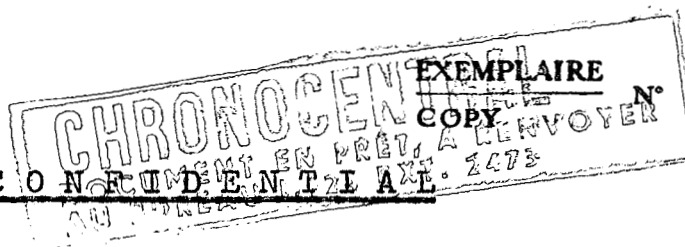


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ECONOMIC COMMITTEE

EASTERN COUNTRIES ECONOMIC REVIEW

HUNGARY: THE ECONOMIC SITUATION AND FOREIGN TRADE

Note by the United Kingdom Delegation

PART I - SUMMARY

The last two years have seen a considerable modification in the New Economic Mechanism (NEM), involving a reassertion of central authority particularly in such matters as investment, prices and earnings. Very considerable progress towards greater economic stability was made during 1972-1973; 1972's gross industrial production plan was fulfilled and that of 1973 exceeded; the shift to a more modern industrial structure continued. The agricultural sector has benefited considerably from the NEM - gross output rose even more markedly in 1973 than in 1972. (Paragraphs 2 to 7.)

2. Foreign trade is particularly important to Hungary. Enterprises still retain the measure of freedom, albeit within tightly controlled limits, given under the NEM in the conduct of overseas trade but concerted efforts by the Government were needed to rectify the record trade deficit of 1971. Exports to both Communist and non-Communist areas in 1972 rose dramatically while imports declined giving a surplus on visible trade with the Communist countries and a much reduced deficit with the West. In the first nine months of 1973 total exports continued to grow markedly, while imports began to expand again; Hungary maintained her surplus on overall trade and on her trade with the Communist countries, but her deficit with the West continued. No significant changes in the commodity pattern of trade in 1972 and 1973 have been noted. (Paragraphs 8 to 12.)

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3. Communist countries continue to account for slightly over two-thirds of Hungary's foreign trade. Her leading Western trade partners are (in order) West Germany, Italy, Austria, the United Kingdom, Switzerland and France; Hungary's trade with the EEC has been expanding considerably more rapidly than that with non-EEC countries and the share of non-agricultural products in her exports to the Community has increased. Trade with the developing countries is making very slow progress. (Paragraphs 13 to 16.)

4. Hungary's recurrent deficit on trade with the multilateral partners is financed by credits and, more important, by loans from Western money markets. Hungary's outstanding debt to NATO countries by mid-1972 represented only about 6% of the total outstanding to the whole of Eastern Europe. She has raised about \$380 million through loans and bond issues on the euro-currency market. (Paragraphs 17 to 20.)

5. Hungary is the most active practitioner in Eastern Europe of industrial co-operation with Western companies as a method of importing sophisticated technology and equipment with a minimum expenditure of convertible currency. 240 such agreements have been signed, mainly involving the engineering industry and the importance attached to this form of co-operation is likely to be even more pronounced in the future. A law permitting foreign investment up to a 49% holding has been passed, but it is most unlikely that Western investment will be allowed on the scale found in Yugoslavia. (Paragraphs 21 to 23.)

6. Economic targets for 1974 are lower than the results achieved last year; the substantial increase in investment planned should have an invigorating effect on the economy. The stringent regulation of the foreign exchange component of investment makes any substantial increase in imports from the developed West unlikely. Hungary's future oil supply situation is somewhat uncertain - the USSR is unlikely to meet all her requirements so that significant quantities of Middle East oil will be required; work on the Hungarian section of the pipeline to the Adriatic (through Yugoslavia) is to start in 1974. (Paragraphs 24 to 26.)

PART II - MAIN REPORT

1. The object of this paper is to review briefly the recent progress of the Hungarian economy, in particular assessing the effects of the modifications made in the reform programme since late-1971. Some of the distortions in the economy which resulted from the reforms (particularly excessive enterprise investment) affected the foreign trade situation adversely and the Government stepped in to correct matters. The second half of the report examines Hungary's foreign trade performance in 1972 and 1973, its financing, the progress of industrial co-operation agreements and prospects up to 1975.

THE ECONOMY

Introduction

2. The Hungarian economy has now been operating for six years under the economic reform programme, introduced as the New Economic Mechanism (NEM) in 1968. The last two years, however, have seen a considerable modification in some of the original regulators involving a compromise between the policies of opposing factions within the Hungarian Socialist Workers Party (HSWP). The original reforms were the most far-reaching of those implemented by the Soviet bloc countries in the 1960s, involving a considerable degree of decentralisation of decision-making on such matters as investment, prices, wages and output. The mechanism has been attended with some success - a slightly faster rate of growth of national income, a better performance in the agricultural sector (arguably the major achievement), an increase in industrial efficiency etc. - but it has also encountered a number of deep-rooted problems which have slowly compelled the government to take a more interventionist rôle and draw back somewhat from the original NEM principles.

3. The first decisive reassertion of central control was in late 1971 when administrative measures were taken and regulators on industrial taxation modified to curb excessive enterprise investment and to limit the mobility of labour. Continued distortions in the economy led to further restrictive measures at the beginning of 1972 which involved a partial return to central control. The process reached its climax at the Central Committee meeting of the HSWP in November 1972, when increased state intervention in most economic sectors was decided upon. The main changes were in the field of investment where the government intervened with various administrative and financial sanctions. To curtail the strong inflationary trend a number of measures were taken to increase central control over prices with the freezing of the cost of basic goods until 1975. In the case of earnings the government announced a special increase for state industrial workers in an

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attempt, inter alia, to redress the imbalance between them and the agricultural workers which had been enhanced with the introduction of the NEM. Economies in the use of labour were also to be effected through the experimental application at some enterprises of a special taxation system. In the agricultural sphere measures were taken to improve the livestock sector, which had not reacted to the reforms as favourably as the crop sector. Finally in industry tighter central control was authorized for certain traditional socialist-planned enterprises(1).

The Current Situation(2)

4. 1971 saw great overheating in the investment field, an extremely adverse foreign trade balance and a higher-than-planned budget deficit. 1972 was therefore a year of "stabilisation", with tighter control over investment financed through enterprise resources and bank credits being one of the major features. The inflationary tendency in the investment sphere was arrested - in fact investment expenditure (at constant prices) was slightly below the very high level of 1971 and demand for investment goods also declined. While in the previous three years the proportion of total investment financed by enterprises and co-operatives had increased, in 1972 it decreased somewhat and central investment rose considerably. Preliminary figures for 1973 indicate that enterprise investment continued to be strictly controlled. Overall investment grew more slowly than planned; otherwise favourable results for all major economic indices were achieved.

5. Industrial production expanded at the planned rate in 1972 attributable to a marked rise in productivity as there was a slight drop in the industrial work force. The modernisation and structural transformation of industry, a priority of the Five Year Plan (1971-75), proceeded as indicated, for example, by the increased consumption of oil and the drop in coal output, and the greater proportion of finished products in the output of the aluminium industry. Information available for 1973 indicates that the target for overall industrial production was exceeded. The favoured "technological" industries appear to have maintained their faster rate of expansion, the mining and metallurgical sectors which performed relatively badly in 1972 began to revive, but the results in the building industry were disappointing despite some progress. There was a further fall in the level of stocks although the authorities had intended to allow stocks to build up again, in moderation. The spirit of economy and restraint injected with the announcements of modifications to the NEM in November 1972 has continued to be the keynote of industrial development.

(1) A fuller examination of the counter-reform measures is given in Appendix X.

(2) See Appendices I and II.

6. The agricultural sector has been the chief beneficiary of the NEM and, with the added help of the improved scientific and technological approach, is now one of the most efficient in Eastern Europe. (It is generally found that such reform of the agricultural sector in the command economies produces fairly immediate positive results, and this has certainly been true in Hungary.) Gross output rose markedly above the planned level in 1972 despite a decline in the numbers employed; preliminary figures for 1973 indicate an even better performance last year. In addition to the greater emphasis on the more profitable livestock sector particular attention is being paid to mechanisation (see Appendix III). However, the original intention for Hungary to import only 40 per cent of her agricultural machinery during the current Five Year Plan and to produce the rest herself is not proving feasible (and it is probable that about 55-60 per cent of Hungary's needs in this sphere will continue to be met through imports). Nearly all the equipment will come from other COMECON countries, but additional hard currency funds have now been granted for Western imports and Western suppliers (including the USA) can expect a special rôle in developing Hungary's new "closed" production systems. The United States-sponsored Corn Production System is the most famous of these schemes, under which those varieties of plant or animal considered particularly suitable to intensive development under Hungarian conditions are selected, and then production is rationalised and mechanised to the maximum extent. Co-operation with the West, and particularly with the USA, has been a vital factor in the introduction of this system. While the scheme has already achieved considerable success, the rapidity with which it can be extended is limited by the need for highly skilled personnel and by the heavy expenditure in convertible currency on machinery and equipment.

7. During 1972 there was much criticism of the poor living standards of workers in large industrial enterprises and particularly of the slow increase in their wages. The countermeasures announced in November 1972, including a special 8 per cent increase for some state industrial workers, were designed to improve their situation considerably. Available figures for 1973 show a higher rate of increase in industrial than agricultural wages (as in 1972).

FOREIGN TRADE AND ECONOMIC RELATIONS

Introduction

8. Foreign trade is particularly important for a country such as Hungary which has limited natural resources and a relatively small domestic market. Among the East European countries, Hungary is third in terms of foreign trade per capita behind the GDR and Czechoslovakia.

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9. Under the NEM enterprises were given considerable freedom in the conduct of their foreign trade in the hope of increasing the volume of profitable exports. But a complex system of central control by means of differential exchange rates, import duties, exchange controls, etc., ensured that the degree of autonomy remained tightly circumscribed. The investment boom of 1969-71 accompanied by a higher level of personal consumption and intensified stock-building led to greatly increased imports of machinery and equipment, particularly from the West. By 1971 a record adverse balance of \$490 million had resulted, roughly equally divided between the Communist and non-Communist partners. Clearly concerted efforts were needed to rectify this situation but this was achieved without any dilution of the responsibilities given to enterprises, which remain directly involved in foreign trade though still under close central supervision.

10. Nearly half Hungary's exports comprise machinery and consumer goods and the balance is divided almost equally between agricultural and food products and semi-finished goods and components. Of Hungary's total imports, over 50 per cent comprise fuels (almost all from CMEA partners), raw materials and semi-finished products. Hungary is a net importer of fuels, raw materials, machinery and transport equipment and is a net exporter of manufactured consumer goods and agricultural and food products.

Main Features of 1972 and 1973

11. Hungary's trade turnover in 1972 reached almost \$6,450 million, an increase of 8 per cent, significantly less than in the previous year (see Appendix IV). As a result of the drastic cut back in imports - an absolute decrease was recorded in deliveries from both Communist and non-Communist partners - and an aggressive promotion of exports to the CMEA countries, especially the USSR and the GDR, coupled with higher prices commanded in the West, a sizeable surplus of almost \$140 million was achieved. Trade with the Communist countries grew faster than that with the non-Communist partners (as in 1971, in accordance with the provisions of the Five Year Plan - see Appendix I); while the large 1971 deficit on Hungary's trade with the Communist countries was translated into a correspondingly large surplus in 1972, the deficit with the developed West continued although at a much reduced level.

12. During the first nine months of 1973 Hungary's trade expanded considerably more rapidly than in 1972, by around 14 per cent. Exports continued to grow markedly and imports began to expand again. Hungary maintained her surplus on

overall trade and in her exchange with the other Communist countries (exports to which expanded rapidly while imports stagnated) but remained in deficit on trade with the developed West. Interestingly trade with the latter group grew significantly faster than that with the CMEA partners during the period.

Trade with Communist Countries (in 1972)

13. Communist countries continued to account for slightly over two-thirds of Hungarian trade turnover with the 4 leading Communist partners, the USSR, the GDR, Czechoslovakia and Poland as usual assuming a 60 per cent share of her total trade (see Appendix V). Hungary had a favourable balance with all Communist countries, except the GDR, Czechoslovakia and Albania, and the net surplus with the whole of this group amounted to over \$250 million (see Appendix VI); this followed the sizeable deficit that Hungary suffered in 1971 and represented a return to the overall situation in the 1966-70 period. The USSR is Hungary's main trading partner, accounting for about 35 per cent of total turnover. Nearly half Hungary's imports from the USSR comprise raw materials and semi-finished products. Nearly all her supplies of crude oil and petroleum products, iron ore and pig iron, the bulk of her imports of timber, phosphate fertiliser and electric power and half her purchases of coke, cotton and rolled steel are derived from the USSR.

Trade with Developed West (in 1972)

14. Hungarian trade with this area continued to account for well over a quarter of total turnover. The leading partners were (in order) West Germany, Italy, Austria, the United Kingdom, Switzerland and France who together accounted for three-quarters of Hungarian trade with the developed West (see Appendix VII). The absolute decline in imports while exports increased by 22 per cent resulted in a much reduced deficit of \$55 million on visible trade.

15. Food, beverages and tobacco figure prominently in Hungary's exports to the developed West; she is the most dependent of the CMEA countries in this category of exports to the EEC (currently comprising just under half the total). As expected, non-agricultural exports to the EEC during the 1968-72 period showed a dramatic increase of 140 per cent, helped in part by special subsidies and industrial co-operation agreements with Western firms (see paragraphs 21-22 below). Nevertheless, exports of agricultural products to these countries, while growing at a slower rate than previously, expanded significantly by 60 per cent. By comparison,

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Hungary's agricultural and non-agricultural exports to non-EEC countries during the same period both rose by only 40 per cent. The Hungarians have realised that the increase in the share of non-agricultural products in their exports to the EEC is inevitable - and not wholly unprofitable. Hungary purchases mainly finished and semi-finished goods from the West, with machinery accounting for a surprisingly small proportion of the total.

Trade with the Developing Countries (in 1972)

16. Hungarian trade and aid activities with the developing countries continue to make slow and unspectacular progress in most parts of the world. An increase of 5 per cent in turnover was recorded in 1972, compared with a decrease in the previous year, and these exchanges continued to account for under 5 per cent of total Hungarian trade. The leading partners in this group in 1972 were India, Egypt and Iran (see Appendix VIII). Hungarian trading activities in the Third World are supported by the extension of medium to long-term non-convertible currency credit facilities to promote exports of capital equipment.

Finance

17. Trade with Multilateral Partners(1) Payments for the greater part of Hungary's foreign trade are conducted through bilateral clearing accounts. Trade with multilateral partners accounted for just under a quarter of her total trade in 1972, compared with 22 per cent in 1971. With these countries Hungary recorded a visible trade deficit of nearly \$54 million in 1972, a considerable drop on the \$150 million deficit recorded the previous year. Probably about 40 per cent of Hungary's debt with the multilateral partners in 1972 was financed by her net convertible currency earnings from tourism(2).

18. Western Credits. Hungary's policy of entering into industrial co-operation agreements with West European companies (see paragraphs 21-23 below) has helped to contain her need to

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- (1) Those countries - including most non-Communist trading partners - with which all transactions are settled both ways in convertible currencies - listed in Appendix IV.
 - (2) In recent years there has been a substantial increase of the order of 15 per cent annually in the number of foreign visitors to Hungary from non-Communist countries. The number of "Guest days" - an indicator of tourism earnings - has continued to rise creating a favourable trend in convertible currency earnings, which are estimated to have risen to nearly \$48 million in 1972.

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borrow convertible currencies or obtain credits from the West. Thus, by mid-1972 her accumulated outstanding debt to NATO countries was only \$152.3 million(1), (representing less than 6 per cent of the total for all the countries of Eastern Europe). Of this total, almost two-thirds comprised credits over 5 years, one of the highest proportions in Eastern Europe. New credits extended by NATO countries in the first half of 1972 amounted to only \$3.9 million (compared with a total of nearly \$400 million for Eastern Europe as a whole). Repayments to NATO countries in 1972 represented only 4.8 per cent of Hungary's exports to these countries. It is believed that the total of credits from non-NATO countries is relatively small, and has probably been mostly provided by Austria, with whom Hungary has close trading links, Sweden and Switzerland.

19. Loans. Hungary, unlike her Communist neighbours, has been notably more active on the euro-currency market than in the field of Western supplier/buyer credit. The loans raised by Hungary since she first entered this market in 1968 amount to about \$300 million (see Appendix IX) and they have been used primarily to finance the convertible currency element of expansion programmes in export-oriented industries such as pharmaceuticals and aluminium. Hungary is the only East European country to have raised euro-dollars through the floating of bond issues, which brings the total of her euro-currency borrowings to date to over \$380 million.

20. The euro-dollar loans constitute the major element in Hungary's debt servicing commitment. When total known borrowings in the West are considered it would appear that at present she has the lowest debt service ratio (well under 10 per cent) of all the East European countries.

Co-operation with the Developed West

21. Hungary has attempted to raise both labour productivity and industrial standards by entering into a series of industrial co-operation agreements (ICAs) with Western countries. She is therefore able to import Western industrial equipment and advanced technology despite her limited potential as an earner of convertible currency. Since 1964 240 agreements covering many different forms of industrial and agricultural co-operation have been negotiated and the rate has accelerated in the last few years. About three quarters of the agreements have involved the engineering industry and the remainder the chemical, agricultural and light industries. About two thirds

(1) This figure only covers medium and long-term private export credits which receive official backing and the accumulated future interest payable

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of the agreements entail exchanges of documentation and joint production, with product sharing and market co-operation types accounting for most of the remainder. It is estimated that over a quarter of the ICAs have been signed with West Germany and a further one fifth with Italy and France combined. Recently Austria has expanded her activities in this field considerably, and Japan and the United States have entered the scene.

22. The most important aspect of many ICAs is the acquisition of licences to use Western manufacturing processes which include the relevant technical know-how and its application to production methods. Resolutions were introduced in 1969 which allowed relief on customs duties, credit etc. for enterprises buying licences and a special enterprise, the Licencia Patent Marketing Enterprise, was set up to deal solely in these products; a considerable expansion in this activity has resulted. The main Western countries supplying licences and know-how are West Germany and France; considerable purchases are made in the USSR. This is by no means a one-way traffic as Hungary sells licences, blue prints etc. to both the West and the CMEA group. On information currently available for 1973, it appears that co-operation slowed down somewhat with the Hungarians wanting to assess the result of past agreements before proceeding further. However, in view of their determination to control imports from the West under normal trading arrangements, it is likely that this will only be a temporary deceleration and that the aim of the Five Year Plan, which emphasises the greater importance to be attached to the purchase of licences, exchanges of technical information and market co-operation, will be pursued.

23. In October 1972 a new law on foreign investment came into effect, permitting the establishment of joint enterprises, particularly for market research and marketing activities. The law provides for both Communist and non-Communist concerns to participate in associations formed in Hungary to the extent of a 49 per cent holding. The Hungarian Government guarantees the free transfer of profits and repatriation of capital in the investor's own currency. However, no joint companies have yet been established and it is clear that Western investment and involvement will not be permitted on the scale found in Yugoslavia.

Prospects up to 1975

24. Economic objectives for 1974 were set out at the meeting of the Hungarian Socialist Workers Party Central Committee held in late November 1973. Economic targets are lower than the results achieved last year. A substantial

increase in planned investment goes some way towards the Hungarian National Bank's call for vigorous reflation while the choice of central investment projects seems less tied to CMEA policies than last year and includes some (meat, textile and cement factories) designed to further exclusively domestic development programmes.

25. With the more careful regulation of the foreign exchange component of investment, any substantial increase in imports from the developed West is unlikely in the near future and instead Hungary will place increasing emphasis on her policy of importing Western technology through co-operation agreements. The acquisition of further medium and long-term credits may well be undertaken, as recommended in the current Five Year Plan. After the large jump in exports in 1973, well above plan, it seems likely that in 1974-75 the rate of increase in trade turnover will be rather closer to that planned (i.e. 7-8 per cent per annum). Within CMEA Hungary is likely to reinforce her links with the more industrialised countries such as the GDR with whom a number of co-operation projects are in progress.

26. Particular interest attaches to Hungary's future oil supply situation. Protracted negotiations have been taking place for the last 2 years on the size of future Soviet deliveries with the USSR requesting Hungary, (and other CMEA countries), to seek supplementary quantities elsewhere. The recent commitment on future deliveries by the USSR avowedly falls short of Hungary's requirements while domestic oil output has nearly reached its ceiling. Consequently the securing of new oil supplies is becoming a matter of increasing concern. For Hungary the import of Middle East oil, particularly from Iraq, is the obvious method of closing the gap and its transportation through the proposed Adria pipeline seems a practical solution. A preliminary agreement was signed in 1971 with a Yugoslav oil concern for the construction of a pipeline to carry imported crude oil from the Adriatic port of Rijeka to the Yugoslav/Hungarian border, whence the oil would be piped under a joint Hungarian/Czechoslovak venture with each country taking 5 million tons of oil per annum. A formal agreement with Yugoslavia to this effect was scheduled for last October and a completion date of 1976 has been set for the whole project which the Yugoslavs have recently reaffirmed; work on the Hungarian section of the Adria pipeline is to start in 1974.

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HUNGARY: MAIN ECONOMIC INDICATORS

INDEX	1972		1973		1974	1971-75 (annual average percentage increase)
	Plan	Result	Plan	Preliminary Results	Plan	
Percentage increase over previous year						
National Income	5.0-6.0	5.0	4.0-5.0	6.0-7.0	5.0	5.6
Gross Industrial Production	5.0-6.0	5.6	5.5-6.0	6.0-7.0	5.5-6.0	6.0
Gross Agricultural Production	2.0-3.0	4.0	2.0	5.0-6.0	2-2.5	2.8
Crop Production		7.0-8.0				
Livestock Production		1.0				
Investment (current prices)		2.0	3.0	2.0	4.0	5.7
Labour Productivity		6.5		6.0 (Jan- July)	5.0	4.5
Consumption	5.0	3.5	4.0-5.0	4.0-5.0	6.0	5.4
Real Wages		2.0	2.0-2.5	2.3	3.7	3.0-3.5
Average Industrial Wage per capita	4.0-5.0	5.0	5.5-6.0			
Average Real Income per capita	5.0	3.5	4.5-5.0	4.0-4.5	5.0-5.5	4.5-5.0
Retail Trade Turnover	7.0	6.3	6.0-6.5	9.0	8.0-9.0	6.7-7.0
Foreign Trade		8.1	7.0-8.0			7.0-8.4
Imports	7.0	-2.9	7.5-8.0	7.0 (Jan- Sep)		7.7-8.4 (Socialist)
Exports	14.0	21.2	6.5-7.0	20.0 (Jan- Sep)		5.1-5.7 (Developed West)
						7.3-7.9 (Socialist)
						5.4-6.2 (Developed West)
<u>Selected Industries</u>						
Building Materials	7	4				
Chemical	11	12				
Construction	3	1				
Electric Power	7	8				
Food	6	6				
Light	5	5				
Metallurgical	4	2				
Machinery	5	6				
Mining	0	-4				

Source: Central Statistical Office
of Hungary

HUNGARY: INVESTMENT BY SECTOR

SECTOR	Million forint (in Current prices)			Percentage		
	1961-1965	1966-1970	1971-1975 PLAN	1961-1965	1966-1970	1971-1975 PLAN
<u>Industry Total</u>	89,484	130,227	196-197,000	<u>42.6</u>	<u>39.8</u>	<u>40.1</u>
Mining	16,670	20,547		7.9	6.3	
Electrical Energy	12,607	15,998		6.0	4.9	
Metallurgy	8,770	14,393		4.2	4.4	
Engineering	15,777	23,572		7.5	7.2	
Building Materials Industry	5,347	8,515		2.6	2.6	
Chemical Industry	14,366	20,785		6.8	6.3	
Light Industry	8,457	12,791		4.0	3.9	
Other Industry	368	1,200		0.2	0.4	
Food Processing Industry	7,122	12,426		3.4	3.8	
<u>Construction</u>	4,896	8,314	12-14,000	<u>2.3</u>	<u>2.5</u>	<u>2.5</u>
<u>Agriculture</u>	36,532	66,582	61-62,000	<u>17.4</u>	<u>20.3</u>	<u>12.6</u>
<u>Transport and Communication</u>	29,712	44,070	83,000	<u>14.1</u>	<u>13.5</u>	<u>17.0</u>
of which						
Rail	17,061	22,618		8.1	6.9	
Road	5,151	9,635	30,000	2.5	2.9	6.3
Urban	3,733	5,945		1.8	1.8	
<u>Internal Trade and Tourism</u>	6,920	11,339	17,000	<u>3.3</u>	<u>3.4</u>	<u>3.5</u>
<u>Communal Investments</u>	42,646	66,923	111-127,000	<u>20.3</u>	<u>20.5</u>	<u>24.3</u>
of which						
Health	3,522	4,209	6-7,000	1.7	1.3	1.3
Social	2,506	5,677		1.2	1.8	
Cultural (Education)	8,191	12,865	16-17,000	3.9	4.0	3.4
Housing	15,295	22,964	56,000	7.3	7.1	11.4
Other	13,132	21,208		6.2	6.5	
GRAND TOTAL	210,190	327,455	480-500,000	100.0	100.0	100.0

Source: Statistical Yearbook, 1972

N A T O C O N F I D E N T I A LAPPENDIX III to
AC/127-WP/375HUNGARY: PERCENTAGE DISTRIBUTION OF AGRICULTURAL AND FOOD INDUSTRY INVESTMENT

SECTOR	1966-70	1971-75	Planned Absolute Investment
			<u>1971-75</u> 1966-70
Crop Production and Processing	38.6	28.4	- 91.3
Livestock Raising and Processing	31.8	38.1	+ 47.8
Mechanisation and Other	29.6	33.5	+ 40.0
TOTAL	100.0	100.0	+ 24.0

Source: Hungarian Ministry of Food and Agriculture

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APPENDIX IV to
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HUNGARY - FOREIGN TRADE 1965-72

	1972				1971				1965				Percentage Change (on forint basis)			
	Turnover	Exports	Imports	Balance	Turnover	Exports	Imports	Balance	Turnover	Exports	Imports	Balance	1972-71	Exports	Imports	1971-70
						<u>i. \$ US million</u>										
All countries	6445.6	3291.7	3153.9	+ 137.8	5490.0	2500.4	2989.6	- 489.3	3029.8	1509.5	1520.3	- 10.8	+ 8.1	+ 21.2	- 2.9	+ 13.9
Communist Countries	4312.9	2282.1	2030.8	+ 251.3	3668.1	1723.9	1944.2	- 220.3	2076.0	1057.8	1018.2	+ 39.6	+ 8.3	+ 21.9	- 3.8	+ 17.5
Non-Communist Countries*	2132.6	1009.6	1123.0	- 113.4	1822.0	776.4	1045.5	- 269.0	953.8	451.7	502.1	- 50.4	+ 7.8	+ 19.7	- 1.1	+ 7.0
of which -																
Developed West	1800.2	872.5	927.7	- 55.2	1529.7	659.1	870.6	- 211.5	758.0	351.0	407.0	- 56.0	+ 8.4	+ 21.9	- 1.9	+ 9.0
Developing Countries	268.5	148.6	119.9	+ 28.7	235.4	128.4	107.0	+ 21.4	195.9	100.8	95.1	+ 5.7	+ 5.0	+ 6.6	+ 3.1	- 3.3
Multilateral Partners**	1599.9	772.9	827.0	- 54.1	1185.3	516.5	668.8	- 152.3	551.0	257.0	294.0	- 37.0	+ 24.3	+ 37.8	+ 13.9	+ 11.5
						<u>ii. Per Cent</u>										
Communist Countries	66.9				66.8				68.4							
Non-Communist Countries	33.1				33.2				31.6							
of which -																
Developed West	27.9				27.9				25.1							
Developing Countries	4.2				4.3				6.5							
Multilateral Partners	24.8				21.6				18.2							

Source: "Vilaggazdasag", Budapest
"Kulkereskedelem", Budapest

Exchange Rates - 1965, 1971 - 11.74 Forints = US \$1
1972 - 10.81 Forints = US \$1

* The discrepancy in 1971 and 1972 between figures for non-Communist countries and the sum of developed West and developing countries is due to accounting of freight costs.

** Multilateral Trading Partners: Europe - Austria (from April 1972), Belgium, Denmark, France, German Federal Republic, Italy, Luxembourg, Netherlands, Norway, Spain (from January 1973), Sweden, United Kingdom, Yugoslavia (from January 1973).
Others - Argentina, Australia, Cameroun, Canada, Iraq, Japan, Kuwait, Lebanon, Libya, Nigeria, United States, Uruguay.

HUNGARY: FOREIGN TRADE WITH PRINCIPAL TRADING PARTNERS 1972
(US \$million)

Trading Partners	Turnover	% of Total Hungarian trade turnover	Exports	Imports	Balance
USSR	2278.4	35.4	1194.5	1083.9	+110.6
GDR	647.5	10.1	323.4	324.1	- 0.7
CZECHOSLOVAKIA	533.2	8.3	264.0	269.2	- 5.2
West Germany	408.6	6.3	193.2	215.4	- 22.2
POLAND	388.5	6.0	230.9	157.6	+ 73.3
Italy	319.5	5.0	208.8	110.7	+ 98.1
Austria	209.0	3.2	93.6	115.4	- 21.8
United Kingdom	153.5	2.4	57.1	96.4	- 39.3
Switzerland	153.2	2.4	75.1	78.1	- 3.0
ROMANIA	138.9	2.2	75.3	63.6	+ 11.7
France	125.5	2.0	41.5	84.0	- 42.5
YUGOSLAVIA	123.6	1.9	69.8	53.8	+ 16.0
BULGARIA	102.8	1.6	62.2	40.6	+ 21.6
Netherlands	87.3	1.4	37.5	49.8	- 12.3
*India	58.9	Less than 1.0	31.5	27.4	+ 4.1
United States	54.1	"	15.3	38.8	- 23.5
Sweden	49.3	"	25.8	23.5	+ 2.3
*Egypt	45.6	"	28.2	17.4	+ 10.8
Belgium and Luxembourg	43.7	"	16.8	26.9	- 10.1
CHINA	39.5	"	22.1	17.4	+ 4.7
Denmark	30.1	"	13.6	16.5	- 2.9
Greece	28.2	"	18.3	9.9	+ 8.4
Spain	27.5	"	18.5	9.0	+ 9.5
*Iran	22.0	"	12.2	9.8	+ 2.4
Finland	21.7	"	12.2	9.5	+ 2.7
Canada	21.5	"	15.4	6.1	+ 9.3
Japan	20.4	"	7.8	12.6	- 4.8
NORTH VIETNAM	19.3	"	18.4	0.9	+ 17.5
*Syria	18.7	"	10.7	8.0	+ 2.7
*Iraq	17.0	"	10.8	6.2	+ 4.6

Source: "Vilaggazdasag", Budapest

Communist countries are shown in block capitals; non-Communist developing countries are marked with an asterisk

N A T O C O N F I D E N T I A L

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HUNGARY: TRADE WITH COMMUNIST COUNTRIES 1972
US \$ Million

	Percentage of Total Hungarian Trade with CMEA countries				
Total Communist Countries	Turnover 4312.9		Exports 2282.1	Imports 2030.8	Balance +251.3
USSR	2278.4	55.4	1194.5	1083.9	+110.6
GDR	647.5	15.7	323.4	324.1	- 0.7
CZECHOSLOVAKIA	533.2	13.0	264.0	269.2	- 5.2
POLAND	388.5	9.5	230.9	157.6	+ 73.3
ROMANIA	138.9	3.4	75.3	63.6	+ 11.7
Yugoslavia	123.6	-	69.8	53.8	+ 16.0
BULGARIA	102.8	2.5	62.2	40.6	+ 21.6
China	39.5	-	22.1	17.4	+ 4.7
North Vietnam	19.3	-	18.4	0.9	+ 17.5
CUBA	13.9	0.3	7.0	6.9	+ 0.1
Albania	12.0	-	4.4	7.6	- 3.2
MONGOLIA	10.0	0.2	7.2	2.8	+ 4.4
North Korea	5.3	-	2.9	2.4	+ 0.5

Source: Vilaggazdasag, Budapest

CMEA members are shown in block capitals

HUNGARY: TRADE WITH SELECTED DEVELOPED WESTERN
COUNTRIES 1972

US \$ Million

	Turn-over	Percentage of total Hungarian Trade with Developed West	Exports	Imports	Balance
Total Developed West	1800.2		872.5	927.7	-55.2
of which -					
West Germany	408.6	22.7	193.2	215.4	-22.2
Italy	319.5	17.8	208.8	110.7	+98.1
Austria	209.0	11.6	93.6	115.4	-21.8
United Kingdom	153.5	8.5	57.1	96.4	-39.3
Switzerland*	153.2	8.5	75.1	78.1	-3.0
France	125.5	7.0	41.5	84.0	-42.5
Netherlands	87.3	4.9	37.5	49.8	-12.3
USA	54.1	3.0	15.3	38.8	-23.5
Sweden	49.3	2.7	25.8	23.5	+2.3
Belgium and Luxembourg	43.7	2.4	16.8	26.9	-10.1
Denmark	30.1	1.7	13.6	16.5	-2.9
Greece*	28.2	1.6	18.3	9.9	+8.4
Spain*	27.5	1.5	18.5	9.0	+9.5
Finland*	21.7	1.2	12.2	9.5	+2.7
Canada	21.5	1.2	15.4	6.1	+9.3
Japan	20.4	1.1	7.8	12.6	-4.8

Source: "Vilaggazdaway", Budapest

* Bilateral partners

HUNGARY: TRADE WITH SELECTED DEVELOPING COUNTRIES 1972

US \$ million	Turnover	Percentage of total Hungarian trade with Developing countries	Exports	Imports	Balance
Total Developing Countries	268.5		148.6	119.9	+28.7
of which:					
India	58.9	21.9	31.5	27.4	+4.1
Egypt	45.6	17.0	28.2	17.4	+10.8
Iran	22.0	8.2	12.2	9.8	+2.4
Syria	18.7	7.0	10.7	8.0	+2.7
Iraq*	17.0	6.3	10.8	6.2	+4.6
Brazil	16.7	6.2	4.7	12.0	-7.3
Lebanon*	10.0	3.7	7.2	2.8	+4.4
Algeria	9.7	3.6	7.2	2.5	+4.7
Libya*	9.0	3.4	9.0	0	+9.0
Peru	8.9	3.3	3.8	5.1	-1.3

* Multilateral partners

Source: "Vilaggazdasag", Budapest

HUNGARY: ACTIVITIES ON THE EUROCURRENCY MARKET

1. LOANS

<u>DATE</u>	<u>SIZE OF LOAN</u>	<u>CONSORTIUM LED BY</u>
February 1968	\$10 million	Lazards
June 1968	\$15 million	Rothschilds
March 1969	\$ 5 million	French Banks and Barings
April 1969	\$15 million	Bank of London and South America
May 1970	\$30 million	Bank of London and South America
April 1971	\$20 million	Moscow Narodny Bank
December 1971	\$50 million	Lloyds and Bank of London and South America
August 1972	\$20 million	Italian Banks
August 1972	\$10 million	Italian Banks and Euro-America of Nassau
August 1972	\$20 million	Deutsche Bank
? 1972	\$18 million	Credit Lyonnais
November 1972	\$ 3 million	Banque de l'Union Europa
September 1973	\$40 million	Industrial Bank of Japan
October 1973	\$50 million	Dairhi Kangyo

<u>DATE</u>	<u>SIZE OF BOND ISSUE</u>	<u>CO-MANAGERS</u>
June 1971	\$25 million	National Westminster Bank Morgan Grenfell Moscow Narodny Bank
September 1972	\$50 million	National Westminster Bank Morgan Grenfell Moscow Narodny Bank

GOVERNMENT COUNTER-REFORM MEASURES OF 1971 and 1972

Investment

The broadened scope for investment based on enterprise self-finance and the expanded rôle allotted to bank credit under the NEM gave rise to an investment boom between 1969 and 1971. Many new projects were started, often of an uneconomic nature, completion periods were lengthened and the construction sector became strained. The government successfully intervened in the latter part of 1971 with various administrative and financial sanctions, although investment spending that year continued at too high a level, exceeding both the plan and the available resources. While production rose by 11 per cent in 1970 and 1971, domestic expenditure increased by 24 per cent. Many enterprises went bankrupt and the state decided to bale them out rather than pursue the original objective of closing unprofitable enterprises. Accordingly further restrictive measures were taken at the beginning of 1972, which involved a partial re-introduction of central control. Investment expenditures for 1972 were held at the 1971 level the final figure being some 2 per cent below the plan; the share of investment financed by enterprises was cut back and restrictions on credit for additional capital outlays were also extended. The investment boom was in fact probably a unique occurrence arising more as a result of a miscalculation by the government as to the size of the profits that would accrue to the enterprises following the introduction of the NEM, rather than from any real surrender of basic control by the central authorities. The government appears determined to maintain the sanctions introduced in 1971, although in March 1973 it passed a resolution on enterprise investment which allows the enterprises to retain their decision-making rôle. But while approval for investment is to be left to the general manager of the enterprise the resolution does require preparatory work for investments and the implementation to be controlled to a greater extent by supervisory bodies. When assessing the extent to which these resolutions represent a retreat from NEM principles it must be noted that even the original reform did not intend to allow enterprise independence to reach the point where the regulating activity of the central authority was pushed too far into the background, as it did between 1968 and 1972. Furthermore, although the resolutions are being imposed as central directives, they do not, for the most part, represent direct interference in the details of enterprise operation. But while firms will still have more autonomy in their investment decisions than their counterparts in other East European countries, it will be more circumscribed than before and its foreign exchange component will be carefully regulated.

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Prices

Under the original price reforms the state retained extensive control over retail prices and social rather than economic considerations continued to play the major rôle in price formation. The major innovation allowing selected enterprises to fix all their prices except those for raw materials, led to large price increases and correspondingly high profits. To eliminate the differential between these and less prosperous enterprises the government taxed the "profitable" firms and subsidised the "unprofitable" ones, but this subsequently led to a distortion of the bonus system which was intended to reward economic efficiency. The strong inflationary trend that developed in the economy led the government to take a number of other measures at the Central Committee meeting in November 1972 to increase its influence. The prices of dairy products, cigarettes and spirits were raised and an increase in meat prices threatened for 1976, but there were to be no further increases in the prices of basic goods or the proportion of free prices before 1975. Stricter pricing control was to be introduced generally with the compulsory reporting of price increases. Despite these modifications to the pricing system, the Government's official aim, one which is proving unexpectedly difficult to implement, is still to evolve a consumer price system proportionate to value.

Incomes

In terms of earnings and general standard of living it is the peasantry and the workers in co-operative industry that have gained most from the NEM at the expense of the traditional chief beneficiary of Communist society - the worker in the large state industrial enterprise. To some extent, however, this situation does represent a continuation of a trend in operation since 1955 although it was not until 1968 that the industrial wage fell below the average wage level for the first time. The countermeasures introduced in November 1972 included a series of measures aimed at redressing this imbalance in incomes. They included a special wage increase of 8 per cent for industrial workers in the state sector over and above the normal annual increase. This is to be applied selectively among different categories of industrial workers. This principle of differentiation is one which is fundamental to the NEM and often by no means popular with the workers themselves or with the conservative opponents of the NEM. The drafting of a table of wages for skilled workers and specialists to be applied on a national scale was also approved, together with the experimental

introduction of a "wage-mass taxation system in some enterprises. The aim of this system is to stimulate greater economy in the use of labour and by requiring taxes to be paid primarily on the total wage fund instead of on the per capita wage level as before. Finally the meeting approved the abolition of regulations tying wages to profits, introduced under the NEM, in coal mining and the power industry. The statutory wage rise represents a fairly clear case of central action being taken to remedy disproportions thrown up by the working of the NEM, as does the introduction of the national wage scale for skilled workers and specialists.

It is clear that, as in the case of certain traditional sectors of Hungarian industry, the NEM has been proved incapable of exercising the full desired influence on earnings and has had to be modified although there is no question of a rejection of the mechanism as a whole.

Manpower

As a result of the shortage of manpower, the 1971 restrictions on labour mobility were extended through 1972 and a concerted drive was made to strengthen work discipline.

Agriculture

The NEM removed a great deal of central control over the farms by allowing much more freedom in the choice of commodities produced and their disposal, the operation of ancillary services and the rôle of self-financed investment. The results, however, have been uneven, with grain output showing a notable increase, but cattle breeding and fruit and vegetable production encountering considerable difficulties. Accordingly changes were introduced to the regulating system at the beginning of 1970, with increased procurement prices paid for livestock and milk, the sale and purchase of fodder liberalised and a 50 per cent subsidy granted for the purchase of livestock equipment.

Industry

In the industrial sector, the comparative disadvantage under which large-scale industry laboured since the NEM was introduced became so marked by 1972 that the authorities decided to step in. In 1973 some 50 large enterprises covering 180 factory units and accounting for

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55 per cent of Hungary's total industrial production were put in a special category and treated with "special attention". This appears to involve a greater and more regular flow of information on sales, profits, exports, assets, manpower etc., from the enterprises to the central authorities who could give orders and provide state support. It has been maintained that such supervision should not reduce the independence of the enterprises nor conflict with the principles of the NEM, but in the case of 6 enterprises which are to be temporarily taken back under Ministerial supervision it is clear that the original NEM measures have proved themselves inappropriate in the more traditional sectors of Hungarian industry.

In all the measures adopted at the Central Committee meeting in November 1972 there was thus a limited, but nevertheless distinct retreat from the basic principles of the NEM, in the interests of re-establishing certain social development priorities close to the traditional model of a Communist economy. Most of the measures had been foreshadowed in statements and speeches made earlier in the year. The NEM was never intended to be a static or unchangeable system, but while it was realised at the outset that subsequent modifications would inevitably be necessary it is important to note that the solutions that were adopted were all concerned with re-establishing some measure of central control rather than introducing more effective financial control in the "market" sense. In this respect the November 1972 meeting represented a compromise between the proponents of the NEM and their conservative critics. This impression has been confirmed since then by various events including the March resolution on enterprise investment, the creation in July of a state planning committee with overall powers to co-ordinate plans, and the subsequent resolution providing for supervision of activities by controlled agencies (particularly Ministries) and inner control by enterprises.

Finally, the changing conditions within Eastern Europe have had and will continue to have an effect on the NEM. When it was first introduced in 1968 the international situation was favourable to such an undertaking, but since then the concept of "integration" within CMEA has replaced "reform" as the dominant economic concern of Eastern Europe.