Pathfinder

CENTER FOR EDUCATION AND RESEARCH IN FREE ENTERPRISE
TEXAS A&M UNIVERSITY COLLEGE STATION, TEXAS 77843

July 1986 Volume 8 Number 3

THE HUNGARIAN ECONOMY: THE CASE OF GRADUAL PRIVATIZATION UNDER SOCIALISM

Interesting developments are taking place in the structure of Hungarian agriculture and industry. The Hungarian government has been permitting more free enterprise. While these reforms have been quite modest, they seem to have been rather successful, and recently the changes have been more rapid.

The first type of business enterprise not corresponding to the state-owned Soviet firm was created in Hungarian agriculture in the 1950s. These "branch cooperatives" support the members' private farms, help with the acquisition and sale of products, and perform certain agricultural tasks. The number of these cooperatives, heavily subsidized by the state, decreased from 144 in 1975 to 62 in 1984.

The "branch groups" are a similar but more loosely structured cooperative form of production. Although organized within the framework of collective farms and other cooperatives, they are independent subjects for taxation and are allowed to employ workers. By 1980, there were 2,578 agricultural branch groups in Hungary with nearly 200,000 members.

Another special kind of cooperation developed in Hungary between the collective farms and the private plots of farmers (about one acre per family). Originally, the products from the private plots of the collective members were for private consumption by the farmers themselves. The state's realization that the private plots were necessary to supply the population with food finally led to a reevaluation of their role in 1968. Since then cooperation between cooperative farms and private plots held by farmers includes all activities, from plowing the land on the private plots to transportation of the crops or selling them jointly. Today, the private plots of collective farm members and other variously organized private small farms produce as much as one-third of the agricultural output of Hungary. The share of some products is between 60 and 90 percent.

The declared objective for creation of branch cooperatives and branch groups in the 1950s was to increase their attractiveness to the rural population by giving people the incentive of self-interest. The state wanted to induce this segment of farmers to engage in "private" economic activity within the framework of the cooperatives. This was designed to increase output. The privatization of some portions of agriculture received more support from the state in the 1970s. According to Hungarian economic experts, the success of Hungarian agriculture in the 1970s shows that these semiprivate enterprise constructions have a positive effect on the organization of agricultural production and on the motivation of farmers.

Because of these successes, Hungarian economic policymakers introduced similar small enterprise firms in industry. In addition, they are attempting to introduce in big and medium sized industrial enterprises certain cooperative elements.

The first attempts were the creation of "small cooperatives" and of "branch groups" in Hungarian industry. Similar to agriculture, industrial branch groups are organized within cooperatives. Because the groups are relatively small, their members are strongly motivated to participate in the affairs of the enterprise. The change in ownership regulations reinforces this motivation. This change violated for the first time the Hungarian principle of the indivisible property of the cooperative. The property of other Hungarian cooperatives cannot be divided—even if a member leaves the cooperative or it is dissolved. In contrast, if an individual branch group is dissolved, the property remaining after the outstanding liabilities have

Continued on next page

From page one

been satisfied can be distributed among the members. For the first time in Hungary there exists an autonomous (non-state) cooperative ownership. Before 1984, there were 392 industrial small cooperatives with 16,000 members. By the end of 1985, there were 2,424 industrial branch groups with 75,800 members.

In 1982, the state authorities also made it possible to create *economic work groups* of between two and 30 members, within state enterprises and cooperatives. The members of these working groups generally do their work for their own enterprises outside the regular working hours, using enterprise equipment. By mid-1985 there were 7,873 independent working groups with 42,516 members, and within enterprises, there were 18,178 working groups with 200,074 members.

In contrast to other Eastern European "brigade movements," regular working hours are not involved; instead, personnel perform overtime work which, for sociopolitical reasons, could not be carried out in the usual form. People in these groups work about 500 to 1,000 additional hours per year and thus help to ease the chronic labor shortages in Hungary. The increased productivity of these groups stems from the higher work intensity of the members. These groups are characterized by initiative and self-monitoring; their members feel responsible for the income of the whole group. Economic authorities have tried for decades, without success, to encourage these qualities in the normal work brigades in Hungary and elsewhere in Eastern Europe.

In 1985, there were 330,000 "small entrepreneurs" in Hungary who earned on average 42,000 forint a year in addition to their regular salaries of about 60,000 forint. But because these workers amount to only one percent of the production of the economy, they have not been able to alter significantly the monopolistic character of Hungarian industry. Their significance lies in creating competition in some services and product groups. They constitute only one third of the economic units and only two percent of the working force. The significance of these small enterprises, not only for the individual members but for the national economy, is much greater than these figures indicate, however. These organizations represent a successful breakthrough in the property regulation of industrial production, a sector of society in Eastern European countries most strongly ideologized.

Semiprivate small firms are quite widespread in Hungarian retail trading and gastronomy. Today, 30 percent of retail sales and 60 percent of restaurant sales are by state enterprises rented to private persons.

In the latest phase of the change, new forms of management are to be introduced in most industrial enterprises within the next two years. Only in public service enterprises and trusts will the manager continue to represent the lowest level of the state's economic control hierarchy. The management of the remaining industrial enterprises will be elected in some cases by the general assembly of the personnel and mostly by an "enterprise council." The new enterprise councils, in which both the management and the personnel as well as delegates of the state are represented, decide on strategic questions of the enterprise. While it is beyond the scope of this article to discuss possible changes in the internal enterprise balance of power, it should be noted that the enterprise councils decide only on *the most important* strategic issues. The personal responsibility of the manager is not supposed to be diminished.

The declared objective of these latest changes is to separate the institutions where economic activity takes place from those where economic policy is made. The rights of the authorities to dispose of economic resources are to be abolished and their power restricted to legal monitoring of the enterprises. The central authorities no longer will be able to examine the appropriateness of enterprise decisions, but only their legality. Some rights of disposal of state property, hitherto controlled by the ministries, are to be transferred to the new enterprise councils.

This new regulation, just as the creation of small enterprise forms, is designed to increase the incentives for the workers and for management by creating a proprietorship interest. For the first time, the state is willing to alter ownership rights in a very ideologized area of the national economy by means of cooperative ownership in industry. The regulation is supposed to end the hierarchical control and surveillance of the enterprises by the state. In the future, the control retained by the ministries is supposed to be clearly related to economic processes and not individual economic units. The regulation will expand the autonomy both of the small enterprises and of the bigger economic units.

Most of these *intentions* with regard to economic policy have, however, existed in Hungary practically since the beginning of socialist development, illustrating how difficult it is to actually implement new regulations in a centrally planned economy. Because of the interdependence of organization of the national economy, old principles may emerge under the surface and reassert themselves.

—Dr. Zolton Sobov
Research Fellow
Free University
West Berlin

TODAY'S OIL SURPLUS IS TOMORROW'S OIL IMPORT CRISIS

"In my opinion, this country is reaching toward a severe economic crisis, as well as an imposition on our national security by our not doing everything possible to increase our domestic production now. To continue along the downward exploratory curve, which we are now experiencing, will surely result in economic chaos. The impact of an energy shortage in this country would be absolutely disastrous.

"Unless there is an appreciable and sustained turn-around in our exploratory activities, I can safely predict that soon we will have an energy crisis in this country that will cause repercussions throughout the width and breadth of this great nation of ours like a devastating earthquake."

Those are the words I said on November 3, 1960, as I concluded a speech in Los Angeles. Unfortunately, the prediction came true with the 1973-74 energy crisis. What I said then applies today. The present volatile energy price and supply situation has many aspects of comparison with the energy dilemmas we faced in the '60s and '70s.

Domestic oil production is falling; drilling is down to a dramatic low equal only to that of the mid-'70s; our oil imports are gradually increasing; companies are going under; massive layoffs are regular occurrences; and budget cutbacks in exploration and production, as well as in research and development, are reported almost daily.

Instead of letting thousands of employees go and drastically cutting back on exploration, companies could take a lower profit and still maintain employees and sustain reasonable and effective exploration activities. In this way, they could build for the future. Such, unfortunately, is not the case and when the turn-around comes, those same companies will not have the benefit of experienced professionals. Instead, they will be forced to hire inexperienced and untrained personnel. Greater sums will be spent on trying to catch up than were saved by cutting back.

As our domestic oil production dwindles and companies further reduce their exploration programs, our imports of crude oil and products from foreign nations will increase. In as little as 36-48 months, we could become as much as 75 percent import-dependent. How could this happen so fast? It's really very simple. With oil prices at uneconomic lows, many U.S. stripper wells will be abandoned—and once abandoned, they're gone forever as resources for the nation. Some 14 percent of our current production is from strippers. Deduct the millions of barrels of oil that *could* have been produced had we been exploring for new reserves, and another shortfall appears. Today we import roughly 5 million bbl/day of crude oil; we produce around 8.9 million bbl/day and draw down approximately 2 million bbl/day from inventories. Our consumption is estimated at roughly 16 million barrels of oil each day. A 50 percent import dependence would be fast arriving. From that point, it would be only a matter of time until imports set record highs and America is once again at the mercy of foreign cartels.

Our domestic petroleum is the only available dependable supply. Other sources are subject to nationalization, expropriation, confiscation by exorbitant taxation, the caprice of foreign sovereigns, war, and other emergency disconnections.

A shift in oil import dependence translates into danger for the country as a whole, and especially has an impact on our national military security. Without secure petroleum supplies to fuel our military complex, we are at a disadvantage among world nations in the event of hostilities or outright war. If our domestic petroleum industry cannot provide those secure supplies, we would stand little chance of sustaining, much less winning, any confrontation.

The world still runs on oil energy, and it will for decades to come. As a result of lower oil prices, most of our alternate energy research and development projects have been curtailed or cancelled. Our nuclear power policy is ludicrous, prohibiting nuclear energy from taking its valuable place in our energy markets. Restrictive fuel use regulations further hamper development of increased energy security. And with the fall in oil prices, other energy resource prices also lose ground.

The petroleum industry, which is so vital to our national security, must be strengthened instead of weakened. To stave off the possibility of another oil crisis we must take immediate and responsible measures. Legislation, which has been proposed by Congress, toward removing the onerous, punitive and counterproductive regulations and laws of past years must be supported, and those proposals that would harm the industry and the country in the long term must be opposed.

If we don't defuse the time bomb associated with the continuous drop in domestic exploration, we will be faced with another, far worse crisis of oil price escalation and oil import dependence the likes of which we have never seen.

—Michel T. Halbouty
Chairman of the Board and CEO
Michel T. Halbouty Energy Co.

THREE MYTHS OF PROTECTIONISM

Myth 1: The trade deficit causes unemployment.

The effect of our unilateral free trade policies has been a decline in employment.
Senator Jesse Helms (R-N.C.)

One million apparel and textile jobs have left these shores since 1972 as a result of low-priced imports—and a million more are at immediate risk.
Sol C. Chaiken
President, International Ladies' Garment Workers' Union

Since 1974, we've lost two-and-a-half million American jobs to foreign competition.
Lee Iacocca

If there is any correlation between the trade deficit and jobs, it is the opposite of that suggested by protectionists. Between 1980 and 1985, the merchandise trade deficit went from $25.5 billion to over $100 billion. During that same period, eight million net new jobs were added to the U.S. economy. We lost jobs in some sectors, but more than made up for the losses elsewhere.

Compare this to the job situation in Europe. The Europeans generally maintain higher trade barriers than the United States, in large part to protect their domestic industries and domestic employment. Many industries are nationalized, and it is nearly impossible to lay off or fire workers. One might think that the job situation in Europe is pretty good, with so much state "protection." Just the opposite is true. Western Europe as a whole has *lost* between two and three million net jobs since 1975. During the same period, the United States added over 20 million net new jobs.

Protectionists like to point to workers in factories who, they say, will lose their jobs to foreigners without trade restrictions. But the protectionists fail to count the number of jobs lost elsewhere in the economy because of these restrictions. For example, the Congressional Budget Office estimated in 1984 that a "domestic content" bill that would prohibit the sale of most foreign cars in the United States would have cost the U.S. economy a net 66,000 jobs. Current attempts by Congress to limit the import of textile products would cost some 60,000 jobs in the retail sector alone. Trade restrictions inevitably cost more jobs than they save.

The ability of an economy to employ additional workers, at ever-increasing wage rates, is dependent on increases in overall economic productivity. Free trade means we can purchase more for less. Capital and labor are freed for higher valued enterprises. The resulting increased productivity will mean that labor becomes more productive and in greater demand.

Myth 2: The United States is a free trade country. It is others who practice protectionist policies.

The United States has permitted imports to gush ashore freely while not demanding comparable access abroad.
Senator Lloyd Bentsen (D-TX)

In the past, the United States blinked at other countries' trade barriers even though our markets are among the most open in the world.
Senator Robert Dole (R-KS)

Free trade is quickly becoming a one-way street.
Representative Morris Udall (D-AZ)

While the United States has freer trade policies than many other countries, it is by no means a sterling example of the free trade philosophy. America uses tariffs and quotas to restrict such goods as steel, autos, textiles, motorcycles, books, sugar, and peanuts.

It is estimated that auto quotas in 1984 cost U.S. consumers between $5 billion and $8 billion in higher car prices. The U.S. steel industry has received periodic protection since the late 1960s. The result: the industry failed to invest in modernization and now has pressured the Reagan Administration into forcing "voluntary" restrictions on steel imports from most steel-producing countries.

Sugar in the United States costs around 21 cents per pound wholesale, 700 percent over the market price, due to trade restrictions. Recently, U.S. customs officials stopped the entry of frozen Israeli pizzas and Korean egg noodles, each of which contains no more than one percent sugar. It was felt that this sugar was getting into the country around U.S. trade restrictions.

The U.S. textile industry provides the most glaring example of U.S. trade protectionism. The United States has placed multilateral restrictions on foreign textile and apparel products since 1961. These restrictions have grown ever tighter over the last decades. Today it is estimated that these restrictions cost U.S. consumers at least $23 billion and perhaps as much as $38 billion per year in higher prices. Recent congressional attempts to further restrict textile trade would add $14 billion, and perhaps as much as $28 billion, per year, to consumer prices.

Those who fulminate against foreign protectionism should remember that our own house is not in order.

Myth 3: The United States need not fear retaliation.

Japan can take action against the United States only by shooting itself in the foot.
Owen Bieber, United Auto Workers

The most devastating trade war in our history occurred as a result of America's Smoot-Hawley tariff, signed into law in 1930. This huge increase of import duties was the final push needed to set off a decade-long, worldwide depression. In reaction to U.S. trade restrictions, other industrialized countries quickly restricted their own markets. This "beggar-thy-neighbor" policy was meant to protect jobs and productivity in the various countries. The result in the United States was a 66 percent decrease in both exports and imports between 1929 and 1933, a 50 percent reduction of GNP during the same period, and unemployment at 30 percent.

Since the end of World War II, the free countries of the world have moved towards a more open trading system. Yet the threat of retaliation for restrictions on trade remain real. For example, in 1983, China cut off purchases of U.S. wheat in retaliation for U.S. cuts in Chinese textile quotas. This cost U.S. farmers half a billion dollars in sales.

Retaliation against U.S. protectionist measures is now much more likely than in the past because there are so many alternate suppliers for goods that the United States exports. Wheat, for example, can now be purchased from Canada, Australia, France, or Argentina. High tech goods can be bought from Japan and increasingly from European and Asian firms. The larger the number of alternate suppliers, the greater the likelihood of retaliation.

Congressmen who deny that protectionist legislation breeds retaliation should be a bit more self-conscious and realize that *they* are retaliating against foreign trade barriers. Protectionism in Japan has not inspired the United States to open its markets further—indeed the opposite has occurred—so there is no reason to suspect that American sanctions will pry open Japanese markets.

Finally, it should be remembered that many countries do not have strong commitments to free trade. They share the misconceptions of U.S. congressmen about the way the market works. The sight of the United States, the most powerful economic nation in the world, turning to protectionism, will no doubt drive many other nations in the same direction.

—Edward Hudgins

Reprinted with permission from Policy Review, *Winter 1985*

VISITORS, APPEARANCES, BOOKS AND AWARDS

VISITING SCHOLARS

Dr. Walter Oi, Elmer B. Milliman Professor of Economics at the University of Rochester, is a scholar of international stature who has published seminal work in several areas including public utility economics and microeconomic theory. During his two-day stay on our campus, Dr. Oi visited with faculty and students in the Department of Economics, and presented a paper on "Employment Relations in Dual Labor Markets."

Dr. Zoltan Sabov from the Free University in West Berlin was our guest for about a week. The purpose of Dr. Sabov's visit was to discuss with Dr. Pejovich his current research on "The Variations of Property Rights in the Socialist Economies of Eastern Europe."

DIRECTOR'S APPEARANCES

During the last two months, Professor Pejovich presented a paper at the international conference on Analysis and Ideology in Interlaken, Switzerland; gave a seminar at the University of Karlsruhe; participated as a panelist in the Texas Lyceum Conference in Austin; and gave speeches to the Chamber of Commerce luncheon in Garland and the Free Enterprise Education Center Conference in Houston.

NEW BOOK

Dr. Peter Bernholz, professor of economics at the University of Basel and a good friend of the center, has just published an important book: *The International Game of Power,* Mouton Publishers, New York.

CHALK AWARD

Each year, the Center for Free Enterprise and the Department of Economics recognize the outstanding undergraduate student and the outstanding graduate student in economics. The award carries a cash prize of $500, and the students' names are engraved on a plaque in the Department of Economics' office.

This year, the undergraduate award is shared by Thomas Greenwood and Sean Royall. Greenwood has a 3.94 GPA. He spent a semester in London where he worked as a research assistant to a member of Parliament in the House of Commons. He will be working for the Hayne & Boone Law Firm in Dallas. Royall has a 3.76 GPA. Next year, Royall will be working as a Senatorial Fellow in Senator Phil Gramm's office.

The graduate award went to Mark Ahlseen. Ahlseen has established an overall GPA of 3.72. As lecturer in the classroom, he has earned a reputation as one of the top instructors in the Department of Economics.

PATHFINDER

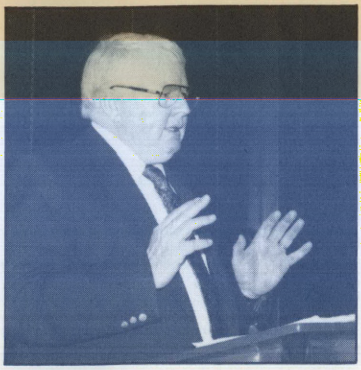
Volume 8, Number 3 July 1986

Published six times a year by the Center for Education and Research in Free Enterprise in cooperation with Educational Information Services, Texas A&M University, College Station, TX 77843. Telephone: 409-845-7722.

Svetozar Pejovich, Director
S. Charles Maurice and Svetozar Pejovich, Editors
Tim Owen, Research Assistant

Contributors of $5 or more received *Pathfinder* for one year; teachers in elementary and secondary schools may receive *Pathfinder* without a donation.

DALLAS CONFERENCE A SUCCESS



Dean Corrigan speaks at the conference.

The Center for Education and Research in Free Enterprise, in cooperation with Highland Park Independent School District, sponsored an economics conference on April 27-29. This conference brought together 27 of Texas' top economics teachers to exchange ideas, thoughts and opinions about high school economics. Its purpose was also to encourage these teachers to act as catalysts for improving the quality of economic education in their respective areas.

Speakers for the conference included Dr. D. C. Corrigan, dean of the College of Education, Texas A&M; Dr. Henry Dethloff, professor of history, Texas A&M; Dr. Winston Power, superintendent, Highland Park ISD; Mrs. H. B. Zachry; Dr. Carl Raba, San Antonio businessman; and Dr. Steve Pejovich. Discussion leader was Jim Lee from Highland Park High School. The conference was a great success. All of the participants expressed their appreciation for the conference and the benefits they received.

Participants and their school districts were: Yvonne Booker, Fort Bend ISD; Bill Bruski, Longview ISD; Noel Corbin, Amarillo ISD; Bud Dunn, Tyler ISD; Marie Farris, Grapevine-Colleyville ISD;

Jack Foley, Bryan ISD; Dorothy Fowler, Ector County ISD; Sandra Haltom, Carrollton-Farmers Branch ISD; Ron Hayworth, Comal ISD; Jess Kirkley, Richardson ISD;

Jimmy Lee, Highland Park ISD; Jim Lund, Clear Lake ISD; Janice Manning, Corpus Christi ISD; Bill Marmion, St. Mark's School of Texas; Patricia Mauldin, Spring Branch ISD;

Mary Meyer, Wichita Falls Public Schools; Rebecca Parks, Eanes ISD; Ron Plunkett, Northside ISD; Linda Reeves, Hurst-Euless-Bedford ISD;

Lottie Repp, Dallas ISD; Kathleen Schock, Northeast ISD; John Wende, Austin ISD; Harold Womack, Lubbock ISD; Pam Young, Houston ISD; Mary Zuschlagg, Alamo Heights ISD; Warren D. Adams, Texas Education Agency.

Comments from participants:

"The notion of bringing economics teachers together from the diverse regions of Texas was wonderful!"

"Our lectures were excellent, and I will be able to use much of the materials in my class lectures . . . ."

"You have been our inspiration. All of us have a deep appreciation for your dedication to the idea of a coordinated network for economic education."

"It gave me the chance to gather teaching information that I would not otherwise have gathered."

"I think it is extremely beneficial for economics teachers to get together in this type of setting to share ideas with one another."

NONPROFIT ORG.
U. S. POSTAGE
PAID
COLLEGE STATION
TEXAS 77843
PERMIT NO. 215

Ms. Tamsen L. Emerson
Texas Documents Collection
North Texas State University Library
P. O. Box 5188 NT Station
Denton, TX 76203