítvány is to help individuals and families by programmes to make informed financial decisions and improve the financial awareness of the population. The Foundation is a non-profit organisation with professional institutions with a reputation and expertise.

Over the years, the Foundation has implemented a number of programmes aimed at disseminating financial and economic knowledge in public education, i.e.: textbook development, content development, teacher training, a secondary-school and an elementary-school network, playful education and the PÉNZ7 (joined the European Money Week initiative).

As a first step in textbook development activities, in April 2016, the Foundation successfully approved its secondary-school textbook *Iránytű a pénzügyekhez* (Compass for Finance), which became the first official financial and economic textbook in Hungarian public education. *Küldetések a pénz világában* (Missions in the World of Money) is the second part of a series intrinsically linked to the modernisation of public education content. This book does not represent theoretical knowledge, but rather dis-

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seminates the logic of practical application, mobilising learners' experiences from everyday life and their families.

In line with governmental intent, the Foundation also attaches great importance to developing teachers' digital literacy and to the delivery of financial literacy through modern methods. Accordingly, the inclusion of e-learning and other digital applications in curriculum development has begun. The Foundation also runs successful in-service teachers' training programmes: the financial courses for secondary-school and primary-school teachers provide free training in several financial topics.

The school network is of great value to the Foundation, as the participating schools are committed to developing students' financial awareness. The BankVelem Financial Instructor Awareness Program offers a complex, hands-on teaching tool that combines sustainability and financial awareness, helps develop students' financial literacy in a playful environment, and contributes to the most important steps of online banking. The BankVelem Traveling School is unique and niche in domestic financial education, as a traveling coaching team "brings home" the player's financial education to schools. Under this program, the Traveling School visits 100 elementary schools each year to improve students' financial literacy through an interactive playhouse. It is important that the program reaches farther located and smaller schools, thus helping peripheral (less developed) areas to catch up.

The PÉNZ7 initiative has achieved remarkable results in recent years: in 2019, 1235 institutions reached more than 205,000 students in extra-curricular classes, doubling their first year access numbers. During a theme week, the Foundation provided full support to the financial lessons at the selected schools. This contributes to the success of the programme for 4 (primary and secondary) age groups, with lesson plans and aids developed by expert teachers and with professional materials to prepare teachers for the lessons, sample lessons and a webinar. The favourable perception of the Foundation's initiatives at schools, and the increasing interest and openness shown by institutions and teachers in financial and economic content are important achievements of the programme. Due to outstanding student participation by international standards, the Hungarian PÉNZ7 initiative received the Global Inclusion Award of the Child and Youth Finance International (CYFI) in 2017, and it was included in the most successful Global Money Week programmes in 2018 and 2019.

Raising the level of financial literacy in the domestic population was formulated as a public policy objective. An inter-institutional working group was set up to outline a comprehensive national strategy, in collaboration with the Foundation, the Ministry of Finance and the National Bank of Hungary. In their corporate social responsibility strategy these institutions have pledged take action in raising financial awareness (Tebeli, 2014).

Conclusions and future directions for research

This paper describes the way the need for corporate social action is linked to networking and how networking is also a crucial aspect of responsible institutions. There are some trailblazing associations in Hungary that offer slightly different solutions in

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responding to social needs. Based on employee community engagements, the author has identified a shift towards skill-based volunteering in the previous years (the benefits are presumably the highest in this form).

For CSAs, the government policy is to support awareness raising and – through the work of, among others, Pénziránytű Alapítvány – to contribute to the education of households. In this regards, CSAs are institutionalised along governmental initiatives.

Consent has been found among market participants to move towards a more strategic concept of social investments, which involves the stakeholders' engagement and is instrumental in understanding the impacts on them. Completing a social impact assessment can help size up the social, environmental and economic value that CSA programmes generate.

Notes

1 "We believe that the key to the long-term success of a company is having a CEO and a management team who are aware of the concept of sustainable development and are able to interpret it in a complex way during decision-making." István Salgó, President, Business Council for Sustainable Development in Hungary (BCSDH, 2013). "Having expressly declared sustainability principles at a company suggests leadership in strategic thinking, commitment and a high level operational culture." Attila Chikán Jr., CEO, ALTEO Energy Services Plc. (BCSDH, 2013).

2 "What I have learned is that there is an abundance of policies in the company. Now reading them for the self-assessment makes me think that there is a need to streamline our policies and map the potential white spots. I am going to draw the attention of the relevant colleagues to this", revealed a large company representative from Hungary (UNDP, 2010).

3 The Hungarian government helps people with special social needs through a variety of care services. Special relief compensation and income support are available to those below a statutory income level for the payment of certain expenditures. Additionally, complex programmes promote the integration of disadvantaged children, including scholarship programmes in the case of multiply disadvantaged learners. The government is also about to adopt and continue a number of measures to prevent the passing on of social disadvantages and to promote social security. Improvement in the labour market prospects of disadvantaged groups is also of primary consideration.

4 The mission of HBLF is to encourage companies to integrate corporate social responsibility and the principles of sustainable development into everyday business practice. Members of HBLF promote responsible leadership for the long-term prosperity of their businesses and the whole of society.

5 www.kovet.hu/en/about-us.

6 www.oka.hu (Centre for Volunteering Association).

7 https://penziranytu.hu/magunkrol.

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Ferenc Molnár

The Role of Electricity in Sustainable Energy Supply

Summary
Ever since the dawn of history, humans have always needed energy, used it in a gradually growing number of fields and found new forms to meet their ever increasing demand. It is no exaggeration to claim that in the absence of energy, the very means of subsistence would cease to exist for today's urbanised society. Nothing would function without electricity: neither the control systems run by IT tools, nor the core and auxiliary equipment of the fundamental supply and care systems. In the absence of electricity, water and natural gas supply would stop, ventilation systems would become inoperable, transport and traffic would shut down, and in the absence of illumination, everything would go dark, buildings would not be heated and cooled, both industrial and agricultural production would stop, the supply of drinking water and food would become unfeasible, communication and security systems would become inoperable, and law enforcement could not attend to their duties either. In other words, the absence of energy would lead to an economic and social disaster. After a description of climate change, the article gives a glimpse of the energy policy of the European Union, and outlines the main pillars of Hungary's new energy strategy.

Journal of Economic Literature (JEL) codes: O13, P28, Q54
Keywords: energy, sustainable development, carbon dioxide, environmental protection, climate change

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Energy appetite and global warming

Today's population of nearly 8 billion consumes multiple times the maximum amount of energy needed for sustainable development. Humanity, rapidly growing in number, is depleting the Earth's energy supply and destroying its natural environment by a ruthless use of energy. If the current trend of "development" in civilisation is not reversed, in the foreseeable future we will eliminate the preconditions of survival for the future generations. It is an apt commonplace that we do not own the Earth; we have only borrowed it from our grandchildren. The damages caused by civilisation include the myriad of diseases and human deaths caused by climate change and pollution, resulting from global warming. The availability of energy is the driving force behind economic development. According to Elkington, sustainable development is based on the optimisation of environmental, economic and social sustainability for companies (Borzán and Szekeres, 2017). For the sake of maximum short-term economic growth, the individual economic operators disregard the environmental aspects that ensure long-term living conditions. This can only be offset in nominal terms by certain processes, such as integrated urban development plans (Pintér, 2015).

The 28 countries of the EU have a population of over 512 million. As the population grows, the use of primary energy will also increase, but energy consumption will increase at a much faster pace. In retrospect, according to a survey in 2000, 16% of the population was already using 80% of the total amount of energy consumed. According to research conducted at the University of California, the largest emitters of carbon dioxide are transport, with 49% and the power sector with 30% (Hejazi, 2017). According to the International Energy Agency, in 1980 the Earth's population consumed nearly 7300 million tonnes of oil equivalent (Mtoe). This value increased by more than two-thirds in 2008 to 12,300 Mtoe (IEA, 2010). Already between 1980 and 2008, there was a strong upward trend in primary energy consumption.

By 2040, the energy demand of the Earth's inhabitants will increase by 25% of the value of 2017. Without energy efficiency measures, this would double the amount of energy consumed in 2017. India's energy consumption could grow nearly double, while China's consumption could increase by nearly one-fifth over the same period.

In the context of sustainable development, the rising share of electricity in final energy use will play an increasingly important role in maintaining clean air, reducing pollution and improving climate parameters. Total electricity generation is projected to reach 45% or 37000 TWh in 2040.

The share of renewable energy sources will almost triple to 66%. Solar and wind farms are expected to see the greatest increase in energy production. By 2025, more than 80% of new capacity expansion is projected to come from renewable sources.

The average carbon intensity of electricity production is expected to decrease globally. From the current 500 grams of CO_2 per kilowatt hour, the target for 2040 will be reduced to about 70 grams of CO_2 per kWh. This is mainly due to the increasing share of electricity in final energy use.

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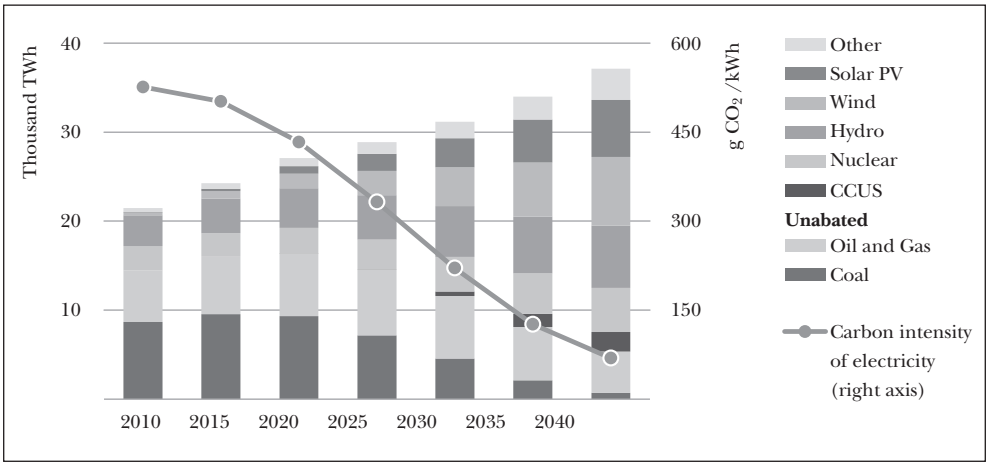
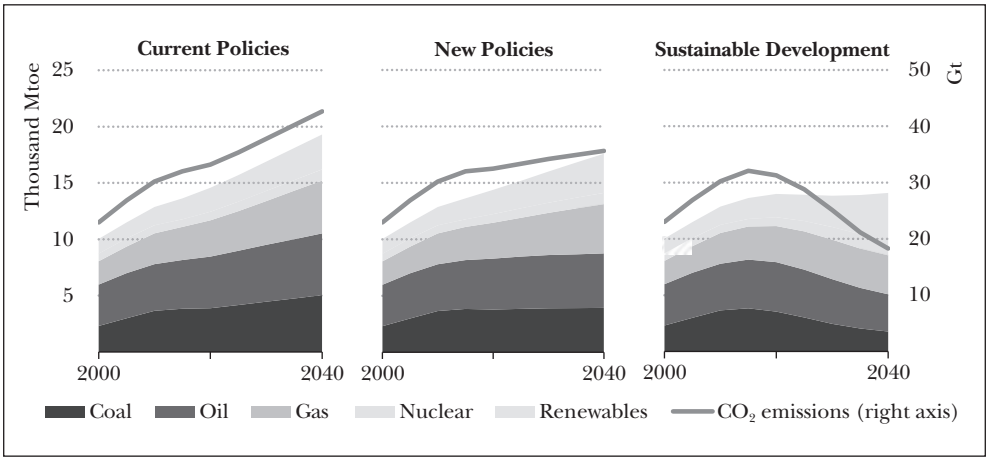
Chart 1: Electricity generation and carbon intensity in sustainable development



Source: IEA, 2018, p. 93

Chart 2: Global primary energy demand by fuel and energy-related CO2 emissions by scenarios



Source: IEA, 2017, p. 78

It follows from these quantities that the Earth's energy reserves are being exploited at a disastrous rate. More than 70% of the energy consumed comes from fossil fuels. The proportion of nuclear and renewable production is a fraction of that of fossil-based applications.

Another, even more serious impact on life on our planet is the acceleration of global warming and the consequent irreversible climate change.

Most energy sources contribute to climate change. There is a worldwide trend of increasing use of fossil fuels in proportion to the increase in energy consumption. Of course, this will also increase the amount of greenhouse gases released into the Earth's

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atmosphere and the amount of gases that are accumulated there. Energy-related carbon emissions have increased from 18.7 billion tonnes in 1980 to 29.4 billion tonnes in 2008 (IEA, 2010). In 2017, carbon dioxide emissions from energy use amounted to 32.581 billion tonnes (IEA, 2018). In 2007, the populations of developed and developing countries had a share of 4.5 toe and 0.7 toe per capita on average, respectively (Tashimo and Matsui, 2008). Most of the energy used today still comes from the burning of fossil fuels, which is also the main source of carbon dioxide emissions.

The global energy trend is driven by the free market, the uncertainties of the political and financial systems, and the impact of the media on users who lack knowledge. Despite the difficulties of long-term energy planning, it is clear that coal-based electricity production will continue to play a leading role in the world outside Europe. In addition to coal, the use of natural gas will continue to be the dominant fossil fuel (Járosi, 2018).

The greenhouse effect is a natural process that provides the atmospheric temperature needed for the Earth's current wildlife. A smaller portion of the sun's rays are reflected back into space, reaching the Earth's atmosphere. Most of the energy coming from the sun enters the atmosphere, warming the surface of our planet.

The temperature required for life is provided by the accumulation of greenhouse gases (GHGs) in the atmosphere of the Earth, by reflecting off, i.e. trapping, a portion of the amount of heat that leaves the atmosphere.

Greenhouse gases include water vapour, carbon dioxide, methane, nitrous oxide, ozone and some artificial chemicals such as chlorofluorocarbons (CFCs). Human activity increases the atmospheric concentration of GHGs, which increases the greenhouse effect, thus accelerating the warming of the atmosphere.

The most important such human interventions are the burning of fossil fuels (coal, oil and natural gas), agricultural activities and deforestation. The main source of greenhouse gases is the combustion process. Of the gases produced by combustion, carbon dioxide is the largest contributor to our environment. The amount of carbon sequestrated over hundreds of millions of years returns to the natural environment in a concentrated form within just a few centuries. This situation is exacerbated by the fact that 300 hectares of rainforests are lost per hour due to humanity's over-consumption and the pursuit of profit.

The natural environment on Earth is thus exposed to numerous dangers and is highly vulnerable. The most devastating process is the global warming of the Earth's atmosphere. Climate change is a direct consequence of global warming. The greatest challenge the human race is facing in the 21st century is addressing the consequences of climate change. The measurements performed in recent years show that the Earth's average temperature has risen by more than 2.5 degrees Celsius. If this trend continues, the number of starving humans will increase by more than eighty million, and more than a quarter of all the mammal species and more than a tenth of the bird species will completely disappear (Hejazi, 2017).

The most obvious solution for reducing carbon dioxide emissions is to increase the utilisation ratio of carbon-free energy sources used in power generation. The use

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of nuclear and renewable energy sources should reduce the proportion of fossil fuels. The carbon dioxide emission of the entire nuclear, solar and wind energy chain is the same, i.e.2-6 gr / kWh. This includes the manufacturing, construction, operation and maintenance processes. Electricity offers the potential to increase energy efficiency through the use of a high degree of automation and smart solutions (Hejazi, 2017).

A glance at the European Union

The European Union's climate protection measures included drafting Directive 2009/28/EC. The directive sets out the exact figures for each Member State's contribution to the use of renewable energies. This means that by 2020 an average of 20% of the EU's gross energy consumption should come from renewable energy sources, including 10% in the transport sector. The 20% average is the average of the individual commitments by all Member States.

In 2016, the European Commission compiled the PRIMES (Price-Induced Market Equilibrium System) energy system model, which aims to support Clean Energy for All Europeans, also known as the Winter Impact Study (European Commission, 2016a). The study analyses the relationships between decarbonisation activities up to 2030, but also provides an outlook to 2050 (European Commission, 2016b). It examines whether or not the competitiveness of the European Union can be maintained in the context of the changing energy market conditions as it is moving towards a low-carbon economy. Electricity generation, energy efficiency and renewable energy are the pillars of transition to a clean energy future (European Council, 2014). The ETS (Emissions Trading System) serves to decarbonise the European Union's energy system by reinforcing the impact of policy measures.

The interaction of synergies was performed by a quantitative analysis using sophisticated methods. The Impact Assessment is an accompanying document to the programme packages prepared for the institutions of the European Union, and relies on two policy scenarios: EUCO27 and EUCO30 (the European Council's two scenarios for achieving 27% and 30% energy efficiency, respectively). It is a review of electricity market rules and risks. EUCO33; 35; 40 (the European Council's 33%; 35% and 40% energy efficiency scenarios) set even more ambitious targets to be achieved by 2030. The EUCO3030 scenario includes plans for an increased ratio of renewable energies in the EU energy mix.

Each scenario aims to help the European Union develop its energy strategy for 2030 and set goals and actions for achieving a low-carbon economy by 2050. All the decarbonisation scenarios are in line with the 2015 Paris Convention, which foresees more than 80% reduction in greenhouse gas emissions by 2050 compared to 1990 emission levels.

Each scenario confirms, in numerical terms, that carbon market pricing has a clear carbon impact and contributes to the development of renewable technologies.

The various energy efficiency scenarios of the EU endeavour to reduce energy consumption.

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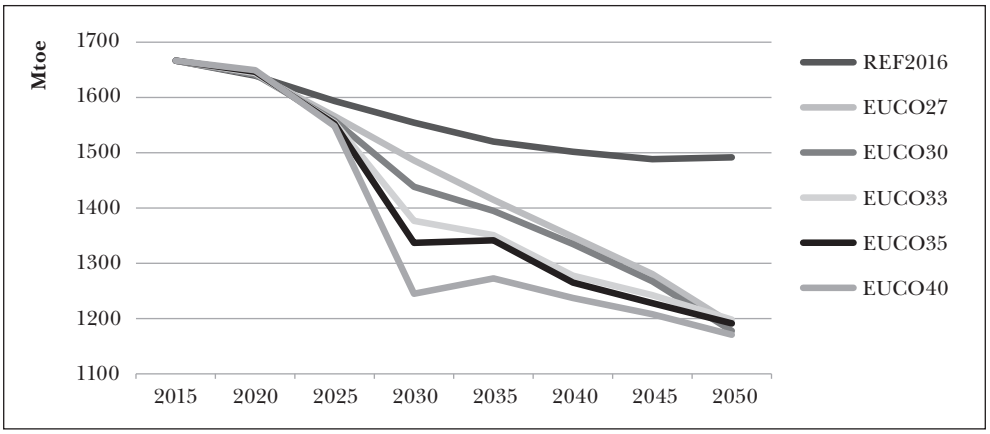
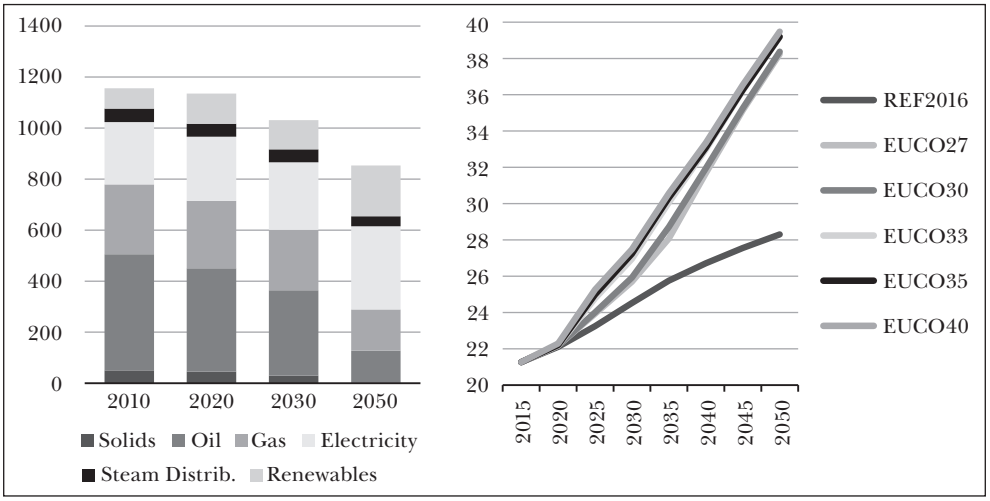
Chart 3: Energy demand in the EU28 according to different scenarios



Source: Capros et al., 2018

The share of electricity in the decreasing final energy consumption is increasing.

Chart 4: The ratio of final energy demand (Mtoe) (a) to electricity in EU28 (b)



Source: Capros et al., 2018

Among the countries of the European Union, Germany is the flagship for the use of renewable resources. The leadership of the country intends to further strengthen this position. At present, it has nearly 106,000 MWp of wind and solar power installed capacity. By 2030, further significant expansion of solar energy sources producing in sunny periods is planned. The diagram of power generation structure illustrates appreciation in the role of regulatory capacities as a result of increase in the share of weather-dependent renewables by 2030. The hectic avail-

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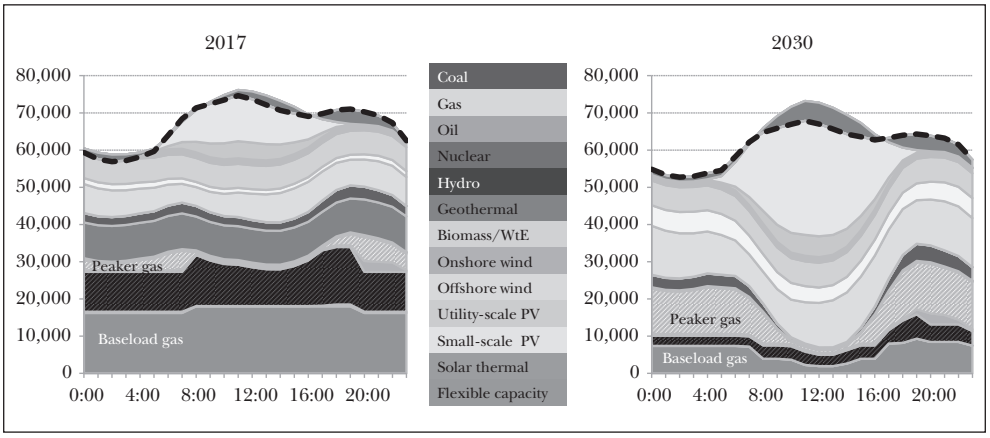
ability of solar and wind energy is for the most part planned to be tailored to the needs of consumers by gas turbines and imported energy. Regrettably, the GHG-free, economically viable source of clean energy as a basic nuclear power plant is missing from the production structure projected for 2030. Germany has already become incapable of meeting its commitments made to the European Union as it has cut its nuclear production, and so its energy and economic policies need urgent reconsideration.

Chart 5: Germany's daily electrical load curve for 2017 and projected for 2030



Source: Bloomberg, 2017

If the EU Member States shut down their existing nuclear power plants, the fossil fuel power plants that replace them would release 700 million tonnes of additional carbon dioxide into our Earth's atmosphere every year (Hejazi, 2017).

Reduction in the EU's energy-related carbon dioxide emission is primarily expected in the energy supply sector: in 2050 only the transport sector is expected to use oil. The use of natural gas in the industry and in the energy consumption of buildings may remain to some extent. The sectors covered by the ETS (Emission Trading System) are expected to have a much larger emission reduction effect than the sectors outside the ETS (Capros et al., 2018).

The feasibility of predictions is worth examining in the light of current global trends. The factual data registered globally up to 2017 shows an increase in carbon dioxide emissions in proportion to the steady increase in energy demand.

British Petrol's (BP) *Energy Outlook* also forecasts reduction in final primary energy consumption in its prediction for the European Union for the period up to 2040. The forecast expects a significant increase in the share of renewables and a drastic cut in the use of carbon-based energy, which also contributes to Europe's depletion of its coal reserves. In addition to transport, oil consumption is expected to remain significant in the chemical industry, but a downward trend can be brought about by increased energy efficiency and e-mobility (British Petrol, 2019).

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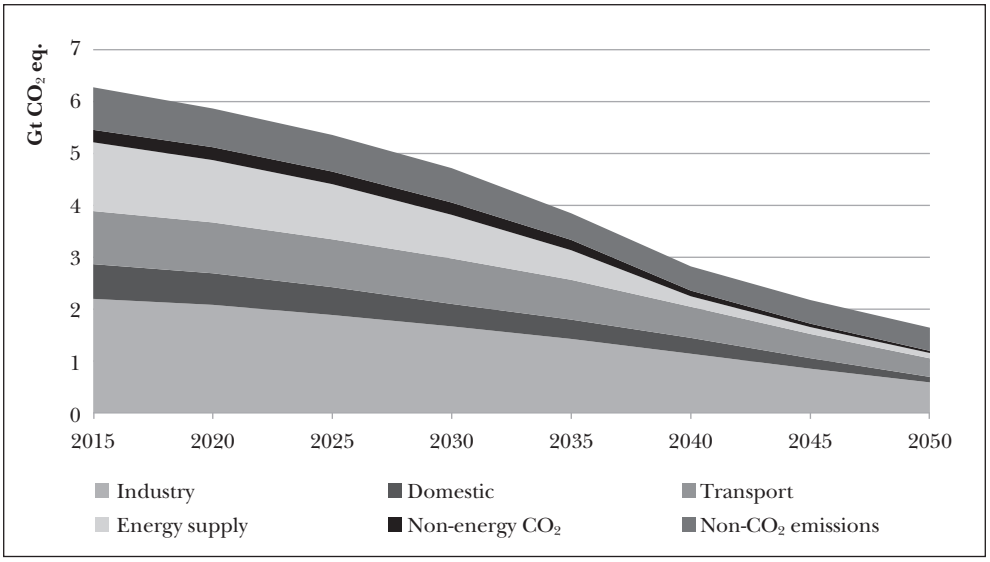
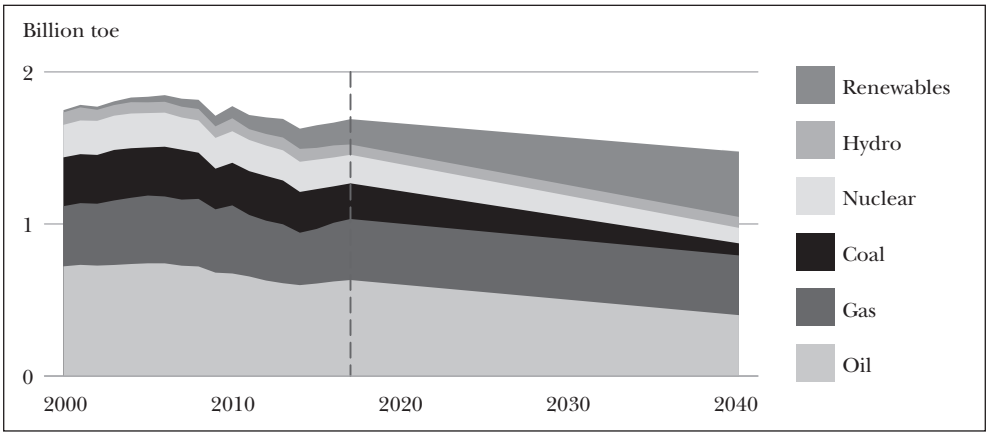
Chart 6: Greenhouse gas emission targets for the EU28 according to the EUCO27 scenario



Source: Capros et al., 2018

Chart 7: Expected evolution of primary energy needs up to 2040, Gtoe, EU Member States



Source: British Petrol, 2019

The expected share of electricity generation also shows significant restructuring by 2040. The growth of renewables is unstoppable. Unfortunately, the ratios of hydropower and nuclear sources, which produce clean energy, are expected to decrease in the primary energy mix. The regulation of renewables and nuclear substitution are also expected to generate additional carbon emissions. The ratio of carbon will decrease, but it will still have a significant impact on atmospheric pollution in terms of climate protection (British Petrol, 2019).

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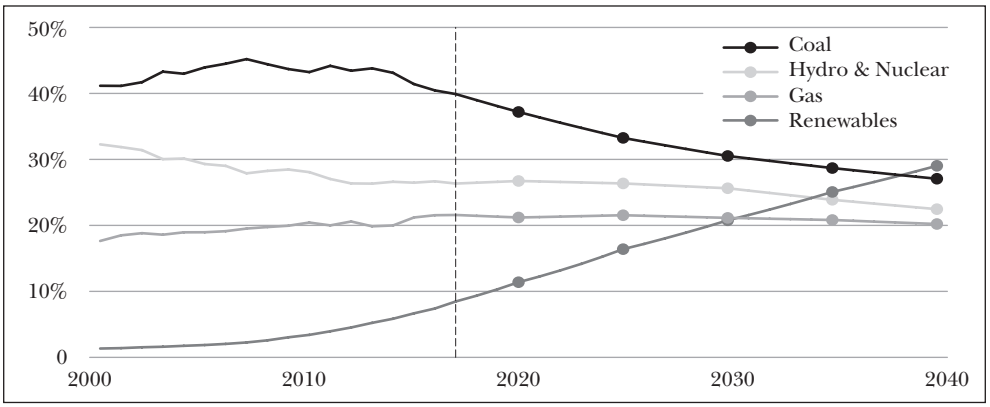
Chart 8: The expected share of electricity production in electricity generation by 2040



Source: British Petrol, 2019

Hungary's new energy strategy concept

In October 2018, Hungarian Parliament adopted a National Energy and Climate Plan (Ministry for Innovation and Technology, 2018), which is in agreement with the Paris Agreement. In December 2018, the government adopted the concept of a new energy strategy that integrates the adopted climate and energy policy. The energy sector is undergoing a radical change worldwide. In this accelerating transition, the policy intends to create a consumer and climate-friendly energy sector in Hungary. Energy use is responsible for more than 70% of greenhouse gas emissions, both internationally and domestically. The competent ministry estimates that one way to reduce the need for oil and gas imports is to use renewable energies and save energy. The government envisages the 3D principle for the development of the electricity sector: decarbonisation of the electricity sector, decentralisation of household and industrial renewable generation and digitisation, or the spread of digital technologies.

The targets set by European Union's technical committees include a 40% emission reduction target at an EU level by 2030 and 80% by 2050 compared to 1990 emission levels. The second National Climate Change Strategy, released in 2018, requires the reduction of emission in Hungary by at least 52% and at most 85% by 2030, compared to 1990 emission levels. The 40% reduction set in the relevant EU requirements means that Hungary will emit maximum 56.28 million tonnes of carbon dioxide per year in 2030. In 2017, Hungary's emission was 64.44 million tonnes of carbon dioxide (Ministry for Innovation and Technology, 2018).

Hungary's energy policy is based on the European Union's energy strategy objectives. However, its objectives and related measures are shaped by the characteristics of domestic energy producers and the country's economic policy without excessive dependence on the European Union. Thanks to the development of nuclear and renewable energy capacities, Hungary will be able to reach 90% carbon-free electricity production by 2030. However, achieving full domestic carbon neutrality can only be

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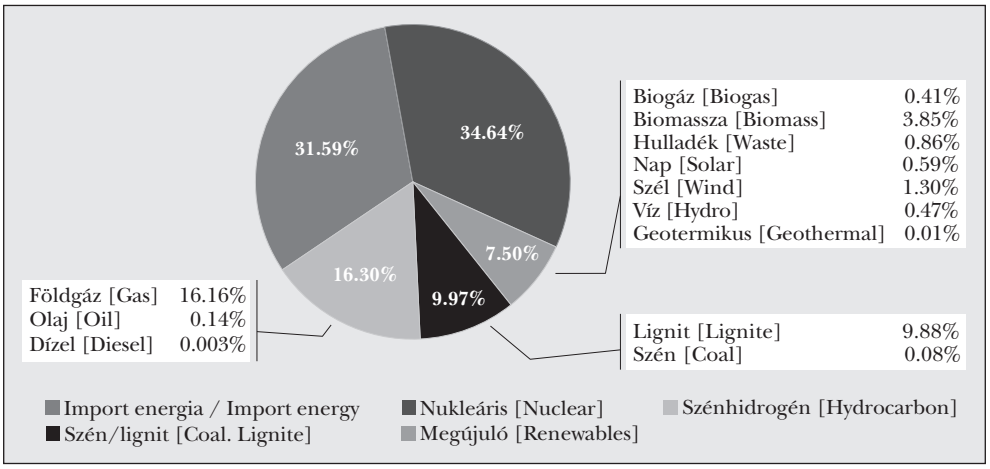
achieved if the competitiveness of the Hungarian economy and the overhead costs of Hungarian families are also taken into account (Portfolio, 2019.)

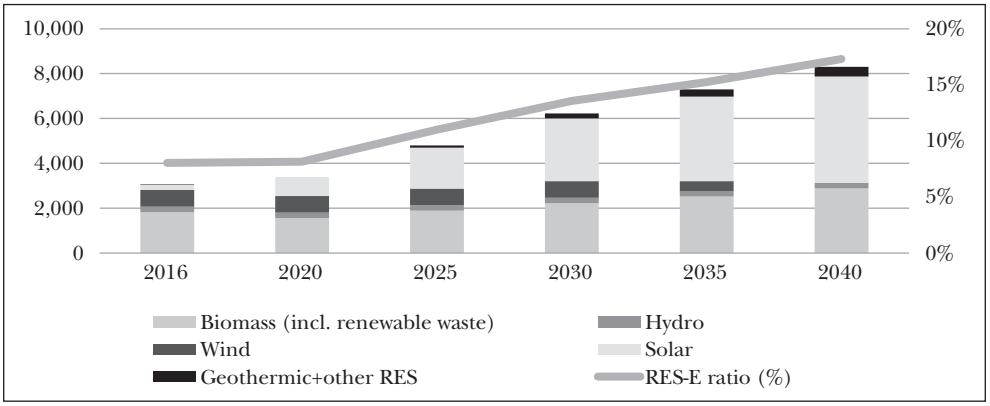
Chart 9: Distribution of domestic gross electricity consumption in 2018



Source: Mavir, 2019

Decarbonisation also involves the exploitation of renewable energy sources. Hungary has committed to raise the ratio of renewables to gross domestic product to 20% by 2030. In the field of electricity generation, the competent ministry is planning to expand the current capacity of nearly 1200 MWp of solar power to about 7000 MWp of installed solar power by 2040. Within this, the share of residential production may increase from the current 400 MWp to 1500 MWp. This degree of decentralised renewable expansion will necessarily bring about the development of electricity networks and their resilience.

Chart 10: Forecast renewable electricity generation (GWh), incl. the RES-E ratio (%)



Source: Ministry for Innovation and Technology, 2020

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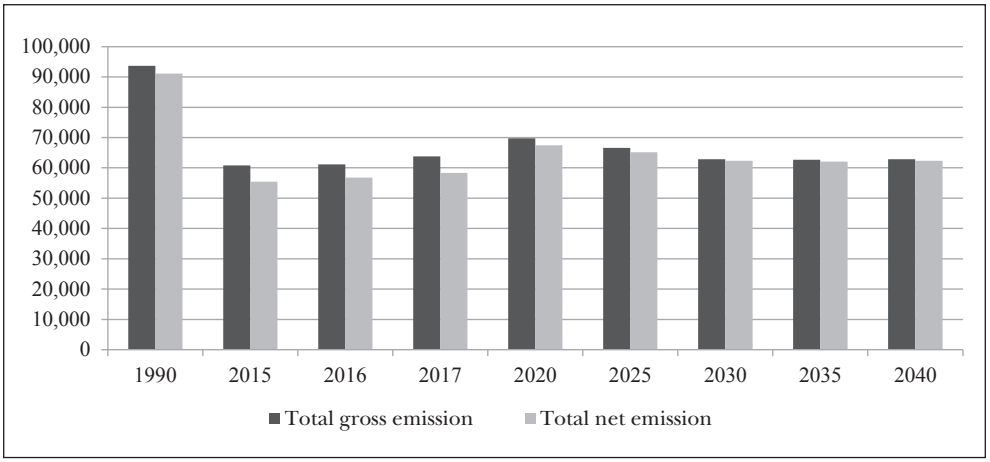
The use of nuclear energy is indispensable for the achievement of the Hungarian energy policy goals.

The Paks Nuclear Power Plant produces the cheapest and cleanest electricity in the Hungarian power generation structure. The security of supply is guaranteed by an average power utilisation rate of over 90% per annum and a sufficient supply of strategic fuel for 2 years. In a nuclear power plant, the cost of fuel is about 15% of the cost of the generated electricity, i.e. a change in the price of nuclear fuel has little effect on the price of electricity produced. As, however, the licensing and provisioning process of nuclear power plants is rather long, replacement of the current capacity, approaching the end of its life cycle, must be resolved as soon as possible by the construction of Paks 2 (Ministry of National Development, 2012).

Chart 11: Forecast GHG emission by the energy sector, incl. the impact of the current policy measures (kt CO2eq).



Source: Ministry for Innovation and Technology, 2020

The competent ministry also intends to involve consumers in carbon-free production using renewable sources, encouraging them to meet their own energy needs, possibly using their own storage capacity and smart devices, thus contributing to the stability of the electricity system. The merger of 'producer' and 'consumer' activities will thus lead to the emergence of the 'prosumer', the active user.

The main elements of the new energy strategy concept are as follows:

– Placing the consumer at the heart of the energy strategy,

– Ensuring the sustainability of utility cuts,

– Improving the security of supply and increasing the use of resources located in Hungary,

– Climate-friendly transformation of the energy sector,

– Encouraging energy innovation for carbon neutrality, including smart technologies, energy storage, etc.

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– The government gives priority to domestic solar energy utilisation: it supports the installation of small-scale household power plants. Small and medium-sized enterprises provide their own energy supply from renewable sources and promote the development of cost-effective renewable power plants on an industrial scale.

Industrial scale power plants with a rated capacity of 50 MW or more require a production license for the generation of electricity. Above the threshold of 0.5 MW nominal power, a combined power plant license is sufficient (Szuchy, 2018).

Hungarian Energy Strategy 2030, with an outlook until 2040

The Hungarian Energy Strategy 2030 completed in 2011 was made to become the foundation document of the domestic energy policy. As part of the European Union, Hungary has to take part in accomplishing the actual EU energy strategy. The changes of the past decade and new European trends have made the upgrading of the Hungarian Energy Strategy 2030 inevitable. The document was adopted on 19 January 2020, as a result of several years of preparatory work. Its major objectives are creating energy independence in parallel with maintaining the security of supply, as well as decarbonisation while retaining energy consumption cost reduction. In the year 2019, the ratio of imported electric energy use in total domestic electric energy consumption was 27,56%, which is equal to 12,59 TWh (Mavir, 2020). To accomplish those objectives, the ministry in charge plans to upkeep nuclear energy production capacity and increase renewable-based energy production. A considerable growth of renewables is expected through utilizing solar energy. Among other renewable energy sources, there are further potentials for capacity growth in the use of biomass, biogas, water energy and geothermal energy with the application of novel technologies. Innovation must play a major role in this, which is a factor that is especially in the focal point of energy policy. Innovative solutions may help the spread of decentralised solar power stations. The new production structure dissimilar to the present one together with novel energy flow directions will generate transformations in the system of electrical power grid. The significant increase of weather-dependent producers will necessitate the development of flexibility capacity. This means the establishment of modern energy power reservoirs and additions the existing gas turbine range. It is practical to substitute the withdrawing coal-fired generator Mátra Power Plant with technologies facilitating the resiliency of the power grid. The system security of the upgraded production structure and the enhancement of energy efficiency puts the application of smart solutions to the foreground.

To provide for our continuously growing energy need, Paks Nuclear Power Plant plays an indispensable role. Almost half of the energy production in 2019 was provided by the nuclear power station. The extended operating time valid today will expire between 2032 and 2037 in case of all four blocks.

The investment in Paks 2 capacity maintenance is an essential condition to secure energy provision and to produce 90 percent carbon-neutral electric energy that Hungary has made a commitment to.

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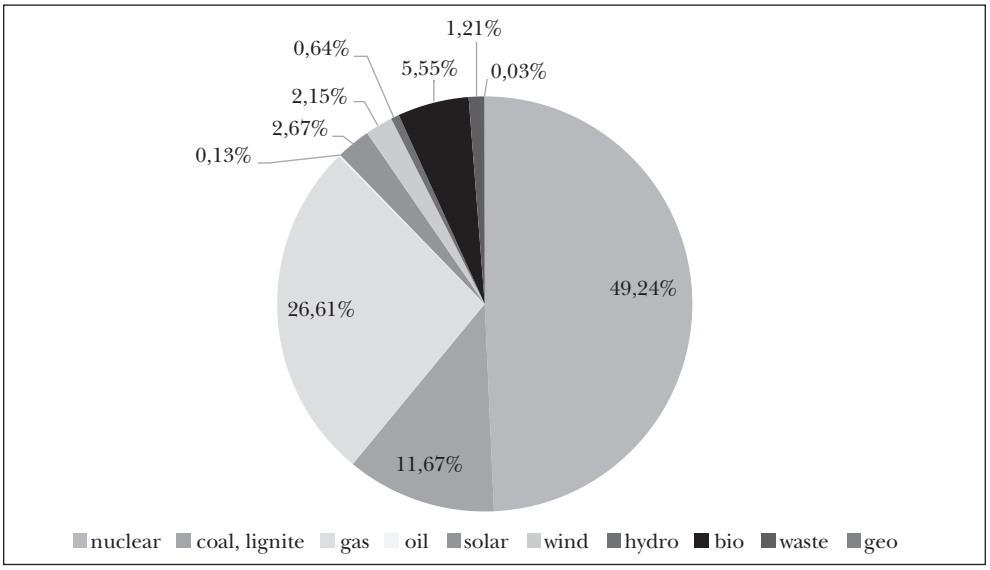
Chart 12: The structure of domestic electric energy production in 2019



Source: Mavir, 2020

For Hungary, it would mean an extra expenditure of 50.000 billion Hungarian forints to achieve full climate neutrality that the European Union expects all member states to implement by 2050.

The following is a short summary of the objectives of the most recently approved national energy strategy expressed in numbers.

32,5 percent of our ultimate energy consumption is based on natural gas. 80 percent of our natural gas need come from import. Due to energy efficiency measures, the introduction of biogas and Renewable District Heating Program, and the transformation of electric energy production structure, the planned proportion of natural gas import will reduce to 70%. By 2040, it will fall below 70%. Between 2013 and 2017, our import energy consumption was 32% on average. As a consequence of expansion in nuclear energy and the incentive for renewable-based production, domestic production proportion will reach 80% by 2040, according to the plans of the ministry in charge. 90% of production is expected to be carbon-neutral already by 2030. A portfolio of more than 6.000 MW solar power station targeted for 2030 is anticipated to rise to 12.000 MW by the document of the Hungarian Energy Strategy. A crucial element of the programme is that the energy produced in a decentralized way must be used in the area of production. By 2030, the proportion of renewable energy consumption will be a minimum of 21% of the ultimate energy consumption. Our emission of greenhouse gases will reduce to 40 percent of the figure in 1990 by the year 2030.

The Committee of Energetics Innovations puts special emphasis on nuclear innovation besides system balance, energy efficiency and renewable-based production. Apart from gaining more experiences in the field of nuclear energy, further plans

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include the establishment of Fuel Rod Laboratory, a Nuclear Decommissioning, Materials Science, Radioactive Waste Management Centre for Learning and Paks 2 Virtual Training and Practice Centre.

Innovation development works have a significance beyond their technical and economic effect, expanding employment and common knowledge equally.

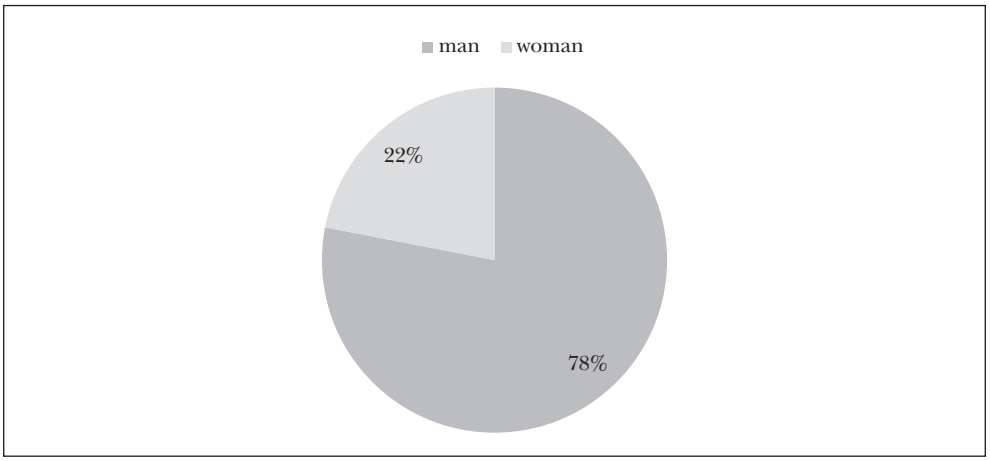
Primary research

Methodological background

A nationwide survey was conducted by quantitative research between October 2018 and April 2019, and over 300 people were asked. The questionnaire was dispatched electronically. Uniform evaluation based on identical bases was ensured by response options provided next to the closed questions in the questionnaire, which was drafted coherently in content and form. Efforts were made at wording the questions without offending the feelings or the privacy of the potential respondents. Particular attention was also paid to not reducing respondents' willingness to answer, and rather, to ask questions that arouse their interest in the topic. It was also important to conduct research in a field not yet surveyed on a national scale: the awareness of the general public of the individual energy sources, their benefits and potential risks. 287 online questionnaires sent by e-mail were completed fully and correctly. For the analysis of the database collected on the online interface, statistical data sorting was performed by SPSS 21 (Statistical Package for Social Sciences).

The responses were evaluated on the basis of the cross tables generated by the SPSS 21 software. Perhaps due to the nature of the topic, the vast majority of the respondents were men: 224 men and 63 women completed the questionnaire.

Chart 13: Distribution of respondents by gender



Source: Author's own research, 2019, N = 287

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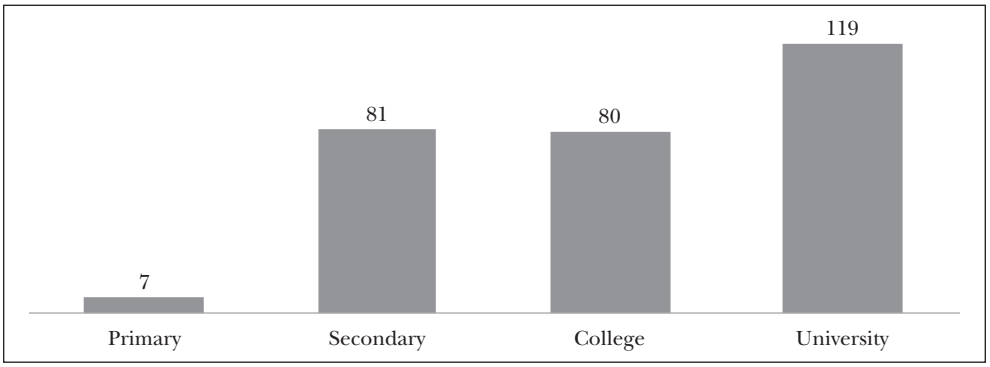
A breakdown by age group shows the highest representation in Generation Y. Generations BB and X contributed almost equally to the questionnaire. Due to their low number, the respondents born before 1946 (2 persons) or after 2000 (7 persons) cannot be considered relevant. The eldest generation is likely to have difficulties managing the online interface, while the youngest ones may not be interested enough in the topic. It is promising that the 7 respondents of the generation born after 2000 already feel it important to support research. In what follows, focus is on the generations significantly represented in the survey.

Chart 14: Distribution of respondents by age

Source: Author's own research, 2019, N = 287

In a breakdown by qualifications, the number of returned questionnaires is proportional to increase in the level of education: the ratio of university graduates was the highest among the respondents. Respondents with only primary education are likely to be predominantly from the youngest age group.

Chart 15: Distribution of respondents by qualification



Source: Author's own research, 2019, N = 287

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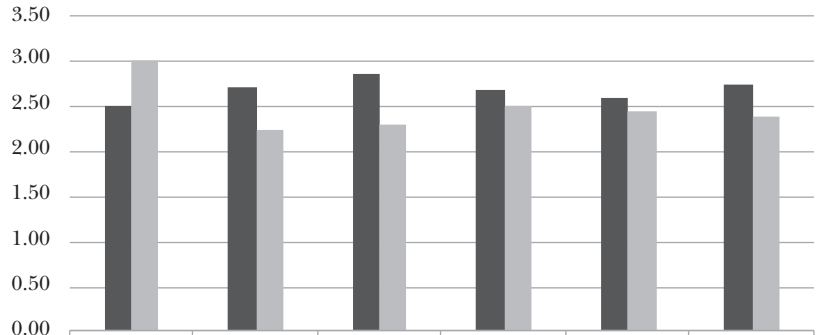
Findings

One of the questions asked during the research concerned the importance using coal, lignite and natural gas in the production of electricity. The answers were analysed according to the ages of the respondents and the following results were obtained with the help of an SPSS program cross-table.

Chart 16: Assessment of the importance of coal, lignite and natural gas in Hungarian electricity generation by the age distribution of respondents



	before 1946	1946–1964	1965–1980	1981–1999	after 2000	Total
Natural gas	2.50	2.68	2.83	2.67	2.57	2.71
Coal and lignite	3.00	2.23	2.29	2.50	2.43	2.37

Source: The author's own research, 2019, N = 287

Respondents born between 1946 and 1999 rated the importance of coal, lignite, and natural gas at a weighted average below 3. The Hungarian electricity system is currently compelled to import more than 30% of the required energy. If almost 20% share in fossil fuels disappeared from the domestic production system, import dependency would further increase, which would pose a much greater risk than the current low electricity prices and the continuity of supply. Coal blocks could be replaced by nuclear technology to perform basic power-plant tasks, and the Paks 2 power plant under construction will be suitable for this purpose. Therefore, it can be stated that this production segment will definitely remain operative in the short term. Over the long term, with the expansion of weather-dependent renewables, even despite the emergence of industrial-scale energy storage, the capacity of gas turbines need to be expanded to ensure network resilience.

Hungary emits more than 66 million tonnes of carbon dioxide a year, and over 70% of this amount comes from fossil fuels. The next question was whether respondents saw any relationship between natural gas-based and coal-based electricity generation and greenhouse gas emission. In addition, respondents were asked if they saw a relationship between greenhouse gas emission (CO2 and methane) and climate change.

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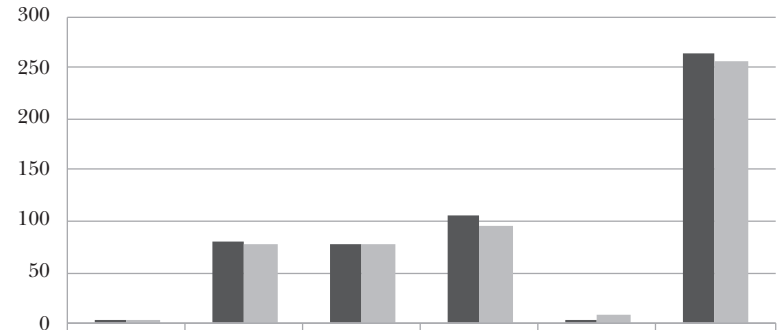
Chart 17: Contribution of coal, lignite and natural gas to the greenhouse effect and to climate change. Responses by age distribution



	before 1946	1946–1964	1965–1980	1981–1999	after 2000	Total
Greenhouse effect	1	78	76	103	3	261
Climate change	1	75	76	95	7	254

Source: Own research, 2019, N = 287

Respondents were given the options "yes", "no" and "don't know". In all the three generations that could be taken into account for the evaluation, over 90% of the respective age group thought that there was a correlation between natural gas-based and coal-based electricity production and greenhouse gas emission. 90.4% of the respondents born between 1981 and 1999, representing the largest sample, responded affirmatively, and this ratio is nearly 5% less than the ratio of those who answered affirmatively the generation born between 1946 and 1964. This is due to the fact that 7% of the younger age group expressed their uncertainty about this topic by checking the answer "don't know". The vast majority of respondents identify the greenhouse effect as a consequence of carbon dioxide emissions, causing climate change. While more than 90% of those born between 1946 and 1980 presumed a correlation between greenhouse gas emission and climate change within their age group, only 83.3% of the younger generation shared the same view. Within the latter age group, the ratio of uncertainty about the question remained virtually unchanged in comparison to the previous question, but almost 9% of them believe there is no correlation. Globally, electricity generation accounts for more than 30% of the total amount of emitted carbon dioxide. As electricity demand is increasing both internationally and in Hungary, only a change in the structure of production by power plants or energy-conscious use can result in reduction in carbon emissions.

Carbon-free technologies should be prioritised during a reform of the power generation structure. Improvement may start in the production of either renewable or nuclear energy. In 2016, the renewable sector accounted for nearly 9% of Hungary's electricity production, while nuclear power accounted for 51.6%.

Decentralised small power plants, as weather-dependent producers using renewables, are unsuitable for replacing the continuously available basic power plants. In order to meet the ever-present demand for power on the consumer side, power plants

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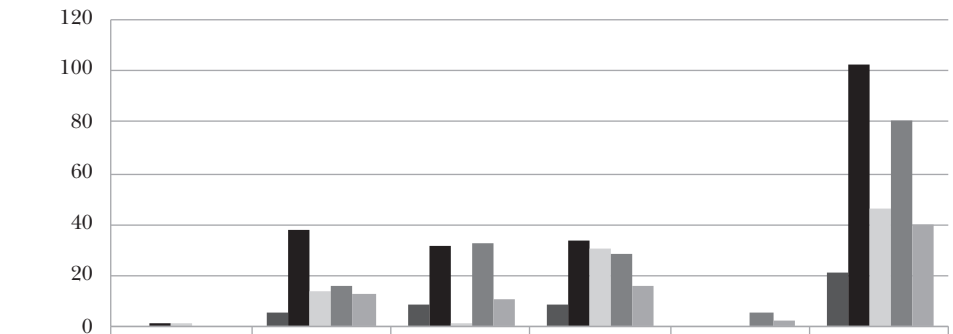
generate a steady supply of large and cheap electricity. Only coal-fuelled power plants and nuclear power plants converting fissionable materials are suitable for performing basic power plant functions. Although these technologies require considerable installation work and high investment costs, but are crucial for the economy. Project financing, as a special form of credit, helps to cover the high set-up costs (Csiszárik-Kocsir, 2016a; Csiszárik-Kocsir and Molnár, 2019). Due to the high risk of project financing as a structured credit market product, banks are only willing to enter the financing side after careful consideration, proactively monitoring the situation and looking for the indications of financial markets (Csiszárik-Kocsir, 2016b). For this very reason, life span is an important factor in their profitability. One of the questions in the dispatched questionnaire was the expected lifetime of the Paks Nuclear Power Plant.

Chart 18: Planned lifetime of the Paks Nuclear Power Plant by the respondents' age distribution



	before 1946	1946–1964	1965–1980	1981–1999	after 2000	Total
20 years	0	5	8	8	0	21
30 years	1	37	31	33	0	102
40 years	1	13	1	30	0	45
50 years	0	15	32	28	5	80
60 years	0	12	10	15	2	39

Source: Author's own research, 2019, N = 287

Respondents were given five predefined lifetime options to choose from. The largest consensus between the various generations was concerning the 30-year lifespan: 35.5% of all respondents chose this response. This was also the most popular within the age bracket, i.e. in the generation BB: 45.1% opted for it. The other term that may be considered significant was the 50-year life span, chosen by 27.9% of all the respondents. The largest consensus about operation planned for 50 years was recorded in generation X, with 39%.

The plant was originally designed for 30 years, and its four blocks expired one after the other: in 2012, 2013, 2016 and 2017. Thanks to successful life extension projects, each unit can continue production for an additional 20 years.

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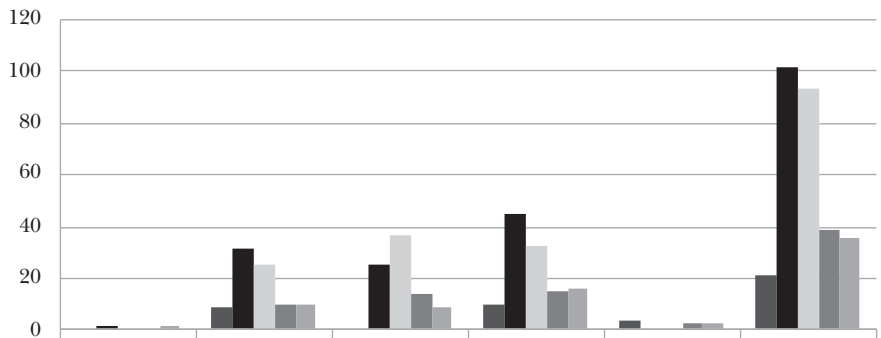
The Paks Nuclear Power Plant is scheduled to be shut down between 2032 and 2037, and the missing capacity will need to be replaced. To this end, the Hungarian government has launched the Paks 2 project. The new facility will comprise two units of generation 3+, with a capacity of 1200MW each. Generation 3+ nuclear technology uses passive systems and offers increased security and regulatory flexibility.

The next question concerned the planned lifetime of the Paks 2 Nuclear Power Plant.

Chart 19: Planned lifetime of the Paks 2 Nuclear Power Plant, in a breakdown by the respondents' ages



	before 1946	1946–1964	1965–1980	1981–1999	after 2000	Total
20 years	0	8	0	9	3	20
40 years	1	31	25	44	0	101
60 years	0	25	36	32	0	93
80 years	0	9	13	14	2	38
100 years	1	9	8	15	2	35

Source: Author's own research

35.2% of all the respondents opted for 40 years. 40.6% of the respondents in Generation Y thought that the planned life expectancy was 40 years. A 60- year life-span was predicted by 32.4% of all the respondents. The largest consensus, i.e. 43.9%, was shown in generation X. The new blocks are actually planned for 60 years. Based on the international experience in nuclear power plants beyond their originally planned lifetimes, a review of the units after 60 years will probably allow operation to continue. Taking utmost account of climate protection and the security of supply, the option of further nuclear capacity expansion would be worth exploring.

Summary and conclusions

Since the dawn of history, people have been using energy to survive. By now, the amount of energy consumed per person has multiplied and is constantly increasing. The continuous availability of energy is a basic condition for the functioning of hu-

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man societies. If exploitation of the Earth's energy resources and goods continues at the current rate, this could easily lead to the end of human civilisation.

In 2040, mankind will be consuming over 25% more energy than currently. The consumption and emission growth rates increase fastest in India and Asia, where the current energy use will have doubled by 2040. Hungary also has a significant development potential in energy management. Energy intensity, or energy consumption to per capita GDP, is more than twice the average of Western European countries. Having adopted the European Union's energy and climate protection policy, Hungary has voluntarily made stricter commitments than required by the EU. These include increasing the use of renewables and reducing greenhouse gas emissions. In 2018, the Ministry of Innovation and Technology prepared Hungary's National Energy and Climate Plan in preparation for the new Hungarian energy strategy.

The use of clean energies, energy efficiency and energy saving in all segments of the economy and society, and consistent adherence to them are the keys to the sustainability of life on Earth. Not using energy is the best way to protect our environment and our future. Sustainability means that we retain the opportunity for future generations to shape their living conditions. The most important element in climate protection and the fight against global warming and environmental pollution is man himself. The conscious or responsible lifestyle of individuals can be one of the most effective means of reducing the human activity that is destroying the Earth, and it is also essential in slowing down the rate of warming. One of the most important tools for developing an energy and environmentally conscious lifestyle is shaping attitudes at all levels of society. In all areas of education, education from kindergarten to university education, it is necessary to introduce environmental.

Policy-prepared climate protection measures could have a positive impact on the development of domestic small and medium-sized enterprises.

One of the objectives of the new Hungarian energy strategy is to keep energy prices low and predictable, which is a win-win situation for all economic players. On the other hand, the large-scale nuclear and renewable-based power plant projects envisaged in the government strategy also represent new business areas for SMEs. They have the opportunity to do business with multinational companies and in niche markets on their own. SMEs flexibility and expertise in innovation, development, design and construction is a need. Specialised companies will be able to use the knowledge and experience gained in the implementation of domestic projects in the international market.

The purpose of my primary research, conducted through a nationwide survey, was to assess the population's awareness and opinion about the availability and use of different energy sources, their risks, the consequences of their use, and the need for additional activities related to them. An analysis and evaluation of the responses led to the following main conclusions: Willingness to respond increased in proportion to increase in qualification, with the largest sample provided by university graduates. Respondents born between 1981 and 1999 were the most active. However, the majority of respondents are adequately informed, and the remaining uncertainties highlight

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the need for attitude formation at all ages. It is encouraging that seven people of the youngest age group have already found it important to assist research with their answers. Personal feedback from the respondents suggests that many people have tried to look for possible good answers when completing the questionnaire. On the one hand, this is due to the relatively high level of knowledge. The other important message is that it is important for respondents to be prepared for the topic, which is why their lack of knowledge and insecurity encouraged them to learn about it.

Pre-defined response options can also play an important role in choosing the right answers. A further breakdown or shading of each answer would probably have made the answers more selective. Furthermore, the relatively good result can be explained by the fact that the respondents were internet users. They are the ones who regularly surf the sea of information and so they were likely to find it important to be open or possibly committed to the topic, and to spend time for and effort at responding.

The results suggest that there is a need for continuous awareness-raising in all age groups and social groups. Topics should include energy saving, energy efficiency, pollution, the benefits and impacts of renewable energy sources, a full demonstration of the use of nuclear energy, and the environmentally responsible use of energy. Awareness-raising can be genuinely effective the level of the population's knowledge is continuously and accurately measured.

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István Tózsa

Innovation and Identity

Summary
Since the spread of mobile Internet, knowledge is being restructured in our minds, because we have access to the entire knowledge of the world. During the last decade, the values that define learned people seem to be changing rapidly. Classical knowledge regarding national historical, geographical and cultural values seems to vanish from the mind of the young generation (the Z one, born after 1996) and new values belonging to the online environment are gradually replacing them. The results of this change can easily be experienced in higher education, where students seem to have forgotten nearly everything they have learnt in primary and secondary school about their national heritage. This article tries to shed light on the consequences of this ongoing process, and explains the importance of national identity in shaping creativity and innovation. Also, it tries to explain the need to reshape the methodology used in primary and secondary education and to reconsider the national values in our decades of dramatically rapid change in the structure of knowledge.

Keywords: creativity, national identity, innovation, the role of unconscious mind in recording memory units, conflict between classical (old) and new values in education

Introduction

The objective of this paper is to draw the attention to a newly discovered close correlation between innovation capacity and the power of national cognitive identity in the human brain, on the one hand. On the other hand, the presentation aims at illustrating the weakness, or even the absence, of national identity in the so-called generation Z (born after 1996) among Hungarian university students at the Corvinus University of Budapest (CUB) and at the National University of Public Service (NUPS).

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According to the latest findings in brain research, the number of memory units in the brain define the capacity of innovation. The more such units the brain has, the more innovative a mind is. Memory units are created in the brain by bioelectric impacts. They exist in the form of links between nervous cells. The strength of bioelectric impact defines the duration of the neural connection. The greater the impact, the longer the neural connection. Dr Tamás Freund, an internationally well-known and reputed professor of the Semmelweis Medical University of Budapest conducted investigations and neurobiological research to find and localise the so-called pacemaker cells in the subconscious mind responsible for regulating the selective memory of the brain. Having been able to localise them, the team sought to identify the external impacts that stimulate these cells. They found that besides emotions, it is the national identity that can stimulate the subconscious pacemaker cells to induce bioelectric impacts creating long-lasting memory units, and thus indirectly innovation capacity, in the conscious crust of the human brain.

In Hungarian higher education there is an optional course on Hungarian national heritage, aimed at improving competence in the preservation, maintenance and management of national values in a business environment. It includes writing tests to prove their familiarity with Hungarian national values to display their level of cognitive national identity, which is significant in innovation capacity and in building a creative personality. An evaluation of the tests proves that between 2013 and 2019, approximately 500 students had extremely low cognitive national identity at CUB and NUPS.

A low level or the complete absence of Hungarian national identity was detected among university students of generation Z. It can be understood as a warning to the government, which communicates the political importance of a nation state and the preservation of Hungarian national values and culture. The risk involved is not only the absence of familiarity with Hungarian history, culture, literature and geography, and thus the absence of a social platform for the Hungarian nation state, but also the impact on the innovation capacity of the young generation. It results in poor urban marketing capacity, as the significant buyers (investors) will not buy a city unless the local population have done so.

The power of the motherland

In Greek mythology when Zeus became the king of the Olympian gods, the primordial Giants that came from his grandmother, Gaia, the mother Earth, attacked Zeus and the gods of Mount Olympus to regain their ancient power over the cosmos that had become completely dominated and restructured by the gods. In the battle the Giants proved to be invincible, since as soon as they were stabbed by the gods or struck by Zeus's lightning and fell to the ground, they immediately regained their power from their mother Earth. Finally, the gods had to seek help from Heracles, a mortal man, because he was the only hero who could kill the Giants by lifting them to prevent their contact with Mother Earth and killing them in the air. (In a symbolic language,

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this is a message that only humankind is able to destroy the Earth.) However, this ancient story also manifests the power of the motherland and draws the attention to the importance of place marketing in regional development, and of local and national values in inducing creativity for economic development.

The role of identity in creativity

Professor Tamás Freund is one of the world's most reputed brain researchers, who was awarded the Brain Prize in 2011 with two of his Hungarian colleagues (Professor György Buzsáki and Professor Péter Somogyi) working abroad. The Brain Prize is regarded as the Nobel Prize in brain research. Freund and his team have concentrated on the role of inhibitory 'interneurons', or small nerve cells that release the neurotransmitter γ-amino butyric acid (GABA), which reduces activity in the nerve cells to which they connect. In the unconscious hippocampus Freund and his team identified three novel types of such cells that connect to other inhibitory nerve cells. He discovered that control over the inhibitory interneurons by other inhibitory cells regulates rhythmic patterns of activity, which are essential for normal memory formation.[1]

What does this mean in simple, everyday language? It is known that unconscious thinking makes up 70% of the brain activity and its operation has been for the most part hidden from scientific investigation so far (25% of the brain activity comprises physiologic functions, and only 5% represents conscious thinking). It is also known that millions of pieces of information reach the conscious brain every day through seeing, hearing, smelling and touching, in public places, at home in the family, at work, via the internet etc. However, the brain creates long-lasting memory cells (from strong bioelectronics discharge between the neurons' axons). Of course, people forget the overwhelming majority of the information obtained through perceptions, no matter how hard they try to remember, especially when they are memorizing for an examination.

The special nervous cells, called "pacemaker" neurons and discovered by Freund, in the subconscious part of the brain prevent the conscious part of the brain from memorizing the information included in these millions of perceptions during the day. So, the number of long-lasting memory cells in the conscious part of the brain remains low because of the pacemaker neurons that control and supervise the information contents of perception. The building blocks of creativity are the long-lasting memory units, and their number is reduced by the subconscious pacemaker cells. A person with 5000 memory units is necessarily less creative than a person with 50,000 or half a million units. The researchers were looking for the impacts that influence the pacemakers to allow strong bioelectronics discharges happen in the conscious brain after perceptions.

They identified the following impacts: (1) emotions, in the first place. If perception is accompanied with emotions, the pacemaker cells in the unconscious allow strong discharges happen among the axons of neurons and thus long-lasting memory units are created that can act as the building blocks of creativity. (2) The second

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impact influencing pacemaker activity was recognised as activity during perception (especially activity in physical – and not digital – communities like parties, co-working, playing, dancing, holiday-making etc.). (3) And finally, the third agent was identified as a place identity with one's motherland. It can be represented in identity with the family and with the birthplace, which may be a city, a region, or a country or nation. In other words, information in the perception of one's birthplace will also make the pacemaker neurons allow the formation of long-lasting memory units in the brain. When people identify themselves with their birthplace, resulting in local patriotism, regional or national patriotism, the local, regional or national identity will make them more creative through building long-lasting memory units.

If a creative personality is to be raised, education policy ought to pay attention to always include *emotions* (1), *activity* (2) and maternal, local, regional or national *identity* in learning (3).

Know, love, defend

Maternal (family), local (urban), regional and national identity can act or can be manifest on three levels: (1) at the cognitive level, showing how much one knows about one's family, city, region and country or nation; (2) at the level of affection, showing one's emotions, love and attitude towards one's family, city, region and country or nation, and (3) at the level of actions, showing what one is ready do in defending, defending, improving, supporting one's family, city, region and country or nation.

The three levels of identity expression accurately correspond to the three steps taken by a local population in place marketing to "buy" their city, region or country. As well-known in place (urban or country) marketing, there are several target groups to buy a place. The first group includes the local population. The most important group includes the managers employed by the investor who can bring foreign direct investment to the city, region or country, and can thus create new jobs and contribute to the local, regional or national budget via taxation. There are many other possible target groups of buyers for a place, like commuting employees, students, patients etc., but their role depends on the presence of big industrial or service companies, universities and hospitals or on the medical treatment infrastructure. However, the buyers who are indispensable for place include tourists, who can also be considered as free means of advertisement, once they had a good time in the city, region or country. In contrast, if tourists are dissatisfied and have unpleasant memories, they can serious destroy the reputation of the city or country.

So in place marketing, the most important regional development tool in attracting capital and investments into a city, region or country, the first buyer, i.e. the local population needs to know their living place before buying it. Once the local population has *become familiar with* their living place (its geography, history, culture, literature, monuments, pieces of arts etc.), there is a chance that they will also *love* it. In other words, cognitive identity can easily be followed by affective identity. If the local population loves their place, they are highly likely to proceed to an action-level iden-

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tity in *defending* it as well. This action can be manifested in willingness to vote, in going on protests, or even in defending the place (usually their country) by force of arms. So when the local or central government sells the place to the local population, the purchasing process is accomplished via (1) getting to know, (2) getting to love and (3) getting to defend the place. We may refer to the place purchase process as the three "gets".[2]

Cognitive identity – the basis of place marketing

What are included in cognitive identity that serve as ammunition in selling a place to the local population? Cognitive identity includes the circles of local, regional or national values. What are they? The geography, the art collections, such as famous or valuable paintings, statues, monuments and buildings, and the cultural heritage, including events, holidays and festive occasions, exhibitions, theatres, music, gastronomy, traditions, literature, famous and well-known people, the history of the place, the famous and valuable products and the beauties of the landscape. Familiarity with these things is required in the course of place marketing. The first step in selling a city or country is collecting the local or national values in a registry that serves as a value audit of the place. Familiarity with the values makes the cognitive place identity of the local population. Since investors, the main buyers of the place, wish to buy a healthy product, the place needs to be bought by the local population first. The place can be sold to the local population when it is known, loved and defended by the local population. The result of the purchase is a clean settlement, a clean region or a clean country. In this respect the term 'clean' means a healthy product (city or country), with low environment – i.e. physical – pollution, and low crime rate – i.e. social pollution. The investor will buy the place only if it is safe to invest (the social pollution is low), and unpolluted (the environmental pollution is low), because only a clean and healthy place (product) displays and proves that the local population has purchased the place (their product). No one would want to buy a product (a city) the seller itself (the city's population) does not want to buy or has not bought. In this sense, cognitive local regional or national identity is the key factor both in selling a city, region or country, and in local, regional or national economic development. The *stronger* the local or national *identity* of the local population is, the *better* chances the city or the country has to *develop* its economy and in attracting FDI via place marketing. Cognitive identity also supports creativity, and as in economic development and investments creativity leads to innovations, place *identity* and *innovation* go hand in hand.[3]

Symptoms of decline in cognitive national identity

At the Corvinus University of Budapest an optional course on Hungarian national heritage was announced in 2013. More than 500 students have completed this course since then. In each grade, there is a short test including questions on Hungarian history, valuable pieces of art, literature and geography. Despite the fact that these

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questions relate to the compulsory national curriculum taught in both primary and secondary schools, no more than 15% of the students can answer them on average. Perhaps, this suggests that a thorough social investigation of the students' national identity would have a rather disappointing result. The reason why university students forget much of the curriculum content after graduating from secondary school can perhaps be explained by simply memorizing for the final exam, i.e. they try to force their conscious mind to remember the teaching material. When learning is not accompanied by emotions and collective activity – or messages related to local, regional or national identity – knowledge fades away within a couple of months or years without a trace.

The adverse impacts of the absence of a cognitive national identity on the young generation are explained by at least two factors: (1) through the non-creation of long-lasting memory units, it influences the conscious capacity of their brains to create ideas and store information, and thus they become *less creative* than otherwise they might have been; and (2) it reduces local, regional and national (cultural, historical, geographical, geological, artistic etc.) values that can be used in urban, regional or national marketing to attract FDI and thus increase local, regional or national economic development. In short, the absence of sufficient cognitive identity *slows economic development.* Therefore, the symptoms of decline in national (regional and local) identity among university students require a revision of the teaching methods in primary and secondary schools. What is to be done?

Emotional Intelligence Quotient (EIQ)

Emotional intelligence is the capability of the mind to recognise and manage emotions in order to guide thinking and behaviour. Nowadays it is getting increasingly known and appreciated in career building as high as, or perhaps even higher than, the traditional IQ. Emotions and the conscious application of emotions should play an ever-increasing role in learning and acquiring knowledge in order to ensure the formation of long-lasting memory units in the conscious mind. Since the members of the new generations are "digital natives", their most common tool, the mobile internet should be admitted and allowed to enter the classroom. Learning should be performed in a community with a wide range of mobile applications. Both emotions and activity should be present in the learning process. Even classrooms can be placed, at least in part, into a virtual space. In addition to classrooms or virtual classrooms, classes may be held at practically any geographical location in the world with accessible virtual space: at volcanoes, waterfalls, in Manhattan or on the Moon. Considering the rapidly developing technology, the implementation of an accessible virtual world is but a matter of years.

During history classes – in order to deepen national identity – using their mobile internet handsets, children can be included in the creation of animated films, perhaps based on romantic and moving love stories, in a real national historical setting. During geography classes, they can either physically travel to places and sights in their

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country, or visit them virtually, in a real-time interactivity with their fellow students and their teacher. During economic courses, children and students may visit factories, company headquarters or banks either in person or in the virtual space, also by real-time interoperability. This will be the reform in education in the near future.

This reform is badly needed as the basic knowledge required for a career had changed very little for many generations before the 21st century. About 200 books in a home library proved to be enough to make a well-educated, literate person. However, the spread of mobile internet has changed everything forever. The currently available knowledge of the whole world is at everybody's immediate disposal in the hand or in the pocket. Knowledge has continuously been restructuring itself. Therefore, the main device to guide the new generation through the endless ocean of information no longer includes the decisions of the conscious mind, rather the EIQ, rooted in the subconscious mind. The better someone can manage his personal EIQ, the more successful he will be in life and career. Clearly, emotions and activity can also find their places in learning in the digital world. But what about place (local, regional, national) identity? Is it going to lose its importance in acquiring information in the form of long-lasting memory units in the near future?[4]

New national identities

With the continuous modernisation of the human environment – ever since the Stone Age – tools, traditions and heritage have constantly been transforming. Many of them have been forgotten and new values have emerged. At the beginning of the 21st century time and technological development have been accelerating at a rate that we are shocked at the pace of forgetting old values, and we are unable to perceive new values replacing them. This also applies to national values and heritage. But the old unconscious demand for identity to the motherland, the birthplace remains, as it is a biologically predestined system. The young generations in the age of acceleration will certainly find their own local, regional and national values. They may not be identical with the classical national values that have been present over numerous generations up to now, but they still will be national. In the case of Hungary, they will be Hungarian values: celebrities, singers, inventions, world records, pieces of new music, new arts, poems, virtual dramas etc.

The Pallas Athene Innovation and Geopolitical Foundation issued an album in Hungarian, in English and in Chinese with the title *Hungarians in the Top Ten of the World*. This album introduces the success Hungarians have achieved at various world rankings between 2012 and 2015. There are 330 world records held by Hungarians in these few years only in the field of gastronomy, wellness, tourism, festivals and events, professional competitions, music, science and research, creative industries, innovations and sports. They new generations will remember them all because they are involved in it, and these outputs, records are Hungarian values strengthening the Hungarian identity among the youth. The older generations should accept that some of their national values and part of their national heritage are unavoidably doomed to

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vanish due to the very rapid changes in knowledge. At the same time, however, new items of national heritage are continuously being created and the members of the new generations will be as proud of them as their ancestors had been of the classical national heritage. So the supply of national heritage is ensured, the old one will be replaced by the new one in an especially heavily accelerated process currently taking place.

Notes

[1] Chamberland S. and Topolnik L. explain control of the unconscious mind over the activity of the conscious crust and the essence of the discovery of the Hungarian brain researchers in a scientific way (Chamberland and Topolnik, 2012).

[2] Maurel MC. explains the significance of local or territorial identity in regional and local development i.e. innovations in the economy, using Central European and Hungarian examples (Maurel, 2016).

[3] Kavaratzis, M. and Ashworth, G. J. present the role of identity in urban marketing in a scientific approach (Kavaratzis and Ashworth, 2005).

[4] Akduman, G. et al. introduce EI as it can be experienced in different generations (Akduman, 2015).

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Free-float Car Sharing Companies in Hungary and a Comparison to Germany

Summary

Car-sharing companies' key argument is the heavily advertised sustainability element in their operation, which can partially be confirmed; however, this study sheds light on the importance of the connection between sustainability reports and financial statements. In order to gain more confidence and provide objective support to voluntary sustainable reports, the key question is if it possible to reconcile these statements to their financial performance and their assets and liabilities. In light of recent market changes in Hungary and the expansion of German car-sharing companies, this is an increasingly important question. Additionally, the study also addresses the significant 2019 market change in Hungary after the penetration of the car-sharing service based in Germany. The reviewed sustainability reports contain insufficient information to be reconciled to financial statements. Additionally, the aspects related to sustainability are recognised through the parent entities' books under environmental liabilities. Each of the reviewed companies considers itself as "the most sustainable entity" in the given segment, which raises serious doubts regarding the reliability of the information. From the perspectives of the basic analysis and profitability, the German companies reported better results than the Hungarian ones; besides, in Hungary, the service providers applied different fleet-financing models and used leases or purchase transactions. The reviewed car-sharing companies seem to operate on profit rather

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than a sustainability basis. Although these services do contribute to a more sustainable future, without proper alignment, the real impacts cannot be validated or traced back to the relevant financial statements. The lack of transparency, as an example of climate-related consequences, could have a significant effect on the companies' performance, and this may be vital and relevant information for investors.

Journal of Economic Literature (JEL) codes: M41, Q56
Keywords: free-float car sharing, financial accounting, sustainability reports, financial accounting, and sustainability reports mapping

Introduction

The motivation and attitudes of market actors are changing. New models are emerging and manifest vitality (Parragh, 2016). The objective of this study is to examine the most important free-floating car sharing companies in Hungary and compare them to their German counterparts in terms of finances and sustainability. The major Hungarian companies in this business segment are profit-oriented; however, based on their actual financial results they appear to be less profitable than other rental service companies.

As a result of the analysis of the Hungarian companies, it was found that in spite of very similar operations and procedures related to accounting and taxation regulations, certain business advantages may arise from lease accounting differences. The implementation of the new International Financial Reporting Standards (IFRS) 16 (Leases) regulation generates a unique situation in Hungary, where, depending on the applied national or international accounting treatment, these companies might face adverse or favourable business impacts.

In addition, the constantly changing market conditions can generate situations where market significant foreign competitors can enter the Hungarian market from other Member States of the EU. Although Hungary is not a significant market, in the future, it could be an example of the free movement of services within the European Union.

Literature review

The free-float car sharing business model was categorised, defined and described in a car sharing business model review by Deloitte (2017, p. 2). Since then other studies have also reviewed the model and the markets, including Munoz and Cohen (2018, pp. 116–143). In addition to a market definition, several previous studies had already raised sustainability-related questions about sharing-economy operational models. Harangozó et al. (2018, pp. 172–181) consider sharing economy as a path towards a beyond-growth economy in contrast to the conventional, growth-based economic

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model, even though there are more sustainability-related concerns to be considered. Geissinger et al. (2019, pp. 419–429) describe and classify the sustainability implications of sharing economy platforms for Sweden. Bernardi and Diamantini (2018, pp. 30–42) explore integration of the increasing number of cities with a sharing economy into the urban agenda, fostering their positive aspects while avoiding their negative externalities, with a focus on Milan and Seoul. Ma et al. (2018a, pp. 356–365) propose an alternative governance model to improve the effectiveness of a collaborative governance regime towards urban sustainability. Ma et al. (2018b, pp. 942–953) argue that two-tier transformations, triggered by the disruptive innovation of the sharing economy and led by urban transformation towards sustainability, mutually influence one another in the fast-changing urban context in Shanghai. Rietmann and Lieven (2019) examine how policy measures have succeeded to promote electric mobility in 20 countries by measuring the influence of monetary incentives, regulations and charging infrastructure. Varga and Cseh (2019) review Hungarian taxation and its structural changes that will have taken place by the fourth industrial revolution and automation, which will impact – based on the relatively low labour costs and high VAT rates – car industry in Hungary. Hartl et al. (2018) address the gap between B2C and P2P car sharing services from the customers' perspective. Overall, these studies on free-float car sharing businesses support the initial assumption that these entities are profit-oriented and their operation can be heavily questioned from a sustainability perspective.

Considering the impact of changes in the international lease regulation, a wide range of studies has been published, including Wheeler and Webb (2015) and Barone et al. (2014), who provide summaries of the expected impact of lease capitalisation and its effect on profitability and leverage ratios. Giner and Pardo (2018) review the value relevance of operating lease liabilities. Furthermore, car sharing can increase eco-efficiency and thus improve the environmental performance of the economy (Harangozó, 2008, pp. 27–36), and the rebound effect neutralises a significant share of the benefits achieved.

Methodology

The business model was analysed on the basis of financial statements. The following elements were reviewed on the basis of the available information:

– Entities registered in Hungary were selected based on their main business activities registered by the Companies Court.

– The profitability review was based on the published financial statements.

– IFRS 16 (Leases) and the Hungarian Accounting Act were compared for certain aspects of lease accounting regulations

– Hungarian and German car sharing companies were compared for fleet size, car sharing costs and registered users.

Sustainability was reviewed based on Penz et al. (2018, pp. 37–54) to explore and explain how, why and when a sustainable lifestyle is adopted, participation in the shar-

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ing economy becomes key, and how sharing economy models and sustainability (sustainable sharing economy, SSE) correlate conceptually in the collected articles. Seven sustainability considerations were addressed:

– producing less,
– idle capacity and under-utilised physical assets,
– reducing waste,
– resource efficiency through use rather than ownership,
– extended use pattern,
– low ecological (carbon) footprint,
– owning less, interacting more and building social capital (Penz et al., 2018).

These considerations were selected based on sustainability reports (BMW Group, 2017; Daimler, 2016) and the Hungarian entities were then reviewed according to them.

Free-float car sharing companies' business models in Hungary and in Germany

The specific free-float car sharing service providers are defined by the car sharing service: vehicles can be rented and parked freely throughout the entire business area without having to determine the start and the end of the rental period in advance. The start and end of the rent is for all vehicles via specific smartphone applications. Payment is based on usage and according to a fixed minute rate.

In Hungary every company is required to identify a core business activity upon establishment. The Hungarian classification of activities is "identical and fully harmonised with the European NACE Rev.2. Statistical Classification of Economic Activities in the European Community, 2008 (Nomenclature des activités économiques dans les Communautés européennes). On the basis of Regulation 1893/2006/EC, effective from 1 January 2008, NACE'08 is used to determine the principal activities of enterprises, in the calculation of economic and social indicators and for the publication of statistical data" (HCSO, 2019a).

Car sharing activities specifically related to passenger cars are classified under Section "N" for administrative and support service activities, in division 77, group 77.1 and in class 77.11 "Renting and leasing of cars and light motor vehicles".

The database of active Hungarian companies contains 362 companies registered with the core activity 77.11. Table 1 shows their distribution according to employee headcounts.

Table 1: Hungarian car sharing businesses engaged in core activity 77.11

1 employee	**2-9 employees**	**Over 10 employees**	**Total**
169 entities	161 entities	32 entities	362 entities

Source: Company register, www.ceginfo.hu

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The aim of this analysis is to cover all the operational Hungarian entities that meet at least 1 criterion above the micro-business level. According to the European Commission, a company is a micro-business if it employs less than 10 people; has a turnover of EUR 2M or less or a balance-sheet total of EUR 2M or less (European Commission, 2019). In order not to limit or minimize the reviewed population, all the companies engaged in the activity 77.11 and employing more than 10 persons were surveyed.

The selected companies' financial statements were reviewed, and based on their annual disclosures, further 5 entities were removed, as their actual business activities were only related to car rental but the core activities were transportation, education or the sale of car parts.

At the time this study was compiled, the latest available financial statements were related to the fiscal year 2017. The diluted population of a total of 28 entities is presented in Table 2.

Table 2: Companies engaged in NACE 77.11 "Renting leasing of cars and light motor vehicles" as a core activity and employing more than 10 people in Hungary

#	Company name	Registered address	Year of est.	Empl.	HUF '000'		Profit %	Core activity
					Revenue 2017	PBT 2017		
1	ALD Automotive Magyarország Autópark-kezelő és Finanszirozó Kft.	Budapest	2001	108	16,471,970	1,108,227	6.73%	Lease
2	ARVAL Magyarország Járműparkkezelő Kft.	Budapest	2002	46	9,598,635	976,847	10.18%	Lease
3	AUTO ReFAIRent Autókölcsönző és Szolgáltató Kft.	Vecsés	2010	52	1,733,054	158,709	9.16%	Car rental
4	AVALON Car(e) Services Kft.	Budapest	1989	24	371,938	29,593	7.96%	Car rental
5	BÉR-ELEK Flotta és Autópark Kezelő Kft.	Budapest	2007	25	1,612,429	99,194	6.15%	Car rental
6	Business Lease Hungary Kereskedelmi és Szolgáltató Kft.	Budapest	2003	29	5,351,868	376,017	7.03%	Lease
7	EuRent Autókölcsönző Kft.	Budapest	1989	59	3,218,105	65,175	2.03%	Car rental
8	EuroFleet Gépjármű Flottakezelő Zrt.	Tényő	2008	34	2,207,047	332,127	15.05%	Lease
9	Euroleasing Kereskedelmi Szolgáltató Kft.	Budapest	1995	56	561,959	3,304	0.59%	Lease
10	GAS-CAR Gépjármű-kölcsönző, Autópark-kezelő és Szolgáltató Kft.	Siófok	1994	56	1,044,191	11,304	1.08%	Car rental

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#	Company name	Registered address	Year of est.	Empl.	HUF '000'		Profit %	Core activity
					Revenue 2017	PBT 2017		
11	GreenGo Car Europe Kft.	Budapest	2014	20	110,788	–158,291	–142.88%	Free-float car share
12	HARUM INVEST-MENT Gépjármű Üzemeltető Zrt.	Budapest	1999	12	1,128,502	4,402	0.39%	Car fleet provi-sion
13	IVANICS Autópark-kezelő Kereskedelmi és Szolgáltató Kft.	Nadap	2005	14	3,283,259	68,525	2.09%	Car fleet provi-sion
14	KÉSZ&GO Flotta és Gépjárműkezelő Kft.	Kecskemét	1993	13	1,195,742	39,497	3.30%	Car fleet provi-sion
15	LAFUT Service Kereskedelmi és Szolgáltató Kft.	Miskolc	2015	22	74,246	722	0.97%	Car rental
16	LeasePlan Hungária Gépjárműpark Kezelő és Finanszírozó Zrt.	Budapest	1994	95	22,451,936	2,082,167	9.27%	Lease
17	Mercarius Flottakezelő Kft.	Budapest	1996	81	4,539,377	767,564	16.91%	Lease
18	Mercur Rent a Car Autókölcsönző és Szolgáltató Kft.	Vecsés	1995	80	5,498,329	291,926	5.31%	Car rental
19	Mobil Credit Kereskedelmi Kft.	Debrecen	2000	14	1,272,146	116,266	9.14%	Car fleet provi-sion
20	MOL Limitless Mobility Kft.	Budapest	2017	32	0	–69,543	N/A	Free-float car share
21	NELSON FLOTTALÍ-ZING Eszközbérbeadó és Autóparkkezelő Kft.	Székesfe-hérvár	1992	38	2,917,894	139,365	4.78%	Lease
22	Otokoc Hungary Autókölcsönző és Szolgáltató Kft.	Budapest	2015	29	2,031,185	–24,873	–1.22%	Car rental
23	Porsche Lizing és Szolgáltató Kft.	Budapest	1993	54	29,728,668	1,047,108	3.52%	Lease
24	Rapid Rent Autó Kereskedelmi és Szolgáltató Kft.	Budapest	2011	25	529,054	1,067	0.20%	Lease

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#	Company name	Registered address	Year of est.	Empl.	HUF '000'		Profit %	Core activity
					Revenue 2017	PBT 2017		
25	RELEASE Zrt.	Budapest	2009	19	592,100	41,393	6.99%	Lease
26	UniCredit Leasing Kereskedelmi Kft.	Budapest	1995	24	1,206,524	–162,445	–13.46%	Lease
27	VR Transport and Rental Kft.	Csömör	2017	10	45,974	6,089	13.24%	Car rental
28	ZENIT-AUTO RENT Szolgáltató és Kereskedelmi Kft.	Miskolc	2017	14	177,215	10,350	5.84%	Car rental

Source: www.ceginfo.hu

Table 2 reveals that only two of the 28 companies (#11 GreenGo Car Europe Kft., hereinafter: GreenGo, and #20 MOL Limitless Mobility Kft., hereinafter: MOL Limo) are the genuine flee-float car sharing companies. Both of the two free-float car sharing companies are operated in Budapest.

Based on their financial statements, the total and average revenues and profits of these companies are presented in Table 3.

Table 3: Total and average revenues and profit of companies engaged in the NACE 77.11 core activity and employing at least 10 people in Hungary

Core activity	Number of entities	HUF '000'			
		Total revenue 2017	Average revenue 2017	Total PBT (Profit before tax) 2017	Average PBT 2017
Free-float car sharing	2	110,788	55,394	–227,834	–113,917
Car fleet provision	4	6,879,649	1,719,912	228,690	57,173
Car rental provision	10	15,806,666	1,580,667	648,189	64,819
Lease	12	96,157,032	8,013,086	6,712,741	559,395
Total	**28**	**118,954,135**	**4,248,362**	**7,361,786**	**262,921**

Source: www.ceginfo.hu

In 2017 these companies recognised a total revenue of HUF 118.9 billion (EUR 384.7 million)[1]. This does not represent the total lease market, as there are also companies engaged in financial lease as their core activity but are classified in different statistical segments, e.g. section K for "Financial and insurance activities". It does, however, represent all the free-float car sharing companies, because this specific service is classified in the single activity 77.11 and no other companies provide free-float

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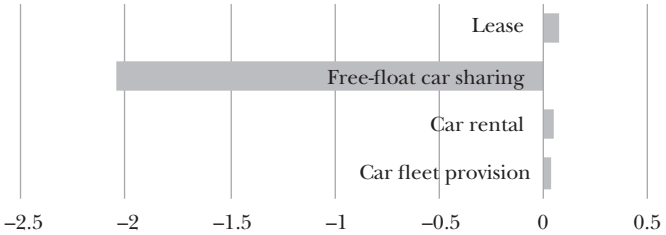
car sharing service as a secondary activity. It can be concluded that in 2017 HUF 110.7 million (EUR 358.3 thousand) was realised in the free-float car sharing market in Hungary.

Chart 1: Average PBT / Average revenue in 2017 per core activity of the reviewed population



	Car fleet provision	Car rental	Free–float car sharing	Lease
Average profit before taxes	0.033241521	0.041007319	–2.056484406	0.069810193

Source: Tóth and Szigeti, 2019, p. 172, www.ceginfo.hu

The aim of this part of the study is to present and analyse their operational models in Hungary and compare them to the business models of Europe's biggest market providers active in Germany (Car2Go, DriveNow). The three key areas of the financial review were as follows:

a) Analysis of the financial statements and review of the financing model
b) Differences in lease accounting
c) Comparison to German companies

Analysis of financial statements and review of the financing model

GreenGo was established in 2014 as the first company in this business segment of the Hungarian market, and up to 2017 it remained practically the only market participant without any major competitor in the free-float car sharing segment. Chart 2 gives a summary of the company's balance sheet items for the period between 2014 and 2017.

GreenGo's asset structure: The long-term asset value increased from HUF 69M (2016) to HUF 102M (2017), comprising intangible assets worth HUF 43M, tangible assets worth HUF 58M, and other investments in the value of HUF 1M. This breakdown provides important information in light of the data published in January 2018, as GreenGo reported 168 available cars, which should be recognised in the value of property, plant and equipment (hereinafter: PPE) if they owned those assets. There was no available public information on any further breakdown, but it is easy to explain

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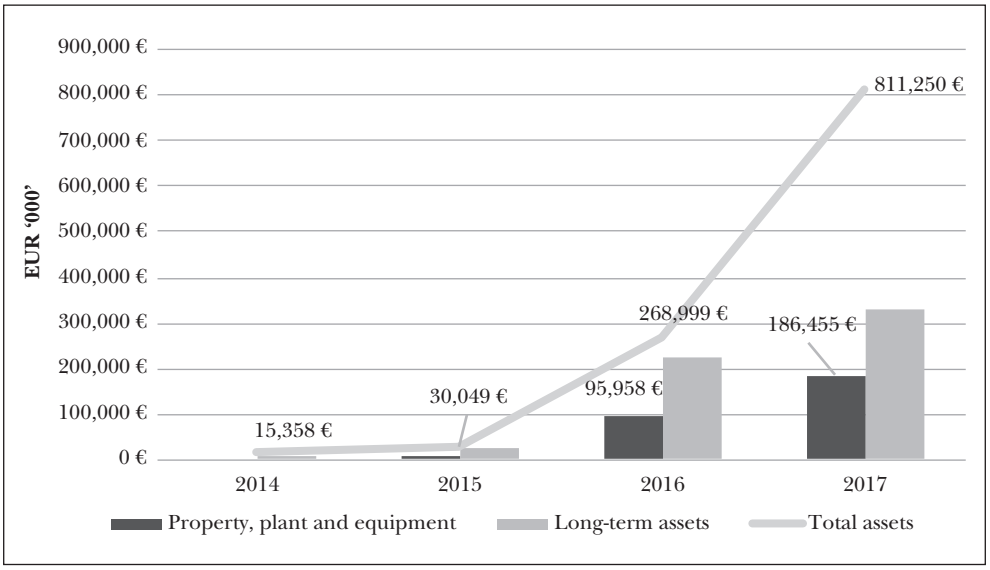
Chart 2: Changes in the asset structure, GreenGo (2014–2017)



Source: www.ebeszamolo.im.gov.hu

the PPE value even if it only includes cars: the result is HUF 57.8M / 168 vehicles = HUF 0.34M (approx. EUR 1060) for the value of a car, highly unreasonable. This means that the company applied operating leases and thus these assets constitute off-balance sheet items.

GreenGo liabilities and equity: The equity remained broadly unchanged over the past two years at around HUF 43M, however, the generated loss increased significantly from HUF -18M to HUF -158M, which was offset by equity contribution from the owners. Further analysis is performed based on the profit and loss statement to identify the potential reasons for the significantly increasing loss. The debt-to-equity ratio also significantly decreased in relation to an increase in liabilities by HUF 129.3M. This seems to be financed mainly from short-term shareholder loans in a value of HUF 115M and from long-term related-party loans worth HUF 16M. Chart 3 sums up the P/L statement of GreenGo for the period between 2014 and 2017.

GreenGo profit and loss statement: The realised revenue increased from HUF 8M in 2016 to HUF 111M in 2017, while expenses increased from HUF 27M to HUF 275M in the same period. This was the key reason for the decrease in the P/L from HUF -18M to HUF -158M. Based on this data, this company did not generate sufficient revenue to compensate the increased value of material expenditures.

GreenGo got into a significantly worse position in 2017, the year when MOL Limo entered the market. Mention must be made of the fact that the owners of GreenGo include private investors and a leasing company, while MOL Limo is owned by the Hungarian Oil- and Gas Company, which is a listed entity. Table 4 gives a comparison between the profit and loss statements of these two entities for 2017.

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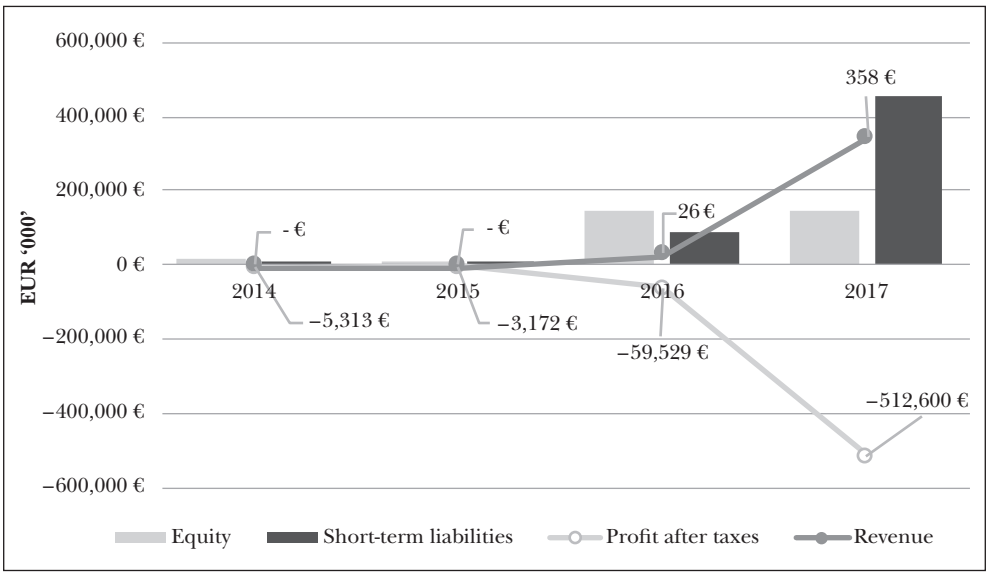
Chart 3: Changes in equity, ST liabilities and main income items, GreenGo (2014–2017)



Source: www.ebeszamolo.im.gov.hu

Table 4: Comparison of the profit and loss statemenst for MOL Limo and GreenGo (2017)

2017 Statement of profit or loss and other comprehensive income (EUR)	**MOL Limo**	**GreenGo**
Revenue	0	374,391
Material expenditures	12,435	677,826
Personal expenditures	1,103	90,262
Other expenditures	201,975	90,812
Total operating expenditures	215,512	858,900
Results from operation (profit + / loss –) (EBIT)	**–215,512**	**–484,509**
Financial incomes	731	4007
Financial expenditures	1,012	31,415
Results from financial activities (profit + / loss –)	**–9,392**	**–27,408**
Profit before taxes (profit + / loss –)	**–224,904**	**–511,918**
Current taxes	0	682
Profit after taxes (profit + / loss–)	**–224,904**	**–512,600**

Source: www.ebeszamolo.im.gov.hu

It is an important fact that MOL Limo had no revenue in 2017 and therefore it could not cause the poor performance of GreenGo. On the other hand, already in the first year of its operation, MOL Limo generated a significantly higher loss than

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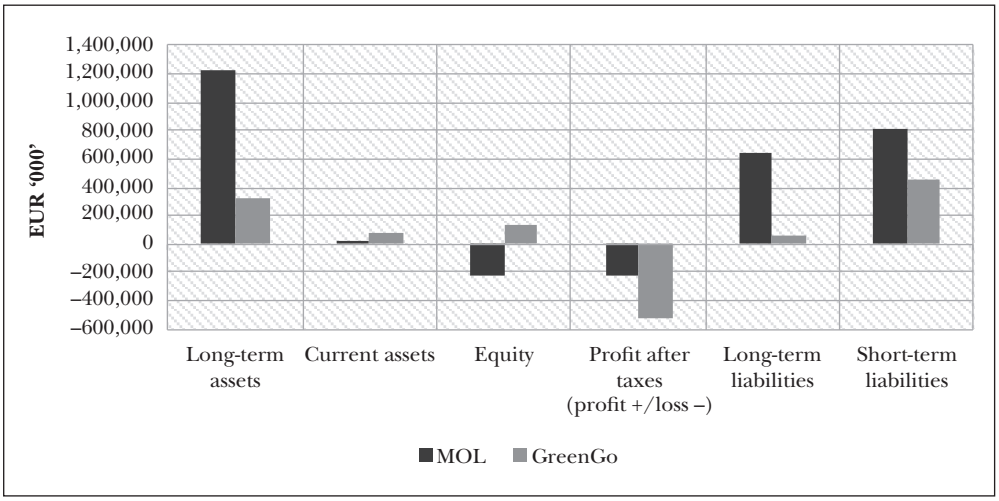
GreenGo, although it is based on the larger scale of operation, also visible in a comparison of the assets and liabilities of the two companies in Chart 4.

Chart 4: Comparison of the statements of financial position for MOL Limo and GreenGo (2017)



Source: www.ebeszamolo.im.gov.hu

MOL Limo's assets value is considerably higher already before the start of operation. This is due to the fact that the company's fleet is recognised in the balance sheet, revealing a specific difference in lease accounting: MOL Limo prepares its financial statements according to IFRS, while GreenGo prepares simplified and unaudited financial statements. In addition, MOL Limo's owner needed to fund the generated loss already in 2017, as the total value of the equity was lost.

In terms of operation, it is important to mention that GreenGo only uses electric vehicles in the fleet in contrast to MOL Limo, which had 100 electric cars out of 400 in January 2019. In January 2019 GreenGo announced that it intended to increase the number of its cars to 300 within the foreseeable near future. Assuming this has been accomplished, these two companies run approx. 10% out of the roughly 4000 registered electric cars in Hungary. Additional information from February 2019 is presented in the Table 5.

Table 5: Registered users, fleet size and costs data for MOL Limo and GreenGo (2019)

Description	**GreenGo**	**MOL Limo**
Number of registered users	30–40,000	40,000
Fleet size	300 electric vehicles	100 electric vehicles 350 petrol vehicles
Costs	from 65 Ft/min	from 66 Ft/min

Source: www.greengo.hu, www.mollimo.hu

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Differences in lease accounting

Act C of 2000 (Accounting Act) and the International Financial Reporting Standards (hereinafter: IFRS) define lease differently. In Hungary financial lease is distinguished from operating lease on the basis of the formal ownership change. In contrast, IFRS defines it as a substance over form and a principle-based standard.

Table 6 shows the key fundamental differences between Hungary's Accounting Act and IFRS regarding operating leases not recorded in the balance sheet. Another difference concerns disclosure requirements, as the Accounting Act allows the recognition of operating lease in the profit and loss statement with periodically invoiced lease fees.

Table 6: Operating lease accounting in the Hungarian Accounting Act and in IFRS 16, from the lessee's perspective

Description	**Hungarian Accounting Act**		**IFRS 16**
	Finance leases	**Operating leases**	**All leases**
Assets		–	
Liabilities	$$	–	$$$$$$$
Off-balance sheet rights / obligations	–	$$$$$	–

Source: Author's comparison of the Hungarian Accounting Act and the IFRS 16 regulation

The principal aim of IFRS 16 is to have operating leases recognised as committed rights (rights of use – hereinafter ROU) among assets and committed liabilities to reduce the value of off-balance sheet items. For the entities reporting under the Accounting Act, this is not a requirement and, for instance, in the case of an independent financial analysis or a creditworthiness test, they may be invisible.

In Hungary approx. 90% of the vehicles used by car sharing companies are financed through operating lease. Consequently, the distinction between balance-sheet and off-balance sheet presentation may be significant for a creditor or for a financial analysis.

Reporting under the Accounting Act, GreenGo recognises operating leases as off-balance sheet items and thus may have a business advantage from a presentation perspective because the leverage ratio does not show the total minimum of liabilities from lease obligations.

Comparison to German entities

In order to present Hungarian car sharing companies in a proper context, they were compared to the top two German market participants car2go and DriveNow. Germany has the biggest car-sharing market in Europe and these entities present lead-

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ing examples. In the German industry 17 companies were found to contribute their services to the car-sharing segment. Nine of them were included in this survey as they had more than 10 thousand registered users. The following table shows the size of these companies on the basis of their annual financial data. These numbers include total assets, equity, income after taxes, revenue, and the annual cash-flow. As clearly seen, the two biggest companies, car2go and DriveNow, contributed more than 80% of the accumulated total assets and equity year by year. At the same time, note that these 2 companies were loss-making in the period reviewed (2014–2017). In contrast, 6 out of the 7 smaller firms were profitable. Note that the two biggest companies are currently merging and investing in their infrastructure, so their annual losses are being justified.

Table 7: Key data of German free-float car sharing companies

Company name	Registered users	Fleet size	Cities
SHARE NOW (Car2Go Europe GmbH & DriveNow GmbH & Co. KG)	3,000,000	7400	7
Flinkster (Deutsche Bahn AG)	315,000	4000	300
Cambio Hamburg CarSharing GmbH	77,000	1600	22
StadtMobil CarSharing AG Stuttgart	63,000	2600	100
book-n-drive mobilitatssysteme GmbH	43,000	1015	14
teilAuto (Mobility Center GmbH)	35,000	1000	19
StattAuto eG München	13,000	450	1
Greenwheels GmbH	10,000	300	22

Source: www.carsharing-news.de/carsharing-anbieter/

Development in the income after taxes and in the total assets were also analysed to assess the growth intensity and potential of the businesses. The following table lists companies in a descending order, based on the number of their registered users. It is clear that 6 of 9 companies show upward trends in their total assets, and 4 of them in their income after taxes. The 2 big companies have and will continue to have the largest share in the German car-sharing sector in the not so far future, while others like Stadtmobil, Stattauto München will be have to rely on local communities to supply them etc.

In 2017 the parent companies of both car2go and DriveNow decided to change the previous reporting practice. Since then car2go has been reporting in Daimler's consolidated financial statements and DriveNow in BMW's consolidated financial statements.

In 2016 car2go had considerably better results: an increase from an almost EUR 7.96M loss to EUR 3.8M. On a gross level, its operating profit also improved from EUR 2.6M to EUR 3.1M, which is consistent with increase in the revenue from sales activities.

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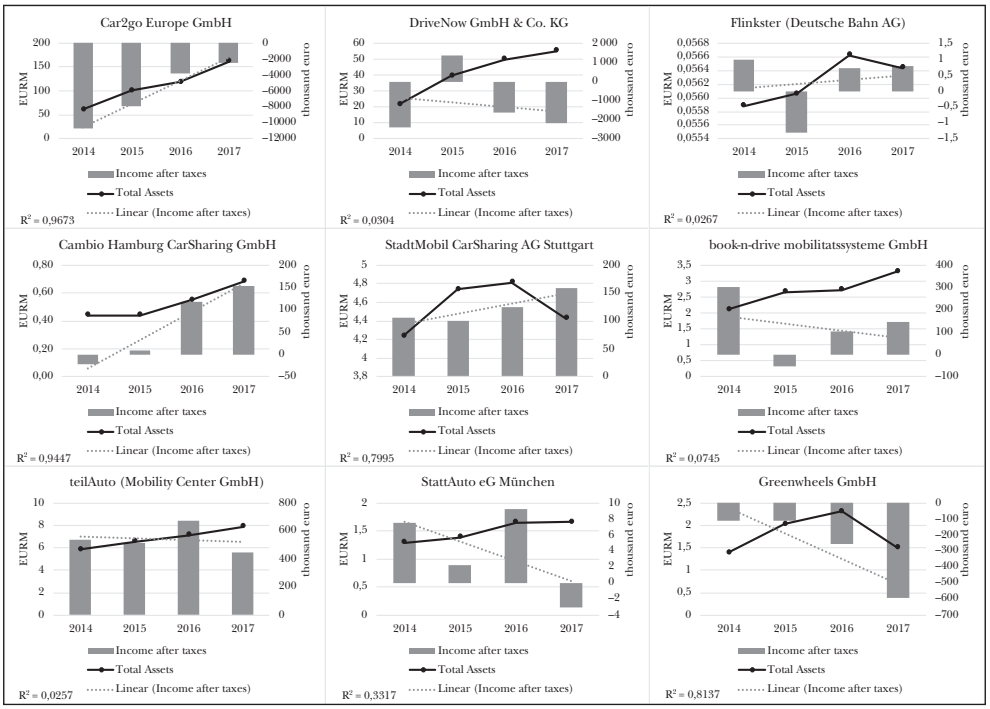
Chart 5: Income after taxes (left axis) and total assets (right axis) of analysed German entities



Source: www.bundesanzeiger.de

As of 31 December, 2016, the fleet of car2go contained 6754 vehicles, including 5900 smart ForTwo cars, 951 powered by battery. In addition, the fleets run by subsidiaries included 854 Mercedes-Benz vehicles.

DriveNow reported a loss of EUR 1.6M in 2016 compared to the previous year's EUR 1.3M profit. The report shows a significant increase in the fleet caused a rapid rise in lease costs from EUR 32.8M to EUR 41.5M. If such an increase had happened in 2016, the results and the lease costs would have increased in line with the sales increase (19.7%), representing only a total of EUR 39.3M, EUR 2.2M less expenses with approx. EUR 0.6M as the annual profit.

In 2016 DriveNow offered a total of 5400 BMW and MINI brand vehicles in eleven cities (3150 of them in Germany). This is to say in 2016 the fleet size was 35% larger than in the previous year (2015: 4000 vehicles).

Note that in agreement with the current market trend, in 2018 Daimler and BMW set aside their competition and released news of an agreement for cooperation in development and cost management. Such an agreement could serve as an example to follow in Hungary.

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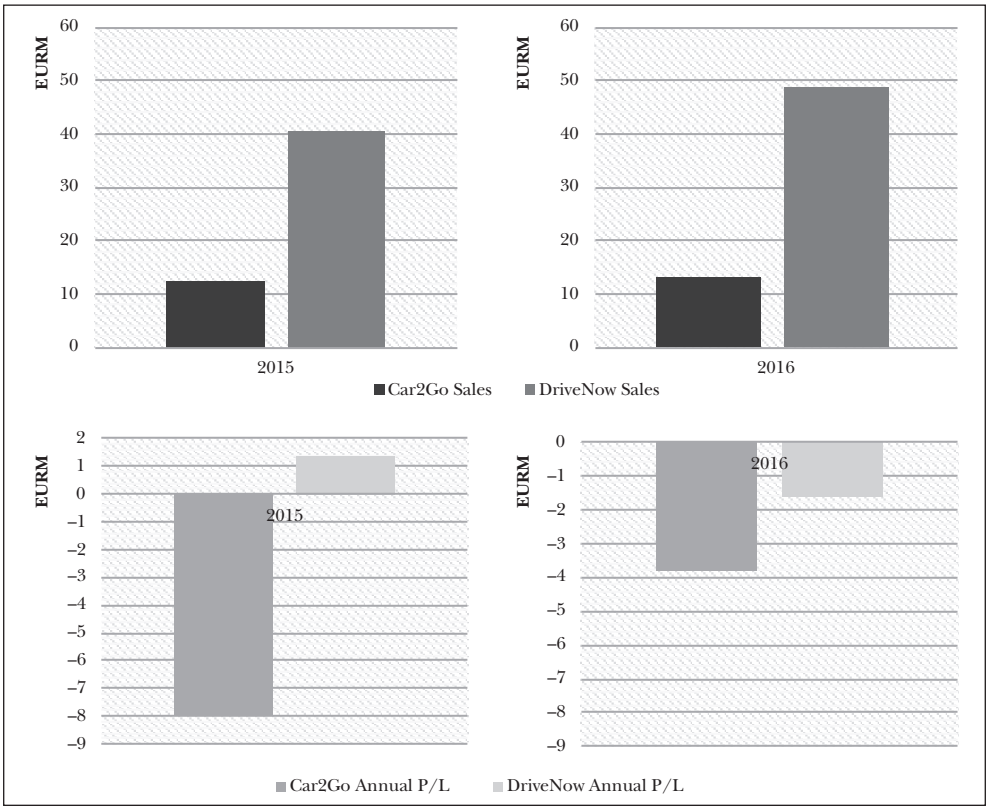
Chart 6: car2Go and DriveNow, sales and annual reports, 2015–2016



Source: www.bundesanzeiger.de

Conclusions of the financial analysis

As the fleet of GreenGo is financed mainly from operating leases, recognised as off-balance sheet liabilities and therefore securing the company an advantage in operation, because the vehicles need not be recognised or financed up-front. In spite of the operational advantage, this situation can involve the significant risk that the shareholders or creditors might not have all the necessary information for a proper market-based evaluation. It remains a question how GreenGo can utilize the fleet properly and whether they can generate cash-flow sufficient to finance the working capital. The company's solvency is rather unstable, as its profit and revenue heavily depend on fleet utilisation.

Sustainability

Table 8 shows the total stock of registered passenger cars in Germany, in Hungary, and in their capital cities. In 2017 Germany clearly had a significantly higher stock of passenger cars, 13 times that of Hungary.

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Table 8: Number of registered passenger cars in Germany and Hungary (2008–2017)

Location	Level	2008	2009	2010	2011	2012
Germany	country	41,183,594	41,321,171	41,737,627	42,301,563	42,927,647
Berlin	capital	1,091,164	1,088,221	1,105,732	1,120,360	1,135,704
Hungary	country	3,055,427	3,013,719	2,984,063	2,967,808	2,986,028
Budapest	capital	596,481	581,991	573,315	566,790	565,563
Pest	county/region	426,629	421,739	418,010	417,922	422,107

Location	Level	2013	2014	2015	2016	2017
Germany	country	43,431,124	43,851,230	44,403,124	45,071,209	45,803,560
Berlin	capital	1,149,520	1,154,106	1,165,215	1,178,417	1,195,149
Hungary	country	3,040,732	3,107,695	3,196,856	3,313,206	3,471,997
Budapest	capital	573,264	583,694	597,337	611,941	633,554
Pest	county/region	434,564	446,788	464,435	486,467	512,819

Source: HCSO, 2019b; Kraftfahrt-Bundesamt, 2019

The ratio of electric cars also differs greatly between the two countries: Germany has a relatively smaller ratio of electric cars due to its total registered passenger car stock of over 45 million. While the total number of German electric passenger cars rose by over 25 thousand, Hungary has a higher relative growth rate at 86.7% against Germany's 52.9% between 2017 and 2018.

Table 9: Number of German and Hungarian electric passenger cars (2017–2018)

	2017	2018									
	Dec	Jan	Feb	March	April	May	June	July	Aug	Sept	Oct
Germany, total	48,005	50,769	53,315	57,107	60,278	62,588	65,239	67,765	67,651	70,008	73,398
Hungary, total	4543	4836	5115	5565	5927	6356	6763	7112	7551	7916	8482
By category											
5E (purely electric)	2129	2238	2352	2611	2768	2959	3066	3190	3364	3522	3773
5N (Range Extension Electric)	1158	1236	1327	1431	1527	1639	1768	1866	1992	2124	2312
5P (recharge-able hybrid)	1255	1355	1430	1517	1626	1755	1928	2055	2194	2269	2396
5Z (other zero emission)	1	7	6	6	6	3	1	1	1	1	1
Regional distribution											
Budapest	2428	2575	2714	2989	3177	3400	3586	3754	3981	4174	4464
Other	2115	2261	2401	2576	2750	2956	3177	3358	3570	3742	4018

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	2017	2018									
	Dec	Jan	Feb	March	April	May	June	July	Aug	Sept	Oct
National statistics											
All passenger cars	633,554										
Ratio of electric cars to all the cars	0.38%										
Number of vehicles in the 2 companies	268										
Proportion of national electric cars	12.59%										

Source: Kraftfahrt-Bundesamt, 2019; Villanyautosok.hu

In the reviewed one-year period, of the four electric categories in Hungary, the number of 5E cars increased by 77.2%, with the number of registered cars peaking in March. The October 2018 increase in 5N electric cars by 188 is an absolute peak, while the total growth rate is near 100%. However, plugin hybrids performed only moderately. According to 2017 data, electric cars only made 0.38% of all passenger cars, of which the two car sharing companies represented 12.6% (268 electric fleet).

Three of the seven considerations appear in the official communications of the companies.

Table 10: Sustainability related considerations of sharing

Sustainability benefits of Sharing	**GreenGo**	**MOL Limo**	**BMW DriveNow**	**Daimler Car2Go**
Resource efficiency through using rather than owning	There is **less** emphasis on **parking infrastructure** and **road expansion.**		Digital parking service ParkNow	The smart ForTwo can fit in almost any parking spot and can manoeuvre around even the craziest downtown rush-hour traffic jams.
Low ecological footprint/low carbon	**300 electric cars**	The VW MOL Limo fleet is 350-strong (**100 electric** and 300 gas-powered)	**900** electric cars in Europe, **1300** in the USA	
	Shared cars are **smaller** than **newer** than those in the average household.			
Own less, interact more, build social capital			digital networking	Over 50% of car2go members don't own a car.

Source: BMW Group, 2017; Daimler, 2016; Penz et al., 2018; www.mollimo.hu/en; www.GreenGo.hu/en

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Table 11: Aspects of a sustainable sharing economy (SSE)

	BMW	**Daimler**
New business model	"The focus will remain on the development, production and sale of vehicles, with a wide range of innovative mobility services on top." (p. 11) "Providing opportunities to test BMW i3 as part of our DriveNow car-sharing scheme." (p. 60)	"Transport infrastructure and transport systems frequently operate at their limits, especially in urban areas. That is why Daimler has developed a range of pioneering mobility concepts." (p. 55)
Geographic expansion	"DriveNow is currently available in 13 European cities. On 8 April 2016, the BMW Group launched an advanced car-sharing programme in the USA under the name ReachNow." (p. 73.)	"The 300 new vehicles are being used in Berlin, and the additional models will also be introduced to other cities in the future." "In 2016, car2go was launched in the Chinese megacity of Chongqing with the brand suffix "JíXíng" (roughly: "drive off immediately"). The Daimler subsidiary car2go is the first international company to implement the free-floating car-sharing concept in China." (p. 55)
Public transport	"DriveNow in Copenhagen is operated by the city's public transport company Arriva. With their "Rejsekort", a card for almost all mobility services in the whole of Denmark, users also gain access to DriveNow. (p. 74)	"From the car-sharing provider car2go and the mobility platform moovel to the taxi app mytaxi, the coach company flixbus, and the Bus Rapid Transit (BRT) system." (p. 55)
Electric vehicles	"The fleet for both programmes currently comprises more than 6,000 vehicles in Europe, of which around 15% are purely electric BMW i3 vehicles. A further 1,300 vehicles are available in the USA. DriveNow is one of the strongest drivers of electromobility in Germany." (p. 71) "Copenhagen is the only city in Europe in which we have operated our car-sharing service from the start with a fleet of purely electric BMW i3 cars. The good charging infrastructure in the city offers ideal conditions for this." (p. 74)	"*car2go has added 20 smart ForTwo electric vehicles to the local fleet. This is the first step in evaluating the feasibility of using electric vehicles in our fleet by relying on Montréal's existing charging infrastructure, as well as determining how the city's climate conditions impact vehicle range and availability.*" www.car2go.com/NA/en/nextgen/

Source: BMW Group, 2017; Daimler, 2016

Conclusions

1. In terms of finances, in the period reviewed neither the Hungarian, nor the German companies (with a one-year exception for DriveNow) realised profit after taxes.

2. Regarding sustainability, three key areas can be identified as targets for the reviewed entities, including a) improvement in the efficiency of resource utilisation; b) minimising carbon footprint and c) building social capital.

3. In the reviewed sustainability reports, car2go and DriveNow were compared in the following four areas: a) new business model; b) geographic expansion; c) public transport; and d) electric vehicles. The basic idea of sustainable mobility is simple: "We need to shape our city mobility in a way that the ease and safety of our everyday

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mobility should not deteriorate but improve the quality of life now and in the future for the generations to come" (Tkatchenko, 2017).

4. With the recent merger of the two German entities (Roy, 2018), the most significant German service providers of this business line have significantly expanded their geographic scope. Nothing can prevent a business of this size from open new businesses in Central and Eastern Europe perhaps already in the near future.

Note

[1] Exchange rate: 2017 Yearly average rate of the Hungarian National Bank was applied 309.21 HUF/EUR. source: www.mnb.hu.

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Bettina Martus

Audit: Means of Sustainable Good Governance

A Review of Book by László Domokos

Summary

The book entitled *Audit: Means of Sustainable Good Governance* by László Domokos was published in December 2019 by the Akadémiai Kiadó, and it is a practical description of the role supreme audit institutions play in achieving social welfare through the establishment of the well-managed state. The book introduces many important ideas and provides guidance in a comprehensive manner.

Journal of Economic Literature (JEL) codes: G3, G18, M4, Y3

Keywords: good governance, sustainability, State Audit of Office, Fundamental Law

The book describes how the key institution of democracy contributes to the welfare of society. The author has comprehensive experience in leadership, and in the past ten years he has been a part of this work, i.e. the contribution to the establishment and maintenance of the well-managed state himself, so the book is an authentic and practical description of the role supreme audit institutions play, both domestically and internationally.

Several events make this book a topical one. The World Bank was exploring the idea of good governance in the 1990s already, and its significance was further increased by the International Organisation of Supreme Audit Institutions (INTOSAI). After the 2008, crisis it became obvious that major changes were required both in national economies and globally, which was bolstered by the Fundamental Law of Hungary, which entered into force in 2011. The United Nations developed its sustainable development goals, and a key goal is transparency in institutions. The list of events that contributed to the creation of this book could go on and on, but what I would like to highlight is an idea that ensures the book will stand the test of time: change is eternal, but it must be managed. Many events that took place in Hungary and in the world

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triggered changes that have affected and will affect society, so it is important that these should be managed properly.

The author describes the characteristics of the concept that is conventionally referred to as the well-managed state in Hungary and how it is related to the concept of good governance. Going through key events, it shows what effects these acts had on the concept of good governance and how the State Audit Office of Hungary as a key instrument of democracy can support international goals. The book also sums up the essence of Domokos's previous studies, e.g. how the static model of good governance is converted into a dynamic one, where, besides integrity and risk management, another major element introduced is change management.

The question comes naturally: what changes must be managed that contribute to the improvement of social welfare? Such changes in connection with the SAO included the increase in the number of audits and analyses, and the establishment of other capacity building tools/activities. The State Audit Office of Hungary is named, and its competences are described in the Fundamental Law of Hungary. The State Audit Office of Hungary performs its duty to protect public funds and public property through its audits and analyses. Over the past ten years, the number of such activities has multiplied, which means that in the course of its work the SAO can reach an increasing number of institutions and organisations, and it can ensure the protection of public funds in an increasing number of areas. Naturally, today we have more and more tools that can help us in capacity building, such as digitalization – the author describes this in detail as well, with a focus on the spread of information technology.

Like all institutions, supreme audit organisations must try to keep up-to-date and part of this involves creating an innovative and self-learning system. This means it is not enough to follow the changes triggered by digitalization, they must keep up with them. One idea doesn't guarantee success, obviously, and it can't be used in a live system first, so-called pilots are necessary. This is what the SAO does as well, so that errors in the system can be detected and corrected before we start converting every process into a non-productive or not very productive one.

As I mentioned in the introduction, the author of the book has accumulated knowledge in leadership and management and can rely on that in his work at the SAO as well. This is clear from chapter 10, where he discusses public sector management and the importance of leadership performance in public sector management. He discusses the importance of criteria like efficiency, economy and efficacy, and the roles of those who exercise proprietary rights and proprietary control (supervisory board) and of those responsible for operation (management). The role of the State Audit Office of Hungary in this is to point out, through its activities, where change might be necessary, what the typical errors are that need to be dealt with, and it also provides advice in these matters.

If organisations have clear and unambiguous organisational and operational rules with set goals and a strategy and if the management is responsible and observes basic ethical principles, we can say that organisations are on the right track to be able to contribute to the well-man-

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aged state. Experience shows that audits by the SAO help organisations correct their mistakes and improve their transparency and accountability, which means these audits are a kind of guarantee that the goal of the well-managed state will be achieved and maintained. It should be noted that changes based on audit findings are only possible if they are managed, so the role of the leader is extremely important.

The book summarises the key Hungarian and international events that underline the legitimacy of supreme audit institutions, and it describes major events from recent years in the SAO's life that also help establish and maintain good governance, including the potential in industry 4.0, change management and the importance of leadership. The book has a practical approach and it includes a glossary that helps the comprehension of readers who are less familiar with this topic: it lists the concepts and provides a definition for all of them, making the book comprehensible for everyone.

László Domokos: Audit: Means of Sustainable Good Governance. Akadémiai Kiadó, Budapest, 2019.

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Balázs Cseh

The History of Public Business Organisations in Hungary – Reflections Taking Further the Logic of the Book *East of Europe, West of Asia*

Summary

The purpose of this study is no more than to give a brief summary of the history of business organisations in public ownership in Hungary along the logic of a recently published large monography. Using the method of descriptive historical approach, facts are established as a result of a kind of syncretistic literature overview. As a basic idea, with a view to the "Sitz im Leben" approach, the evolution of public business organisations may be compared to the development of public finances, and should be managed embedded in the latter, similarly to the economy, which always functions embedded in the society.

Journal of Economic Literature (JEL) codes: B10, G01, N10, P10, P20, Y3

Keywords: public finance policy, public utility and public business organisations, Austro-Hungarian Monarchy, socialist planned economy, transition to a market economy, Hungary

Introduction

Public business organisations have a relatively short history in Hungary. Their development can be analysed since the 19th century. In my opinion, the existence of public business organisations as peculiar legal entities should be compared to the development of Hungarian public finances as they are closely and inalienably related to state finances and the general government. Due to this interrelationship, on the review horizon I describe the overall public finance environment of

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the given era, as a background to public business organisations and the hotbed of their existence and operation.

The evolution of public business organisations may not look back to times before the appearance of business organisations and their regulation by Hungarian company law, as the establishment of business organisations presupposes that of public business organisations. This follows from their conceptual definition, as under the currently effective statutory regulations, a publicly owned business organisation is nothing else than "a business organisation in which the Hungarian State, a local government, a local government's partnership having legal personality, a multi-purpose micro-regional council, a development council, a minority government, a minority government's partnership having legal personality, a budgetary organisation or a public foundation have majority control, either separately or jointly."[1] I have performed all this along the logic of and reflecting, among others, on two monographies by Csaba Lentner.[2]

Between the 19th and the second half of the 20th century

As Tekla Papp also correctly establishes, the first, perhaps somewhat weak, initiatives taken for the codification of Hungarian company law started with Act XVIII of 1840 (Papp, 2000). Of the corporations relevant for our topic, the joint stock company was first defined in this act (in addition to general partnerships and limited partnerships), and has remained one of, and also the most characteristic, legal forms of public companies ever since then. However, this legislation merely outlined a rudimentary formation of a joint stock company, which was unsuitable for construing the foundation of public businesses. The merit of this work is that it can be considered as the very first codification in Hungarian company law, which remained in effect up to the entry into force of the monumental Trade Act (which entered into force on 1 January 1876), in other words, up to the period after the Compromise. In 1867, nearly two decades of opposition and lengthy negotiations, the compromise between Austria and Hungary was born with Act XII of 1867. The Austro-Hungarian Monarchy, a state with two centres, which was established at that time, meant the alliance of two legally equivalent states. Common affairs included foreign affairs, military affairs and especially – perhaps most importantly, as, to quote General Raimondo Montecuccoli, "War requires three things: money, money and money" – finances, required to provide coverage for the first two. Csaba Lentner points out that the Compromise marked the beginning of some fifty years of a spectacular economic development (Lentner, 2019), and this is consistent with a similar assertion by historian Dániel Szabó (Szabó, 2001). That period already saw the appearance of significant economic thinkers, like Széchenyi, Wesselényi and Bezerédj, and specialised policy-makers managing finances, like Ferenc Duschek. Both Ernő Huszti (2001) and Lentner (2019) recognise this statesman's conceptual achievements in public finances.

The majority of finance ministers after the Compromise appropriately managed financial policy as well as the executive apparatus, but three personalities, Menyhért Lónyai, Kálmán Széll

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and Sándor Wekerle, stand tall among them (Lentner, 2017). Their knowledge, professional grounding and managerial skills were extremely high-standard, and it was no accident that all the three were also academicians, as recognised by Gábor Hamza (2015). The first public business organisation, the Hungarian state railways, which celebrated the 150 years anniversary of its incorporation recently, was established in this period. After 1846, exclusively privately owned railways operated in Hungary, disregarding a short period between 1850 and 1855, when the management in Vienna was considering state-owned railways. By 1855, the Austrian state treasury had been completely exhausted by the operation of state-owned companies; railways were once again given into private ownership. Then the wise Hungarian government realised the importance of a public holding strategy, and in 1868 it took a significant part of the railways into state ownership, and then in 1869 it established the Hungarian Royal Railways in the form of a joint stock company. This state-owned joint stock company continued its unbroken development up to World War I, and by the way, the company made profits. The other successful state-owned company was the strategically important Hungarian River and Maritime Navigation Limited (Suba, 2018). As a preliminary, mention should be made of the fact that the Danube Steamboating Company, established in 1829, had monopoly up to 1858. At the recommendation of István Széchenyi, this shipping company built the largest shipyard in Óbuda. For a long time, this was Hungary's largest industrial plant, which introduced a new work style, working methods and occupations with English contribution along the River Danube. After the 1867 Compromise, Hungarian national economic concepts and interests could be increasingly enforced within the Austro-Hungarian Monarchy. One such important transport-related business interest was breaking the predominance of D.G.T. in shipping by the establishment of an independent, state-owned shipping company that served Hungarian interests. In terms of public finances, this joint stock company could only be established from the reserve of the Hungarian Discount and Exchange Bank. However, this financial institution was Hungarian only in its name, as there was no independent Hungarian central bank at that time, and it met Hungarian companies' demand for external resources and acted as a lender to the government in a period when the one-tier banking system under the control of foreign capital (Kövér, 1992). The drawbacks of the liberal money management and allocation, characteristic of the time, are comparable to the recent past – I mean the period of history immediately preceding 2010.

The significance of state-owned companies in the national economy was particularly illuminating during the Great War, and then the period reviewed in this study falls between the two World Wars. state-founded and state-owned Workers' National Patient Support and Casualty Insurance Fund, which entered the market of insurers and provided insurance products citizens could initially use on a voluntary basis. On the other hand, the state-owned shipping company continued operation as an exemplary company, ensuring a peculiar ethos for its employees and was surrounded by general social recognition (Szávai, 2017). However, it

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is important to note – and I agree with Csaba Lentner's assumption – that the most important, landmark action taken in the financial and economic field in this period was the establishment of the National Bank of Hungary on 26 April 1924 and the setting up of independent monetary administration. Undoubtedly, this wise government decision has the highest impact on Hungary's current finances (Lentner, 2019). A similar conclusion is made by Károly Bognár (1994). In the life of the profitable and developing state-owned companies, the processes triggered by the 1920 Peace Treaty of Trianon – specifically, the damage caused to Hungary's territory, population and economy, which reduced Hungary to the smallest, economically and militarily weakest and, due to the international constraints, the most vulnerable country in Hungary's surroundings – caused drastic changes, and the government responded by their reorganisation, but without reducing state contribution, as it recognised that the state had an outstanding role in the national economic strategy. As a result of changes in the borderline, the country's economic structure was fundamentally re-arranged. The remaining economic structure became disproportionate, development halted and these trends were further increased by the mutual isolation policy. The previously uniform market was replaced by new customs borders, customs tariffs and economic policies.

The key characteristic feature of the early years in the period was that after several centuries of "limited independence", the country regained and created it sovereignty in every respect. In order to establish financial stability, a new national currency, the *pengő* was issued. The primary task of the first few years was stabilisation: the framework of the country's operation had to be set up and re-shaped, the internal and external political and economic relations had to be re-organised and the national currency had to be created. Lentner correctly recognises that the economic consolidation and the stability of public finances may be best related to Prime Minister István Bethlen; however, he critically notes that the statesman should not be placed on a pedestal (Lentner, 2019). The country successfully stabilised the economy, society and the political institutions, and despite difficult circumstances, by 1929 the national income had increased by 10 per cent, while an impressive economic growth had been achieved relative to the low point seen after World War I.

The defensive economic policy of the era, increase in state holding and ownership, and strengthening Hungarian working capital increased the number and weight of state-owned companies: state-owned industrial factories were established one after the other, and the hotel business, recreational and spa facilities flourished. However, the 1929–1933 global economic crisis broke the impetus of development and contained companies' opportunity to operate. Financial problems were encountered in Hungary in 1931, but already in the previous years, several countries in the region had accumulated short- and long-term debt, and primarily American and British lenders, who did not feel safe, started to withdraw their loans, causing serious payment problems to the state. In 1931 the disclosed collapse of the huge Viennese bank Creditanstalt further accelerated

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the process. The purchase of foreign currency by Hungarians increased and significantly reduced the central bank's currency and metal stocks – similarly to the developments seen during the 2007–2008 crisis. Hungarian financial institutions, with ownership and shareholder structures already showing signs of increasing state role, satisfied all demand that were made, and nevertheless, the risk of panicky deposit withdrawal was threatening, and did actually take place in Bucharest, Sophia, Athens and Germany. Bank closure could not be maintained for a long time, since not only payments were not transacted but taxes were also not collected and wages could not be disbursed either. In 1933, the nominal value of the national income dropped to 55 per cent of the corresponding 1929 figure, and even in 1938 it only exceeded the pre-crisis level by 7 per cent. As a result of the crisis, austerity measures were taken, e.g. public servants' salaries were reduced significantly, and as this hindered state operation – and the functioning of state-owned companies, which were major employers –, it also impeded the government's crisis management. The economy of the new Hungarian state proved to be vulnerable. In 1937–1938 the per capita national income was about USD 120 or 130 of the time, amounting to approximately 60 per cent of the average of Europe. Starting from 1924, foreign capital came in the form of short- and long-term loans, and was then followed by a major influx of working capital into the industry. Primarily American, British, German and, to a lesser extent, French capital bought interest in the Hungarian economy. In 1929, the ratio of foreign capital was 28 per cent, which gradually decreased to merely 24 per cent in 1938. After the outbreak of the war, due to German economic penetration, the share of foreign capital increased again. Drawing conclusions from the experiences of the crisis of the time, Lentner cautions against attracting extensive foreign direct investment, borrowing from abroad and exposing the Hungarian national economy (Lentner, 2002; 2016; 2019).

Second half of the 20th century

After World War II, Hungary was excluded from western financial modernisation for a long time. Our region was placed under the influence of the Soviet Union, which liquidated the market economy built on private ownership and forced its own social and economic system of a "collective dimension" on the countries of the region. For example, in 1946 the above-mentioned state-owned shipping company was liquidated and a Hungarian-Soviet shipping company (Magyar–Szovjet Hajózási Rt.) was established, which was subsequently replaced in 1955 by the Hungarian shipping company (Magyar Hajózási Rt.), which has been attending to river and maritime navigation, operating and supervising harbours since then. The harmonic and balanced coexistence of public and private business organisations was disrupted. In fact, only the banks taken into state ownership (National Bank of Hungary and the Hungarian Commercial Bank of Pest) and foreign trade companies (e.g. Export Trade and Goods Purchase Ltd. and the Hungarian Foreign Trade Ltd.) operated in the form of commercial businesses, for the most part as joint stock companies and only an insignificant number of them were lim-

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ited liability companies (Perbíró, 1950). The annihilation of the institutions of civil society, private capital, private companies and the private market, or their reduction to purely formal entities, was accompanied by the confinement of market economy ("money economy") at the end of the 1940's. Economic procedures were replaced by the planned economy regime. Law-decree No. 20 of 1949 ordered the taking of medium-sized industrial companies and enterprises in state ownership. This action also required the establishment of a new kind of controlling organisation due to the large number and diversity of companies. Decree No. 102/1950. (IV.4.) Mt. fulfilled this demand by subjecting state-owned companies to control under an association (Papp, 2000). Lentner (2019) gives a critical description of the poor finance policy of the period; however, his critical tone does not contain exaggerated catchphrases or unreasonably sharp remarks. Katalin Botos (2007) also recognised and highlighted the fact that social tensions were traceable not simply to economic difficulties. With this assumption she refines Gremuska's findings. Gremuska does not draw a dividing line between the Rákosi and the Kádár regimes (Germuska, 2012), in contrast, Lentner (2019) demonstrates that there are essential differences between the finance policies of these two periods, and ascertains that from the late 1960's, Hungary moved towards the implementation of a planned economy saturated with market elements and giving residents every chance to succeed. Due to domestic political efforts at restauration and the displeasure of the soviet political leadership, supported by foreign political and military pressure, this transformation could not be completed, however, it provided a good basis for start of transition to a market economy at the end of the 1980's, although opportunity for the latter was, for the most part, seen in the attraction of external market participants to Hungary. I agree with Lentner who compares the downfall of Hungary's own method of planned economy mostly with the failure of the 1968 reform efforts (Lentner, 2019). In addition to state companies having a homogeneous and monopolistic role, this period was characterised by the fact that the Finance Ministry merely administered financial transactions, as planning was given priority and money was assigned a passive role. Pricing was applied in the planned economy, but indicating relative shortage was not included among the primary tasks of the price regime. Factories did not produce because goods had low prices, as prices were essentially set by the authorities, who also decided in any other matter. For this very reason, in the case of state companies, profitability or efficiency were excluded and not applicable. Although public business organisations have the most profound role in the People's Republic of China, and Chinese public business organisations are in the focus of research and the international literature, they significantly differ from the public companies that were operative in the People's Republic of Hungary (Milhaupt, 2020). This goes to show that the state companies of those days and the current ones should not be blurred, despite the fact that the same expression is used when they are referred to, as we can squarely state that differences between them can be demonstrated in everything else.

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In the period of transition to a market economy, in other words, between the change of regime and the turn of the millennium, a compulsive assertion of the correctness of the government's financial decisions was a constant practice. In this respect, Erzsébet Gidai (1996) was of the opinion that the largest obstacle to financial stability was external indebtedness. The assumptions that Hungary would be raised by the influx of direct investment and that its government deficit could be offset by new borrowing can be considered incorrect. Moreover, they urged the privatisation of nearly the total amount of assets held by the state, and complete termination of all the companies in state ownership, and they wished to accomplish the full annihilation of the government's role. One of the decisions that can be considered especially flawed – mainly in the case of state-owned companies – was the promotion of the philosophy underlying the Washington Consensus, which says that the state should withdraw from economy influencing and the government's role should be reduced in order to create a vigorous, efficient and successful market economy, or to put it in another way, the neoliberal economic policy that characterised the 1990's (up to 1998) in Hungary. In contrast, György Matolcsy (1998) recognised as early as 1998 that there was a need for the state to undertake a greater role, and so state ownership should be increased in the strategic sectors. Using a perfect and neat argumentation, Lentner (2019) demonstrates the misguided political decisions that resulted in Hungary's significant exposure to the 2007–2008 global economic crisis. These did not include the decisions adopted to consolidate finances and stabilise the economy in the period between 1998 and 2002. We have to agree with Csaba Lentner and Nobel Prize awarded economist Joseph E. Stiglitz, who think that the macro-economic models used by neoclassical economics were unsuitable for forecasting crises; they were built on flawed premises, and unreasonably justified an even supply of information and that stakeholders always made reasonable decisions. In Stiglitz's opinion the absence of an appropriate theory also misleads economic decision-makers and triggers crises. Lentner traces back Hungary's crisis to these misguided decisions, and concludes in addition that the decisions made by the various governments between 2002 and 2010 blindly followed the neoliberal market economy model, and consequently, innovation in banking products was not followed by innovation in the supervisory and regulatory regimes, which led to the unfolding of a crisis not only in mortgage lending but also in the entire neoliberal economic regime, as also believed by Tibor Tatay and Krisztina Szegedi (Lentner et al., 2017). We should agree with the claim that the first step on the road leading out of the crisis was increasing the role of the government (Lentner, 2019), consequently the strengthening of public business organisations, especially the repurchase of the shares in MÁV (the Hungarian State Railways), the acquisition of shares in MOL (the Hungarian oil company) or the establishment of an increasing number of waste management companies in local government and the state ownership, and increasing the state's share in the energy market (district heating, Paks Nuclear Power Plant etc.).

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In addition to increasing state ownership in companies operating in strategic sectors, increasing the number of public companies and their role in the economy, favourable developments took place in fiscal policy, including the placing the Hungarian tax regime on a new footing after 2010. The principal elements in this change included a change in the structure of taxation, through reducing taxes on labour and capital while simultaneously increasing taxes on consumption (Varga, 2017), which improved the efficiency of public companies' operation. Legitimisation of the tax system and the entire economy and the reduction of the shadow economy have turned general distrust in public business organisations and the opinion that they were the hotbeds of corruption and the embezzlement of public funds. The efficient and successful controlling and supervisory role of State Audit Office had no small part in this, as by statutory authorisation, it has regularly audited state- and local government-owned business organisations since 2011. Another major contribution was the incorporation of elements like the ideas represented by leading economists György Matolcsy (2016) and Domokos László (2015) in thinking about public finance. With the restoration of the institutional approach and with the appreciation of transparency, a public finance management approach, unconventional economic policy and illiberal economic thinking, a new era commenced in the operation of public (government and local government-owned) business organisations. For this reason, these companies have become the engines of economic growth, and as the professor puts it: "If there is growth, and financial balance underlying growth, and if companies and employees are interested in expanded reproduction, economic policy leads to success" (Lentner, 2019, p. 250). The most recent milestone in the favourable trend seen after the crisis is the amendment of Act CXXII of 2009 on the more economical operation of business organisations in public ownership, which affects most businesses in local government or state ownership. The amended regulation, which entered into force in January 2020, represents a significant change in the requirements related to the management of public organisation, primarily in respect of requirements relating to internal control and supervisory boards, to the personnel of internal control organisations and to their work performance, and to the newly established compliance organisations. In addition, Hungary seems to be joining the developed European states through the good practice of public business organisations (Kecskés, 2019).

Conclusion

In conclusion of the brief overview of the history of 150 years and of the historical experiences, although the brief history Hungary's publicly (state and local government) owned business organisations had its ups and downs, due to the favourable changes implemented in the most recent past – in the field of public finances – gives a forward-looking picture. Initially (in the first half of the 19th century) we could experience that such companies were established with a delay compared to the West, as the state or government, acting as legislator, only recognised its significance considerably later.

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Due to the favourable fiscal environment after the Compromise, the gap was closed and well capitalised Hungarian state companies of strategic significance and representing national interest were established and rapidly developed for more than fifty years, although naturally, the world historical impacts broke this curve after the Peace Treaty of Trianon, and then again as a result of the 1929 crisis. It can be established that during socialism, an economic approach unfamiliar to Hungarians and inflicted on the country by external force, state farms were by nature extremely different from the public companies that operated before or that have been operating since that period. In the period of privatisation and during the spread of the neoliberal market economy, the significance of public business organisations declined considerably, due to the flawed fiscal and public finance policy characteristic of the period. Proof positive of the close and inalienable relationship between public finances and public companies is the change that took place in this respect.

Notes

[1] Article 1 b) of Act CXXII of 2009 on the frugal operation of business organisations in public ownership.

[2] In relation to the books by Lentner, 2019, and on the same topic: Lentner, 2020.

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Balázs Botos

Review of the Book Entitled the *Preservation of Values in the 1950's. The Story of Gyurka (György Rozgonyi) and His Youth Movement*

Summary

The "illegal" youth movements that evolved in District XI of Budapest in the 1950's set the objective of preserving the values of the "old tradition" the socialists wished to change: those of the middle-class culture and heritage of Europe. Giving a glance of the activities of these communities, the hidden life of the church, hiking built on scout traditions and the state power's reprisals, the authors' picture and analysis of the period may be of wide interest.

Keywords: György Rozgonyi, church ethos, Catholic youth movement, soviet type dictatorship, 1950's, Budapest

This above-mentioned, recently published book was written by György Rozgonyi, leader of his youth movement in the 1950's and two other members of the group, Gábor Papanek and Gábor Veress. The book gives an overview of the history of a major Catholic youth movement, considered as illegal by the regime of the time, and provides information about the participants' subsequent lives. It is an accurate historical record, recommended not only for those interested in that period, as it reads well and draws the attention to values and experiences that remain valid today.

This community was established in 1952 in the heart of District 11 of Buda-

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pest (called Szentimreváros), and was active until 1961, when it was terminated by the government. In the beginning there were five to eight members aged 12–16, but their number quickly increased as a result of Gyurka's efficient organization: within a few years the group had 100, 150 and then 200 members. They were occasionally replaced: older ones left and young teenagers joined, but later on university students also became part of the community. It was not a proper organization as it was unnamed and had no officially established seat. It did not develop a hierarchy, and its leaders did not have titles or set competences and duties (the leaders were called by their first names or nicknames). Throughout the years the movement consisted of small independent groups of five to eight members, led by people who were a few years older, without much interaction between the groups. Nobody has been able to compile a complete list of all the participants' names, not even the State Security Network.

The book begins with a preface by historian Dr Frigyes Káhler, followed by the author's short introduction. The first chapter gives an overview of the historical background, emphasizing that in the late 19th and early 20th century, Szentimreváros developed fast and most of the inhabitants newly settled in the district were intellectuals. Its predominantly Christian middle-class background was first ensured by local chapels, later churches, and then also by educational institutions such as the Technical University of Budapest, the Cistercian Secondary Grammar School and the St Margit Secondary Grammar School. After 1945, this spiritual orientation came into sharp conflict with the new Muscovite government's aims and actions taken to gain and maintain power, which often included sending people to forced labour in the Soviet Union, notoriously known as "malenkiy robot" (Russian for "little work"), political assassinations, dismissals or forced retirement for political reasons, internment and deportation. However, these actions of the "dictatorship of the proletariat" triggered general aversion in society, which was further enhanced by the nationalization of well-known high-quality parochial schools, dissolution of the monastic orders teaching in these schools, and the termination of the scouts' movement, which had been doing an excellent job in child training.

The predominant claim made in the next chapters is that the "illegal" youth movements that emerged rapidly in the wake of these power policy endeavours actually set the preservation of the European middle-class culture (in modern terminology: values) as their objective.

– Their priority aim was to familiarize the youth with the two to four thousand years old Judeo-Christian teachings, with focus on the most beautiful Bible stories, the moral principle of "love your neighbour as yourself", and the most important religious ceremonies.

– During their community gatherings (after Bible studies and during short cultural and fun activities, games and discussions around campfires etc.) they inevitably talked about the unspoken essential elements of "erudition" (newly discovered scientific facts, important or new historical knowledge, world-famous works of art – and also the principals of cultured social behaviour).

– As they followed the traditions of scouting, including events such as train-

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ing and hiking in small groups led by older teenagers, they could preserve the previously successful educational practice.

– In addition to these values, equality was practiced in the community; and the activities of boys' and girls' groups only differed in minor, specific aspects.

The second chapter is about the formation of large numbers of new youth groups in District 11 of Budapest (similarly to a general trend throughout the country) from the end of the 1940's. Numerous priests, former scoutmasters, teachers and parents joined forces, in spite of persecution, to teach their children the basics of morals and ethics and to ensure that they spend their free time in Christian communities. Young people refused to replace these activities and ideas by the new concept of class warfare and the romanticism of partisanship, instead, they wished to acquire middle-class "erudition" and to experience the adventures of scouting. These communities mushroomed without official approval; some, ignoring the fact that scouting had been prohibited, continued their scouting activities along with teaching divinity and religious values. Others sought to achieve these goals in Indian camps, hiking and cave exploration clubs. In the first years, Catholic Benedictine, Cistercian, Pauline, Piarist and Regnum priests, and Lutheran and Calvinist ministers undertook leadership in these communities. When the religious persecution of priests and clergymen intensified, certain Catholic circles endeavoured to achieve their goals without direct help from the church. In Protestant communities young people were confined within the boundaries of church institutions.

The third chapter is the longest and most important one, as the information about Gyurka's community, unfamiliar for most of the present generation, featured the secret life of the clandestine church, as put by the author of the preface. It is divided into three parts according to the age groups of the participants.

What may be understood as "news" for many people nowadays is that the school curricula for primary schools between the 1st and 8th grades was mainly built on former religious schoolbooks, which focused on famous Biblical stories, life changing events of church history, Catholic liturgy, the presentation of the sacraments, and the basic teachings of ethics. These included the Books of Moses and some of the historical books of the Old Testament, showing God's love for the world he had created and especially for humankind. It was taught that, despite the fact that they had been granted free will, people should behave according to God's will and keep his laws, and those who violate them commit a sin and should expect its consequences. However, it was strongly emphasized, in accordance with the New Testament, that whoever repented of their disobedience would find mercy and forgiveness from God. Learning about the sacraments and church ordinances such as baptism, confirmation, the Holy Mass, confession, the Holy Communion and assistance to the celebrant in a liturgical service were also important parts of the curriculum.

The young tutors, whom the students often shared their problems with, had to prepare thoroughly for teaching these Christian principles, since the smart students often had questions about the conflict with the atheist ideology taught at

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schools. At the end, however, these tutors were filled with joy to see their students finally learn these values despite the fact that they would only apply them as adults.

The young tutors, mostly between 16 and 20, also encountered considerable challenges in teaching teenagers using typed texts, jokingly called "holy lettuces", in addition to schoolbooks. The challenge was not a comparison with the mandatory official, low-quality materialism taught at school at that time, since the latter was easy to exceed, rather the exchange of views with the students interest in "serious" topics, who asked for and read related books, and readily participated in discussions about them. Although the students did not expect infallibility, they would not have tolerated factual ignorance concerning religious topics, such as Biblical names, dates and sites. Teaching Christian ethics and morals had its pitfalls not encountered in secular school education. One such challenge the young teachers faced was helping their teenage students – who were familiar with the practices of the Rákosi and then the Kádár era – understand the strict moral standards set by religion without offending those living with family members who already did not follow these norms. For example, they had to convince these students that telling lies and stealing were unacceptable despite the fact that it was widely practiced everywhere in the state hierarchy and had become increasingly accepted societal norms. They had to address sensitive topics, such as whether not telling the truth to the officers of the State Security Department was a violation of religious or moral principles, if premarital sex or abortion were acceptable, and how to behave with those who did not follow these recommended principles.

The authors especially emphasize that the knowledge passed down in Gyurka's communities was not limited to religious and ethical issues. Students received a wide variety of information about numerous other topics. For instance, relating to creation, they discussed information about astronomy, nuclear physics, biology, while on other occasions, history, literature or art history were discussed. The altar boys' duties included learning some Latin, occasionally with an outlook on the spiritual background of the texts. The musical culture of the youth was also improved through singing folksongs while they had a rest during hiking and around campfires. Due to the success of the first dance occasion in the early years, similar events were organized later on, and served as opportunities for learning the basics of polite social behaviour. Those who undertook leading roles could also gain experience in leadership and were actually trained in management from the very beginning of the movement.

Hiking, based on scouting traditions, was another fortunate complement to religious education. The participants had the chance to recognize that although (in a myriad of topics) their leaders knew a lot more than they did, yet they endeavoured to expand their knowledge. In addition, as a positive lifetime experience they could see their leaders put the proclaimed principles into practice: during their hikes they represented the community's interests, gladly took care of the younger ones, undertook to address all the problems faced during the programmes, bore the biggest burdens, and did not expect any advantage in return.

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The next years and decades evidence that despite all the difficulties, this community training has been successful. Most of the former participants interviewed in the late 1980's and in 2017–2018 claimed that they had industriously studied the community curriculum and it had a profound effect on their future behaviour and on their whole life (Kamarás, 1992, p. 110, 179).

A unique part of this chapter is the information about the one-time university students' small group. Also called Forum, it consisted of ten to eleven members, who discussed pre-selected topics at their monthly self-study group gatherings. Most often a member – or occasionally an invited outsider – compiled and presented a brief introduction to the subject, and on other occasions they read out short stories and poetry, listened to music, watched slides, or organized visits to theatres and then discussed the parts they considered worthy. The specific topics of the programmes varied greatly, but unfortunately, a full inventory has not been retained. There were hardly any specifically religious programmes. Several members reported on scientific problems in their respective professions. A member working as a physician raised "health" topics several times. Occasionally, issues concerning social sciences were also discussed, and some arts and sports-related gatherings were also successful. All the participants found these meetings useful, as they could increase their knowledge.

Despite the fact that the community made little effort at concealing its activities, it was not until 1958 that its work became a matter of interest for the State Security. From that time on, the participants were investigated, attempts were made at sending undercover informers to the gatherings and later on, some the participants were approached and requested to act as snitches. At night on February 6, 1961, the homes of several members[1] of the (Catholic) communities considered illegal, including Gyurka, were searched. About 80 people, including Gyurka, and many other leaders and members of similar communities were arrested that night. During the interrogations, most of them were incarcerated on remand. In the months following the mass arrests, additional people were also interrogated and arrested. Those arrested were accused of being involved in the "Black Ravens" conspiracy to illegally organize a "Christian-Socialist bourgeois regime" (Hollós, 1967). Gyurka and his community were accused of being part of this conspiracy by joining the so-called Christian Front (a small group of about 20 supporters, which became a political party in 1956). As physical torture was stopped perhaps in the late 1950s, evidencing the allegations during the investigations and interrogations was unsuccessful despite extreme verbal abuse, inhumane detention conditions, psychological pressure and threats. Nonetheless, the prosecutors insisted on their concepts, the courts indicted a hundred and eighty people in seventeen lawsuits, and eighty-six of them were imprisoned for a term between one and seventeen years (Gyurka was sentenced to three and a half years) and additional eighty people were sentenced to other punishments. Another hundred and eighty indictees were retaliated without any court hearing (Soós, 2017). However, the society did not accept the courts' position already back at that time, and so

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most of the rulings were overturned after the change of regime following the fall of the Soviet Union.

The forth chapter provides information about the fate of the "illegal" groups of the 1950s, particularly Gyurka's community, after 1961. It also records that most Catholic youth communities terminated their activities in 1961, so in the late Kádár era religious education was limited to the few remaining Catholic schools, and in an extremely low number of communities (small groups gathering in the sacristies of Catholic churches and in various rooms in Protestant churches), which were all kept under surveillance. Gyurka's community also fell apart. In the following years, the time spent in prison and other state security interventions without court hearing resulted 5–15 years of delay in the careers of many participants. Therefore, by 1990, by the ages of forty to fifty, none of the members had been able to advance beyond middle management positions (and, as a result, they were unable to use the knowledge they had gained in community or in broader social circles). Despite the fact that the "illegal" community activities were terminated in the particular circles, the state security continued to monitor them for a long time (regardless of its cost, use and consequences). Until the 1970s and 1980s, data was collected about their private personal meetings, the places of their excursions or rowing. The leaders and several members of the former youth communities were wiretapped. Those who yielded to pressure became informers (about nothing). As a consequence of the latter practice, the gap between Hungarian society and politicians deepened, counter-selection in human management continuously increased, and the economic development rapidly declined. Shortly (after the failure of Gorbachev's attempt to correct the harmful effects of the soviet terror), these processes led to the overthrow of the Hungarian socialist leadership.

Due to a lack of documentary knowledge of historical perspectives, the authors could only make a few comments about the activities after the change of regime. They mention many positive changes beneficial to society. State security interventions were terminated. The standard of living and travel opportunities for the participants of the former "illegal" communities, including the surviving members of Gyurka's community, have improved. Christian education was no more a duty undertaken by a few marginalized, self-serving small communities, it was returned to churches and (ecclesiastical) schools. The overvaluation of post-regime progress would be a mistake as it could mask our duties to continue to develop.

The fifth and final chapter aims to summarize the lessons of the book, and touches upon the things to do in the future. As during their work, the authors frequently faced the absence of information concerning the "illegal" activities of the communities, they feel it is imperative to collect and compile information regarding that era. What they consider most crucial is the use of this historical experience. The book sheds light on the fact at that time quite a few former teenage leaders successfully handled pedagogical situations many professionals failed in and would still fail in today, during the current worldwide educational crisis. Therefore, the authors con-

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sider this past experience worthwhile to examine.

A different question is how to make use of the findings of an analysis of this past experience. The authors primarily address the conclusions regarding education. They urge a deeper than the current presentation of the key elements of European culture, and within that framework, mandatory familiarization with the Catholic religious traditions. Nevertheless, the matter they identify as really important is that schools should not only teach, but also edify. Within this framework, they should more broadly capitalize on the potentials in scouting. At the same time it is mentioned that success indispensably requires support from the society, especially from the parents, just as much as in the past. The current crisis of values (the undervaluation of integrity and professional knowledge, and the overvaluation of wealth and high contacts) is identified as a significant obstacle to future advancement. In addition, the authors express their hope that the Hungarian society will re-adopt traditional European cultural values, namely, it will regard knowledge and learning as vital; will treasure faith in the maintenance of its citizens' freedom and equality; and will preserve the Christian principle of loving one's neighbour. In the epilogue, the Jesuit Father Szabolcs Sajgó asks God's mercy to allow the authors' hopes come true.

The information given in the book is confirmed by rich bibliographic references, a register listing 200 members and more than 30 photographs.

Gábor Papanek, György Rozgonyi and Gábor Veress: Értékőrzés az '50-es években. Gyurka – Rozgonyi György – ifjúsági közösségének a története [Preservation of values in the 1950's. The story of Gyurka (György Rozgonyi) and his youth movement]. Cistercian Student and Scout Foundation – Cistercian St. Imre High School in Buda, Budapest, 2019, 203 pages.

Note

[1] Typically, there wasn't even an approximate number found in the literature. Tibor Pethő wrote in the *Magyar Nemzet* issue of 19. 05. 2012 that there were more than 1000 search warrants in the Black Ravens case. According to Miklós Csapody, however, more than 1,000 actions were realized on the single night of February 7th. According to Viktor Attila Soós, however, between November 1960 and March 1961, barely more than 200 house searches were conducted (Soós, 2017, p. 136).

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Tamás Prugberger and Erika Sebestyén

Three Leading Intellectuals on Hungary's Changing Situation – Ramblings in Relation to the Book *Hungary in a Changing World*

Summary

Following its 2015 release by Éghajlat Publishing, the collection of interviews with three leading Hungarian intellectuals, Mihály Patai, László Parragh and Csaba Lentner, sharing their ideas of the world and, more specifically, of Hungary's 21st-century perspectives, was also published in English in 2019. The thinkers portrayed in the book recall their experiences obtained during the period of socialist economy, their personal calling, the events of the nearly three decades that followed the collapse of the soviet bloc, including transition to a market economy, and of the last nearly one decade since the 2007–2008 crisis, especially the new Hungarian economic and social policy model in the making since the 2010 change of government. The book was published by Éghajlat, with support from the National Bank of Hungary, and includes a foreword by Academician László Palkovics, Minister for Innovation and Technology, edited by Lajos Péter Kovács and Klára Lengyel and proofread in English by the late Dr Roger G. Roe, who has, unfortunately, deceased since then.

Journal of Economic Literature (JEL) codes: A2, B1, E6, F11, F65, G01, H6, N10, O15, P20, Y3

Keywords: Hungarian economic and social policy, socialist planned economy, neoliberal transition to a market economy, proactive state model, European Union, world economy, globalisation

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About the book

A collection of interviews made with Chairman of the Hungarian Banking Association Mihály Patai (currently serving as Deputy Governor of the National Bank of Hungary), Chairman of the Hungarian Chamber of Commerce and Industry László Parragh, and professor and leader of the Institute for Public Finances and the General Government at the National Public Service University Csaba Lentner was published by Éghajlat with the title *Hungary in the Changing World*. The interviews were moderated by Lajos Péter Kovács, director of Éghajlat Publishing.[1] In the book, Hungary's economic policy is discussed from the collapse of the socialist planned economy, in other words, from the 1990 political and economic change of regime of these days, seen from the perspective of the aforementioned three leading economists. This novel and non-traditional book of interviews examines problems in a complex manner and provides proposals worth consideration for the political and economic management. The English version of the book resembles a roundtable discussion, with the interviewer practically acting as a moderator. The structure of the book is outside the box. In order to make the exposés more interesting and gripping, the interviews are imagined in a conference hall, with the interviewer acting as a moderator and the informants as participants of a roundtable discussion. There are two reviewers among the listeners (professor Tamás Prugberger and Erika Sebestyén), who have recorded the essence of the responses to the questions and have added their imaginary contributions to the report and now present their ideas to those who live in English-speaking territories and speak English.

Now let us discuss the content of the chapters

The first topic addressed by the roundtable took the economic policy of the Kádár era preceding the 1990 change of regime as its starting point. In response to the moderator's question about how everyday people could live in relative welfare compared to the so-called "genuine socialist" countries of the soviet sphere of influence in Central and Eastern Europe, which gained Hungary the reputation of the "most cheerful barrack" of the COMECON member states. The respondents show that people could secure this relatively high living standard by semi-legal ways that evolved and were tolerated during the Kádár regime. At that time the state not only tolerated but – at a later phase – even supported it. As also mentioned by the "three professional tenors" of the roundtable, this included various economic and corporate economic partnerships and under-the-table work done after or during official working time, and in cahoots with one another, company employees could make additional private incomes using state-owned companies' materials and instruments. The spontaneous and public administration-controlled privatisation preceded and followed the change of regime under these conditions. In response to the moderator's question, the participants sitting around the fictitious roundtable mentioned that the application of various corruption techniques and methods prevented the government from realizing considerable revenues from either spontaneous or gov-

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ernment-controlled privatisation, as the overwhelming majority of foreign companies wound up the majority of the companies transferred to them and reorganised during the 1980's from loans, in other words, their goal was market penetration rather than the maintenance of the operation of these companies. The speakers also mentioned that Hungarians (with notable exceptions) also acquired considerable business assets, however, most of them wasted them instead of investing them in business, or simply used them up without even establishing a business. This also characterised the newly established commercial banks, which granted loans under lenient conditions, went bankrupt as a result, and had to be topped up from public assets. Then they were sold by the government to foreign banks and continued operation as subsidiaries of the latter. In their comments the reviewers spoke of their experiences obtained in relation to privatisation. Already before the change of regime foreign companies had contracted cheap Hungarian outworkers for the manufacture of their products. When it came to privatisation, they agreed with the corporate management to undervalue the company, transform it to a company limited by shares and acquire it cheap, allowing, in their capacity as new owners, the managers to retain their employment as executives in addition to the palm grease they were paid. The undervalued sales prices were accepted by similarly bribed employees at privatisation offices. In order to sell their arable lands to foreign businessmen for building hotels and guest houses in recreational areas, cooperatives obtained authorization from the Ministry of Agriculture for taking the land out of agricultural production by slipping the amount of bribe established by the employees of the authorising ministry into the pocket of the proceeding civil servant. However, in the three leading intellectuals' assessment of the change of regime, despite the mentioned drawbacks, the evolution of market economic institutions and the change in the ownership structure is seen as favourable developments, as Hungary has joined the developed world, re-joined Europe, and the production performed here has been included in the value chains of international companies.

In the panel about the collapse of socialism and the evolution of capitalism, it was discussed that after the Soviet Union had run short of funds available for the support of the loss-making provinces of their overgrown empire, Hungary was compelled to take loans from the IMF and the World Bank, and so it started to run into debt. In this context it is worth highlighting the words of Mihály Patai, who mentioned that after the change of regime, negotiations were held about the option of Hungary repaying only the principal amount of the loan, without any interest accrued. All Patai said in response to the moderator's enquiry was that "József Antall simply interrupted the negotiations". He did not mention that in this matter he was under direct pressure from the US and indirect pressure through the social democratic party (SZDSZ)[2]. In the reviewers' opinion, Social Democrats and József Antall, who collaborated with the US and the social democratic party, are utterly responsible for the fact that, unlike Poland, we are still in the throes of the debt service.

Quite rightly, Csaba Lentner pointed out that after the change of regime, Hun-

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gary was only given one single option: the adoption of market economy. However, according to the professor of economics, the problem was that adoption was too fast, and the Hungarian population was unprepared for it. As also explained by the other speakers, the overwhelming majority of the population wanted to get rich quickly and were incapable of using their semi-legally obtained wealth in a moderate, disciplined and professional manner, and this was manifest in the operation of Hungary's production, service and banking sectors alike. Being far more disciplined and capable of reasonably enforcing their interests, foreign companies and financial institutions could purposefully use all this to the country's disadvantage.

Finally, a few words were said about the unconventional economic policy that helped Hungary get rid of its dependence on IMF. In relation to this, Mihály Patai noted that Matolcsy's achievements in central banking and the government's results in financial policy should be coined 'new-orthodox' rather than 'un-orthodox'. All the participants agreed, however, that the currently middle-aged and older economists still follow the anachronistic neoliberal trend they were once taught at school.

In the next topic, in response to the moderator's question, the participants of the roundtable discussed the rather aggressive enforcement of interests by the multinational companies that entered Hungary during the 1990's and early 2000's, and the way they suppress domestic businesses. They take almost all their profit to their foreign centres and barely leave anything in Hungary. During the conversation it was made clear that in the course of their operation, foreign production and trading companies, similarly to the subsidiaries of foreign banks, insufficiently help Hungarian businesses in development, most of them only enforce their own interests and take the total amount of profit out of the country. For this reason, although to different extents, they are positive about the inclusion of foreign companies in the circle of taxpayers and about the introduction of bank taxes after 2010. The interlocutors also pointed out the social problem caused by the unfair procedures adopted by foreign banks operating in Hungary in the course of FX lending, backed by irresponsible propaganda from previous leftist-liberal governments, and that after the 2013 change in monetary policy, the government and the central bank could solve a significant part of the social problems by conversion and derecognition of FX-loans.

These government actions led to serious tensions between the current centre-right government and MNCs, considered natural by the interlocutors. They think that the stakeholders must note that companies relocated from abroad will primarily consider their own interests; however, the latter must also note that the host state and society have expectations towards them. For this reason, in Hungary's economic policy efforts must be made at a compromise with the companies operating in the country, in the spirit of mutual respect for each other's interests, in order to secure long-term operation. This is the only way to develop useful cooperation between small, medium-sized and large corporations, on the one hand, and Hungarian and foreign companies, on the other, to turn the allegorical "zoo" friendly.

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In the *In the drift of global developments*, the talk centred on the previous and current courses of this drift, and Hungary's place in it, and more specifically, within the current world economic and political power centres. The interlocutors set out from the fact that with the collapse of the Soviet Union, the two power centres, namely the eastern Soviet and the western US, ceased to exist. Consequently, a unipolar economic and political centre evolved with US predominance. On the other hand, as László Parragh mentioned during the discussion, this unipolar power is increasingly torn into a multipolar one by the economic rise of China and India. The moderator leading the discussion suggests that in this emerging power centre, once again heading towards a multipolar system, a place is demanded by a renewed Russia, which is regaining strength and does not wish to give up her imperial status. They agree that Russia and the US are fighting a tough battle for Ukraine, a country brought into the US's scope of interest. At the same time, the Crimean Peninsula, which previously belonged to Russia, was annexed by Russia. The European Union, located in the buffer zone, placed Russia under embargo on request from the US, however, the EU and its Member States will get the worst end of it, while the USA makes profit on it, since – as concluded during the discussion – the goods missing because of the EU's embargo are purchased from the US.

During the discussion the interlocutors mention that in this rearrangement, the EU is weakening despite the fact that the centralization that set out from the US has also started both in the banking and insurance business and in the industry and service sectors. It was also discussed that the oil crisis and the banking crises that started in 2007 hit Europe harder than the US. The interlocutors give excellent analyses of both. The relevant professional financial analyses by Patai and Lentner are worth special attention, while the impacts on industry and trade are explained by Parragh. Mention is made again of FX-lending, which also appeared in certain Western-European states, but caused serious financial and social problems mainly in the Eastern and Central European post-Communist countries. While discussing Hungary's case, the interlocutors conversing in the book mention that the transformation of this form of lending through conversion into the national currency was a socially acceptable, appropriate solution by the government, acting in concert with the National Bank of Hungary.

Returning to the lines of power, it turned out that among the member states of the EU, Hungary is in the most difficult situation in the Russian–American conflict, as she lies on the borderline of the cultural areas of the historical Western Roman Empire, a catholic state, and the orthodox Christian Eastern Roman Empire, just as she has always been along her history going back to a thousand years. This was one of the reasons why Hungary had significant markets in the Slavic east, lost partly during privatisation and partly to the embargo resulting from the Ukrainian conflict. As a result of the discussion it was concluded that the emphasis of Hungarian economic policy should fall on regaining these markets, which is also justified by the country's economic geographical situation.

In the fourth topic the interlocutors discussed the benefits of the adoption of

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euro for the countries that have joined the euro area and the disadvantages or perhaps benefits for those who have not joined the euro area. In the roundtable participants' opinion, the related analyses focused heavily on Hungary. The various governments of Hungary put accession to the euro area on the agenda, and then extended its deadline on several occasions for failure to meet the requirements. As however, this failure has become permanent, the country has not joined the euro area. The reasons for Hungary's failure to meet the accession criteria are explained in detail and at length by Csaba Lentner, and the consequent disadvantages are summed up by Mihály Patai. During the discussion of the related correlations, another mention is made of the Russian-Ukrainian conflict and the trap the EU made for itself with the embargo, weakening the euro to the US dollar.

Moderator Lajos Péter Kovács mentions that highly conflicting developments are taking place in the euro area because the strengths of the participating economies vary. In response to the moderator's point, Csaba Lentner noted that the European Central Bank endeavoured to strengthen economically weaker states (typically in the Mediterranean) by purchasing the sovereign securities they issue. In László Parragh's opinion, the problem in these states is that due to the weakness of the central governments, structural reforms have been postponed, and this resulted in very high unemployment rates. In order to strengthen the euro, this situation must be changed, in the respondents' opinion.

The fifth topic of the discussion tackled *the revival of regions*. László Parragh thinks Hungarian foreign policy has been led to a blind alley in this respect. He explains that Poland has adopted a maverick economic policy, has markets of her own, and Galicia is her only region that once belonged to the Austro-Hungarian Monarchy. For this reason Hungary and Poland do not belong to the same region. Hungary should be comprised in a region with Romania, Slovakia, Serbia, Croatia, Slovenia and Austria. However, Austria, a country that can be classified in this region, would look at Hungary and the aforementioned other Central European countries as if they were her colonies. Regarding the issue of migrants, and in several other matters, Romania represents a position that differs from that of Hungary and the considerable part of the other countries mentioned above. Moreover, as referenced in the book, due to the suppression of the rights of Hungarian minorities living in the neighbouring countries, Hungary has serious conflicts with Romania and – in this question – also with Slovakia. As for Serbia and Croatia, no problems are encountered in relation to the Hungarian minorities living in these countries; however, there are considerable differences between their approaches to halting the migration and easing its pressure, as also voiced during the discussion. It should be noted, however, that since the publication of the book (in the summer of 2015), a favourable turn has taken place in Austria, Croatia and Serbia, and cooperation between the Visegrád (V4) Member States (Poland, Slovakia, Czechia and Hungary) has become full-fledged. Incidentally, the reviewers also note that Romania's views have also changed in a favourable way in the matter of migration. Similarly

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to Hungary, Romania does not allow migrants who arrive for economic purposes to enter its territory.

Nevertheless, the roundtable has also "established" that there are considerable differences between the standards of the various countries classifiable in this region, and their economic standards should be levelled out. At this point, the interlocutors primarily alluded to the differences between Slovakia, a member of the euro area, and Hungary, outside the euro area, to the advantage of the previous one. The interlocutors arrived at the conclusion that Hungary should first and foremost close the gap by reducing the said drawbacks, analysing foreign solutions and taking them into consideration. The banking system, higher education, the management of unemployment and the promotion of employment should be reformed to a certain extent on this basis. Regarding the promotion of employment, all of them were of the opinion that those community work areas which still remain unproductive should be channelled, even more than at present, towards useful directions, primarily towards production. They went into more detail about the proposals affecting the economic and financial system and already mentioned in the previous topic, namely that the economy should be "directed" more positively towards competiveness.

The sixth topic of the "roundtable discussion" concerned *bank loans, growth* and *opening to the east.* The conversation started with a historical reference to the transformation of a single-tier, centralised Hungarian banking system into a two-tier one in the second half of the 1980's, with the second tier, called commercial and economic, initially lending to the retail and the business sector alike. It was also mentioned that due to irresponsible allocations made with all too favourable conditions, second-tier banks went bankrupt and needed recapitalisation before they were sold to foreigners, with the exception of OTP Bank. OTP Bank was also sold, but the internal management was given a significant role in it, and by now this bank has become the leading bank in the region, and perhaps even in Europe. The Hungarian subsidiaries of banks sold to foreigners – as mentioned several times during the discussions – took a considerable part of their operating profits to their parent banks. The problems caused by FX-lending was repeatedly mentioned, as foreign parent banks do not assume any liability whatsoever for such transactions.

As to the character and role of Hungarian capitalists, the interlocutors find them rather uncreative, as they came into existence with state support rather than on their own. An argument evolved around the political affiliation of the new Hungarian capitalists. Csaba Lentner is of the opinion that over the longer term they are shifting towards the right (in Lentner's opinion capital tends to draw to the right), which is, however, contested by the other two interlocutors based on the assumption that this layer is always reasonably attracted to the side that can best serve its interests. In relation to this, László Parragh suggested and Mihály Patai agreed that a Hungarian business stratum should be created. In response, Csaba Lentner mentioned that in the framework of the Funding for Growth Scheme, the National Bank of Hungary had invested several thousand billion forints into Hungarian business-

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es, primarily SMEs and agricultural small producers.

The discussion also covered the issue of a correlation between company subsidies and corruption. The question was raised whether the assignment of the majority of public procurement tenders to a single company should be considered as corruption. In Mihály Patai's view the related concerns are ungrounded. Csaba Lentner thinks that corruption is ruled out when the majority of public procurement tenders is granted to a tried and proven company that seems to be most apt for fulfilling the order. The participants mentioned the need of establishing strong, large corporations in Hungarian ownership in Hungary that would contract small and medium-sized businesses.

Opening to the east and the efforts made at penetrating eastern markets were raised as a final topic, covering not merely Russia, but a more extensive area including the Middle East. In relation to this, the Russian contribution to the renovation of the Paks Nuclear Power Plant was mentioned, which is found correct and undisputed by several Member States of the EU, as they have realized that this is the most efficient solution for securing long-term energy supply in Hungary. The interlocutors also agreed that Hungary needed an economic policy with equal emphases on maintaining western economic relations and opening to eastern markets. The CIS member states, which evolved from the former Soviet Union, are ready to import any amount of apple from the Szabolcs region just as the Soviet Union once did. We were not ousted by Western European states through their higher-quality products, but we ourselves pulled out during the Antall Government. Due to Hungary's favourable climate, we could regain these markets for our agricultural products that are higher quality than those produced in Western Europe, primarily those of the Netherlands.

During the "fictitious meeting", the seventh topic included a discussion of the three interlocutors and the moderator who channelled their conversation about *Hungary's international reputation.* Lajos Péter Kovács thinks the West still has a very low tolerance to Hungary, and he asks why this was so. Mihály Patai thinks the West does not blame Hungary for her interest in eastern markets; they merely disapprove the management of the Norwegian Fund, the tax levied on advertising revenues, the comparison of Moscow to Brussels and Illiberalism. In his opinion the most serious problem is the non-diplomatic depiction of Hungarian politicians to the West. On the other hand, Csaba Lentner is of the opinion that the West has no moral basis to criticise us, as they are competing against us in the eastern markets. László Parragh attributes Hungary's adverse image in the West to the fact that the Hungarian economic policy has broken with the mainstream economic policy, has chosen to become independent of IMF through loan repayment, and has stopped FX-lending and the PPP programme. In addition, he thinks that any measure taken in national interest is a pain in the neck for westerners, because they hamper the integration goals of Brussels and the US. The interlocutors arrived at the conclusion that for the West the main problem is that Hungary sympathizes with an economic system close to social market economy rather than the market economy based

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on the merciless competition supported by Brussels.

The last point in the roundtable conversation was about *the starting points for the market economy of the future*. To launch the conversation, the moderator asked the interlocutors about the most important factors that needed to be considered for planning the future economy. Taking the floor first, Mihály Patai pointed out that the European Union has less than 8 per cent of the world's population but produces 25 per cent of global GDP, and this situation is untenable over the long term. Consequently, a change is expected and will set out from an "extraneous" environment. In their interruptions the reviewers named this change, which has already started: it is the migration threatening Europe with an invasion, which is irresponsibly mismanaged by the EU leaders.

Another factor in fast and constant changes is the movement of multinational corporations towards more favourable commodity and labour markets, which has a positive impact on employment at the time of penetration, however, their departure causes thorough economic and employment problems. To avoid the latter, compromise must be reached with MNCs, but efforts must be made to enable Hungarian companies relocate and take roots abroad. In Csaba Lentner's opinion, primarily agriculture and food processing should be developed, while László Parragh considers the harmonization of social resources as the important factor that enables us to manufacture high-standard technical devices (e.g. sensors and navigation software), to replace low-standard assembly jobs. All the three agreed that a favourable direction in Hungary's future depends on high-standard business and supply activities. This, however, requires a reform in specialised education, vocational training and healthcare, and improvement in the infrastructure.

Rating by the Governor of the National Bank and a ministerial recommendation...

In order to reflect the social and public significance of this specialist book and its authors, it is worth quoting the ideas worded in the Prologue by Minister László Palkovics, to make it clear that the content of the book is thorough and the authors are authentic. "Hungary's competitiveness is no longer manifest in the sale of tasty apricot pálinka from Kecskemét, resilient Rába Steiger tractors and Ikarus buses in western and eastern markets, but in the manufacture of Audi, Mercedes, BMW, Opel and Suzuki cars in Hungarian factories. All these need intellectual capital, creative workers, special engineering know-how, Hungarian small and medium-sized enterprises capable of cooperation with international MNC's, and the government's control capabilities, Hungarian universities, efficient financial interest representation and a highly developed banking system to surround them. These institutions are the strongholds of Hungarian competitiveness, and the authors of the book serve in these fortresses. In the words of György Matolcsy, governor of the National Bank of Hungary, Mihály Patai, László Parragh and Csaba Lentner are the bodyguards of the strong post-2010 Hungarian model, and their intellectual auras, ambition and performance make them emblematic figures."

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Moreover, Minister Palkovics goes into further details to acknowledge the merits of the authors as follows. "The authors, who were just coming into their prime, testify to the talent, ambition and peculiar development trajectory of the Hungarian nation though their own life, in a description of the material and intellectual fields from the breakdown of the soviet system and the beginning of the change of regime in Hungary. Mihály Patai, President and Chief Executive Officer of the Hungarian subsidiary of the international bank UniCredit, Chairman of the Hungarian Banking Association, and at the time of the publication of the English version of this book, also Deputy Governor or the National Bank of Hungary and Chairman of the Budapest Stock Exchange; László Parragh, Chairman of the Hungarian Chamber of Commerce and Industry and a member of the Competitiveness Council, and Csaba Lentner, professor of economics granted the Wekerle Sándor Life Achievement Award and the civilian Commander Cross of the Order of Merit of Hungary, and serving as Director of the Institute for Public Finances at the National Public Service University are all personalities who have created future-proof value at their duty stations in the past thirty years; they manage various systems and in the past more than a decade, they have been acting as the "system managers" of the competitive Hungarian economy that has found its own course of development and of academic life."

What else can a book reviewer add to these sublime thoughts and ambitious personalities? We hope that their ideas shared in the book will be a worthwhile material and beneficial pursuit not only for the members of the Hungarian nation but also for anyone all over the world interested in the decades that followed soviet occupation in Hungary and Central and Eastern Europe in the decades and in the peculiar development of market economy, as this novel and unconventional book tackles problems and phenomena in a complex way. It is worth reading.

Mihály Patai, László Parragh and Csaba Lentner: Hungary in a Changing World. Éghajlat Publishing Ltd., Budapest, 2019, 200 pages.

Note

1 The address of Éghajlat Publishing Ltd.: H-1117 Budapest, Karinthy Frigyes út 9. Hungary, eghajlat@eghajlat.hu.

2 "Alliance of Free Democrats". After consecutive election and government failures, in the early 2000's the party that orchestrated the change of regime had degraded along with numerous other parties that participated in the change of regime (e.g. Independent Smallholders' Party or the Forum of Hungarian Democrats).

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Gábor Hamza

Codification of Hungarian Private (Civil) Law in a Domestic and International Comparison

Summary

The study analyses the centuries-old process of the codification of private law (civil law) in Hungary. The author believes that the Roman law tradition in Hungary survived at both a legislative and a theoretical level. Romanist (mainly German Pandectist) influence can be observed in various draft civil codes of the country. The first Hungarian Civil Code, promulgated in 1959 and put into effect in 1960, was a socialist-style civil code. The procedure of harmonisation with the law in Europe influenced the new (second) Hungarian Civil Code promulgated in 2013.

Keywords: civil law, codification of law, harmonization of law, Pandectist legal tradition, private law, Romanist legal tradition

Roman law and private law as disciplines in the 19th century[1]

The first significant influence in Hungarian civil law, which already meant a shift towards "Europeanisation" in the modern sense of the word, was the impact of German Pandectists (Romanists, Pandect Law or the discipline of pandects), hallmarked by the name of Friedrich Carl von Savigny (Hamza, 2009; 2013). Its earliest traces are demonstrable in the work of the first great private law solicitor of the 19th century, Ignác Frank (1788–1850), who can be considered as "the trailblazer of a new era", as László Szalay has put it, despite the fact that he consistently opposed codification. In his work entitled *Specimen elaborandarum institutionum iuris civilis Hungarici,* published in 1823 and still reflecting the influences of a move-

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ment termed "rationalist natural law" (Vernunftrecht, or the "law of reason"), primarily the impacts of Christian Wolff, Ignác Frank uses the terms of Roman law to discuss Hungarian land ownership, and these terms also appear in his other works depicting Hungarian law. As demonstrated by Elemér Pólay, Ignác Frank cannot yet be considered as a representative of the Historical School of Jurisprudence (Historische Rechtsschule).

The Historical School of Jurisprudence, and more specifically, Pandectistics (Pandektenrecht or Pandektenwissenschaft) is fully manifested for the first time in the works of Gusztáv Wenzel (1818–1891), Ignác Frank's student. In his study about *The System of Hungarian Private Law,* he applied the system of pandects, and he was the first in Hungarian jurisprudence to explain the theory of legal relationships, legal institutions, legal facts and legal transactions on a Pandectist footing. Although Gusztáv Wenzel was clearly a Pandectist, naturally, in his works he frequently refers to Roman law.

From the second half of the 19th century, Pandectistics had an increasing impact on Hungarian jurisprudence, and thus also judicial practice, through the work of the "universal private law solicitor", Gusztáv Szászy-Schwarz (1858–1920). As practically all of our Romanists and private law solicitors were the disciples of German Pandectists (Szászy-Schwarz and Mihály Biermann, a lecturer at the Győr and then at the Nagyszeben academy of law learnt from Rudolf von Jhering, while Elemér Balogh, who demonstrated outstanding merits in comparative law, attended the lectures of Heinrich Dernburg), they promoted the transposition of an increasing number of German Pandectist legal elements into Hungarian judicial practice through their legal writings.

The role of Roman law in the codification of private law[2]

The preparation of Hungarian *ius privatum* for codification was launched by Act XVIII of 1791 by commissioning a board of law (*deputatio iuridica*) to prepare a private law bill *(Proiectum nonnullarum utilium civilium legum).* This draft version, completed after two years but printed, i.e. published only decades later, in 1826, does not reflect any impact of Roman law in either its structure or its content, and cannot be considered as a draft code in its nature. It stands to reason that the adoption of the French *Code civil,* considered by László Szalay as ideal, was ruled out, and as a result of the political developments, the second attempt at codification required by Act XV of 1848 also failed.

After 1853, the General Civil Code of Austria (ABGB, Österreichisches Allgemeines Bürgerliches Gesetzbuch) entered into force in Hungary and in Transylvania, and therefore a restart of codification was delayed until the Compromise. The general part (1871) of the Code of General Private Law was elaborated by Pál Hoffmann (1830–1907), a renowned legal expert in Roman law, who was a lecturer at the Pest university of sciences. It follows the parts in the 1863 Saxon Civil Code (Bürgerliches Gesetzbuch für das Königreich Sachsen), mainly influenced by Georg Friedrich Puchta (1798–1846), and practically codifying the Pandectist literature and the law of pandects.

Bálint Ökröss (1829–1889) was a member of a school that advocated the codifi-

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cation of Hungarian private law according to the pattern of rules set out in the ABGB. Both the structure and the orientation of the draft law of inheritance (1882) by István Teleszky (1836–1899) are based on the Saxon Civil Code, however, in respect of the institutions of the law of inheritance, the latter had principal regard for local Saxon law. Similarly to a recommendation traced back to Pál Hoffmann, the chapter on the law of contractual obligations (1882) drafted by István Apáthy (1829–1889), influenced by the 1866 Dresden Draft (*Dresdener Entwurf*), which paved the way for the subsequent BGB (the German Civil Code, or Bürgerliches Gesetzbuch), followed the (Willenstheorie) hallmarked by Friedrich Carl von Savigny in its regulation of legal transactions. The same applies to the draft General Part, compiled by Elek Győry (1841–1902) in 1880. The part on the law of rights in rem (1882) Endre Halmossy and the law of marriage, personal and property rights drafted by Béni Grosschmid (1852–1938) are less influenced by Pandectistics.

The idea of compiling a uniform code of private law became prevalent in 1895, when Minister of Justice Sándor Erdélyi established the committee for the preparation of a consolidated draft civil code, which included Romanist and civil law solicitor Gusztáv Szászy-Schwarz (1858–1920) as a member. The part on the law of inheritance was elaborated by Szászy-Schwarz.

The draft version prepared in 1900 with a structure and legal institutions bearing marks of the German BGB breaks with the practice of piecemeal codification. This draft consisted of four parts (personality rights, family law, the law of contractual obligations, the law of rights in rem and inheritance law) without a general part (Allgemeiner Teil), as the first titles under the law of contractual obligations have that function. The draft made in 1900 already follows the principles of declaration theory (Erklärungstheorie) in its discussion of legal transactions (Rechtsgeschäfte). The German Civil Code (Bürgerliches Gesetzbuch, BGB) had a higher impact on the next, smaller-scale private law bill compiled in 1913, although it did not contain a general part either.

The 1928 proposal for a Code of Private Law, called *ratio scripta* by courts, worded with the prominent involvement of Béla Szászy (1865–1931), aptly called the "Hungarian Eugen Huber", strongly reflects the influence of the Swiss Civil Code (Zivilgesetzbuch, ZGB) and the Swiss Act on the Law of Contractual Obligations (Obligationenrecht, OR).[3] Although for several reasons the Draft Code of Private Law failed to become a law, in other words, it never had a *vigor legis,* not even despite the provisions of Act XXII of 1931, certain legal institutions included in it, thus mortgage, regulated in Act XXXV of 1927, were approved by legislation (Szladits, 1932).

After World War II, the Council of Ministers set up a codification committee in December 1953 for the elaboration of a civil code. The committee included lecturers from the civil law departments of the three faculties of law – in Budapest, Pécs and Szeged –, from the civil law department of the university of economics, staff members from the Institution of Law and Political Sciences of the Hungarian Academy of Sciences, and the representatives of the Supreme Court, the Chief Prosecutor's Office and

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the Ministry of Justice. Following several years of preparatory work, the first draft had been compiled by September 1956. After a smaller committee established by the Minister for Justice reviewed the fundamental questions of the draft in the spring of 1957, the editors amended the draft. This draft was published and discussed. The final version, repeatedly reviewed by a committee of the Ministry of Justice was submitted to Parliament as a bill in 1959. The code was approved in 1959, and the consolidated Civil Code entered into force in Hungary on 1 May 1960. Despite its socialist key features, the Civil Code reflects the influence of the German BGB, the Swiss OR and ZGB, and the 1928 Hungarian Code of Private Law. From among socialist civil codes, the editors of the code took into consideration the Soviet-Russian code that was approved in 1922 and entered into force on 1 January 1923, the Czechoslovakian civil code adopted in 1950, the 1955 Polish bill and the Bulgarian act regulating ownership and approved in 1950.

The Civil Code approved in 1959, which remained in effect up to 15 March 2014, consisted of six parts, and the individual parts were divided into chapters. The first part contained the introductory provisions (Articles 1–7), however, this cannot be considered as a general part (*Allgemeiner Teil*) in a Pandectistic sense of the term. The second part contains individual rights (Articles 8–87), however, family law was regulated in a separate statutory regulation: Act IV of 1952. (The act on family law regulates the institution of custody and guardianship.) The title of the third part was "Ownership Rights" (Articles 94–197). The fourth part contains provisions of the law of contractual obligations (Articles 198–596). The fifth part discusses the law of inheritance (Articles 598–684), while the sixth part contains closing provisions (Articles 685–687).

The 1959 Civil Code did not follow the system of pandects (Földi, 1986). Regarding its structure, it is comparable to the system applied in Gaius's *Institutio,* with the fundamental difference that civil procedure and the above-mentioned family law were regulated in separate codes, and the law of inheritance was placed last. There were numerous elements of Roman law in the Civil code, which served as the fundamental source of Hungarian private law (civil law) for several decades (Földi and Szájer, 1985). The part on personality rights recognised the conditional legal capacity of foetuses, however, in contrast to Roman law, the statutory establishment of the time of conception was a rebuttable presumption.[4]

As a peculiar feature of the 1959 Civil Code, despite the fact that Part III is entitled Ownership Rights, for certain dogmatic considerations it regulates rights in rem, and contains numerous casuistic provisions. Among these regulations, Roman law traditions are especially clearly reflected in the provisions relating to taking the fruits of a thing or to taking possession of property that has no owner (*bona vacantia).* Partial titles to the various forms of ownership – the concept of *uti, frui, habere, possidere* and *abuti* – reflect the impact of Uplianus.

In relation to possessions, Hungarian law only recognised *possessio civilis,* and ruled out *possessio naturalis.* Originally, the act did not regulate possessory protection, but it was subsequently developed through judicial practice. Regarding the transfer of ownership, the Civil

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Code of 1959 followed the principle of tradition: in addition to the ownership title (*causa*) it also required the transfer (*traditio*) of the thing owned. The Hungarian regulation of adverse possession was less influenced by Roman law, as only the thing suitable for adverse possession (*res habilis*) was required, and good faith (*bona fides*) and a legal title (*iustus titulus*) were not. The Hungarian Civil Code considered easements as independent rights of use.

The law of contractual obligations was not divided into general and special parts, it is rather focussed on the two institutions considered fundamental: contracts and liabilities. The individual types of contracts also showed the influence of Roman law. The individual sub-types of contracts for work were reminiscent of the individual types of *locatio conductio*. However, in contrast to the gratuitous *mandatum* defined in Roman law, as under Hungarian law a mandate, an agency contract or a contract for services is onerous, as a rule of thumb.

To meet the requirements of the socialist (state socialist) economic and social order prevailing during its codification, the 1959 Civil Code gave a detailed regulation for agricultural product sales contracts, naturally unknown in Roman law, due to the level of development in production back then. Nevertheless, the essence of agricultural product sales contracts can be traced back to sale and purchase agreements not only known but meticulously elaborated in Roman law, specifically to the forms constituting the special kind of sale and purchase termed as *emptio rei futurae* or *emptio rei speratae*. The code contains a general rule on liability and allows certain exceptions. These provisions seem more or less casuistic, and are rooted in Roman law, with the exception of liability for risk in unsafe work environments, which is naturally unknown in antique laws. Certain legal institutions under Roman law, including *receptum nautarum cauponum et stabulariorum*, *actio de deiectis vel effusis* and *actio de positis vel suspensis,* were actually transposed in the regulations on increased liability by hotels and restaurants and on liability for damaged to buildings (Mihály, 1959; Grzybowski, 1961; Fesztl and Tamás, 1967; Eörsi, 1974; Gabor, 1982, Vékás, 1987).

The *regula Catoniana* (Article 234) and the *pignus Gordianum* (Article 267) manifest the survival of Roman law traditions. Return to the traditions of Roman law is reflected by the Supreme Court's Civil Law Decision in Principle No. XXIV, which interprets Article 192 (2) and allows both possessory and petitory actions in property protection.

As the Hungarian law of inheritance is based on the principle of *ipso iure,* in contrast for example to Austrian law, it does not recognise the concept of vacant succession or *hereditas iacens*. In contrast, among others, to German and Austrian law, the Civil Code of 1959 expressly prohibited pupillary substitution, despite its actual origins in Roman law, and only allowed residuary legacy (Tóth, 2001; Boóc, 2002).

The Civil Code of 1959 was amended on numerous occasions. Among the amendments performed before the change of regime, the changes approved in 1967 and 1977 were especially important. In terms of Roman law traditions, the amendment enacted in 1991 is particularly notable, as it allowed the Civil Code

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to include, similarly to numerous other European private law jurisdictions, like the German, the Swiss and the most recent Dutch civil law, more specifically the new Dutch Civil Code (Nieuw Burgerlijk Wetboek), the category called "objective good faith", and provided that it must be broadly used in private law relationships as a general clause (Földi, 2001). Act XIV of 1991 deserves special mention, as it prohibits the conclusion of contracts that are in conflict with *boni mores*. Another example of return to the traditions of Roman law included the mortgage right codified in Act XXVI of 1996. Note that the complete legislation on mortgage by legal charge was re-regulated in Act CXXXVII of 2000 based on the current economic requirements and on the basis of the traditions of Roman law. The Civil Code is not the only body of regulations to ensure that the individual Roman law institutions survive. Other examples include Act XLIX of 1991 on bankruptcy, liquidation and dissolution procedures. Subject to a judicial approval, agreement between the parties is reminiscent of *cessio bonorum* in numerous cases (Hamza, 1989; 2001).

Note that the Civil Code was not the exclusive regulation of Hungarian private law (*ius privatum*). Family law was regulated by Act IV of 1952 on marriage, family and custody, promulgated on 6 June 1952, entered into force on 1 January 1953, and amended, in the period prior to the change of regime, in 1974 and 1986. Pursuant to the amendment adopted in 1986, the conclusion of a pre-nuptial agreement was allowed once again under Hungarian law. After regulation in a decree, labour law was regulated in an act adopted in 1967 and amended several times subsequently. In 1992 a new labour code was adopted. Copyright was regulated by an act adopted in 1969 and replaced by a new act in 1999. The provisions of international private law were included in a decree-law adopted in 1979.[5]

Notes

1 For more details on this topic see also Böszörményi Nagy, 1970; Pólay, 1976; Zlinszky, 1997. About Ignác Frank see Villányi Fürst, 1935; about Gusztáv Wenzel see Balázs, 1990; about Gusztáv Szászy-Schwarz see Szladits, 1934; and about Elemér Balogh see Hamza, 1999.

2 For more details on this topic, see Dauscher, 1862; Dell'Adami, 1877; 1885; Teleszky, 1887; Meszlény, 1901; Szászy-Schwarz, 1909; Asztalos, 1970; Bernáth, 1970; Mádl, 1970; Weiss, 1970; Peschka, 1970; Csizmadia, 1974; Basa, 1996; Harmat, 1999.

3 It is highly instructive to give a brief overview of the impacts of Pandectistics on (non-fault) strict liability. The draft compiled in 1900 regulated liability in accordance with the German Civil Code (BGB), although not relying on its literal translation, based on fault. Based on the second (1887) draft of BGB (Zweiter Entwurf), Article 1486 of the 1913 draft already gave room to the principle of damages based on objective liability. The famous Article 1737 in the 1928 Code of Private Law, which regulated equitable liability, followed, although indirectly, the second draft version of BGB when it allows the subsidiary enforcement of the objective principle of liability for damages.

4 About the Roman law institutions mentioned in this study, see Földi and Hamza, 2018.

5 In Hungary the codification of the new civil code began on the basis of Government Decision No. 1050/1998. (IV. 24.). The editors of the draft code also took Hungary's legal harmonisation goals into consideration. Their aim was to make the new code suitable for providing a private law regulation that meets the social and economic requirements of the 21st century. It is worth mentioning that the concept of the new civil code was published at the beginning of 2002.

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Attila K. Molnár

Thomas Molnar and the Conservatives in the US

Summary

Thomas Molnar, a Hungarian Catholic emigé, was a well known fugure in the American conservative movement. In spite of the warm welcome of his works criticizing leftism, he stayed at the margin of this movement. Molnar never accepted the fusionism, he was critical concerning free market, and he openly refused many presuppositions of the Anglo-Saxon liberal democracy. He transported elements of the French Catholic conservative thinking into the US like the attraction to monarchical authority and hierarchy. For him the idea of time-tested tradition was hardly important, when he used the notion of tradition he referd to its perennialist meaning. The paper argues that his criticism of (political) modernity was form by the *Pascendi dominici gregis*.

Keywords: Thomas Molnar, Catholicism, conservative, egalitarianism, authority

In the period of transformation of Hungary during the early 90s, the term "conservative" had rather bad connotations. On the one hand, it meant hard-line communists who insisted on the party state, and on the other hand, it meant old or strange people behind the times, having outdated and anachronistic ideas. History and the final success were thought to be obviously on the side of progressives, who, by means of their extraordinary talents and moral insight, could understand the necessity of historical changes and progress.

The use of this attribute in a positive sense was started by a few people around the governing Centre-Right party in 1991–1992, but in those days no politician or media self-identified as conservative in Hungary. The monopoly of triumphant liberalism – as even the post-communist party used liberal rhetoric – was slowly broken, and in this process Thomas Molnar had an important role.

Up to now, those who contradict liberal hegemony have been labelled by them as radicals or populists, if not worse, but never as conservatives, because this attribute was gradually assigned an increasingly positive connotation in Hungary

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during the two decades after 1990. This brand was so much transvalued that there has emerged a debate around its ownership. As many decades before in the US, in Hungary the positive rebranding of the term conservative was followed by the emergence of the term pseudo-conservative used by leftist and liberals to devaluate their opponents.

Thomas Molnar, an American *emigré*, had a non-negligible role in the revaluation of the term 'conservative' in Hungary. After 1990 he returned to Hungary from the US, and then every year he spent several months in Hungary.

Although he was an American citizen and a respected member of the conservative circles there, he did not belong to the mainstream in the US. He always stayed away from fusionism, he was always European, too much European.

The history of the American conservatives – against from the story told by progressives – is not the fight between of the elite defending its privileges and the people, and the contemporary Hungarian situation was similar. Here, just like in the US, the conservatives were not established at all – in the US there has been a liberal hegemony, while in Hungary a communist dictatorship and after 1989 a liberal hegemony, too –, moreover in both places the conservatives challenged the established and hegemonic progressive elite. Maybe, the belligerent or critical tone of conservatives in both countries is originated from this situation. Because in the 20th century the progressive established themselves and they have became the political, economic, media and cultural elite, they formed a new rhetoric against conservatives. Not their alleged selfish defence of privileges and interests has been the main accusation against conservatives, but the triumphant progressives have emphasized that only they recognized the progress. That is why they had been successful, and the conservatives had been hopelessly behind the time. According to the progressivist self-image, because of their special knowledge of the iron laws of historical progress, only they could recognize the dictates of progress and adapt themselves to them, therefore the conservatives have been necessarily losers. Conservatives failed the moral and epistemological challenge of modernity. It has been a clearly social-Darwinist argument: adapt or perish. And, in case of conservatives, they did not feel any moral imperative to help the less successful people and express compassion towards marginalized groups of conservatives people.

The definition of conservative thinking has been the subject of debate. Conservative politics, and mainly its Anglo-Saxon version, seems to be fairly successful, a real alternative to progressives. What is more, progressivism seems to be out of fashion today.

An important issue within the debate on the definition of conservatives refers to its ideological or non-ideological character (Huntington, 1957). Conservatives typically refuse the label of ideology. The other important issue of this definition debate is connected loosely to the first one. This second debate is between those who define conservative thinking in terms of time (speed and time-testedness) and the problem of change (its modesty or slowness) and those who define conservative thinking by substantive elements. Obviously, the last one is closer to the rationalism or the creation of an

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ideology (Wilson, 1941; Holmes, 1993). One can find all of these interpretations among American conservatives, but the mainstream formed during the 1950s was fairly ideological and emphasized substantive elements, principles or beliefs (Kirk, 1993; 2018).

To indicate Thomas Molnar's place in the conservative topography, it is enough to mention only three main elements of American Conservative thinking:

1. The defence of a free market economy against the New Deal economy and the interventionism of a welfare state (Lloyd and Davenport, 2013). The reaction against the welfare state formed libertarian thinking in which Southern anti-federalist tradition merged with the teachings of the Austrian School (Hayek, Mises) (Miles, 1980; Tate, 2005). They criticized the welfare state in the name of freedom – mainly in the name of economic freedom, and economic effectivity and growth. Against the Democrats, emphasizing social equality and welfarism, the Republican Party has become the party of free market and economic growth.

This pro-market argument has been based on rationalist anthropology saying that every individual rationally calculates his costs and benefits apart from any communal ties or cultural bias. On a free market, containing these kinds of individuals, spontaneously there will emerge an order and a flourishing economy.

The conservatives picked the idea of free market partly because it seemed to relieve the state and solve the government problems of the 1970s: they hoped that the frustration emerging from unequal distribution of goods probably would not turn against the state and political order if it resulted from the blind operation of a market, and not from the redistributive policy of state. And they also hoped that the flourishing economy, produced by the free market, would temper social frustration.

2. As it is well known, the other branch of the American conservative thinking is from Russell Kirk's, Burkean traditionalism. This way of thinking argued against rationalism and egalitarianism and instead on behalf of the authority, tradition and values of the Anglo-Catholic thinking. They have stood up against moderns and progressives – liberals or leftists – and have started the *Kulturkampf*. This social or moral conservative argument has stated that modernity has been unsustainable and barbaric. Their critical stance towards a welfare stance joined with the free market criticism of welfarism.

This moral or social conservative argument, rooted in the European tradition and emerging during the 1950s in the US, was so strange in the American context that even the Republican candidate, Barry Goldwater, named their ideas "so bizarre, so archaic, so self-confounding, so remote from the basic American consensus" (quoted Brinkley, 1994, p. 411). Because of the existing liberal consent, the conservatives were called neo or radical Right, or pseudo-conservative, implying that the real conservative would defend the liberal consensus and establishment (Higham, 1959).

The first generation conservatives were taken as strange, mad ('kooks', 'crackpots'), without any chance for effective political action (Hofstadter, 1948). As Trilling put famously: "conservative impulse and the reactionary impulse do not, with some isolated and some ecclesiastical exceptions, express themselves

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in ideas but only in action or in irritable mental gestures which seek to resemble ideas" (Trilling, 1950, p. ix).

But the public mind in the US turned Right after 1968 – which was a kind of 1789 or 1793 year for many Americans (Brennan, 1995). After then, Meyer's (Meyer, 1960) fusionism has become the mainstream among the American Conservatives (Meyer, 1962; Nisbet, 1980; Goldwater, 2010; Smant, 2002; Hart, 2005; Lee, 2014; Allitt, 2009; Dunn and Woodard, 1996; Preece, 1980; Schoenwald, 2001).

3. In the original version of fusionism, the third element was not present. It is the *grandeur*. This element was connected to anti-communism for many years, a bond of several conservative branches (Haddigan, 2010). However, after the collapse of the Soviet Union this bond disappeared, and the emphasis on national interests gained importance (Dorrien, 2004; Kagan, 2002).

Fusionism could survive the incoherence of Kirkian traditionalism, social conservatism and libertarianism and free-marketism, but fusionism was broken by the unusual democracy export of the Republicans, which generated the conflict between paleo- and neo-conservatives.

Though it was not called fusionism then, this package appeared in Hungary after 1990. In the period of the first free, Antall government of 1990–1993, the centre Right followed a free market policy combined with the emphasis on national sovereignty and the defence of traditional culture and religions. And this Hungarian combination of free-marketers, social or moral conservatives and nationalists worked at least for one and a half decades. (The first Orban-government between 1998–2002 followed this combination, more or less.) But in this country this combination was not as sound as in the US. Partly, because everyone – even the post-socialists – was using the free market rhetoric and policy, so it was not a real political marker for the Right. Also, because the free market rhetoric was used for unscrupulous privatization and the creation of the crony capitalism of post-socialist technocracy. And under the flag of a free market the foreigners could gain an unusual influence on economic life after the collapse of the socialist economy. Beside the moral criticism following the corruptions of privatization and the market economy, it was crucial that the elite that were managing the free market couldn't build an effective and prosperous Hungary. As it is well known, beside the freedom argument, the most important argument for the free market was its effectiveness vis-à-vis a planned economy. Hungary, under the leadership of the post-socialist elite, using free market rhetoric, descended into high unemployment, indebtedness and economic crisis. Thus, because of practical and political reasons, the Right broke with the local version of fusionism, and the ideas of the free market have got out from the thinking of Right of Hungary.

In Hungary conservative thinking divorced from free marketism in the first decades of the 21st century. Here the traditional suspicion concerning the free market has become rather widespread: conservatives suspect that the market relations transform or destroy the family, nation, traditions and religion, as it was described by Daniel Bell (Bell, 1976) or Marx.[1] In spite of this suspicion and the

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obvious incoherence of the values of free market and moral or social conservative values, still there are some thin bonds between conservatives and free marketers like anti-egalitarianism, anti-communism, meritocratism and patriotism.

Obviously, Hungarian-born Thomas Molnar stood out of the fusionist mainstream. There is no reference in any of his works to the Austrian School or libertarians. In general, the criticism of the welfare state in the name of freedom and/or economic efficiency was distant from him. And, he was similarly critical towards the export of democracy. He was, probably, too European or too much of a Francophile. European, mainly continental, conservative thinking, differs clearly from the American one: the first difference is characterized by the Roman unity of tradition, authority (hierarchy of men) and religion based on the Tomist tradition. These are fused into the concept of a sacred monarchy like the divine imperators in Rome, the *rex Christianissimus* kings of France and the godly princes in the Protestant countries (Arendt, 1990, p. 117). The European conservative tradition insisted on the idea of the natural inequality of men and on the idea of the incompleteness of man: because man is incomplete, he needs some completion from without, like from magistrates, culture or other institutions independent from an individual's will. The conservatives in the US were much closer to the liberal anthropology: they were ready to except the ideas of equality and individualism as well as the consent of the governed as the only acceptable basis of political order.

Vis-á-vis the Anglo-Saxon conservatives, tradition interpreted in terms of time – speed of change like modesty and durability – was not interesting for continental conservatives. Continental conservatives interpreted tradition as something perennial, originating from the nature of man, and at the same time they were more critical by condemning the political, cultural or other forms of modernity than the Anglo-Saxons were. This rather solid anti-modernism was logically connected to the perennialist understanding of tradition. As in the case of Thomas Molnar, one can hardly find any concession to modernity among continental conservatives. Thomas Molnar's work can be understood mainly in terms encyclics of *Syllabus Errorum* (1864) and *Pascendi dominici gregis* (1907).

Thomas Molnar referred to de Maistre, Donoso Cortes, Voegelin and Carl Schmitt, but his thinking stood closest to Bernanos and the French circle of Charles Maurras (Molnar, 2011; 1995b) The idea of tradition as something time-tested and that survived the trial-and-error experiments, so important for Anglo-Saxons, was much less important for Molnar than the idea of authority and the idea of perennial tradition. The backbone of his thinking was God and authority, and their relation. In general, the authority became a marker for anti-modernist conservatives, probably because the modernist was not able to domesticate this idea, while the Anglo-Saxon notion of tradition was absorbed by many modernists.

According to Molnar, modernity is a hopeless, lost cause by origin because it is the fruit of the rebel: modernity is a shift from the transcendental interpretation of the world towards an immanent one. This rebel hopes that the world is self-sufficient, it can be made perfect, therefore

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it doesn't need God, nor Revelation, nor its teacher, the Church. Molnar, like his continental exemplars, always criticized the *liberalismus triumphans* as responsible for modernity.

The modernists' rebel means for him that modernists refuse the notion of incomplete man and that he needs some completion from without. Some kind of *forum externum*. Accordingly, politics is not a separate sphere or a second order activity, but the most intensive appearance of the problem of basic human relations, as Carl Schmitt wrote in his *The Concept of Political* (Schmitt, 1996). Therefore, the sharpest consequence of human nature is authority. Politics is not a sphere beside many others, but it is itself the problem of human relations, and their institutional solutions is the established authority. This thinking on the parallel of politics and theology haphazardly follows St Augustine's description of *civitas Dei*: without grace the sinful man loves himself, therefore he rebels and seeks power, so he desperately needs an authority, a *forum externum* to make human life possible. The (sinful) nature of man requires his subordination to some scheme or principle of order not, in its essence, made by himself.

Hobbes' question, according to Carl Schmitt (Schmitt, 2008) – *Quis iudicabit? Quis interpretabitur?* – refers to the epistemological side of the human condition: instead of methodology, a political decision may decide the epistemological ambiguities, such as what is reality or what is the meaning and what is the motivation of a certain action? Because of the imperfection and inscrutability of *conditio humana* (motives, consequences are obscure and contingent), there is need for compulsion to make order from plurality and ambiguity. Therefore, the monarchy is the core structure of the world.

In Molnar's implicit political theology, human life is founded on metaphysical presuppositions and not on conventions or experiences. By means of these ideas he questioned the liberal or modernist contractarian thinking characterizing the Americans who founded the state on individual autonomy and the consent of people. Obviously, in the thinking based on the idea of original sin, there is no practical place for the will of people.

The modernists – that is, the heretics according to *Pascendi dominici gregis* – would solve Leo Strauss' problem[2] by bracketing it. According to Molnar, this is the source of tensions in modernity. The modernists would eliminate theology and politics by utopism, because they seek to liquidate enforcement and obedience by their metaphysical turn, called humanism (Molnar, 1978). Molnar's interpretations of politics and theology are critical towards modernity because modernity basically refuses the incompleteness of man and its concomitant results, the need for hierarchical relations and institutions. Meanwhile, mainstream conservatives in the US have accepted modernity and egalitarianism.

The core idea of Thomas Molnar's works is that man, on the one hand, is *zoon politikon* and, on the other hand, open for transcendence, as well, and the tension between these two spheres is characteristic of the human condition. That is why man is anxious (Molnar, 1978) and looks for certainty, which is the source of his utopical propensity, that is, his search for this-worldly salvation from his anxieties. This utopism dominates modernity as

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the "synthesis of all heresies" (Pope Pius X, 1907). Not the double nature of man, but rebellion against his nature was seen by Molnar as the source of problems in modernity. In this sense, modernity is not modern at all, it is only a new version of human rebellion; what is new in modernity is the triumph of heresy: "Were one to attempt the task of collecting together all the errors that have been broached against the faith and to concentrate the sap and substance of them all into one, he could not better succeed than the Modernists have done. Nay, they have done more than this, for, as we have already intimated, their system means the destruction not of the Catholic religion alone but of all religion. With good reason do the rationalists applaud them, for the most sincere and the frankest among the rationalists warmly welcome the modernists as their most valuable allies" (Pope Pius X, 1907).

The meaning of the modernists' rebel is the hope that man can get on his own, that is, he is able to become, god and self-completed (Molnar, 1987).

Original sin – in this thinking – necessitates political and ecclesiastical authority. The *status naturalis* is the *status civilis*. Any anti-political or utopical hope is against (sinful) human nature that needs authority – that is – some control from without. The social life needs the limitation of human passions, ambitions and wishes and not their liberation. Man is not rationally, nor morally autonomous. Thomas Molnar quoted Bonhoeffer to criticize the modernists' optimism that evil was declining in the world and man's power to make good had increased (Molnar, 1978).

With this thinking the *ordo rerum humanorum* ant the *corpus politicum mysticum* are always coincided. Man needs a hierarchy where authority limits his judgements and restrains his will. That is, order comes from inequality and enforcement. To get rid of them and live a decent human life at the same time is impossible – which was called "utopia" by Molnar. Only angels and animals can live peacefully without some inequalities, whereas human being needs authority (Molnar, 1995a).

The conservatives on the Continent have only moderately trusted in education or any methods on the modification of consciousness, called enlightening or consciousness raising, because the human order, first of all, is not a problem of knowledge as modernists since the Enlightenment have supposed. Modernity is full of epistemological debates about how to get the proper knowledge and what the proper knowledge is, but Molnar was pre-modern in this context. He couldn't see the moral and political problems in terms of epistemology, because these are anthropological and metaphysical ones.

For him the problem of the authority of state and church was eminently the problem of modernity. Both of these institutions are necessarily authoritative, and both are equally important to save order.

Neither conservatives nor Thomas Molnar wanted an uncontrolled or unlimited state, because politicians are fallible, too. But the control of the state by citizens – or any kind of contractarianism – wouldn't solve the problem, according to Molnar. Molnar, just as non-American conservatives generally, regularly criticized contractarian thinking and the new-left ideal of civil society, because in this thinking everyone joins to a contract by his own judgement to fulfil his wants and

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interests. Contractual relations are created to be instruments to get something. Therefore, it is easy to step in or out from them. The problem for Molnar was that an instrumental relation would never have compelling authority. As de Maistre said, man doesn't respect what was created by him and can be easily changed. Duties and loyalties connected to contractarian relations can be easily denounced. Therefore authority, in the proper sense, limiting and disciplining people for the sake of order, cannot emerge from a contract. What is more, any contractual arguments contain an anarchistic notion of freedom as something originated from the pre-social or pre-political condition. Therefore anyone may step out from these relationships. Any state founded on the notion of a contract will be in a state of permanent rebellion and resistance, because everyone wants to change the contract as a useless instrument. Modern people tend to modify their relations instead of restraining themselves. Continental conservative logic is simple: authority cannot depend on those people's permanent consent who should be disciplined by this authority. With any relation founded on personal consent, it is easy to quit the relation in case of any unwanted discipline or limitation.

If the state would be controlled directly by citizens, it would end the disciplining functioning of a state, which is necessary because of human nature. So, the control of a state is understood differently by continental conservatives: on the one hand, they suppose a transcendental world and its institutional embodiment, the Catholic Church and the pope (see Joseph de Maistre), as a reality existing above the state (Lovejoy, 2001; Molnar, 1988; Maistre, 1994). While liberals would limit the state by unlimited personal interests and wishes, Thomas Molnar would limit the state as well as its citizens. The presupposition of a reality above politics means also that there is something more important than politics, and a lot of issues cannot be solved by politics. Politics are not able to provide salvation in this world. The transcendental or sacred world – mediated by church, priests and rites – is the source of authority, and only this authority can integrate with the human world by disciplining people and by evoking obedience and loyalty from them. These effects of authority are connected to the same effects of morality which limits authority and is defended by authority.

Thomas Molnar found the sociological description of the sacred in Weber's notion of charisma – which in his last paper, *Politics as Vocation* (Weber, 2004) was not only on ideal type of legitimate order, but tacitly characterized any politician – and is what put the mysticum back into its place (Molnar, 1988).[3] The notion of the sacred assimilated charisma and the Burkean notion of the sublime, but Molnar took this notion mainly from Rudolf Otto's notion of *mysterium tremendum et fascinans*. For Molnar, power is sacred: it frightens and excites at the same time (Molnar, 1988).

The two institutions of power are the church and state – like in case of Weber. Without the sacred and these – by definition authoritative – institutions, the existence of a human order is questionable, which is necessarily a religious community (*universitas fidelium*) in the Gallican tradition. At this point Thomas Molnar was rather selective: he referred positively to

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Fustel de Coulanges, while refusing those French modernists who belonged to the same tradition like Rousseau, Comte and Durkheim. He explained the decline of the state and church by the ascent of "molecules", that is, the individual's conscience had become the source of the sacred (Molnar, 1988). Molnar argued that the essence of modernity/heresy/utopianism was the idea of the self-sufficient man (*ens completum*).

Thomas Molnar was especially interested in the Catholic Church, and beside modernists he criticized modern Catholics, too, following Pius X: "the partisans of error are to be sought not only among the Church's open enemies; they lie hid, a thing to be deeply deplored and feared, in her very bosom and heart, and are the more mischievous, the less conspicuously they appear. We allude, Venerable Brethren, to many who belong to the Catholic laity, nay, and this is far more lamentable, to the ranks of the priesthood itself, who, feigning a love for the Church, lacking the firm protection of philosophy and theology, nay more, thoroughly imbued with the poisonous doctrines taught by the enemies of the Church, and lost to all sense of modesty, vaunt themselves as reformers of the Church; and, forming more boldly into line of attack, assail all that is most sacred in the work of Christ, not sparing even the person of the Divine Redeemer, whom, with sacrilegious daring, they reduce to a simple, mere man" (Pope Pius X, 1907).

Practically, this is the core idea of his *Christian Humanism: A Critique of the Secular City and Its Ideology* (Molnar, 1978): The Catholic Church is threatened by the danger of becoming in its visible form a different church.

The crisis of modernity originates, according to Molnar, in the takeover of society. Instead of the sacred, (civil) society would control political and ecclesiastical power. Metaphysically, modernity is a new version of human rebellion, and sociologically, modernity is the rebel of (civil) society. Therefore, modern problems are coming from this rebellion. In this respect, he continued the criticism of revolutions and capitalism in the 19th century and the criticism of mass society in the 20th century.

The two institutions of authority are connected to the sacred, but (civil) society is not, therefore the last one cannot be the source of order, it cannot invoke *tremendum* and *admiratio*. For him, (civil) society is connected to plurality and self-interest, but pluralism gives birth to relativism and self-interests produce immanentism – i.e. there exist only this-worldly and individual realities (Molnar, 1988) – which characterizes modernity in the *Pascendi dominici gregis*. Society is not able to create order because of its contractual and permanently bargaining nature. (This social criticism of society was connected in his case to the moral criticism of hedonism and eudaimonism.) In modernity what are called state and church are not state and church in the proper sense, because they are curtailed from authority and sanctity. Modernity is the world of society.

There were and there will always be some frustrations in this-worldy life, there is no return to the trouble-free Paradise from the *condition humana*, even if man aspires to it. Those who think politics, authority and inequality are permanently necessary for a decent life usually accept this troublesome characteristic of human

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life, as well. And they, like Thomas Molnar, instead of hoping for a trouble-free world, accept that frustrations and conflicts are perennial, and authority has to exist because it is the only chance for a decent, less-than-perfect life.

„In like manner, the other pains and hardships of life will have no end or cessation on earth; for the consequences of sin are bitter and hard to bear, and they must accompany man so long as life lasts. To suffer and to endure, therefore, is the lot of humanity; let them strive as they may, no strength and no artifice will ever succeed in banishing from human life the ills and troubles which beset it. If any there are who pretend differently – who hold out to a hard-pressed people the boon of freedom from pain and trouble, an undisturbed repose, and constant enjoyment – they delude the people and impose upon them, and their lying promises will only one day bring forth evils worse than the present. Nothing is more useful than to look upon the world as it really is, and at the same time to seek elsewhere, as We have said, for the solace to its troubles" (Pope Pius X, 1907).

But in modern politics, ambitious leaders can get support from the mobilization of people by promising frustration- and a conflict-free world. In modernist thinking, governing is crisis management founded on proper knowledge – the newest and newest waves of modernists think that existence, constructed by the previous versions of modernism, is unbearable – and are not capable of making decisions. In their mind being governed means being lead to utopia, and may go together with hard frustrations and troubles which should be taken to get to utopia. The progressives want to emerge with a much better world, while the conservatives are satisfied by running a decent or liveable one. What is desirable is not necessarily possible, and the action following logical arguments does not necessarily result in the desired results. For the modernist the future is not ambiguous, but it is simply the question of real knowledge (science, expertise) and benevolent decision.

As it can be seen, Thomas Molnar separated from the American mainstream not only by his aversion to the free market and libertarianism, but more fundamentally, by his open refusal to many elements of American conservative thinking coming from a liberal heritage. From these antithetical ideas the most important ones are equality, authority, hierarchy and the sacred. He imported Continental – dominantly French Catholic – conservative ideas into the US, but these stayed isolated in the conservative coterie.

Notes

1 „All fixed, fast-frozen relations, with their train of ancient and venerable prejudices and opinions, are swept away, all new-formed ones become antiquated before they can ossify. All that is solid melts into air, all that is holy is profaned." (Marx and Engels, 1969)

2 The fundamental political and moral problem according to Strauss is: „whether men can acquire knowledge of the good without which they cannot guide their lives individually or collectively by the unaided effort of their natural powers, or whether they are dependent for that knowledge on Divine Revelation. No alternative is more fundamental than this: human guidance or divine guidance". (Strauss, 1953, p. 74) See Meier, 2006.

3 However, he was rather ambivalent concerning the concept of charismatic domination. See Molnar 1995a.

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Bálint Teleki

From the Sanhedrin to Foreign Currency Loans in Hungary

Cases of Groupthink from History

Summary

The term 'groupthink', coined by Irving L. Janis in 1972 is a phenomenon that is one of the worst factors distorting decisions. Groupthink evolves under peculiar antecedent conditions (or pre-requisites) and shows specific symptoms when in action. In this article, these conditions and symptoms are reviewed, examples are given from global history to demonstrate its adverse impacts and the management of the phenomenon is illustrated by positive examples. Then an attempt is made at proving that the rise and fall of foreign currency lending, perhaps the largest economic disaster in post-communist Hungary, can be traced back to the phenomenon called groupthink.

Journal of Economic Literature (JEL) codes: D14, D22, D23, D91, E71, G41

Keywords: corporate governance, diversity, foreign currency lending, groupthink, Hungary, Sanhedrin of Israel

What is groupthink and why do we regard it as a problem?

When it comes to the term 'groupthink', virtually every literature essay quotes the recognised works of Irving L. Janis (Janis, 1972; 1982), who coined this word to describe the phenomenon also examined in this article.

According to Janis, members of high-status decision-making groups may develop such extreme forms of camaraderie and solidarity that they suppress dissent, valuing group membership and harmony above else. This silencing of ideas that depart from the majority thinking can have devastating results: it may lead to the distortion of reality, to the adoption of risky policies, and to the abandonment of ethical considerations (Schnall and Greenberg, 2012). Similarly, the Merriam-Webster's dictionary defines this expression as "a pattern of thought characterized by self-deception, forced manufacture of

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consent, and conformity to group values and ethics" (Bénabou, 2013). Moreover, in the literature the terms "collective denial and wilful blindness", "Mutually Assured Delusion (MAD)" (Bénabou, 2013) and "collaborative spiralling of irrationality" (Szanto, 2017) also appear as descriptions of groupthink.

As it is obvious from the definitions above, groupthink is a very dangerous phenomenon, which needs to be diagnosed and handled if and when it seems to occur, in order to avoid great problems. In this paper, after describing the accurate general characteristics of groupthink, diverse relevant examples are analysed in terms of groupthink, in order to demonstrate the versatility of the phenomenon. The examples are taken from various ages in history: from ancient times to contemporary problems of the 21st century. These examples are divided into two groups, separated by the correct or incorrect handling of groupthink in the given situation.

Antecedent conditions and symptoms of groupthink

As Janis and subsequent researchers have stated, the so-called antecedent conditions are the observable causes of groupthink. In other words, they are the conditions "that produce, elicit, or facilitate the occurrence of the syndrome" (Golkar, 2013).

One primary and several secondary *antecedent conditions* have been identified. The primary antecedent condition necessary for groupthink is a highly cohesive group. Secondary antecedent conditions can be clustered into two sub-groups. The first sub-group contains those related to the structural or administrative faults of the organisation, namely: 1) insulation of the group; 2) leader preference for certain decisions (in other words, directive leadership); 3) lack of norms requiring methodical procedures; and 4) homogeneity of the members' social background and ideology. The second sub-group includes conditions related to the decision-making context, including: 1) high stress from external threats with low hope of a better solution than the leader's; 2) low self-esteem, temporarily induced by the group's perception of recent failures, excessive difficulties on current decision-making tasks, and moral dilemmas (Golkar, 2013).

Here we need to take a quick glance at the accurate meaning of the more important one of the above-listed antecedent conditions. *Group cohesiveness* can be described as the members' overall attraction to a particular group, which is a result of the 'esprit de corps' (a feeling of pride and shared mutual loyalty) and amiability between the individual group members. *Directive leadership* is defined as a group member's perception of being influenced by a leader who pre-meditates a viewpoint early in the decision-making process and ignores procedures for evaluating alternatives. *Group insulation* refers to the perceived isolation from external opinions in a social decision-making process (i.e. the experience of a strong social homogeneity but less strong ties to society). *Stress* generally refers to any environmental, social or internal demand which requires and individual to adjust his/her individual patterns of behaviour, and is experienced when important decision outcomes carry a high threat of loss and are perceived to be one's personal responsibility (Breitsohl et al., 2015).

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The observable *consequences or symptoms of* groupthink are seen as follows: 1) an illusion of invulnerability; 2) an unquestioned belief in the group's inherent morality; 3) collective efforts to rationalise; 4) stereotyped views of enemy leaders as evil, weak or stupid; 5) self-censorship of deviations from the group consensus; 6) a shared illusion of unanimity; 7) direct pressure on any member who expresses strong arguments against any of the group's stereotypes; 8) the emergence of self-appointed mind guards to protect or screen the group from adverse information. These eight symptoms are the primary factors suitable for identifying groupthink (Golkar, 2013).

Preventing and handling groupthink

Let us see a few characteristic cases of groupthink in history with focus on how the phenomenon was or could have been prevented and/or handled, and on the possible methods of promoting the efforts to combat them.

How harmful groupthink can be? Negative examples

This part includes cases with adverse outcomes in order to analyse what exactly went wrong, and how it fitted into the framework of groupthink.

USA-related wars

As a result of their analyses of wars related to the very existence and the modern history of the USA, certain authors concluded that the pattern of groupthink was observable. In relation to the Independence War, or more exactly, to the British military intervention of 1768, and much later, to the Bay of Pigs fiasco, the Vietnam War and especially to the 2003 Second Gulf War against Iraq, it is rather apparent that groupthink-related factors played a huge role (York, 2011).

Neil L. York compares the mistakes made by King George III and by President George W. Bush in their decisions to use military power instead of peaceful alternatives. York claims that in both instances policy-makers argued that they had virtually no other option. There may have been a certain amount of deceit and disingenuousness in what they claimed publicly, but it also appears that they often meant what they said, and that they acted sincerely, however illogical or ill-informed their actions may now appear to have been (just remember, for instance, the alleged Weapons of Mass Destruction possessed by President Saddam Hussein). Reality is a construct of our brain, a construct we devise: so it was for George III and George W. Bush (York, 2011).

In these cases, the homogeneity of the advisory circles surrounding the two statesmen included people of homogeneous backgrounds and political preferences (in case of President Bush e.g. Dick Cheney, Donald Rumsfeld, etc.), who also filtered the information for the president, thus insulating the ultimate decision-maker.

The May 1996 Mount Everest disaster

On the tragic day of 10 May 1996 two separate expeditions – guided by the New Zealander Rob Hall and the American Scott Fischer, respectively – attempted to reach the summit of Mount Everest, and

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lost several people. Both teams ignored the normal turnaround time of 14:00 hours, and climbed while a severe storm was approaching. Moreover they did not have enough oxygen in their canisters to do so (Burnette et al., 2011).

Several antecedent conditions of groupthink are well observable in this case. Group cohesion manifested in a rather unorthodox way, because as one of the team members put it: "we were a team in name only". There was, however a sense of solidarity, friendship and mutual respect within the group, and most importantly, as a superordinate goal, there was the sole purpose of reaching the summit. Thus directive leadership occurred as a consequence of self-censorship to attain the superordinate goal. Stress is apparently related to such extreme mountaineering expeditions, but in this case recent failures added extra stress (Burnette et al., 2011).

The symptoms of groupthink are diagnosable – all in connection with the superordinate goal of the groups – such as the overestimation of the group, pressure towards uniformity, and closed-mindedness in the group. All these occurred because of the sole purpose to reach the summit, and distorted the sense of reality of even such experienced mountaineers, costing them the lives of their majority (Burnette et al., 2011).

'Volkthink'

The *'Volkthink'* model is a specific advanced form of groupthink, and is defined as the association of certain policies with a cohesive but depersonalised social identity in a way that these policies function as a form of identity preservation or promotion. Consequently, the antecedent conditions are 1) high level of social cohesion and of homogeneity; 2) a strong but depersonalised group identity; and 3) a situational relationship between group identity and specific policies. National identity may be the most obvious example of this pattern (Carolan, 2016).

The special vulnerability of small states, such as Ireland and Iceland, to Volkthink is an interesting idea. Reports of the economic difficulties in both countries reveal similar patterns of excessive interest-group influence, inadequate regulatory capacity, inappropriately close relationships and a dominant social and political consensus, intolerant to opposing viewpoints. Both countries are of relatively homogeneous population, with smaller monitoring systems and less competitors in the market. In both sectors, the economic success of particular sectors – in this case perhaps most importantly, the banking sector – was positively associated with national and social identity (Carolan, 2016).

Therefore, any criticism of the economic success was understood as a threat to the social identity of the state. It is not surprising that in such an environment, the necessary steps to prevent or, later on, to handle financial disasters could not have been taken, because this attitude had led to a system of dysfunctional public policies. As a consequence, financial bubbles evolved and existed for a prolonged period of time (Carolan, 2016).

Online financial communities

Groupthink theory also has an impact on micro-finances, as revealed by financial online communities. In this case the

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largest problem is conformity-seeking behaviour within these communities, which is connected to stress, cohesiveness and group insulation, and the lack of information from outside. Stress has a role here, because such online communities have a very strong stress-mitigating effect, but in many cases this effect has an adverse impact on financial decisions. In-group homogeneity and the strong intra-focus of the group lead to cohesiveness and to group insulation. Finally, the lack of statistical support to decisions – due to the absence of external information – may lead to directive leadership, further increasing the adverse impact on individual financial decisions made by the group members. Many disadvantageous financial decisions can be traced back to these phenomena, and their effects were particularly clearly visible during the financial crisis after 2008 (Breitsohl et al., 2015).

Dysfunction of EBA's stress tests

The European Banking Authority (EBA) is one of the three micro-prudential financial supervisory agencies of the European Union, established after the 2008 crisis in order to enhance control over the financial markets of the EU. One of its main tasks is to conduct stress tests of the market. The failure of the system became apparent when, after the 2011 stress test of Spanish banks, which confirmed that everything was in order, in June 2012 the EU had to bail-out the Spanish banking sector by more than a hundred billion euros. We cannot tell for sure what exactly happened, but most probably a sort of groupthink effect worked, i.e. the national delegates of the EBA Board did not want to vote against a specific country in fear of a possible future retaliation against their own countries in a similar situation, and as a result, they decided in a more "conservative" way (Szegedi, 2018).

How to handle groupthink? Positive examples

Mention must be made of two positive examples when groupthink was prevented and/or handled appropriately. One of them includes the Sanhedrin of ancient Israel, and the practices and processes that may be adopted and built in our contemporary practices. The second one deals with genuine contemporary solutions for corporate governance.

The Sanhedrin of ancient Israel

In ancient Israel, since the period of the Second Temple, the Great Sanhedrin had become the supreme judicial forum, although it also had political functions besides acting as a court. Even after the destruction of the Second Temple in 70 CE, it managed to maintain its position, although with restricted powers (Jany, 2016).

Perhaps the most important case heard by the Great Sanhedrin, the trial of Jesus Christ, was conducted in the period of the Second Temple. One would argue that this procedure would be the best example of the malfunctions of groupthink. However, the crucifixion of Jesus – from the believer's perspective – was a crucial and inevitable part of God's Plan of Salvation, and therefore cannot be deemed as adverse, but more importantly, according to the relevant literature, the Great Sanhedrin had very good practices to

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prevent groupthink, and what happened to Jesus before the court was more of a politically motivated exception.

According to the Talmud the Great Sanhedrin's leadership system was very effective in preventing a single person's opinion from dominating others. The leadership was divided between multiple individuals to prevent harmful domineering and giving too much latitude to dissenters. The "Aboth" ("Ethics of the Fathers") part of the Talmud dictates that "one should hate acting superior" [Aboth 1:10] and also that "judge not alone, for none may judge alone save One [G-d]" [Aboth 4:8]. The essence of impartial leadership is encapsulated in this statement: "Say not 'Accept my view' for they are free but not thou" [i.e. "they are free to concur, but not thou to force them to concur"] [Aboth 4:8]. In plain English, the last sentence says that no juror of the Sanhedrin can be forced to concur i.e. agree with the majority (Schnall and Greenberg, 2012).

Besides that, open debates were prompted between the members, and in some cases even the *nasi* (the president of the court) could be removed in order to prevent directive leadership (see e.g. the story of Hillel [Pesahim 66a] or the debate between the rabbis Yehoshua and Gamliel [Rosh Hashana 25a, Berakoth 27b, Bekoroth, 36a]). Another very important similar instruction was that the junior members had to vote prior to seniors, so that the less powerful and influential could not be influenced by the opinions of the more powerful and influential [Sanhedrin, 32a]. It was explicitly prohibited for a member to refer to the majority vote as the ground of his own vote, and the 'devil's advocate' position was introduced [Sanhedrin 29a]. In capital cases even stronger pre-cautions were made. For instance, if all members supported the conviction, the final decision was mandatorily postponed until the next day [Sanhedrin 40a] (Schnall and Greenberg, 2012).

Even around the trial of Jesus there are signs of this way of thinking, the proofs are recorded in the Holy Bible. Nicodemus seems to provide an example of an in-group member who pursues the exploration of all the effective alternatives from a very rational perspective. Nicodemus deemed necessary to meet Jesus beforehand [John 3], offered a tentative defence for him during the trial [John 7] and finally helped to bury him [John 19] (Bell, 2016).

Unfortunately, these practices were somehow not transferred to the early Christian communities, where many factions or sub-groups of the church came to existence in a very short time, who did not entirely agree with the mainstream and became rival groups. Paul, who was in many cases very tolerant and benign as a leader, took charge of combating the Judaisers' views even to the point of confronting Apostle Peter of Antioch [Acts 15:1] (Bell, 2016). This argument absolutely reflects group insulation and cohesiveness along with directive leadership.

What can we learn and adopt from the practices of the Sanhedrin in the 21st century? According to Schnall and Greenberg, especially the "devil's advocate" and the "second-chance meeting" are relevant for corporate and organizational decision-making, but also the diverse membership of the board can help. (The Sanhedrin also consisted of members with a homogeneous social status

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and ideological/religious background, but made steps to prevent the failures stemming from this.) It can be a realistic solution if diverse groups (e.g. investors, creditors, etc.) nominated at least a part of the board members (Schnall and Greenberg, 2012). Encouraging diverse options in decision-making – which is in the heart of the Sanhedrin's practice – is one of the most important means of combating groupthink (Kelman et al., 2017).

Corporate governance without groupthink

There is another type of diversity, preferable for corporate and organizational decision-making boards, namely *gender diversity*. According to studies, gender diversity can be an antidote to groupthink in several ways. First of all, diversity itself provides more psychological independence than the current system of 'independent directors'. (This is also true for educational and occupational diversity.) The main advantages of employing female directors has its roots in the fact that as female directors must overcome many system barriers to attain board positions, they tend to be highly motivated and prepared for meetings. Also, female directors typically come from outside the groups and networks most directors come from, and this makes them 'outsiders', therefore giving them a different perspective (Kamalnath, 2017).

Another useful tool to combat groupthink is the *Group Support Systems (GSS)*, which has been in place for more than two decades. GSS is basically a constantly evolving computer-based technology for teamwork. It structures the group decision-making process in three major ways: 1) focusing on group members' efforts on the task or problem to be solved by the group; 2) equalising group member participation; and 3) increasing consensus-reaching. Being a technological solution designed for group decision-making, it aggregates the opinions of the group, promotes process structuring, expands the information processing capabilities of the group, and broadens the perspective of the group by facilitating access to external information. Through all these functions, it is able to provide a larger number of alternatives, reduce the time required for making a decision, and increase the use of external information and improve the decision quality (Miranda and Saunders, 1995).

Studies in the field of behavioural operations management increasingly focus on the psychological factors and dynamics that drive operation on the level of the individual worker. They have identified 'Groupthink Behaviour' (GTB) as an adverse group behaviour pattern. The relevant studies and the literature have found that the negative impacts of GTB on project work can be counterbalanced by a high level of (individually) perceived internal control and conscientiousness, and to a lesser degree, by a high level of interpersonal evaluation among the group members (Riccobono et al., 2016).

Groupthink and foreign currency loans in Hungary

According to Farkas "a foreign currency loan, regardless of the fact whether it is disbursed and repaid in a foreign currency or […] in different currency, does not differ from any other loan" (Farkas, 2017). However, foreign currency loans triggered significant changes in the prac-

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tice of lending in Hungary. The complexity and the absence of transparency of the loan contracts were especially problematic. As Bodnár puts it, "these contracts were rather complicated, and their evaluation required a level of professional banking understanding the judiciary naturally did not have". And in this quote he refers to that part of the judiciary, which had to try to serve justice in lawsuits related to these loans (Bodnár, 2013).

It started in the early 2000s, when foreign currency loans were authorised, originally only in the case of real estate loans. After 2004, however, the socialist-liberal government made this construction available for home equity loans as well. Interest rates were compelling, and many people wished to take advantage of the foreign currency margin. However, as the global economic crises escalated after 2008, the advantage turned into a disadvantage, and the worth of the instalments became multiplied sums of the original ones. This led to a disaster in many ways (Neményi, 2009). The accumulated worth of the loans reached HUF 15 billion between 2008–2011, and although the new conservative government in power from 2010 introduced many helpful measures to solve the problem, the accumulated worth still remained HUF 4 billion in the summer of 2014 (Bodzási, 2015).

The extensive popularity of foreign currency loans in the years preceding the crisis was due to a sort of groupthink pattern. An empirical study carried out by young researchers on the reasons underlying the spread of the foreign currency loans traces it back to three main factors: 1) the successful aggressive marketing campaigns carried out by credit institutions; 2) the lack of basic financial literacy among the population; and 3) that the few warnings about the possible adverse consequences could not get through. (These three factors are, of course, interdependent.) Regarding the first factor, the advertisements of the banks involved – especially the advertisements on television – used a sort of extremely manipulative tone and symbols to convince people that these products were the easiest way to receive funding, in comparison to ordinary credit assessment procedures. Regarding the second factor, two other empirical studies should be quoted. The 2010 OECD assessment of financial literacy found that even in comparison to other countries in the CEE-region, the Hungarian population was the most uneducated in this field. The 2011 research carried out by the National Bank of Hungary on financial literacy also had worrying results. Although 67% of the respondents claimed to make regular efforts at understanding finances, other responses revealed that 40% were not absolutely or mostly confident in this field, and only 20% claimed to be completely confident. One seventh of the population did not have experience with any kind of financial product at all, including the simplest bank account. Regarding the third factor, the Hungarian Financial Supervisory Authority – which was then integrated into the Hungarian National Bank in 1st October 2013 – had no power to restrict foreign currency lending. Nevertheless, they warned credit institutions as well as the population, but without much success. Also, a small part of the media published articles with warnings, but these also remained ineffective (Bagány et al., 2015).

Now, the above facts clearly suggest that the antecedent conditions and symp-

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toms of groupthink are in place. The case is also somewhat similar to the negative example of financial online communities mentioned above. Regarding the antecedent conditions: 1) *stress* stems from the need for funding (of a real estate transaction or any kind of spending); 2) *group cohesion* and *group insulation* can be traced back to the part of the population trying to take advantage of a solution they did not really see through or understand in its complexity; and 3) in connection with these, the aggressive marketing campaigns of the credit institutions, along with the peer pressure and the lack of proper warnings to the population, means that the intentions of the banking sector turned into a virtual *directive leadership* in this case. Many of the symptoms were also found: the unquestioned belief in the group's inherent morality; the efforts to rationalise (on the basis of the irrational); self-censorship about the possible adverse consequences, and once the problems had escalated, false hopes in some kind of a miraculous redemption; and so on.

To sum it up, in the author's opinion, the foreign currency lending disaster is an example of groupthink, and perhaps one of the worst ones in modern Hungarian history. It could have been prevented by a more responsible approach of the incumbent government, by a stricter financial regulatory and supervisory system, and most importantly with proper financial education.

Instead of a conclusion

It is relatively difficult to draw a general conclusion or to suggest a general solution for combatting groupthink, since the latter has not been developed yet. What seems to be sure is that the antecedent conditions and symptoms of groupthink are well identifiable in most cases, and this enables decision-makers to take steps to combat groupthink or to mitigate its adverse impacts. Among the possible means, diversity seems to be the most time-honoured solution. Due to the gravity of the problem, further research and studies will likely be conducted on it in the future, and new methods will certainly be devised. However, we should not forget that the simplest but most significant practices have been available since Biblical Times. Another important thing to keep in mind is that governments and competent authorities should always be careful in granting authorisation for loan constructions, because the groupthink effect can manifest itself and lead to grave consequences.

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Szilárd Egyed

How Income from Parental Contribution Helps Young Hungarians Become Consumers

Summary

This article analyses the most important aspect of learning housekeeping and of eating habits, the basis of individual experience, young people's independent income in 3 regions populated by Hungarians: Budapest, the neighbourhood of Tatabánya and Slovakia. The study reveals that in all three geographical regions, the allowance giving habits of parents are less supportive in developing children's ability to learn basic economy, and at the same time hinder the evolution of health-conscious eating habits, too.

Journal of Economic Literature (JEL) codes: D12, D14, I12, R22

Keywords: pocket money, consumption, food, health, children, parents, mother

Introduction

It is easy to comprehend that one of the main wishes of parents is for their children to have a happy, balanced and healthy life. Financial stability, that is, prudent and responsible money management is absolutely essential in achieving a happy and balanced life. The best way to teach prudent money management and financial responsibility is to provide opportunities for self-sufficiency and experiential learning (Fulk and White, 2018), as the knowledge that young people gain in this way will be entrenched and maintained throughout adulthood (Kim and Chatterjee, 2013; Amagir et al., 2018). However, in order for experiential learning to take place, young people need to have an independent income they can use independently.

Consuming food that is good for the human body is a prerequisite for a healthy lifestyle. For a young person to learn what foods are beneficial to their health (and how to obtain and prepare them), the best way is through experience. Longitudinal research has led to the conclusion that individual experience in relation to food is significantly stronger and more lasting than any other form of learning

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(e.g. verbal learning, Pedersen et al., 2015; DeCosta et al., 2017). Accordingly, parents should also encourage and support their children in making and implementing independent decisions (Pratt et al., 2017). At the same time, this autonomy necessitates the existence of an independent income.

At this point, we can see that the acts of learning prudent and responsible money management and of developing healthy eating habits synergise, as both acts are based on the existence of an independent income that enables individual experience.

Independent income can be obtained by children through the involvement of their parents. Parents can choose to supply the independent income to their children in the form of pocket money or by motivating their children to earn their own income by doing formal or informal work. For the sake of simplicity, in this article, the concept of pocket money includes regular allowances as well.

Opportunities for self-employment are age-dependent, as the characteristics of children (up to 13 years of age), adolescents (14–18 years of age) and young adults (over 18 years of age) differ significantly.

While children are given money as a gift or as pocket money, young adults are old enough to work and earn money. Adolescents, on the other hand, have the opportunity to receive both pocket money and income from informal or formal (part-time) work.

Moreover, the amount of income needed also varies considerably, as children and adolescents do not normally have to bear the cost of their living and to pay such costs as rent, overheads and student loans. However, parents often expect their adolescent children to meet some of their own expenses. (Indeed, some young adults benefit from the phenomenon of the so-called "mum hotel", which means that these young adults still live at home, they do not run their own households, and the majority of the cost of their living is paid for by their parents.) In addition, adolescents go out with their friends more often than children, and on these occasions, they have a much greater choice of services than members of the younger age group. Last but not least, adolescence is the very period when young people want to become independent of their parents, and fight for their autonomy through experimentation and trying new things (Otto, 2013). This process of becoming independent requires a significantly higher independent income than the one that children receive.

Based on the above, it can be stated that the existence of self-sufficient income is particularly important for becoming an independent consumer and therefore the examination of the related processes is of paramount importance.

However, regardless of the importance and timeliness of the topic, the scope of local social and economic studies is rather small. A quantified, representative series of surveys is needed to expand the scope and to provide a real assessment of the current situation. The aim of this study is to provide basis to this series, and to deeply understand and explore the problems in the research field.

Literature review

As mentioned above, parents can help their children to earn an independently disposable income by motivating them to

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do income-generating activities such as informal work (e.g. babysitting or gardening for a neighbour) or formal work (e.g. summer jobs, extracurricular part-time jobs). The main benefit of this approach is that children become accustomed to the world of work and they learn to take responsibility for the tasks they perform; moreover, they earn an income from outside the family and, in return, enjoy true and complete autonomy (Batten, 2015).

At the same time, parents can provide their children with an independent income by giving them pocket money or allowances.

Pocket money can be given on a regular basis (e.g. as a fixed amount of weekly or monthly payment) or on special occasions (e.g. as a gift on birthdays, graduations or at Easter Sprinkling). These approaches provide predictability and hence enable conscious planning. Accordingly, pocket money that is given randomly at unpredictable occasions tends to have a negative effect on children by encouraging immediate spending (Samcik, 2014). According to experts, giving pocket money at the request of the child should also be avoided. This approach teaches them that there is an unlimited availability of funds and thus leads to over-spending (Kaczmar, 2016; Hajdók, 2018). One should also consider the fact that giving money at request actually means parental control over the child's spending. The Netherlands is an excellent example for the above mentioned arguments: Dutch parents assume that little pocket money carries a low risk, which means that there is no need to control how the money is spent. How much pocket money is 'little'? Dutch parents give the least pocket money in Western Europe (even in absolute value); and even Polish parents give more pocket money to their children (ING, 2014). As a consequence of the small amount of pocket money, parents have to bear a significant part of their children's costs (e.g. buying clothes, paying for entertainment and ICT using costs, etc., Blanken and Van der Werf, 2016). However, using this method corresponds to giving pocket money on request. This is important to note because the primary goal of Dutch parents – who, according to experts, are at the forefront of conscious parenting – is to raise independent and self-sufficient children through prudent and purposeful education (Acosta and Hutchinson, 2017); however, based on the above, the Dutch methods of giving pocket money seem to be counterproductive.

Besides the above-mentioned examples, parents may also give pocket money to their children without expecting them to do anything in exchange for it; and they may also give pocket money as a reward for a certain desirable behaviour or habit (e.g. doing housework or performing well at school). Theoretically, both methods of giving pocket money / reaching self-sufficiency have their advantages and disadvantages. Since it is always up to the person who evaluates the methods to decide what importance they attach to the advantages and disadvantages, there is no consensus on which of these methods is the best.

The considerable advantage of a fixed amount of pocket money provided regularly and without any prerequisites is the simplicity for the parents and the absolute predictability for the children. Predictability is imperative in the process of learning how to plan spending (Pálinkás-Purgel, 2018).

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The opponents to the above mentioned method argue that in a system like this, children take income for granted, and they do not learn that in the world of adults money is indeed earned with hard work (Batten, 2015). In addition, parents may feel that they give free money to their children, so they feel entitled to control their children's spending. In most cases, strict control is seen by children as a major violation of their autonomy, leading to severe conflicts; while parents should completely avoid these kinds of conflicts in protection of the emotional bonding between them and their children (Khurana and Dang, 2017).

At the same time, several specialists – including Magyary and Horváth (as cited in Hajdók, 2018) – believe that children should enjoy full autonomy in relation to pocket money, and that parents should respect this autonomy (Vekerdy, 2013). In this case, complete autonomy goes hand in hand with complete responsibility, and as a result, children learn the gravity of the consequences of their decisions through personal experience. Accordingly, parents should let their children make mistakes, and consequently, preventing them from making mistakes cannot be an argument for controlling their spending.

A counter-argument is, however, that allowing mistakes cannot be equal to complete autonomy, because even in this case, compliance with basic rules is necessary (Sadeghi et al., 2015). On the one hand, for instance, children should be taught not to spend on products that violate official rules and laws (e.g. firecrackers), on the other hand, they should understand the importance of health and healthy eating habits (e.g. minimising or avoiding the consumption of junk food).

Those who favour the other basic method – giving pocket money in return for work – argue that this method teaches responsibility because it makes the child accountable. Furthermore, they say that having to make an effort to earn the money, children learn to value it more (LeBaron et al., 2019). Another argument on behalf of the supporters of this method is that this way parents can trust their children more, and so children have to face significantly lower levels of parental control. Another great benefit of this method is that children not only learn the value of money and labour, but also learn to stand up for themselves and their interests, as the negotiation about what they have to do in exchange for the pocket money is similar to a wage negotiation. This way, children will be prepared and competent when it comes to real and serious wage negotiations.

During wage negotiations, children develop and continually test their set of tools based on parental response (Othman et al., 2013). This set of tools basically consists of two sets of solutions: one group includes positive interactions, that is, activities for co-operating with the parent (e.g. persuasion based on logical reasoning and collaboration-oriented negotiation, etc.); the other group includes tools for exerting pressure (confrontation, e.g. asking / begging, emotional pressure /emotional blackmailing/ and quarrelling, etc.) (Bodkin et al., 2013).

As a result of the characteristics of the parent-child relationship, parents are significantly more willing to use the collaborative techniques and they also encourage their children to do the same (Othman et al., 2013); consequently, children also gain greater influence if

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they tend to use these techniques. Fundamentally, children do not want to damage the emotional connection with their parents, so primarily they start with a positive interaction and only switch to exerting pressure when they have failed with the first attempt. At the same time, older children are more knowledgeable, better prepared and more convincing in arguments than younger ones, so they reach their aim with positive interactions, while younger children are forced to resort to emotional tactics (Kim et al., 2017).

However, the opponents of this method accuse it of encouraging children to do the housework only if they get something in exchange; they say that children should get used to having tasks at home that they should do without reservation, as they will have to do so in the case of their own independent household as well (Lovas, 2017).

It should be noted that a PISA research series that was carried out with the participation of – among others – fifteen-year-olds living in Australia, Brazil, Chile, Italy, Lithuania, the Netherlands, Peru, Poland, Russia, Slovakia, Spain and the United States, has highlighted that there is no plausible correlation between receiving pocket money and the level of financial expertise (OECD, 2017).

In addition, a longitudinal analysis of the data of the British Household Panel Survey (BHPS) of the United Kingdom's population shows no evidence of a correlation between the availability of pocket money and subsequent savings (Brown and Taylor, 2016).

A longitudinal analysis of the data of Dutch DNB Household Survey also led to similar results. However, the analysis also highlighted that giving children pocket money without expecting anything in return from them, discussing and enforcing some basic rules, and advising on budgeting and savings has a strong positive impact on the existence and amount of future savings (Bucciol and Veronesi, 2014). Nevertheless, the findings of this analysis ought to be treated with caution, since it only examined the relationship between savings and income, but did not address the cause of the higher saving rate. It is easy to comprehend that eating cheap but low quality food can result in increased savings, but in the long run leads to deterioration in health.

Even if giving/receiving pocket money has no significant impact on future money management, the study of pocket money-related processes is nevertheless especially important. On the one hand, individually disposable income is a very important element of experiential learning; on the other hand, it is not at all certain that by giving pocket money, parents wish to achieve a long term goal or the teaching of money management.

Research purpose and questions

Research in international literature does not provide a clear answer to the following questions: What is the purpose and role of the particular type of independent income parents provide for their children and why is it so? Also, how and under what conditions do children want to obtain their independent income and why do they want to do so? Because of the absence of a clear answer to these questions, the aim of this research is to explore the issue in relation to the Hungarian situation. This article sets out to explore the issue along the following research questions (RQ's):

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RQ1: How do parents provide the pocket money, what do they expect in return and what is purpose they want to achieve by it?

RQ2: How proactive and how active are children, i.e. what role do they play in pocket money-related discussions and why?

RQ3: How independently and in what ways do children use their pocket money?

RQ4: Why do children do remunerative work?

RQ5: What are parents' attitudes to children's remunerative employment and why?

Research methods

Data collection and analysis

The research takes a two-pronged approach. As part of this two-pronged approach, young people were interviewed on the one hand and their parents on the other hand. The method of interviewing these young people was the semi-structured in-depth interview. Parents responded to the questions in writing. The questions that were asked from the parents replicated the questions addressed to the young people (clearly, each question was modified according to the person to whom it was addressed). The texts of the in-depth interviews and the written answers were analysed using the method of content analysis. Subsequently, the answers given by each child and by their parents were compared. This method provided an opportunity to explore how parents and children see/understand the particular methods and phenomena; and it also provided a chance to look at the consequences of the differences between the parents' and the children's interpretations.

The sample

There are significant differences regarding the characteristics of giving pocket money between Budapest and the rest of the country (Regiojatek.hu, 2018); therefore, in Hungary, respondents were selected from two different areas. These two areas are Budapest and Tatabánya (and its immediate vicinity). In addition, Hungarians living in Slovakia were involved as a control group. (The classification was made based on the municipality the interviewee had officially belonged to for the longest period of time before reaching adulthood. Naturally, parents were assigned to the same municipalities as their children.)

Furthermore, as there is a significant difference between boys and girls in Hungary in terms of work performance and perception of work (Provident, 2015), the same number of boys and girls (5 per area) was surveyed. All of the young people interviewed had either already graduated or were still in tertiary education at the time of the interview. This was ensure that they were on the way to becoming independent of their parents due to their age characteristics; and that they had presumably received financial (and perhaps also other kinds of) support from their parents – because of the high level of their education and their achievements in education. Moreover, in order to make sure that the effects of becoming independent of the parents can be observed, only those young people were interviewed who had been living in dormitories for longer periods of time

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(during their secondary and/or tertiary education) and consequently had to regularly manage buying meals/groceries.

With one exception, the parents interviewed were all women, since both in Hungary (Zsótér, 2017) and in Slovakia (Mendelová, 2014), children's financial education is mainly the task and responsibility of mothers. In one exceptional case the father was interviewed because, in that family, due to the mother's less considerate spending methods, the children's financial education was the father's task and responsibility. In addition, all parents interviewed had graduated in tertiary education; since the higher the educational level of the mother (the person who is responsible for the children's financial education), the higher the level of financial education and financial awareness of the children (Grohmann and Menkhoff, 2015).

According to the above, there were a total of 60 respondents (5 girls and 5 boys per area, and one parent to each child). First names are not included in this article for compliance with the GDPR (General Data Protection Regulation); so where the original text uses a first name, it is replaced in the article by the expressions "our son" or "our daughter"). However, in order to indicate the relationship between the child and their parent, respondents are coded. For example, respondent child number 1 is indicated as#C1 and their parent is indicated as#P1.

Based on the above, the set of respondents was established as follows *(Table 1.)*.

Main findings

Meaningful responses from the interviewed young people and their parents have yielded rich results, which provide an opportunity to deepen the analysis of the phenomena, processes and (influencing) factors related to young people's independent income. Nevertheless, it is important to note in advance that in all three geographical areas, contrary to the preliminary expectations, there were no significant differences between the goals, attitudes and actions of the parents or of the young people involved in relation to the independent income of young people. For this reason, the responses from the three geographical areas are discussed together in the article. In addition, the results of the answers received are presented according to each of the surveyed topics.

RQ1: How do parents provide the pocket money, what do they expect in return and what is purpose they want to achieve by it?

The purpose of giving pocket money

Five of the parents interviewed admitted not to give their children pocket money. They explained arguing that pocket money would not have been justified, because the children received everything they needed or specifically asked for.

"Our daughter does not get any pocket money because she has got everything she needs." /#P7/

"We do not need to give any pocket money. She has got everything she has asked for." /#P19/

It should be noted that the answers to the interpretive questions given by the young people indicate that what the parents thought the children needed was significantly different from what the children actually wanted (or even asked for).

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Table 1: Codes for respondents

	Children				Parents		
Budapest	#C1	Male	25 y.o.	Student	#P1	Mother	56 y.o.
	#C2	Male	23 y.o.	Student	#P2	Mother	51 y.o.
	#C3	Male	23 y.o.	Student	#P3	Mother	59 y.o.
	#C4	Male	24 y.o.	Student	#P4	Mother	65 y.o.
	#C5	Male	24 y.o.	Graduated	#P5	Father	61 y.o.
	#C6	Female	22 y.o.	Student	#P6	Mother	47 y.o.
	#C7	Female	21 y.o.	Student	#P7	Mother	42 y.o.
	#C8	Female	21 y.o.	Student	#P8	Mother	46 y.o.
	#C9	Female	22 y.o.	Student	#P9	Mother	48 y.o.
	#C10	Female	21 y.o.	Student	#P10	Mother	48 y.o.
Tatabánya	#C11	Male	21 y.o.	Student	#P11	Mother	54 y.o.
	#C12	Male	23 y.o.	Student	#P12	Mother	49 y.o.
	#C13	Male	25 y.o.	Student	#P13	Mother	52 y.o.
	#C14	Male	24 y.o.	Student	#P14	Mother	50 y.o.
	#C15	Male	23 y.o.	Student	#P15	Mother	43 y.o.
	#C16	Female	21 y.o.	Student	#P16	Mother	51 y.o.
	#C17	Female	25 y.o.	Student	#P17	Mother	50 y.o.
	#C18	Female	21 y.o.	Student	#P18	Mother	54 y.o.
	#C19	Female	22 y.o.	Student	#P19	Mother	51 y.o.
	#C20	Female	20 y.o.	Student	#P20	Mother	48 y.o.
Upland	#C21	Male	23 y.o.	Graduated	#P21	Mother	47 y.o.
	#C22	Male	24 y.o.	Graduated	#P22	Mother	50 y.o.
	#C23	Male	20 y.o.	Student	#P23	Mother	49 y.o.
	#C24	Male	22 y.o.	Student	#P24	Mother	56 y.o.
	#C25	Male	22 y.o.	Student	#P25	Mother	53 y.o.
	#C26	Female	25 y.o.	Graduated	#P26	Mother	51 y.o.
	#C27	Female	20 y.o.	Student	#P27	Mother	54 y.o.
	#C28	Female	25 y.o.	Graduated	#P28	Mother	49 y.o.
	#C29	Female	22 y.o.	Student	#P29	Mother	52 y.o.
	#C30	Female	20 y.o.	Student	#P30	Mother	57 y.o.

Source: By the author

"I had to ask for money for everything. ... I didn't really ask, I didn't really spend much. … If I wanted to go to the cinema, I couldn't always go… they didn't give me money. Sometimes they came with me… my friends rather paid (for the cinema ticket)." /#C7/

"I asked… but sometimes in vain. … It happened that I wanted to buy a top, but Mum didn't like it. … If she didn't like something, I didn't get the money to buy it." /#C19/

In addition, it is important to note that all five of the above mentioned par-

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ents acted this way with their respondent daughters; and those of the four parents who have children other than their daughters (every child is a girl), the same is true for all their children. Considering this attitude, it is possible that the genuine reason for the financial support provided on request is not to meet the needs of the child but the preventive control of the girls' spending (even though parents did not specifically mention this in their responses).

Besides these – although the research was not aimed at examining the characteristics of young people's family relationships – the responses of the girls receiving financial support only upon request revealed that the significant difference between the sisters' ways of communication and their different levels of courage / pushiness caused significant differences in the amount of financial support received; and this difference put a heavy burden on the relationship between the sisters (since it generated several conflicts).

Based on the above, five respondents had to ask for financial support from their parents for any spending. However, another 17 young people interviewed were not in a significantly better situation than them in this regard. Their parents gave them pocket money, but the opportunity to spend it was severely limited, because the purpose of the financial support was to enable the child to pay for school meals (breakfast or morning snack) and / or to commute between their homes and their schools.

"She got money to buy breakfast at the school." /#P11/

"We gave our daughter pocket money so she could buy her morning snack, and we gave her money during the high school so she could buy a monthly pass for travelling." /#P16/

The children's responses highlighted that this parenting practice encouraged young people to save money on certain meals and to skip meals in order to be able to put some money aside for buying other things freely, and to seek financial support separately for everything else they wanted to spend on.

"I got pocket money for breakfast, but sometimes I didn't buy sandwiches. I would rather spend the money on chocolate or soft drinks. … Sometimes I bought ice cream. … If I wanted anything else, I had to ask. I didn't like (asking), I didn't want to." /#C11/

"I only got money for morning snacks, and then later for travelling. … I didn't get money for anything else. If I needed money for something else, I had to ask for it." /#C16/

It is important to note that young people's responses revealed that parents were mostly aware of what their children were buying, that is, what they were eating as morning snacks. They were eating cheap sandwiches (e.g. buns with salami, or in the case of college students, homemade butter rolls) or sweet pastries (e.g. chocolate rolls), and their substitute products were smaller bars of chocolate and sugary soft drinks. As a result, the children consumed less healthy food, but the parents' primary concern was whether their children had eaten during the day. At most, parents expressed their dismay if they learned that their children had eaten chocolate instead of – in the traditional sense – proper food.

"They asked me if I had eaten. I told them I had. … Sometimes they asked me

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what I had eaten. … I told them, but that was it." /#C23/

"When they asked, I told them what I had eaten. … Not always, usually not, but sometimes I also told them that I had eaten chocolate. Then she said (my mother) that I should eat something proper (food)." /#C5/

Another parent said that they had given their child pocket money so that he could cover any – urgent – expenses he might have.

"We gave our son pocket money so that he had money on him if he needed something." /#P22/

Yet another parent did not give their child any pocket money because their child, being an athlete, received a subsidy for sportsmen. However, the remaining six parents (parents of 3 respondent girls and 3 boys) clearly stated in their responses that they had given their children pocket money to make sure that they learn how to manage money.

"We gave our son pocket money to help him learn how to handle money." /#P3/

"The reason was to make him learn how to manage it." (They gave their son pocket money to help him learn money management.) /#P12/

It should be emphasized that parents whose reason for providing pocket money to their children was to teach them money management provided the money without any labelling and their children could use the money completely freely. In addition, they all expected their children to save a certain amount of the pocket money they had received. Only five of the respondents complied with this condition. One of them saved the money without any definite goal, but four of them set it aside to buy a product of high value (e.g. a bicycle, a mobile phone, etc.) The remaining one young person (a woman) could not save money in the long run when she was receiving pocket money, nor is she currently able to do so (despite the fact that her earnings are significantly higher than average). This person spent her pocket money mainly on clothes and cosmetics.

Expected/required service in return for pocket money

It is important to note that only six of the parents (the parents of the interviewed girls involved in the research) stated that they had expected/required a service in exchange for the pocket money. Nevertheless, four parents made the service a condition for additional income, since the "basic pocket money" was provided without expecting anything in return. The expected service for these four parents was good school grades (for three of the parents) and washing their car (for one of the parents).

"We gave him pocket money (without asking for anything in exchange) weekly. … We gave him (some more) monthly for car washes." /#P6/

"We provided pocket money (without asking for anything in exchange) on a weekly basis. … For good school grades we gave him (more) pocket money monthly." /#P29/

Apparently, two parents made housework or good school grades the condition of providing pocket money, but children's responses revealed that the expected conditions or their fulfilment had no real effect on receiving pocket money.

"Yes, they said I had to get good grades. … That I got the pocket money

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for good grades, ... but that was not a (real) condition. I always performed well at school." /#C20/

"Housework was the condition, but it didn't matter. … I knew I would get it anyway." /#C9/

However, according to the answers of the young people, for the majority, it would not have made sense to be offered pocket money for help (e.g. housework, gardening, helping with the shopping, etc.), because the children would not have accepted it.

"Pocket money for helping them? Ah, no. It goes against principles. By no means. I help because I do a favour. … I would have never expected anything from my family as a reward." /#C18/

"I always helped both of them (my mother and my father). I'm not saying I was always happy to do so, but I helped them. … I don't think they wanted to give me money for that, but they didn't have to. … I didn't ask anything for it (for the help). I have never even thought of that." /#C24/

Regularity of pocket money

Of the young people who received pocket money, each received it weekly. The parents only provided additional allowances (e.g. in return for good school grades) and travelling costs on a monthly basis.

RQ2: How proactive and how active are children, i.e. what role do they play in pocket money-related discussions, and why?

Parental interpretation of discussions on financial support

As mentioned earlier, there are certain types of financial support that parents consider pocket money; but these types of financial support – by definition – cannot be referred to as pocket money. These are the cases when parents only give money for a specific product/service upon request. In these cases, the parents – quite understandably – believe that the children had a rather active role in the negotiations, simply because they always initiated them (they started the discussions by asking for something).

However, initiating a specific request for a product/service cannot be considered as asserting one's interests because the request was not aimed at an independently spent income. For this reason, it is much more important in this research to look at discussions where the goal was to earn and increase the amount of independent income that can be considered as pocket money.

In the case of pocket money for morning meals or commuting between home and school the children were never proactive and they did not play an active role in the discussions, but accepted the parent's will.

"Whatever they said, I accepted it. … Actually, I didn't want to ask for anything. … Sometimes I asked to be allowed to go out at weekends." /#C1/

"They said (my parents) that I got this amount for the school's snack bar. And I said okay." /#C30/

It is important to note that those who had their pocket money increased over time (especially after the age of 16) also played a passive role in the discussion about the increase, and it was not them, but the parents who initiated the rise. The reason why the parents increased the amount of the pocket money was to allow the child to go out with their friends.

However, it should be noted that parents and children have a different view

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of who was the initiator of the rise and also about the specific reason for the rise. Parents believe that the children were the initiators (they constantly asked for something that the parents accepted and then they "made it part of the system").

"Our daughter regularly went to the cinema with her friends, so we increased her pocket money." /#P10/

Children, on the other hand, think that they have only accepted the will of the parents.

"I got it (pocket money) for breakfast from the age of 14. Then, when I turned 16, they increased it so I could go to the cinema with my friends sometimes. … No, I didn't ask for it. My parents decided to increase it. … I didn't bargain over the amount either." /#C10/

If those young people who got pocket money for food/transportation only wanted to spend on something other than the labelled activities, they had to ask for it separately. However, the same issues concern these requests as those already mentioned in relation to those young people who only got pocket money upon request. However, it is extremely important that in cases where parents provided their children with freely disposable pocket money to teach them money management, parents initiated all discussions and were the more active negotiating party.

"It was given to me to learn how to handle money. … They gave me the money and I accepted it. … It was my parents' money. … I thought it was not up to me to decide." /#C21/

In these cases, the parents also see themselves as the initiators and the more active negotiating parties.

"It was us who proposed that he should receive pocket money. … When he (our son) went to university, we increased the amount." /#P21/

In the case of pocket money – because they feel that it is their parents' money – young people play a passive, accepting role, and if parents do not initiate, they do not apply for a regular income that can be spent individually from their parents.

RQ3: How independently and in what ways do children use their pocket money?

Self-sufficiency

By definition, it is not possible to talk about spending independently in the case of young people who do not receive pocket money. It is possible, however, to talk about independently spent money if they receive it for buying meals, although this autonomy can only be interpreted within rather narrow limits. Nonetheless, children enjoyed a high degree of autonomy because, as discussed above, they did not have to face any considerable or severe control, expression of dismay, or retaliation (at most, parents objected to their eating chocolate instead of "proper" meals). Behind this parental practice is a reason similar to the Dutch one, that is, if the child receives little pocket money (and the child spends their pocket money on meals) then, according to the parents' understanding, they cannot spend money on things parents would have to seriously worry about. (The meaning and importance of the words "according to the parents' understanding" cannot be emphasized enough, as unhealthy eating habits have grave consequences in the long run.)

However, based on the above, it would only be possible to talk about purely au-

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tonomous use if the children had been given pocket money in order to make them learn money management. It is actually possible to talk about autonomous use of money if the condition of having to make savings is not taken into consideration. However, this condition does not constitute a significant constraint even if taken into account (and it constitutes no constraint at all in the case of one out of the five young people), since the four young people could eventually, if not immediately, spend their pocket money on whatever they wanted.

Consumption

As mentioned in the section on the purpose of giving the pocket money, the pocket money the children received for buying meals was spent on unhealthy (high in energy but low in nutrition) foods. At the same time, it should be noted that in the case of a higher amount of pocket money, which could be spent on entertainment as well, it was spent almost exclusively on cinema tickets. As a result, only a fraction of the social bonding activities were accompanied by visiting fast food restaurants and consuming unhealthy meals. In addition, the young people asked for extra financial support for these fast food restaurant visits, but the number and proportion of actual visits made was minimal.

"I got pocket money for the snack bar. … It was increased when I turned 16. It was enough to go to the cinema every once in a while. … I had to ask for money for everything else. For buying clothes, for example. … It happened, but very rarely, that I did (I asked for money) so I could go to a fast food restaurant." /#C8/

It should be noted that in the case of children who received pocket money to practice money management, their parents provided the daily meals separately, so they did not have to spend their pocket money on food; but sweets and sugary soft drinks accounted for a significant part of the low-amount purchases. Those who could put aside savings spent them on higher value products (e.g. bicycle, mobile phone). (The one person who did not make any savings spent money on clothes and cosmetics as well as on sweets and soft drinks.)

"I set money aside. I put most of it aside. Then I bought the bike from that. … I bought some things from it (from the pocket money that was not put aside). … Small things. Soft drinks, chocolate… and ice cream in the summer." /#C12/

However, it should be noted that young people did not only spent on themselves, but also bought gifts. Although the purchase of gifts was not carried out using their regular pocket money but from the money they received on special occasions (e.g. birthday, graduation, Easter sprinkling, a gift from the grandparents, etc.), or the financial support requested from the parents specifically for these occasions.

RQ4: Why do children do remunerative work?

With the exception of one athlete and one other person, all respondents worked for money for a longer period of time during their secondary education. For six young people, this extended period of time included regular work during the school year as well, while the others worked only during the summer break. In terms of causes and goals, there is no meaningful difference between working

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during the school year and working during the summer holidays only; therefore, these two types of work are discussed together below.

The motive

Of the 28 young people working during their secondary education, seven began to work as a result of strong parental influence. The cases of these seven people are presented in the Parental Attitudes section.

It is noteworthy that of the 21 young people who started working based on inner motivation, 20 chose to work because they wanted to be financially independent/self-sufficient and no longer wanted to have to ask their parents for money. Nevertheless, it is important to point out that the reason for rejecting subsequent requests for money is not the wish to spare the family budget, but the reluctance and rejection of the act of request. These young people felt that having to make a request (for money) was humiliating for them and they were ashamed to do so.

"Actually, I didn't want to ask for anything. … I wanted to work so I no longer had to ask for anything." /#C1/

"I had to ask for everything. ... I didn't really ask, I didn't spend much. … (I started working) to become independent… so that I could provide for myself and never have to ask again. … It was a bad feeling to ask." /#C7/

The remaining one person of the 21 young people who started to work on their own initiative decided to work for money because they had seen it in their family, had been raised in this spirit, so it was the obvious choice for them.

"(I started to work) because everyone in our family works. … I didn't really think about it. I started to work as soon as I could." /#C19/

It is noteworthy that three of the young people starting work on their own initiative were motivated not only by financial independence, but also by the acquisition of real professional and work experience. (They wanted to experience was it was like to work (for money) at a real workplace.)

"I wanted to try what it was like (working for money). … I went there (to work for the company) to learn." /#C6/

In addition to the foregoing, another significant point is that while a representative CIB Bank study conducted in 2018 among young people completing their secondary education shows that the vast majority of students work or want to work because their parents cannot control the handling of their earnings (CIB, 2018). However, no young respondent in this present study provided such a response. (This suggests that, unlike open scrutiny and accountability, concealed control – as seen in the Dutch example – is not perceived by young people as a serious violation of their autonomy.)

Use of labour income

The use of the income of the seven young people who started working under strong parental influence is presented in the Parenting attitude section. Of the 21 young people who started to work as a result of inner motivation, one did not use their income at all, but saved the whole amount and added it to the savings that were started from the pocket money they received for learning money management.

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"I did not buy anything from it (the labour income). I didn't have to. … If I did save money anyway, I added it (the labour income) to my savings." /#C17/

When planning the use of labour income, the other 20 young people who started to work on their own initiative aimed for the acquisition of some specific products and/or services. It is worth noting that four people deliberately divided their income into three parts: they set aside the greatest part of it for buying an apartment, a smaller but significant amount for holidays/festivals and only up to 5-10% to meet their – almost – immediate needs (e.g. buying necessary clothing).

"I set aside almost all of it (my income from work). … For the apartment. It was at least half of it (of my income), perhaps more. At that time, we used to go to festivals with my friends. I saved some money for that, too, usually from what was left (after I set aside money for housing). … I didn't really spend it on shopping. Only when I really needed something. Like new shoes, for example. Then I bought them. … I didn't spend much even then, though. The tenth of my income, at most." /#C4/

Concerning products: There were three people who wanted to buy information communication devices (e.g. mobile phone, notebook, etc.).

"I saved money for buying a laptop. I worked all through the summer for a laptop." /#C21/

Another nine people planned for a significantly longer time span than the three mentioned above and set a much larger, more ambitious spending target: they wanted to buy a car and/or apartment from their income.

"I didn't spend on anything. I set it aside (my income from work). … For a car and an apartment." /#C3/

"I wanted a car. A car of my own." /#C16/

Concerning services: eight young people mentioned especially short-term savings, as they spent their earned income on vacations/festivals during the summer they earned it.

"I did physical work. I did everything just to be able to go with my friends (to a festival)." /#C1/

"I spent it (my income) on vacation. … I was at a festival." /#C30/

Two young people were consciously working during their secondary education to earn their tertiary education fees.

"The school required a tuition fee, and I knew my parents wouldn't pay it." /#C7/

"I heard that rent prices were awful (in Budapest). … I didn't know back then that I would be admitted to a dormitory." /#C26/

It is important to point out that young people who set financial goals requiring a significant amount of money did not realise (and were not aware even at the time of the interview) that the ambitious plans they had and the resources available to implement them were not compatible with each other. For instance, it would have taken at least a decade to collect the necessary downpayment for buying an apartment from their savings. (The vast majority of the respondents were not in a significantly better financial situation even at the time of the survey.)

RQ5: What is parents' attitude to children's remunerative employment and why?

The parents of the aforementioned athlete supported their child's athletic

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career in every way they could – with the exception of pocket money. In addition, since he was not in remunerative employment at the time of his secondary education, his mother did not express her views on the possible employment of her child in her replies. However, the parents of 28 young people who worked during their secondary education gave clear answers to research question number 5. Eight of them had an unfavourable opinion of their children's employment.

"We didn't want him to work. We wanted him to focus on his studies. That's why we gave him pocket money." /#P3/

However, the vehemence of their opposition was insufficient to prevent their children from working. All the young people interviewed worked whenever they wanted and had the opportunity.

"They (my parents) were not happy about it (me working). … They told me that… but nothing more." /#C3/

Another 13 parents approved that their children worked and they let them do so. (In all cases, when the work took place during the summer holidays, parents were "neutral in a good way".) Furthermore, the parents whose children wanted to continue work during the school year set the condition of performing well at school.

"We agreed with him (our son) that he could work as long as it was not at the expense of his good school performance." /#P23/

Nevertheless, it is strongly questionable how seriously these conditions were taken: the overwhelming majority of the parents were in fact content and supportive of their children's employment.

"It was well received (by my parents) that I was going to work. I think they were actually happy about it. … Yes, there was a condition (for me to having a job). They said (my parents) that my grades could not deteriorate. … I don't know what they would have done because my grades didn't get worse... but I think they would have let me work anyway." /#C23/

The remaining seven parents pressed their children to work. Five of them clearly expected their children to work in order to help the family and contribute to the family budget. (The children had to do the work their parents undertook on their behalf.)

"We wanted it (our son to work) so that he could pay for his spending. At least for the phone and for the internet." /#P13/

"We asked her (our daughter) to help (the family). For example, we asked her to do newspaper delivery (weekly)." /#P28/

"We told our son to work and earn the money he could spend and so he didn't have to ask from us." /#P15/

In these cases, the expenditure structure of these young people also supports the family budget by significantly reducing the family expenses generated by the young people (they paid for – almost – all of their expenses) and/or by increasing the family income (contributing a significant part of their income to the family budget).

Nevertheless, it is important to note that these young people did not express any negative opinion in their responses concerning the work they did on parental influence. Under the circumstances prevailing at the time of the interview, they accepted and agreed with the fact that they were in remunerative employment

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and acknowledged that it was congruent with their own will.

"They (my parents) told me to work, but I wanted to help them (my family) anyway. … I paid for everything. … And I brought home some grocery money." /#C13/

It is noteworthy that in the remaining two parents' intention to urge their children to work was not having them to contribute to the improvement of the financial situation of the family, but to teach them to take responsibility.

"We wanted him (our son) to work so that he learned to take responsibility." /#P5/

It is important to note that in these cases, as the expenses of the young people were still covered by the parents, the children generated additional income, and they did not spend it but saved it in its entirety.

Conclusions and future research directions

The present research contributes to the examination of the role of young people in the process of becoming independent consumers through parental involvement in an empirical way. In this context, the research examines the purpose and role of the children's income of this certain type, and also the cause of choosing that particular purpose and role. The research also examines how, under what conditions the children want to obtain their independently disposable income, why they wish to do so and what they spend it on.

In doing so, the research lays particular emphasis on exploring the link between young people's independent income and the food they consume.

This study uses a qualitative research method and a relatively small sample, so the limitations of this approach should be taken into account when utilising the research findings.

It can be stated that the vast majority of the parents who provide their children with pocket money do not exactly intend to support long-term goals for their children (e.g. learning money management); they rather intend to make their (private) life easier in the short run (e.g. giving pocket money instead of buying / making breakfast, giving pocket money for housework / good grades).

In addition, parents – even though not (completely) consciously – use covert control, that is, they provide little pocket money (and limit its possible usage to buying meals, for example), so their children have to require further support for their spending. (This procedure does not seem to impose a significant burden on the parent-child relationship, as young people do not perceive covert control and accountability as a major violation of their autonomy.) It is important to point out that young people reject having to make further requests for money. Moreover, this rejection is not based on the intention of saving of the family budget, but on the aversion and rejection of the act of requesting. The young people felt humiliated by having to make requests (for money) and were ashamed to do so, and that is the primary reason why they decided to pursue a job with a salary.

It is important to note that the examination of the practice of parental control highlighted that parents are aware that the pocket money children spend on meals is used to buy less healthy food

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(high in energy but low in nutritional value), however, they do not take steps to make their children spend money on healthier meals.

As a result, it seems that parents may not be actually aware of healthy/unhealthy foods and it is the task of the education system to counterbalance the negative effects of this situation. However, the knowledge about healthy foods itself has no significant impact on healthy eating habits (Inhulsen et al., 2017), so projects with experience-based learning are needed. The project called *Expanded Food and Nutrition Education Program / Supplemetal Nutrition Education Program – Education* has been created in the USA for this reason. This project not only teaches students between the ages of 14 and 18 to cook cheap, easy-to-make and healthy meals and to make daily meal plans, but also involves the friends of their students so they can share their experiences (Price et al., 2017). This is particularly important because the project can provide an opportunity for bonding with friends and this way it could substitute visits to fast-food restaurants and eating junk food.

Last, but not least, due to the limitation of this survey, it is important to quantify and examine the surveyed questions representatively for the complete Hungarian youth in the Carpathian Basin. As this survey leads to the conclusion that Hungarian parents use allowance similarly to the Dutch (providing a small amount of income for limited use), the series of surveys should include the questions of the international study that describes the Dutch situation and provides tangible comparability. As such, the series of surveys should determine the amount of money parents actually give to children, its conditions and purpose, and the kinds of direct and indirect monitoring parents apply.

What is more, the surveys should also cover the actual sources of income young people have, the amount of these incomes from each source, the purpose they use it for (whether they deposit or use the money), the method of saving, and the manner and purpose of spending the money. Besides, the surveys should strongly focus on the amount young people spend on food, the kinds of food they buy, and the occasions and circumstances that lead to the purchase and consumption of the mentioned products.

The descriptive series of surveys, as the cultural and economic effects on Hungarians within and outside country borders are significant, should be representative of young Hungarians in the entire Carpathian Basin. This requires a stratified sampling would be needed, where the strata factors would be the 17 to 25-year-olds' regional and education level distribution.

Such a descriptive series of surveys would enable both parents and public health professionals to take the necessary steps for improving children's health based on an accurate picture presented from the findings.

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Areas of Improvement in Hungarian SMEs Competitiveness – Corporate Financial Literacy in Focus

Summary

The 2007–2008 global financial crisis exposed the problems arising from systemic risk management on a micro- and a macro-economic level. This period was particularly challenging for the entire economic system of individual countries, including all the participants of economy. Post-crisis changes require appropriate awareness and financial determination and an adequate level of financial literacy of market operators. When it comes to financial literacy, innovation should be mentioned, since the parallel development of these two factors has a favourable impact on economic stability and on the competitiveness of a country. Overall, the level of financial literacy and the capacity for innovation have an influence on the stability, growth potential and competitiveness of enterprises and of the entire national economy. Therefore, improving financial literacy is in priority national interest, and as such, it must be at the centre of attention at all times.

Journal of Economic Literature (JEL) codes: O11, O44, G41

Keywords: global financial crisis, financial literacy, competitiveness, company

Introduction

In the past decade economic operators, future entrepreneurs and economic experts have still kept referring to the crisis, its long-lasting effects and they take it into consideration how much change the 2007 crisis brought in both the world

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economy and Europe. The global financial crisis hit Hungary hard, due among others to inappropriate state operation, which created a poor incentive scheme (Kolozsi et al., 2017). Hungary was unprepared for such a large-scale crisis. In his book, Bod (2018) describes the phenomenon as follows: "Then the 2008 autumn crisis struck Europe, and Hungary was particularly hard hit. The next young generation's social conditioning was radically changed: today's university students have grown up learning about the world always in the context of some kind of a crisis…" The same is emphasised in a 2012 book by Gary B. Gorton's, who points out that when the financial crisis broke out, the majority of economists were caught off guard and were not prepared for it. Gorton (2012) also adds that "the personal experience of an event is not substituted by reading or studying about it. If someone was a witness in some form of the 2007–2008 panic or experienced the negative consequences of that, then that person will think about financial crises in a different way than a person who met that only as a dry, historical data set".

The 2008 crisis shed light on the fact that the economic operators need to change in order to avoid economic recession of such a grand scale in the future. The key to change may be changing the financial behaviour, which plays a key role in improving a country's competitiveness (Lentner, 2019). From the point of view of corporate growth and competitiveness, it is indispensable to have stable economic policies, as they help develop a business-friendly environment. Its creation requires close cooperation between those in charge of fiscal and monetary policies – and this criterion has been even more significant since the 2007–2008 crisis (Lentner, 2017) –, and education, the tax environment and the healthcare system have a significant role in it (Lentner, 2007a; 2007b; 2015).

In order to achieve the above goals, that is, a paradigm shift in financial behaviour, the following tasks are seen as priorities:

– Drawing the attention of businesses to the fact that they need knowledge appropriate for the fast-paced and turbulent development in the financial and business environment, and an innovation-driven way of thinking;

– Encouraging businesses to mainstream the need for identifying, mitigating and diversifying risks in operations at all times, alongside pursuing financial results;

– Raise businesses' awareness of the key role that capital structure optimisation plays in their effective operation;

– Point out that the inappropriate understanding of financial transactions and the absence of financial (expert) knowledge have a adverse effect on corporate profitability, can undermine efficiency and significantly hinder company growth and investment decisions.

In addition, the present study also aims at describing the links between competitiveness and financial literacy, emphasising the positive effects of financial awareness on macro-economy. Particular attention is drawn to innovation as a factor in competitiveness. It is relevant to note here that instead of providing a theoretical literature review, the study is built on timely information and the authors' personal opinion.

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Preconditions for improved competitiveness

Improving competitiveness in the Hungarian economy is a prioritised strategic objective, which can be viewed in micro- and macro-economic terms. In meeting this key government objective, the sector of Hungarian-owned small and medium enterprises (SME sector) plays a pivotal role. Given that the Hungarian SME sector has an economic performance stabilising and balancing role, its extensive support may be one of the keys to the future. Uninterrupted development in this sector, improving financial literacy, and supporting adaptation to changes in the external environment in a broad sense are of major importance. An area of primary concern is helping SMEs carry out production and/or service provision at the highest possible standard in order to provide high added value. Under the current circumstances, perhaps one of the most prominent factors of competitiveness is the added value a business can generate, as this is what enables economic operators to enter Hungarian and EU supplier – and supply – chains. Furthermore, productivity, efficiency, financial awareness, and the economic operators' competence in updating and developing them in accordance with the technical and social requirements of the age, are also considered as economic competitiveness criteria. Change in only one component does not suffice, and increased unilateral focus on certain elements may prove to be a double-edged sword: productivity can only be improved if interactions among the factors are taken into account. A good example is the recent increase in Hungary the quantitative macro-economic indicators (such as employment, GDP, government debt, unemployment, investments, etc.) unaccompanied by improvement in efficiency, awareness and institutional factors, which results in barely any change in the Global Competitiveness Index.

An additional competitiveness factor is high growth over a sustained period, conditional upon the following:[1]

– Open economies that are integral parts of the world economy (having competitive, and efficient exports, which significantly contribute to GDP growth, high ability to raise and allocate capital, positive external and current account balances that can keep debt levels in control);

– Macro-economic stability (balanced and sustainable growth over the long term, relatively low debt levels and relatively low unemployment rates);

– Low levels of external and internal debt (without the risk of the so called twin deficit, which is hard and painful to handle);

– A high rate of household savings (which, alongside growth, has a beneficial effect on state self-financing, in other words, stability, and thus reduces the external exposure and vulnerability of the country);

– A high investment rate (fundamentally based on domestic sources and on relatively high household savings);

– Market-based resource allocation (with the state having a key role in setting strategic goals, the development of relevant and appropriate regulating systems. Using a sports metaphor: the strict rules of football are established by a central regulator, but on the field every team plays and competes to its best knowledge, in accordance with the rules);

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– A flexible labour market (i.e. the speed of returning to the long-term equilibrium trend determined by wages and by the workforce, see Pula, 2005);

– Clearly defined public goods (which, depending on the relative level of development, provide the individuals with social security and growth opportunities, and therefore the individuals more easily identify with central decisions. Community investments and their development play a vital role in guaranteeing these services – the priority areas of community investment are infrastructure, education and research).;

– Credible, transparent, highly professional and low-cost governance;

– An optimum and competitive tax system (which aims at efficiency, simplicity and fairness, and helps growth by minimising the tax burden, but at the same time providing the necessary state revenues);

– Conscious corporate culture with a high level of financial literacy.

However, a significant improvement in competitiveness and the retention of the current favourable economic growth rate pose serious challenges to the sector:

1. Digital transformation in the current economic and social systems. More precisely, businesses that aim to retain their favourable competitive position need change in several areas concerning the undertaking (such as procurement, sales, logistics and transport, CRM systems, corporate management systems, etc.). Basically they have to come up with a partially or totally new business model to help stabilise and improve their competitiveness.

2. This is all closely related to a continued need for innovation, which can partly be traced back to a fast change in consumer habits. Innovative activities require awareness, focus on the future and on performance, financial and human resources from entrepreneurs.

3. The absence of appropriate human resources hinders growth. The company needs to be able to attract professionals capable of responding to modern requirements. But employee retention, motivation and improvement are perhaps even more important. Certainly, this needs to be manifested on the strategic level; without it the company suffers mid- and long-term competitive disadvantage.

The current Hungarian labour market could be briefly described as a tight labour market. According to the latest report by the Hungarian Statistical Office (HCSO), in July and August 2019, the average number of unemployed was 157 thousand, accounting for a 3.4%, still a record low. Over the past few years the unemployment rate has been continually decreasing due to certain government measures, to a favourable business environment and to world market processes. However, the current labour market reserves are hard to restructure, which also means that unemployment may only decrease slowly. Lately, an increasing number of analysts and company leaders have communicated that the Hungarian labour market has reached its quantitative limits, and so there is labour shortage in several areas. Clearly, the number of jobs which require specialist expertise and experience is increasing (as a trend on the way towards a knowledge-based society). The trend is that a less employable and often totally unskilled labour force is available – which evidently raises the importance of education. Although this

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should be handled on state (policy) level, at a micro-economic level, businesses also play a key role in this process.

In today's turbulently changing business environment, due to the increasingly shortage in professionals, the retention of talented employees has become one of the focal issues in corporate strategy. A growing number of employees find it important to constantly learn something new, which also means that employers need to meet these employee requirements. Based on company reports, labour migration causes problems for companies and forces them to constantly monitor its minimisation. In our understanding, a plausible way of reducing turnover is offering employees different professional training opportunities. Firstly, they improve employee efficiency (thus complex corporate productivity might improve), and increase their recognition and wages. Corporate practice shows that employees feel valued at a workplace when their company promotes their personal development. As special training courses unequivocally contribute to strengthening corporate culture, a well-designed human resource development strategy may bring a plethora of benefits for businesses.

4. Generation handover and succession mainly cause problems in the case of family businesses. As the majority of these enterprises were founded after the change of regime in Hungary, most of the founders have reached the retirement age. A Budapest Business School's Budapest LAB – Entrepreneurship Centre research has revealed that based on data from founders, in slightly less than a third of the businesses there is no one to pass the assets or leadership to, which means that after the founders have retired, the company will most likely cease to exist (Heidrich, 2018). Moreover, having successors does not guarantee a successful owner/management handover. Two thirds of family businesses do not survive it (Konczosné Szombathelyi and Kézai, 2018). This can have serious consequences on the national economy and so this is a cardinal question that affects Hungary's future corporate structure and economic performance. Choosing the right successor, experience and passing down company-specific knowledge can have a significant effect on the future performance of today's businesses. Consequently, the targeted and controlled management of this topic is vital. Nevertheless, when family transfer is not viable, selling the company could be the reasonable option. In this case, the source of funding can come from the Hungarian Development Bank's Generation Change Venture Capital Program, which aims to help financing business takeover and intensify the Hungarian SME sector's M&A activity through its resource support venture capital program.[2]

5. Based on international experience, businesses – and national economies – integrated into global supply chains and producing or providing services to the export market are more competitive, effective and financially stable. As the Hungarian market is small, proactively seeking export should become the standard for Hungarian businesses. This needs to be supported and encouraged, since businesses present on the export market are more likely to generate higher AV, which entails employing highly qualified professionals. Knowledge is a competitiveness factor, and Hungary has to aim at becom-

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ing a knowledge- and innovation-based economy in a short time.

Domestic businesses require a paradigm shift in order to find the untapped potential in foreign markets. There is a large number of prospering Hungarian-owned companies in the market, which, in the absence of appropriate motivation and incentive, have not opened towards foreign markets. We assume that a stable economic policy, the increasing entrepreneur-friendly business environment and the targeted government measures will give Hungarian businesses the right incentive to expand to the export market. It should also be highlighted that today the business world is also undergoing a digital transformation, but only a fraction of entrepreneurs are looking for ways of meeting the challenges of the 21st century. Innovation, proactive strategies, high added value and expertise can help Hungarian companies achieve significant growth in an international comparison.

It is common knowledge that companies active in international processes beyond the Hungarian market operate more effectively and efficiently. However, to become a supplier, or potentially appear in the export market, a company needs to be efficient, profitable, and capable of creating value and learning, all at the same time. In addition, it needs an appropriate and up-to-date technology for increasing productivity (Vakhal and Palócz, 2018) and optimising their economic position. Moreover, it is essential that they have pro-active company leaders who are open to the challenges of the new environment, and can integrate these technologies and innovative solutions efficiently into their everyday activities.

It is often mentioned that the economy benefits from the ongoing weakening of the Hungarian forint as it stimulates export and requires increase in the number of jobs; thus contributing to growth and eventually improving competitiveness. However, it should be noted that it stems from international economic developments (Brexit, the trade war, the new stimulus package of the European Central Bank, the slowing German industrial growth and unfavourable developments in the German car industry; other international processes such as slowdown in the world economy, the new European Parliament and European Commission, the new EU programming period, the U.S. presidential elections, the ailing economy in the euro area, the oil market situation etc.). In relation to exports it is always worth examining the import demand for the exported goods (given that a low exchange rate increases the cost of import), since it has a considerable effect on the final outcome. Secondly, businesses should not make the exchange rate their main motivation for export activities. Instead, they should be encouraged to constantly have products and/or services that – irrespective of the current exchange rate – are in demand in the international market.

6. Corporate competitiveness is also influenced by both financial literacy and business culture. For this reason their improvement should be considered highly significant, since responsible decisions can only be made in possession of adequate quality information in sufficient quantity. The ultimate goal is to raise the Hungarian business sector among the best in an international comparison

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in terms of financial awareness within a short period of time.

7. Another constraint is the low productivity of the Hungarian SME sector. It should be emphasised though that this can be viewed as a considerable potential for growth in the Hungarian economy. Taking a closer look at the productivity of the sector, its importance is clear from the fact that although the sector gives around 73% of employment, it only generates 50% of GDP, and Hungarian SMEs only contribute 20% to exports. Moreover, the productivity of an average Hungarian small and medium enterprise is one third of that of large companies. In Hungary the productivity of large multinational companies is more than one and a half times the domestic average, while the corresponding data for almost fully Hungarian-owned small enterprises employing less than 9 people, dominating the Hungarian economy, is half the domestic average, and micro-businesses employing 1 person are even less productive. The difference in productivity can be multiple (3-4 times). It should be noted that in Europe Hungary has the largest productivity gap between large companies and SMEs. The productivity problems encountered by the large number of SMEs are manifest in the following comparative data: the ratio of SMEs to the total number of businesses and the ratio of the people employed by them to the total employment are nearly the same in the European Union and in Hungary. However, on the average of the EU, SMEs generate 56% of added value, while in Hungary the corresponding contribution is only about 40%. SMEs give 56% of the net turnover in the European Union, compared to 42% in Hungary. They contribute more than 50% of the total export in the EU; and slightly more than 20% of exports and less than 10% of innovation in Hungary. More than 40% of the EU investments come from SMEs, in Hungary only 30%. In addition to the above, it is quite telling that the average added value of Hungarian SMEs does not reach the half of the EU average. The productivity of a German micro enterprise is at least four times that of a similar Hungarian company. Even in a V4 comparison, Hungary is at the bottom: its SME productivity is 10% lower than in V4 countries.

This suggests that interventions are required. It is also confirmed by the fact that improving SME productivity is a major part of the National Bank of Hungary's (MNB) competitiveness programme. According to an MNB study, a 6% annual growth may halve the productivity gap between SMEs and large companies by 2030. Improved productivity can be achieved, among others, by improving technological skills and abilities, increasing innovative activity and raising the qualifications of the human capital. Immediate action is needed in this area, because if sector productivity reaches the regional average and moves closer to that of large companies, gross domestic product would increase by 3-5% (based on MNB calculations).

It is worth considering another factor related to productivity. Economic growth and the prosperity of enterprises in Hungary are also significantly influenced by the available workforce (see above). It is clear today that all this cannot be achieved by low wages. On the contrary, low wages often hinder productivity (given the fluctuation due to the wage pressure).

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Aims in improving financial literacy

Under today's globalised and turbulent world economic conditions, economic operators increasingly emphasise management systems principally comprising information that supports financial decision-making, planning, strategy-making and investment structure development. To develop their vision of the future and their strategy, and to define actual objectives and tasks, businesses heavily rely on internal financial and funding perspectives (Zéman, 1997, 2019; Kaplan and Cooper, 2001), and the quality and predictability of their relations (Reszegi and Juhász, 2014, pp. 47–59). However, it should be remembered that these activities constantly change and require uninterrupted "movement and activity" on the part of the management. In his new book Professor Paul Dembinski (2018) claims that "the operation of the financial world has fundamentally changed. Therefore, the aim of achieving financial results, which measures the world according to the coordinate system of risk and gain, does not solely define the financial sector any more. Not only has it become part of the corporate world, but it also influences economy and the lives of individuals. This process, often called financialisation, has exposed increasing areas of society to the logic of financial paradigm". In other words, financial matters are omnipresent and omnipotent. The turbulent change of financial complexity requires financial literacy and know-how from decision-makers. Financial ethics and/or culture play an important part in this (Grifoni and Messy, 2012). Both Hungarian and international research dealing with the analysis of financial literacy usually primarily focuses on the complexity of financial literacy of the citizens (households). However, financial literacy does not only cover citizens' skills and awareness, but also those of businesses, due to their corporate social responsibility (Lentner, 2017), which may define the atmosector and position of the whole society and national economy (Atkinson and Messy, 2012).

Continuous improvement in financial literacy is an increasingly frequent objective of national economies, including Hungary, where the 2017 Strategy for Improving Financial Awareness outlines the specific aims and the related action plans and provides frameworks for improving the financial awareness of people, as the standard and quality of financial literacy is in the common interest of all economic operators (Tebeli, 2018). Over the past few years, several international scientific studies (Johnson and Sherraden, 2007; Klapper et al., 2012; Suganya et al., 2013) have shown that improving financial literacy is not only in the interest of households and businesses, but also that of the state, since those national economies which have a higher standard of financial literacy, also have a better competitive – therefore on international competitiveness rankings a higher – position (Tóth et al., 2018). It is also important to highlight that households and economic operators having a higher financial literacy standard are more likely to avoid disadvantageous financial decisions and make such economic – and financial – decisions which have a positive effect on the entirety of corporate operations. This all indirectly contributes to the stability of the financial system in a given country; and to an increase in government revenues by

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means of strengthening tax awareness, a part of financial literacy (Sinkáné, 2018). The above suggests that the financial awareness of individuals cannot be fully separated from company leaders' awareness – it is worth examining them together. To sum up, in Hungary stable sustainable economic growth and improved competitiveness call for financially aware people and businesses with extensive and up-to-date knowledge.

To this end, a financially aware entrepreneurial circle needs to be educated, potentially opening the horizons for stable operations in the Hungarian economy on a macro-economic and a national economic level. In this regard, the following factors are emphasised:

– Businesses need conscious planning to develop financial strategies that fully serve corporate stability and increase performance. In today's globalised and turbulent world economy, economic operators need to put increasing emphasis on applying management systems that principally comprise information that supports financial decision-making and thus facilitate planning, strategy-making and investment structure development.

– It is common knowledge that external financial sources and loans granted by financial institutions play a key role in corporate growth. However, businesses need to use them more carefully and considerately, and most importantly, with increased awareness.

– We are witnessing the birth of an innovative ecosystem, which also calls for a change by business actors. The innovative solutions that can significantly improve Hungarian corporate effectiveness and efficiency should be applied and integrated with increased awareness. Innovative solutions are also of paramount importance.

– Companies need to pay special attention to one of the most important resources: the human capital. Investment in human resources, constant training and professional renewal may also serve as a defence mechanism in the life of every business, and also as a competitiveness factor.

– Finally, it is worth mentioning the importance of corporate culture, to be developed by every company on its own. This is what brings employees together, strengthens the sense of togetherness, which in turn makes it possible to react to unexpected events in close cooperation.

Improvement in financial literacy must be made a major factor, since economic operators can only make responsible decisions in possession of a sufficient quantity and quality of information. Such decision is, among others, the decision about corporate capital structure, which alongside effective, economical and efficient operation is one of the keys to stability, liquidity, profitability and corporate competitiveness. In their study Győri and Czakó (2019) show that "the mortality rate of SMEs is high, which is partly attributed to SME leaders' low level of financial literacy" (Bosma and Harding, 2006). This has an adverse effect on the assessment and understanding of different funding opportunities, and leads to poor financial decisions, loss or even failure (Joo and Grable, 2011). In the case of a potential recession, to ensure rapid reaction and efficient recovery, formally or informally, and in various depths, every single company should be forward-looking in terms of their management of finances (as

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well) and consciously plan its finances, including capital structure. This train of thought is confirmed by Szóka (2008), who said that today efficient corporate financial management is a necessity, since the proper regulation of liquidity, sound investment and financing decisions can help strengthen a company's financial, profitability and market position, and ensure its effective operation and longevity. Bad financing decisions can have serious – even fatal – consequences. Nevertheless, for companies to be enabled to make appropriate plans about finances, financing, including the ones about capital structure, a high standard of financial literacy is needed, given that developing the financing structure, determining the proportion of financing sources is one of the most difficult professional tasks (Gyulai, 2013). More precisely, after calculating the resource requirements and taking into account a combination of several factors (such as the type of the project/investment to be financed, loan interest rates, risks, the business size, the corporate lifecycle and the economic environment), the resource should be chosen, and the right proportion of the sources should be determined to make it the most fitting possible for the company. This must be coordinated with the general corporate strategy, as operative decisions also represent the implementation, and when required, improvement and modification of the strategy (Sinkovics, 2010, pp. 132–133). The situation is further complicated by the fact that for every objective to be achieved, different proportions are optimal, and the optimum 'mix' is subject to changes in the external, economic and legal environment. Owners need to take the effects of all decisions of economic nature into consideration with the aim of providing distributing sources efficiently so that they have a beneficial effect on the financial situation of the company (Túróczi, 2014; Katits, 2002). Moreover, the soundness of financial and management decisions (professional formal knowledge) improves the chances of innovativeness (Győri and Czakó, 2019).

Major institutions and programmes participating in Hungarian financial literacy improvement

Improving financial literacy is in the common interest of all economic operators in the public and business sectors alike. Today, financial literacy development is also a headline target in Hungary.

Government

These thoughts are confirmed by the increasingly frequent government communication that the incumbent governments need to support the population in making informed financial decisions. It should be stressed that the Ministry for the National Economy has developed a comprehensive national strategy for improving people's financial awareness, which includes long-term, extensive financial literacy developments that are in line with economic policy objectives. This is important because decisions that have several financial implications are made on a daily basis. To create a well-functioning economic, social and political system, consumers with a high-standard financial literacy are a prerequisite. The government strategy aims to create a genuine opportunity for financial education with-

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in the framework of public education, with a view to strengthening responsible financial behaviour and household financial resilience.

The National Bank of Hungary (MNB)

Following the 2008 financial crisis public confidence in financial institutions had to be restored and wazs had to be found for banks to better serve sustainable social and economic development (Lentner et al., 2015). The answer lies in the corporate social responsibility of institutions. Therefore, among others, the MNB set the objective of becoming an institution that is capable of responding appropriately to the latest economic and financial crisis. The Governor of the MNB says that the entire society needs an adequate level of financial literacy, and "money must be managed wisely". According to György Matolcsy, financial literacy improvement is a competitiveness factor. There is a close link between the high standard of financial literacy and the level of economic development; a low level of financial and economic literacy endangers the stability of the financial system as well. Improving financial literacy and developing a competitive education in economics serve as important bases for social development and convergence in Hungary. Thus the management of the MNB decided to create the Pallas Athena Public Thinking Programme, which aims at renewing the training of economists and economic thinking. A series of economic and monetary policy books were launched by Governor György Matolcsy in 2015, which not only contribute to the renewal of Hungarian financial literacy and economic thinking but also to a collective thinking about major economic policy areas. The volumes published so far help shape the training of economists (from bachelor to doctoral levels). The MNB has also developed efficient cooperation with several universities. In the spirit of cooperation, the MNB has entered into partnership with the Corvinus University of Budapest, and founded a separate and well-functioning MNB Department at the university.

Money7

The Money7 programme 2015–2016 was launched by the Hungarian Banking Association and the Money Compass Foundation for Financial Awareness (*Pénzirányt*ű *Alapítvány*). In the 2017–2018 academic year the programme was extended with the help of the Ministry of National Economy, and in the next academic year the Ministry of Finance and the Ministry for Innovation and Technology also joined the partnership. The programme aims at helping financially-minded students to improve their knowledge.

Hungarian Chamber of Commerce and Industry's National Entrepreneurship Mentor Programme

The financial awareness sub-project mainly targets companies registered in Hungary that fall into the category of micro-, small and medium enterprises. The programme offers complex awareness-raising with special focus on the human factor and multidimensional education. Within the frameworks of financial and entrepreneurial awareness raising, tradi-

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tional business areas have been identified that contribute to effective and efficient business operation. The modules included in the programme are basic financial and business skills, complex financial management skills, and the corporate financing module built on these, which encompasses both the external and internal elements of financing, as well as the special cases of financing.

OTP's Fáy András Foundation

OTP Bank's Fáy András Foundation was set up in 1992. In the beginning it served as a patron supporting young people in their career choices and focused on teaching adult life skills. Later on, in the spirit of improving financial literacy, it set the objective of improving students' financial and economic literacy, and then, to enhance results, it also took up teachers' training. In order to achieve these objectives, the foundation has launched its Basic Programme student and adult courses, a career orientation and advice website, provides online counselling and takes part in exhibitions and festivals. To promote sciences and scientific work, in October 2010 the Knowledge Upload Programme, the related website and the "Days of Knowledge" Programme were launched. The Model School Project has been running since 2011, with focus on financial education, economic and management know-how and future-orientation.[3]

Final thoughts in the light of alliance

The programmes run by the Hungarian Government, the National Bank of Hungary and the Hungarian Chamber of Commerce and Industry are the most significant ones in improving financial literacy. It is welcome that the specific programmes are not competing; instead, they are complementary. This cooperation is necessary to achieve economic growth and social development in Hungary. A source of the economic success is that economic and monetary policy, as well as the Hungarian Chamber of Commerce and Industry representing businesses are able to meet current economic challenges in cooperation and also to create the opportunities and the tools for improvement – among others, in improving financial awareness. According to Patai et al. (2019) the key to success is that economy, education, research and development and additional sources cooperate effectively and efficiently to make Hungary the winner of the day after tomorrow.

In addition to the above, it is clear that one of the largest reserves of the Hungarian economy lies in the financial world. This field should be prioritised and the resources provided by specific institutions allocated. This is has been proven in practice, since one of the key areas in economic policy today is capital market development; that is, giving the corporate bond market the chance to succeed.

Notes

1 Based on Dr Mária Findrik's personal opinion, complemented by the authors.

2 www.mfb.hu/vallalkozasok/mukodo/tokebefektetesek/mfb-generaciovaltasi-tokeprogram-t121-p121.

3 www.otpfayalapitvany.hu/otp_fay_andras_alapitvany.

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