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The Historical Background of the Hungarian Economy

From the Declaration of the Austro-Hungarian Monarchy to the Regime Change

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Abstract

This paper presents an analysis of the economic history of Hungary, from the establishment of the Austro-Hungarian Monarchy in 1867 to the regime change that occurred around 1989. This is situated within the context of a broader study that aims to examine the potential for economic collaboration between the V4+ countries. During the Austro-Hungarian Monarchy, Hungary was a prominent European economic powerhouse, experiencing substantial growth due to the Industrial Revolution and robust economic integration within the Monarchy. However, World War I, the subsequent Treaty of Trianon, the dissolution of the Austro-Hungarian Monarchy, World War II, and the Soviet regime resulted in substantial territorial and economic losses, which had a significant impact on the country's industrial and agricultural sectors and the consequences of this are still discernible today.

Keywords: *Hungarian economy, historical background, Austro-Hungarian Monarchy, Dualism, Industrial Revolution, Regime Change, V4+ countries, economic collaboration*

Introduction

Hungary is considered one of the key economies in the Central European region and the V4+ countries. According to data provided by the International Monetary Fund[1], the country is only considered as a middle power, being the 57th largest economy in the world in 2018 in terms of nominal GDP, and 52nd in purchasing power parity in 2020.

This was not always the case. The Austro-Hungarian Monarchy's establishment in the late 1800s created a favourable market environment for the Hungarian economy. This, combined with the simultaneous arrival of the first and second industrial revolutions at the end of the century, made Hungary one of Europe's leading economies. Yet, subsequent historical events, including the First and Second World Wars, the fall of the Iron Curtain, the formation of the Eastern Bloc, and the Soviet invasion set the country on a course that, despite some countervailing measures, led directly to the devaluation of the former economic superpower.

This study is part of a larger research effort to explore the potential for economic cooperation and to promote the development of possible economic and political collaboration between the V4+ countries. Understanding the historical background of each country's economy is essential for gaining a deeper comprehension of its current economic structures. This supplements the knowledge gained from current economic indicators. The paper aims to explore the historical background of the Hungarian economy, from the establishment of the Austro-Hungarian Monarchy in 1867 to the change of regime. Moreover, it will delve into the economic changes around the turn of the millennium, and will identify the historical events that have significantly shaped the development of the Hungarian economy. The economic structures and policies formed by these events are outstanding as they characterise the country's economy today, particularly in the international economic situation after the COVID-19 epidemic and the Russian-Ukrainian war of 2022.

1. The period of the Austro-Hungarian monarchy

The late 19th century was a significant period in Hungarian history for a multitude of reasons. First, 1867 was the establishment of the Austro-Hungarian Monarchy, which introduced a unique state structure that brought alterations that are still evident today. Second, during the 1880s and 1890s, Hungary experienced the first and second waves of the Industrial Revolution simultaneously. As a result of these two events, Hungary underwent technological and economic changes within an imperial framework.

The uniqueness of the new form of government lay mainly in its duality. On one hand, the Monarchy functioned as a single state in terms of foreign policy and international law, and the empire was indivisible and inseparable under the Pragmatica Sanctio, specifically under Article I; II of the 1723 Act. On the other hand, the security of the region had to be managed jointly by Hungary and Austria, who were considered equal parties, and who both had complete autonomy in their internal affairs.

Accordingly, the countries relinquished part of their national sovereignty. Not only the person of the emperor, but the different ministries concerning military and foreign affairs have become the same. Concerning the financial issues, a quota was set for financing these common affairs, with Austria contributing 70% and Hungary contributing 30%, which was reviewed every ten years. The language of command of the army was also standardized. Nevertheless, both countries had their own parliaments for lawmaking and their own governments for executive power. Furthermore, each of them retained the symbols that signified their independent statehood. For example, they kept their own capital, flag, and anthem while their inhabitants remained citizens of either Austria or Hungary.

This demonstrates that the dualist form of government, commonly referred to as the real union, was more than a typical inter-state relationship or personal union. This merger not only caused a political transformation but also had a significant impact on various other areas, including the economies of both countries. Furthermore, although the Monarchy was dissolved after the First World War, almost 50 years of collaboration initiated political and economic processes that continue to be crucial factors for the economies of the successor states and the Central European region. In addition to political reconciliation, there was also economic reconciliation. This included a customs and trade treaty between Vienna and Budapest, intended to last for a decade and requiring renewal every 10 years. The purpose was to allow the Monarchy's economy to adapt to changing times and correct mistakes from the previous period.

The imperial framework and the customs and trade treaty had a positive impact on Hungary's economy. The reconciliation removed political uncertainty in the Monarchy and boosted the economy. The economic treaty created a customs union between the countries, which formed a unity both inwardly and outwardly, protecting the Monarchy's economy and providing a secure market for Hungarian products through trade with the provinces. Additionally, the treaty facilitated the unrestricted movement of capital and labour between the countries and there was a significant increase in Austrian capital investments in the country, which was further boosted by large-scale state subsidies, such as railway construction and industrialisation.

However, it should not be forgotten that the Compromise also had some adverse effects on the Hungarian economy. The economy suffered from a significant lack of capital, competition, and inequalities within the Monarchy, which led to political disputes. Despite these disadvantages, the economic benefits of cooperation outweigh them. Overall, it can be concluded that the era of dualism brought positive changes to Hungary's economy.

Agriculture

Hungary's agriculture has encountered numerous challenges over the years. A significant lack of capital for modernisation has resulted in some advocacy organisations facing a constant shortage of credit and export opportunities. Additionally, the dichotomy of land tenure structures has taken a distorted and unfavourable form, with the proliferation of small and dwarf estates on one hand, and the creation of huge giant estates through land consolidation on the other. The phylloxera disease epidemic in the early 1880s worsened the situation, affecting the wine grape, and consequently the mainstay of the distillery industry.

Despite this setback, there were significant advancements in agriculture. Due to river regulation and swamp drainage, the proportion of arable land increased by approximately 20%. This led to the widespread adoption of newer farming systems, such as crop rotation and intensive horticulture, as well as industrial crops, new animal breeds, and livestock housing. Additionally, threshing machines were introduced on larger estates by the turn of the century. Furthermore, the damage to the vineyards mentioned above prompted farmers to cultivate new, more resilient vines and to utilise the sandy regions between the Danube and the Tisza, where the phylloxera pest could not survive, as a suitable area for grape cultivation.

Industry

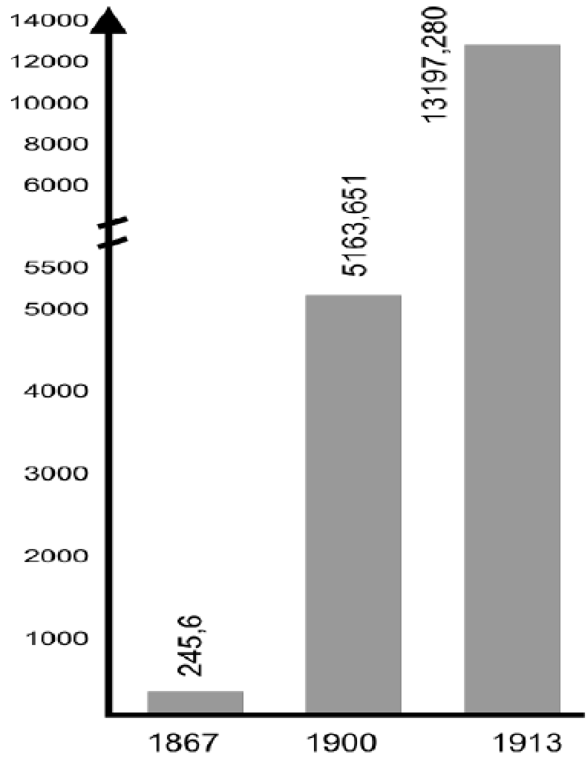
The food industry played a significant role in the industrial revolution in Hungary. The milling industry, in particular, was prominent, with Budapest being the world's largest milling centre until 1900 when it was overtaken by Minneapolis in the United States. The meat industry also experienced rapid growth, with companies such as Herz and Pick, as well as sugar and spirits. In addition to food, Hungary had a prominent mining industry, with rapid growth in coal mining. The country remained the second-largest producer of gold in Europe. Although the country lagged behind Austria and the Czech Republic in light industry goods, the chemical industry experienced a boom after the turn of the century. Major companies such as Richter (1901) and Chinoin (1911) were created during this time.

Furthermore, during this period, the mechanical engineering industry underwent a rise, including shipbuilding, car manufacturing, railway equipment, agricultural machinery and steam engines. The electrical and electrotechnical industries flourished, with the establishment of the Ganz Electricity Works in 1877, which from 1881 became one of the most important power generation and street lighting companies not only in the Monarchy but in the whole of Europe. In addition, the military industry was established with the Weiss Manfréd canning factory producing first ammunition magazines and then military equipment. Moreover, In 1913, a cannon factory was set up in Győr as a joint venture between the Krupp Works and Skoda.

The impact of the Industrial Revolution

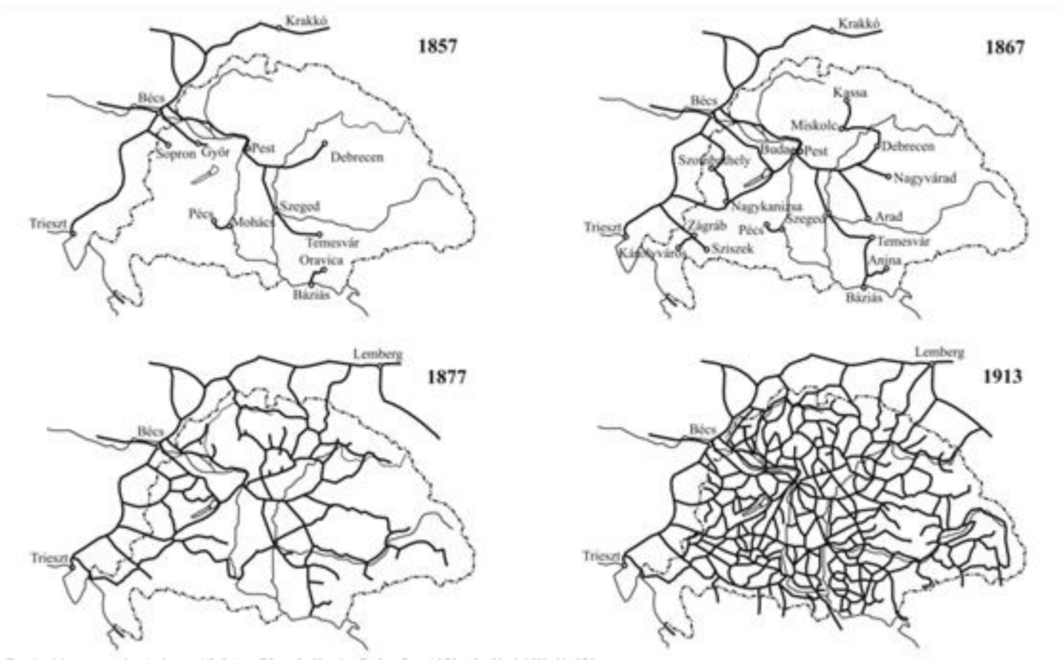
The "delayed arrival" meant that the industrial revolution in the country needed state support, and the level of state intervention increased after the crisis of 1873. The distribution of subsidies between agriculture and industry was the source of serious disputes and considerable social tensions, because part of the landed classes was interested in agriculture, which had previously been the dominant sector, while another significant layer was interested in the new industries that were booming. In addition, the state required a significant amount of capital for subsidies, which could only be raised from abroad due to the lack of domestic capital. Therefore, the development of infrastructure was essential.

To achieve this, the domestic financial system had to be restructured, creating a new banking and credit system that could provide a financial basis for further infrastructure development. The state established five large banks using foreign capital. These banks became part-owners of major joint stock companies through equity investments, provided state loans to companies, and secured credit for trade and transport development.



The capital stock of credit institutions in Hungary during the period (million kroons)[2]

Transport, particularly railways, has become a crucial sector for developers, making it a highly profitable form of investment for private companies. However, private railways have often varied in their development and construction, leading to compatibility issues. As a result of the crisis of 1873, the Hungarian railway system was nationalised and unified by the Minister of Transport, Gábor Baross. This led to the establishment of the Hungarian State Railways (MÁV), which continues to operate today. Thanks to the increase in railway construction and Baross's intervention, the number of railways multiplied between 1867 and 1913. By the early 20th century, the most dense railway network in Central Europe had been built, which later played a vital role in the mobilisation of soldiers during World War I. In addition, Hungary made significant progress in flood control and river regulation, resulting in the construction of Europe's most extended system of dams in just a few decades. This development greatly boosted shipping, making the Danube an international waterway. The Adriatic Shipping Company, founded in 1881, also enabled maritime shipping from the centre of Fiume.



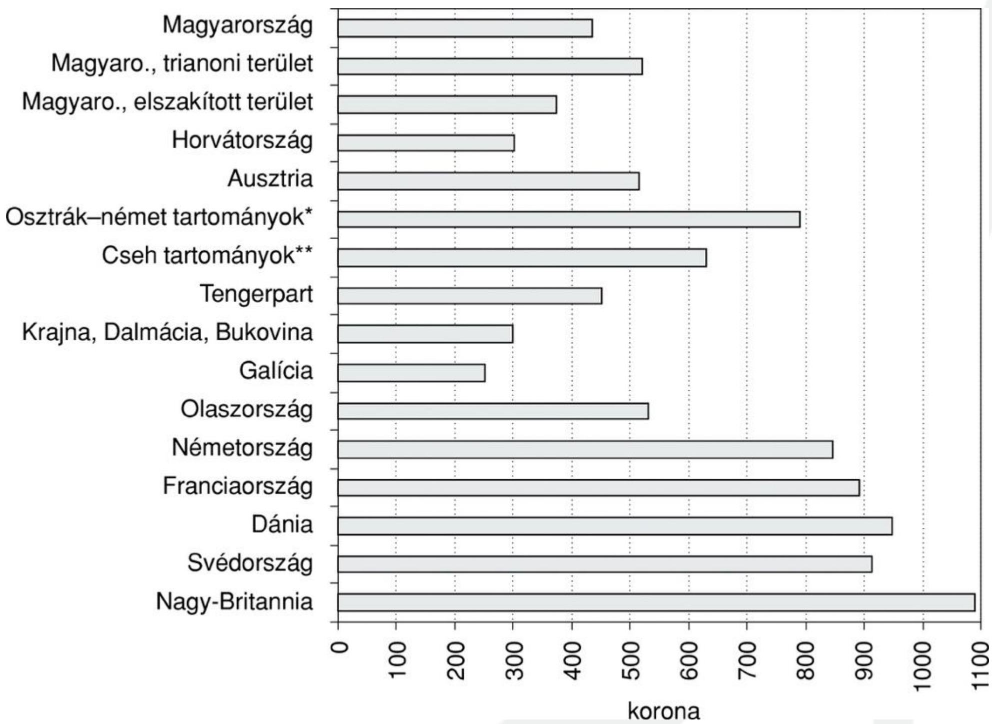
Development of the Hungarian railway network[3]

In terms of the distribution of economic areas, Budapest stood out as the country's economic centre, with a strong industrial area around it, the world's second largest milling centre and the convergence of the railways. Alongside the capital, two other major industrial regions during this period were Gömör and Krasso-Szörény counties. Moreover, important heavy industrial cities such as Kassa, Timisoara, Brasov and Győr were formed.

Overall, Hungary's economy underwent remarkable change and development during the dualist period. The economy was unified, and the various regions complemented each other, maintaining lively links through railway lines. The economic structure of the country was transformed, and the agrarian economy of 1867 had become an agro-industrial one by 1910, outstripping the European average in terms of growth. Nevertheless, this rapid and harmonious development was slowed down by political developments at the beginning of the 20th century and completely stopped by the First World War. Overall, if the First World War had not broken out and interrupted the development of Hungary and the other countries, the Austro-Hungarian Empire had the potential to become one of the greatest economic power in Europe.

Performance of the economy in %			
	1867–1870	**1900**	**1913**
Agriculture	79,0	63,6	61,9
Mining and smelting	2,0	2,7	2,2
Manufacturing industry	7,0	16,2	19,1
Small industry	6,0	5,7	6,6
Trade and transport	6,0	11,8	10,2
Total	100,0	100,0	100,0

The development of the Hungarian economic structure in the dualism era[4]



Gross domestic product (GDP) per capita in 1913, in Austro-Hungarian crowns[5]

2. The impact of the First World War on the Hungarian economy

The fall of the Austro-Hungarian Monarchy

After the First World War, the political landscape of the world underwent a radical change. The most significant transformations occurred in Europe, where several empires, including the Austro-Hungarian Empire, collapsed and were replaced by smaller buffer states. This had a significant impact on the Hungarian economy and its development. Regarding the Austro-Hungarian Monarchy, it is crucial to note that while the war was the primary catalyst for its disintegration, there were three main factors contributing to its break-up, two of which had already begun before the World War.

Firstly, in the 19th century, states such as Romania, Serbia, and Italy emerged along the borders of the Monarchy. These states sought to exploit the outcome of the war to further their irredentist aims and claim ethnic and historical rights to annex the territories of Hungary and the Monarchy.

The second major factor was the increasing aspirations of the nationalities for independence, which had been growing since the beginning of the 20th century. During the world war, leaders of individual nationalities formed organizations to express their desire for secession. The Yugoslav Committee was the first of these, representing the southern Slavic peoples of the monarchy in 1915. It was followed by the Czech National Council in Paris in 1916 and soon after by the Czech National Council in 1917, also in Paris. The Polish National Committee was established in Paris in 1917. That same year, the Corfu Declaration was issued, in which the Yugoslav Committee agreed with Serbia on a state uniting the peoples of southern Slavs. In April 1918, the nationalities of the Monarchy formed the Congress of Rome (of the oppressed peoples), whose main aim was to achieve complete independence.

Thirdly, during the war, the international situation changed significantly, giving new leeway to territorial acquisitions and secessionist ambitions. The war aims of the Entente countries did not initially include the dismemberment of the Monarchy into new nation-states, and therefore did not support all separatist ideas, such as those of the Czechs and Poles. However, they did support the Romanian and Serbian movements due to the alliance with Romania and Serbia.

In 1916, however, a turning point occurred as the Monarchy came under increasing German influence, and it was feared that it could no longer play the balancing role in European politics that it had done. As a result, the Entente was no longer interested in keeping the Monarchy together. The international situation became favourable to nationalist aspirations, and the newly formed national councils declared their secession from the Monarchy[6]. In 1918, Emperor Charles attempted to prevent a complete break-up of the Monarchy by proposing a confederation of independent nations in his October Manifesto. However, this attempt failed due to the increasing demands for national self-determination.

For Hungary, the consequence of these was that the economy, which had begun to flourish within the framework of the imperial state, had to face the consequences of the war and the Trianon peace treaty within the framework of a nation-state.

The Economic Consequences of the Treaty of Trianon

Following the end of the First World War and the collapse of the imperial background that had previously provided a favourable economic environment, Hungary underwent significant territorial losses, as a result of which it lost two-thirds of its population and territory, and the economic structure of the country changed significantly.

The fall of the Austro - Hungarian Monarchy[7]

Due to the territorial decoupling, a significant portion (62%) of the vineyards, which were essential for agriculture, remained within the country's borders, while 89% of the forests were lost. Moreover, the industrial sector has undergone significant changes, with only 2,078 out of the original 4,688 factories remaining in the country. As a result, industrial production has declined to 56% (Mátyus - Bori, 2016). Additionally, industries have been forced to rely on imports to compensate for the scarcity of raw materials and ore metals (Domonkos, 2021). Another issue is the shift in the proportion of industry and industrial districts. Several industrial districts around Budapest, which previously supplied the entire Monarchy, became oversized after the Treaty of Trianon.

The new borders also had an impact on the infrastructure network. The losses in this area were not due to the numbers but to the upheaval of the structure. For instance, the spider web-like railway lines were affected as the transversal lines connecting the main lines in the centre of Budapest were disconnected, making rail transport more difficult in peripheral areas. As a result, access from the north-east of the country to the south is only possible via Budapest. After the war, Hungary lost its coastline, which eliminated maritime shipping and trade. Dealing along the Danube became more complicated as the river route, which had been largely within a single customs border, now passed through several countries with their own customs borders. As mentioned in part above, trade has also been reorganised. An excellent example is the timber trade, where Hungary was an exporter before 1920, but after Trianon, it was dependent on imports.[8]

Overall, after Trianon, Hungary's economy became more open and vulnerable, at a time when the number of customs borders in the region increased, tariffs rose and the former allies in the Carpathian Basin mutually closed themselves off from each other, but most of all from Hungary. Therefore, besides political stabilization, the consolidation of the economy was one of the most important priorities of the post-war Hungarian leadership.

Economic Policies Between the Two World Wars

During the post-war period, under the premiership of István Bethlen, political consolidation could only be achieved in conjunction with economic stabilisation. However, significant efforts were required to achieve this, due to the burdens of the First World War, the war economy, the economic blockade of the Entente, the revolutionary period, and the subsequent Romanian occupation. These events caused great losses and crises in the Hungarian economy, with economic sectors performing at less than 50% of their pre-war level. Additionally, the crown was increasingly inflated, and the pre-war economic external relations and market of the Monarchy practically ceased to exist.[9]

The Teleki government and, initially, the Bethlen government attempted to address the economic crisis through anti-inflationary measures, tax increases, and self-reliant fiscal policies. But from 1921 onwards, after these policies failed, the government changed its strategy and tried to stimulate the economy by creating a new, deliberately controlled inflationary conjuncture.[10] The bank squeeze was implemented, and the state provided economic agents with not-valorizable loans, which are loans not fixed in terms of loan-to-value ratios. This increased business activity and, with inflation rising, there was no issue later in repaying the nominal value of these loans. Additionally, like other European countries, Bethlen limited the volume of imports, thus protecting the domestic market and supporting market access for domestic companies.

Although deliberate inflationary policies and a revival of investment lifted the Hungarian economy out of its trough, they placed a significant burden on society. High inflation has led to a rapid depreciation of wages. Therefore, to maintain economic progress and social stability, it was necessary to curb inflation, which required fiscal consolidation for what the country needed foreign loans.[11] In 1922, Hungary joined the League of Nations and the following year, the Bethlen government requested a long-term loan from the League of Nations. After extensive negotiations, the League of Nations granted Hungary a long-term loan of 250 million gold crowns[12] with a relatively high interest rate. The loan was taken up by the Magyar Nemzet Bank, which was established in 1924 to manage monetary policy. With the assistance of the loan and the new monetary policy, Hungary was able to bring inflation under control. As a final step towards stabilisation, Hungary introduced the new, stable, gold-based currency, the *'pengő'* in 1927.[13]

Following consolidation, the Hungarian economy experienced rapid growth. However, opportunities were largely determined by the new economic environment created by the Trianon peace treaty. In terms of industry, output in 1929 was 12% higher than in 1913. Sectors that had previously been at a competitive disadvantage under the Monarchy, such as textiles and clothing and leather, made spectacular strides forward, and new sectors such as chemicals, pharmaceuticals and electricity boomed,[14] while some factories and products, such as Ganz motor trains and Orion radios, became competitive on the global market. In contrast, the food industry, agricultural machinery, and vehicle manufacturing have declined in the country or lost their former importance due to a shrinking market.

	Percentages of industrial output		
	1913[1]	1929	1938
Iron and metal industry	15.5	11.3	14.2
Engineering	13.8	10.2	9.7
Electric power	1.5	4.2	4.4
Building materials	4.3	4.8	3.7
Chemicals	7.8	7.4	9.7
Predominantly producers' goods	42.9	37.9	41.7
Textiles	4.8	14.2	15.3
Clothing	1.5	2.2	2.4
Leather	2.7	3.2	3.9
Wood	2.5	3.2	2.5
Paper	0.6	1.2	2.1
Printing	2.6	2.4	1.7
Predominantly consumers' goods	14.7	26.4	27.9
Food processing	42.4	35.7	30.4

Note: on the 1920 territory, calculated in current prices.

Hungarian industrial production by branch in 1913–1938[15]

In fact, post-war agriculture stagnated[16] with its production value by the end of the 1920s was only 1.2% higher than before the war, and its weight in the national economy steadily declined,[17] since in 1929 it contributed only 38.5% of national income. Moreover, although the level of mechanisation was increasing, it was still far below that of the developed Western countries.[18]

The Great Depression of 1929 severely impacted the Hungarian economy, interrupting the process of economic reconstruction and causing a prolonged agricultural and credit crisis. Industrial production also began to decline. The agricultural sector faced difficulties due to falling prices on the world market, with wheat prices dropping by 70%. This led to a shift in the price ratio between agricultural products and manufactured goods, favouring the latter. In 1930, the crisis in agriculture was followed by an industrial crisis. The main cause of the latter was the contraction of the domestic market, which led to a sharp decline in the production of iron, metal, machinery, construction materials, and wood. On top of this the country was hit by a financial crisis in 1931, when international credit became completely unavailable. To prevent national bankruptcy in the summer of 1931, the Bethlen government implemented a three-day bank blockade and introduced a currency peg. This involved freezing gold and foreign exchange reserves, abolishing the free convertibility of the pengay, and restricting foreign exchange transactions related to foreign trade to the Magyar Nemzeti Bank. In addition, a covert devaluation of the currency was undertaken, as an open devaluation would have increased the amount of public debt.

Although the measures introduced improved the economic situation slightly, they were not sufficient. As a result, István Bethlen resigned as Prime Minister. He was succeeded by Count Gyula Károlyi, who suspended the repayment of foreign loans in December 1931. However, the recovery from the crisis finally began in 1932 under the premiership of Gyula Gömbös. In the summer of 1932, Hungary's reparation obligations were abolished and in 1934, after Gömbös's negotiations in Germany, Hungary signed new treaties with Germany (German-Hungarian trade supplementary agreements 1933; 1934), Italy and Austria (the so-called Rome Protocols of 1934), which provided secure markets for Hungarian agricultural exports.[19]

After the crisis, mixed farming replaced one-sided cereal production in agriculture. Traditional fruit-growing districts, such as 'Szatmár', famous for its plums, or 'Szabolcs', known for its apples, were established. Furthermore, the industry received a boost from the production of motor vehicles, which was further boosted by the surge in military orders in the late 1930s, patents for incandescent lamps and the production of optical instruments, which became a leading industry, while both the chemical and oil mining industries grew rapidly.

In spite of all this, in the economic development of the 1930s, the increasingly strong German orientation became very important. All in Hungarian-German and Hungarian-Italian and Hungarian-Austrian economic relations, there was a shift to clearing, which in bilateral relations meant the pursuit of a currency-free trade balance. The parties mutually traded goods, with Germany supplying industrial goods in exchange for Hungarian agricultural products, and only at the end of the year did the settlement take place. The remaining difference in trade was settled in foreign currency. This system of relations made Hungary, together with the other states in the region, dependent and vulnerable by the end of the 1930s, since more than 75% of Hungary's foreign trade in curricula commodities was with Germany, while the German side was less and less compensated for Hungarian exports and delayed in restoring the balance in foreign currency. In this way, Hungary and the other states in the region were effectively providing commodity credit and becoming servants of the Third Reich. The resulting unequal structure, which was highly disadvantageous for the servicing economies, laid the foundations for the economic situation in the countries of the region, which was further aggravated by the Second World War.

3. From the Second World War to the Regime Change and the Millennium

Characteristics of the Kádár regime

Following the Warsaw Pact of 1955 and the 1956 revolution, the Kádár regime implemented significant changes to both the political and economic landscape of the country. In terms of agriculture, the government abolished agricultural levies, but reintroduced collectivisation in three stages: first in early 1959, then in the winter of 1959-60, and finally in the winter of 1960-61. To convince the public, the government employed a mix of restrictions and compromises that aligned with the 'old-new' system it had implemented, with the primary goal of improving living standards. Furthermore, socialist state model farms were established in various municipalities, including 'Bábolna', and measures were taken to maximize agricultural productivity. Firstly, an energy programme was implemented to increase coal and oil mining. Secondly, efforts were made to boost the production of raw materials to replace imports. Thirdly, the industry underwent structural changes to modernise. However, the country's economic dependence on the Soviet Union grew disproportionately. Despite supplying the Soviet Union with large quantities of agricultural products and finished goods, Hungary gets only cheap raw materials from Moscow.

In 1967, supporters of economic reforms within the leading party (MSZMP - Hungarian Socialist Workers' Party) gained strength. From January 1968, they established a new economic mechanism. The central idea of the new system was to introduce some aspects of the market economy into the Hungarian economy in order to achieve socialism. Hence, the planned economic system was relaxed, allowing enterprises to operate based on market conditions. The state introduced new subsidies and deductions. In agriculture, the cooperative form was recognised as equal to state ownership. Secondly, the previously artificial price relations were adjusted to the market, but the prices of basic foodstuffs and energy were retained in their former maximum or fixed form. Thirdly, a new wage system was introduced to incentivise higher productivity at both individual and company levels.

Notwithstanding that the reforms successfully boosted the economy, they were halted in 1972. This was due to Hungary being left alone in its reform attempts after the Prague Spring, and the so-called 'hidden capitalism' also faced significant ideological opposition. The shutdown occurred during the most challenging period as the global market boom of the 1950s was disrupted by the oil price explosion of 1973. Despite the Hungarian government's efforts to demonstrate that the boom had no impact on the domestic economy, exchange rates deteriorated, energy prices increased domestically, and the country began to accumulate debt.

To address these issues, the government implemented several measures with varying degrees of success. The increase in energy prices prompted the initiation of several large-scale projects, including the 'Eocene Programme' in 1976, aimed at enhancing lignite mining. However, most of these projects failed to meet expectations. As the problems worsened and the second oil price boom came in 1979, the government implemented major austerity measures. Prices of basic foodstuffs rose, imports were restricted, and the possibility of rescheduling loans was raised due to the country's indebtedness. But it was ultimately not implemented, as it would have meant admitting insolvency.

Hungary's gross debt in convertible currencies (in thousands of millions of dollars)

1970	1,000	1980	9,090
1971	1,511	1981	8,699
1972	1,867	1982	7,715
1973	2,315	1983	8,250
1974	3,105	1984	8,836
1975	3,929	1985	11,760
1976	4,531	1986	15,086
1977	5,227	1987	17,739
1978	7,586	1988	17,349
1979	8,300		

Source: Economist Intelligence[20]

All this, combined with an unfavourable international situation in the early 1980s (Soviet intervention in Afghanistan and Polish strikes in the 1980s), led to a further deterioration in the country's economic situation. In 1982, Hungary joined the IMF without consulting the Soviets in order to obtain additional loans, but the steady rise in living standards over the previous two decades could not be sustained, and the economy was no longer able to meet consumer demand (travel, consumer goods), so the system needed further reforms. Therefore, from 1980, small enterprises using company resources, i.e. economic work communities, were allowed to be set up in state-owned enterprises, providing workers with additional income outside official working hours. From 1984, a series of measures were prepared to introduce market conditions into the system, with the aim of building a market economy based on mixed ownership. These included the bankruptcy law, personal and income tax and the restructuring of the entire banking system. As a result, macroeconomic equilibrium was restored, the government budget was in surplus, the external current account was in balance, gross convertible foreign exchange reserves reached a level equivalent to six months of imports, and growth, albeit modest, returned. However, the turnaround largely reflected a reduction in imports and investment; there was no comprehensive effort to address the structural causes of excess demand, low productivity and the industry's inability to compete in Western markets.

Macroeconomic imbalances resurfaced in 1985-86, and output growth stagnated again. The deterioration was partly due to external factors, such as successive droughts and the weakening of important external markets, particularly in the Middle East. There were also significant terms of trade losses, although at least some of these were due to a failure to shift the composition of output towards sectors with stronger external demand. However, the imbalances were also the result of deliberate policy decisions to loosen fiscal policy. This coincided with renewed efforts at economic reform aimed at increasing decentralisation, enterprise autonomy and reliance on market-based signals. Greater autonomy for firms, together with easy access to subsidies and bank credit, led to wage increases well in excess of productivity growth.

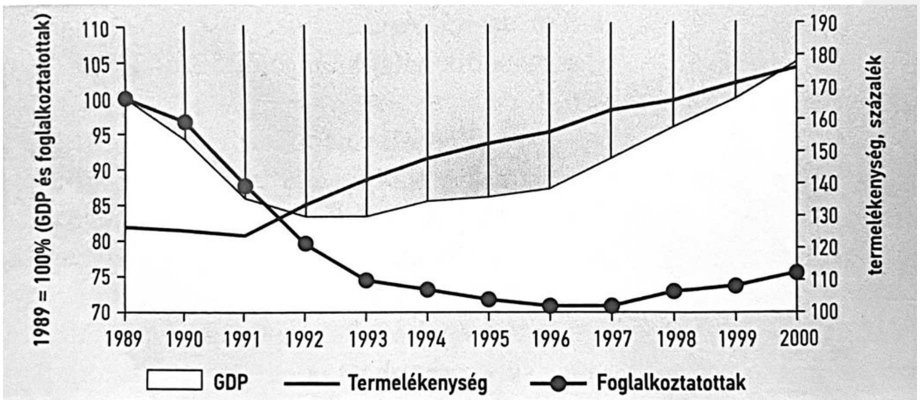
Despite higher taxation of state-owned enterprises, the government's proliferation of subsidies and transfers led to a general government deficit in 1985, which widened to 3.1 percent in 1986. These deficits were largely financed by domestic credit to the banking system, with total domestic bank credit increasing by almost 20 percent in 1986. The disappointing results of 1985-86 continued in the first half of 1987. At the start of the year, the Hungarian National Bank provided generous credit lines to the newly established banks following the introduction of the two-tier banking system. However, due to potential external financing difficulties, the authorities tightened fiscal policy during the year. This led to a significant real depreciation of the forint, with a cumulative depreciation of over 20% in 1986-87. In September, the government presented a three-year stabilisation and structural adjustment programme to parliament. The programme aimed to halt the accumulation of convertible currency debt by 1990.

The transition to a market economy and its consequences

Private ownership is essential for transitioning to a market economy, as opposed to privatisation. According to the classical conception of a liberal market economy, the state's role in economic processes is minimal.[21] In Hungary, the growth of private ownership in the ownership structure began in 1988 with a spontaneous privatization. This process operated on an *ad hoc* basis, based on the companies' own decisions, and was still without conscious central state control. In the 1990-1993s, the Antall government implemented a policy of government-controlled privatization, with the explicit goal of maximizing ownership by the Hungarian population. However, due to a lack of capital and inexperience, this goal was not fully realised and many assets were instead transferred to foreign investors.

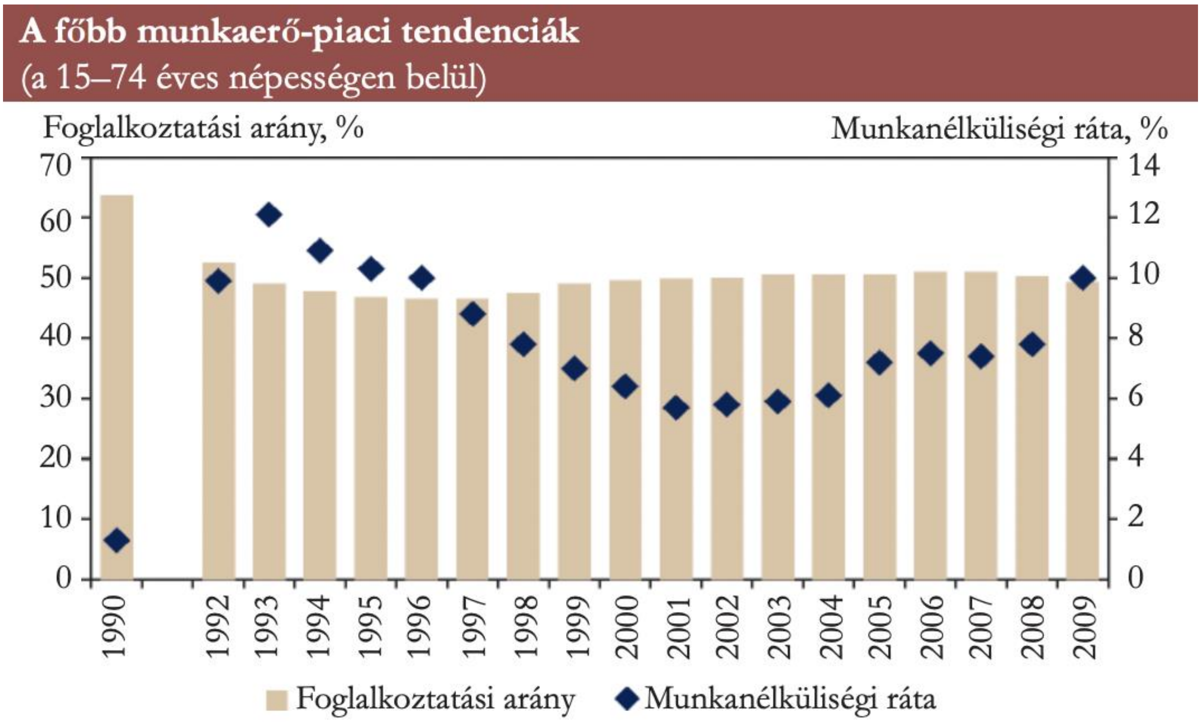
The privatisation process in Hungary was finally completed during the premiership of Gyula Horn (1994-98) following a change of government. Approximately three-quarters of state assets were privatised, and privatisation revenues tripled under the Horn government. Foreign capital gained even more space in the country, with Hungary being the largest recipient of foreign capital in Central and Eastern Europe until 1995, with 55% of GDP generated by foreign companies. Following Germany, the largest investors were the United States, France, and Austria. After a significant increase, privatisation slowed down during the first Orbán government, with only agriculture undergoing major restructuring.

The governments that implemented the transition to a market economy, along with privatisation, were heavily influenced by the regime change in Hungary in 1989 and its consequences for the economy. The change of regime resulted in a significant economic downturn, leading to the closure of many state enterprises, a decline in agricultural and industrial production, and a plummeting GDP. Between 1989 and 1993, GDP decreased by 20 percentage points. Although it began to grow after 1994 due to economic modernisation, it did not reach the nominal level of 1989 until 1999. It is important to note that this GDP was produced by a market economy rather than a socialist system. Its structure has shifted significantly, with a sharp decline of 5% in agriculture and a 28% fall in industrial production, which have been replaced by the services sector, now accounting for 67% of the economy.



Main labour market trends (within the population aged 15-74)[22]

Furthermore, following the change of regime, unemployment rates increased, reaching their peak in 1993 at 12%, before gradually decreasing and stabilising at approximately 6%.



Main labour market trends (within the population aged 15-74)[23]

The change of regime had a significant economic impact, resulting in a sudden acceleration of inflation. In 1991, inflation peaked at 35% and then gradually decreased, with minor fluctuations.

Evolution of consumer prices compared with the previous year[24]

The economy's structure has undergone considerable change as a result. The large socialist enterprises have been replaced by medium-sized and small enterprises better suited to market conditions. Looking at the structure of the largest Hungarian firms, they still include state-owned companies like MOL and BKV, as well as listed Hungarian companies such as Magyar Telekom, OTP Bank, and subsidiaries of large multinationals like Suzuki, Audi, and Philips.

The structure of GDP has also changed, resulting in a shift in employment from the industrial and agricultural sectors to the service sector. Currently, 34% of workers are employed in industry and 60% in services.

The structure of foreign trade has also changed, with an increase in the number of consumer goods imported and a significant share of exports being dominated by foreign firms in the machinery sector, while the share of raw materials in imports remained high. After 2000, the European Union, including Germany, replaced the former CIS countries and the Soviet Union/Russia as Hungary's most significant trading partner in terms of foreign trade. Additionally, Hungary became a member of crucial international economic organizations such as the WTO and the OECD.

Conclusion

Reviewing the past century of Hungarian economic development, it can be concluded that the country experienced a prosperous era during the Austro-Hungarian Monarchy, with advancements in various sectors. Unfortunately, this period came to an end due to the First World War and the Treaty of Trianon, which resulted in a significant economic decline for Hungary. Despite the economic reforms of the 1920s and 1930s that brought the country back into balance, the subsequent period was marked by constant crises. After 1956, during Soviet dominance, the Kádár regime attempted to consolidate the economy. However, international events such as the oil crises and the disintegration of the Eastern Bloc presented constant challenges. Although the change of regime in 1989 had the potential to consolidate the economy in the long term, it only brought further challenges in the first few years.

Overall, the Hungarian economy, after a bright period, has faced nearly a century of struggle, the effects of which are still being felt today. These historical experiences have important implications for current economic policy in the post-COVID-19 situation and the time under the Russian-Ukrainian War. In examining the potential for economic cooperation among the V4+ countries, it is essential to consider the significant difficulties that Hungary has incurred over the past century. In addition to losing a considerable portion of its territory and economic influence, Hungary has also been compelled to undergo a substantial economic restructuring in response to the Trianon decisions and the challenges it has faced in subsequent years. Nevertheless, following the Regime Change, Hungary has made significant progress in strengthening its own economic position and that of the broader Central and Eastern European region. A tangible illustration of these endeavours is the economic collaboration between the V4+ countries. Enhancing this partnership could prove instrumental in augmenting the economic clout of the region and, consequently, Europe's influence on the world stage.

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