The Painful Learning Process of Market Economy: Comparative Analysis of the Economic Policies of Slovakia and Hungary from the Change of Regimes Up to Our Days

Ms. Zsuzsanna Tóth
Ph.D. student
Hungarian Pannon University
45, Jókai utca, Zalaegerszeg, 8900 – Hungary

Abstract

The paper is organised around the question as to what path the economies and economic policies of Slovakia and Hungary have followed for the last twenty years. The two national economies were characterised by different economic and social problems in the analysed period to which they gave different economic political reactions. The paper lists the economic measures and their respective results, and analyses the impacts of the financial crisis of 2008 and the responses given by the two nations in an effort to mitigate the effects of the recession. The conclusion we can draw from the analyses is that the two countries have exchanged their respective economic positions taken up in the convergence process in the past twenty years; the Slovakian economy has become one of the front-rankers while the Hungarian economy has become a laggard from an 'eminent student'.

Key words: *hungary, slovak republic, change of regimes, economic policy, crisis, convergence*

1. Introduction

I was motivated to write this paper by the fact that the economic and social differences between Slovakia and Hungary have undoubtedly become striking up to our days; the period from 2004 to date has brought about far-reaching changes in the two analysed countries. At the end of 2011, Hungary is struggling with a continuously deteriorating macroeconomic situation, while Slovakia, having recovered from the crisis, has started out along a growth path again. The situation was just the opposite prior to and at the time of the EU accession.

2. The past forty years of Hungarian economic policy

2.1. The change of regimes and initial experience

The more than thirty years of creating the market economy in our country were characterised by the duality of measures embedded in the framework of a socialist economic organisation that were meant partly to increase efficiency and partly to inhibit reforms. In Hungary, attempts were taken as early as the 60s to reform the economic system of the time. Within the operative framework of the socialist system several experiments were given the green light in order to step up the efficiency and growth potential of the Hungarian economy; the Kádár administration were striving to develop the private sector and in order to serve this purpose altered the (agricultural) ownership relationships in rural areas. In 1968, as part of the 'new economic mechanism', further attempts at reforms were implemented that ensured a more favourable fiscal environment, widened the scope of those eligible for operating licences and motivated the companies to produce profits by loosening economic regulations.

The positive results of the first five years of economic organisational reforms (the increase in per capita consumption, exports and imports, the decrease in the shortage of parts and the growth in economic performance) are unquestionable, still the investment activities and efficiency failed to increase and the balance of trade was characterised by constant cyclicism and began to show an obvious deficit after 1973 due to the explosion of oil and base materials prices. The need to finance ineffective investments, companies in debt and costs of imports assumed from the households caused not only external indebtedness but also internal imbalances became typical in our country. Slow growth and the appearance of the twin deficit resulted in a further loosening of the legal conditions for private enterprises in the 80s (Balogh et al, 1985).

In 1987, through the transformation of the Bank of Issue, the two-tier banking system was established in Hungary and as a result of the measures introduced between 1989 and 1991 the creation of the market economy commenced in Hungary. The economic and institutional reforms of József Antall, the leader of the first democratically elected government, followed the principle of gradualism but the extent of the state's role still remained significant in the period of transition. The government pursued an expansionary policy favouring growth, which was necessitated by the fact that Hungary's GDP growth had a negative sign between 1990 and 1995 and the rate of unemployment increased gradually while the employment rate reduced. The increase in per capita consumption stopped, real earnings became lower and lower. These problems were coupled with inflationary pressures (Table 1). As a result of the Act on Bankruptcy and the capital injection given to commercial banks in 1992, Hungarian public debt increased gradually.

In parallel to this, besides the measures to facilitate growth, the government also had to comply with the requirements of the IMF due to the loan taken up in 1990. The Ministry of Finance and the Hungarian National Bank define the creation of a stabilisation strategy to improve the public debt structure as its primary task. To this end, they made foreign exchange reserves dependent on external debts management and meant to keep the surplus of the current balance of payments, which attempt had already failed by 1993, and proposed a strict budgetary and monetary control. As a result of this stabilisation policy, the rate of foreign direct investment (FDI) was continuously increasing but was still unable to compensate for the foreign trade deficit. It is the indirect effect of the Mexican 'Tequila crisis' of 1994 that international banks became distrustful of countries with significant external imbalances. Our country's current balance of payments exceeded 9% of the GDP at the time. Furthermore, Hungary's main macroeconomic indicators were also indicative of a crisis.

The increasing rates of unemployment and inflation, the falling GDP and the twin deficit all called for a clear-cut intervention by the state. The required measures were defined by Lajos Bokros, who enjoyed the trust of the IMF, and who, as a minister of finance, put forward one of the most remarkable restrictive packages in the history of Hungarian market economy. The primary aim of the package was to reduce the budget deficit (by cutting back the number of public sector staff, increasing the import duty supplement, increasing taxes and reforming the pension system), and besides this, a further important effort was made to improve Hungary's international competitiveness. In order to achieve these aims, the Hungarian forint was depreciated by 9% in one step and crawling parity exchange rates got introduced. As a result of the series of measures both budget deficit and gross public debt decreased, the balance of payments improved but the negative effects of the restrictions also appeared; internal demand dropped significantly and therefore GDP growth slowed down. Per capita consumption reduced by more than 5% and real wages fell steeply in this period. These restrictive measures carried a positive message for foreign investors and capital inflow remained lively while exports, the only remaining catalyst of economic growth, increased due to the international competitiveness resulting from low real wages. The strict fiscal and monetary policies met enormous social resistance and the Horn administration lost not only the citizen's trust but also the elections in 1998 (Mommen, 2004).

Table 1 - Hungary's major macroeconomic indicators between 1991 and 1997

Description	1991	1992	1993	1994	1995	1996	1997
Rate of real GDP increase (%)	-11.9	-3.1	-0.6	2.9	1.5	1.0	4.3
Consumer Price Index (%)	35.0	23.0	22.5	18.8	28.2	23.4	18.3
Rate of employment (%)	7.5	12.3	12.1	10.4	10.4	9.6	9.0
State budget to GDP (%)	-3.02	-7.24	-7.81	-7.13	-6.42	-3.17	-4.66
Public debt to GDP (%)	51.4	62.9	65.0	72.1	67.5	70.9	59.2
Current balance of payments to GDP (%)	0.8	0.9	-9.0	-9.5	0.2	-1.6	-1.0
ECU/HUF exchange rate as of 1 December of the given year	101.22	101.38	112.44	135.76	178.80	204.89	224.54

Source: IMF and World Bank

2.2. On the upswing

The first months of the new civilian administration were busy with fending off the effects of the Russian financial crisis on the Hungarian financial system; MATÁV and MOL required beefing up and Postabank was clearly in need of being rescued. The improvement of macroeconomic processes was also urged by the IMF and in parallel to this, Hungary's integration in the European Union also started.

The government had to take steps in order to cut taxes and social security contributions, increase the employment rate, harness inflation and the rate of unemployment and curb the budget deficit and public debt. In the first two years of the administrative cycle a positive change occurred in Hungarian macro-level indicators; the inflation and unemployment rates reduced, the balance of the budget improved and public debt, remained at a sustainable level (Table 2) (Mommen, 2004).

Table 2 -. Hungary's major macroeconomic indicators between 1998-1999

Description	1998	1999
Rate of real GDP increase (%)	5.2	4.2
Consumer Price Index (%)	14.2	10.0
Rate of employment (%)	8.4	6.9
State budget to GDP (%)	-4.8	-3.7
Public debt to GDP (%)	61.1	60.0
Current balance of payments to GDP (%)	-2.1	-2.1
ECU/HUF exchange rate as of 1 December of the given year	255.70	254.92

Source: IMF and World Bank

2.3. 2000-2008: the period of mistaken decisions

Boosting economic growth was among the initiatives of the Orbán administration, and in the two years leading up to the elections, they started an expansive economic policy in order to stimulate consumption and thereby increase internal demand. The increase in expenses became more pronounced in the year preceding the elections and the elections of 2002 were again won by the socialist party.

In the following administrative period, the country's economic indicators further deteriorated; the twice 100-day periods of 'allocation' of the Medgyessy administration with the 50% wage increase for nearly 600,000 public servants and teachers, pushed up the budget deficit to GDP ratio from 4.1% to 9.4%. In parallel to this, the structural weaknesses of the budget prevalent since the change of regimes were becoming perceivable. Besides the budget deficit, public debt also increased, economic growth slowed down and this held back exports, the to date propulsive sector of the economy. Export activities fell back and therefore the current balance of payments deficit reached 4% of the GDP and was to be financed by increasing net external debt (Table 3). The start of the EU accession and completion of healthcare privatisation, considered necessary by the IMF and the European Commission, were the achievements of the period (Zádor, 2010). Upon the EU accession in 2004, Hungary assumed the obligation to meet the criteria defined in the Maastricht Treaty and to join the euro zone within an unforeseeable period of time. By this step, our country's integration started and the need to balance external and internal factors has become a major challenge for our state's leaders ever since. In order to deliver upon this objective, restrictive measures have become constant since 2005. Against the restrictions, however, the cyclicism of the budget triggered by its dependence on the elections did not change, the budget deficit to GDP ratio reduced only slightly, public debt was increasing year on year, the domestic currency was continuously depreciating, the quality of the subsystems of the state budget was deteriorated ever further and their sustainability was becoming ever questionable.

The reason for the worsening indicators was that the ruling governments of the time set the economy on a trajectory to increase internal, state and household consumption artificially after leaving the former growth path controlled by exports and investments while encouraging savings. They did so by state subsidies funded from loans and by wage increases exceeding the rate of productivity growth. It is evidenced by the transformation of the schemes to stimulate home buildings and home purchases, which scheme evolved from the high level of social political subsidies and personal income tax benefits introduced by the civilian administration into the 'cheap' foreign exchange loans preferred by the socialist administration and has had its influence felt even to date. They drastically increased the country's indebtedness, worsened its competitiveness and the performance of the domestic economy (Békesi, 2010). After the elections in the spring of 2006, the country's leaders recognised the need for a change, and bearing this in mind, prepared Hungary's Convergence Programme in cooperation with the Hungarian National Bank, which was approved by the European Union in Brussels in September and the Hungarian government was called upon to implement the programme as soon as possible.

Having considered the inherent benefits and drawbacks, domestic and foreign analysts largely concluded that these restrictive measures were unavoidable. Still, due to the inadequate structure of the measures, the rate at which incomes increased was a lot higher than the one at which expenses decreased and there was no guarantee that the programme would yield the expected results or that the danger of reversion would cease. In 2007-2008, the impact of the adjusting measures could definitely be seen; internal demand and the rate of employment reduced and growth faltered.

Table 3 - Hungary's major macroeconomic indicators between 2000-2008

Description	2000	2001	2002	2003	2004	2005	2006	2007	2008
Rate of real GDP increase (%)	6.2	4.1	4.4	4.3	4.7	3.9	0.8	0.8	0.8
Consumer Price Index (%)	9.8	9.1	5.5	4.4	6.8	3.6	3.9	7.9	6.1
Rate of employment (%)	6.4	5.7	5.8	5.9	6.1	7.2	7.5	7.4	7.8
State budget to GDP (%)	-5.2	-11.2	-16.9	-10.1	-6.2	-8.7	-11.7	-6.4	-9.3
Public debt to GDP (%)	54.9	52	55.6	58.3	59.1	61.8	65.7	66.1	72.3
Current balance of payments to GDP (%)	-3.2	-1.8	-2.9	-2.2	-2.2	-1.8	-1.8	-2.1	-2.4
EUR/HUF exchange rate as of 1 December of the given year	264.9	246.3	235.9	262.2	245.9	252.7	252.3	253.3	264.8

Source: IMF and World Bank

2.4. The effects of the global financial crisis

In 2008, the developed world was confronted with the first economic crisis of the 21st century, which, differently from the former one, started with a global financial crisis. As a result of the spiralling crisis, due to the speedy drop in the forint exchange rate, material operating disturbances appeared in the financial markets. Let us only refer to our foreign exchange exposure resulting from the high rate of foreign exchange-denominated mortgage loans. In parallel to this, Hungary was struggling with balancing the budget and revitalising the economy. The socialist government lost it political integrity and after the resignation of Ferenc Gyurcsány, in April 2009, a crisis management government was set up under the leadership of Gordon Bajnai and Péter Oszkó as its minister of finance. The main purpose of the economic decision-makers was to restore investors' confidence and the proper operation of the financial markets. In order to realise this aim, the Hungarian National Bank gradually reduced the prime rate, increased to 11.5% in October 2008, as a direct crisis management measure, to 10% by December 2008 and to 6.25% by December 2009. In order to stabilise the financial system, the government considered implementing the following measures necessary,

- liaising with the international institutions continuously;
- protecting those with foreign exchange-denominated loans;
- modifying certain Acts on supervising the operations of financial intermediaries;
- reviewing the consumer protection regulations regarding clients involved in crediting by banks, and
- creating the forward looking supervisory competences of the PSZÁF (Hungarian Financial Supervisory Authority).

The government continued to implement a strict fiscal policy. Hungary's budget deficit and the extent of public debt narrowed down the opportunities of the Hungarian economy both in the medium term and in the long run and, for this reason, there practically was no sufficient elbow room within the Hungarian budget (Magyar Köztársaság Kormánya, 2009). The main fields and measures of the unavoidable budgetary restrictions are summarised in Table 4.

Table 4 - The measures of the Bajnai administration

Field	Measures
Public sector	* blocking the gross wage bill of the public sector; * removing the 13th month's pays; * reducing municipal supports;
Pension system	* not paying the 13th month's pensions; * removing the 13th month's pension payments from 2010 and introducing a pension bonus tied to the GDP instead; * adjusting early retirement pensions;
Social benefits	* reducing sick benefits by 10%; * reducing the GYES and GYED (types of childcare benefits) period to 2 years; * suspending housing benefits;
Taxes and contributions	* reducing employers' contribution; * increasing the lower limit of the personal income tax; * increasing the VAT rate and introducing a VAT of 18% on basic provisions; * introducing the super lumpsum tax table: increasing the tax base;
Government savings	* reducing the salaries of ministers and secretaries of state by 15%; * reducing the per diem payments to state leaders for their trips abroad; * maximising the salaries of state leaders;

Source: Válságkezelés és bizalomerősítés 2009

In order to maintain aggregate demand and employment, the most important initiative was to accelerate calling down the support from EU structural funds and to use these funds more efficiently. In itself, however, it was too little for Hungary to be able to join a growth path in the short run.

In the elections of 2010 the winning party was FIDESZ-Magyar Polgári Szövetség, whichparty was allowed to form a cabinet with a two-third majority. The government wished to meet a dual challenge,

* to stimulate the economy to reverse the negative GDP growth;
* to realise restrictions and reform the subsystems of the state budget in order to manage internal and external indebtedness.

The current measures are still characterised by this duality, though with changing priorities. However, the efficiency of these policies cannot now be properly analysed for the shortage of the timespan.

Table 5 - Hungary's major macroeconomic indicators between 2009-2010

Description	2009	2010
Rate of real GDP increase (%)	-6.7	1.2
Consumer Price Index (%)	4.2	4.9
Rate of employment (%)	10	11
State budget to GDP (%)	-4.4	-2.5
Public debt to GDP (%)	78.4	80.2
Current balance of payments to GDP (%)	0.4	0.2
EUR/HUF exchange rate as of 1 December of the given year	270.84	278.75

Source: IMF, World Bank and MNB

Analysts are forecasting the following for year 2011,

* GDP growth is expected to increase by about 2 – 2.5% as a result of agriculture performing well against last year.
* The employment and unemployment rates shall probably remain the same and CPI shall be around 4%.
* The state budget to GDP ratio may reach a surplus of 2%. This estimated surplus is, however, due to the nationalisation of the assets in the private pension funds without which the balance would show a deficit of 7%. Due to the one-time character of these incomes and the high risks of their realisation, the excessive deficit procedure was not terminated against Hungary despite the surplus.

* In June the public debt to GDP ratio was estimated at about 75%. As a result of the early final repayment proposal announced by the government in September (those indebted in Swiss francs or euros are allowed to repay their loans at the exchange rate of 180 HUF/CHF or 250 HUF/EUR, respectively) the domestic currency weakened fast – to over 300 HUF/EUR – and the rate of public debt climbed higher than the initial level, to 82% (GKI, 2011).

2.5. The problems of the Hungarian economy

2.5.1. Problems arising from the budget

In the following, the factors and phenomena are described that have lead to the budget deficit the government has been struggling with ever since the change of regimes,

* Extreme redistribution and a high level of reallocation of incomes.. The structure of redistribution is unfavourable; some expenses are far too high while others are lower than desirable in international comparison. Loss-making state-run companies (MÁV, Magyar Posta, Málév, MTV, etc.) trigger enormous expenditures and causes indebtedness for the budget. State subsidies are about 3-5% of the GDP, several times the average rate within the euro zone. The reform of the state budget left the distinction between state-funded and privately funded services unclarified. In free education and healthcare, e.g. gratuity is a widespread practice and therefore a mixed and intransparent funding system has evolved.
* The high percentage and the higher than average pay of public sector employees (about one forth of all employees), which is unjustifiable in terms of productivity.
* The high level and inadequte structure of taxes and contributions as compared with the newly joining countries. Labour-related taxes are high while those on capital and capital gains are low or do not exist at all. The unfair taxation system therefore basically restricts performance, fails to meet the principles of taxation (transparency, simplicity, etc.) and strengthens the black and grey economies and encourages tax evasion. (Gáspár et al, 2004)

2.5.2. The 'semi-peripheral' situation

Hungary has been an open economy since the change of regimes; its export and import activities have been expanding year on year. At least two-thirds of its GDP circulate in the international markets causing difficulties in both exports and imports. Hungary's exports to GDP almost reaches 90% meaning that Hungary's economy is only operable if the goods produced can be sold abroad at such a high rate. Hungary is too much dependent upon Germany and Austria; with the related sales exceeding 40% of total exports, and the slowing down of those two economies restrains the Hungarian economy too. Excess import is dangerous since almost the whole of the domestic economy is partly or wholly dependent on the import of energy, raw materials, semi-finished or investment goods. This exposure to imported interim goods leads to a low-level of competitiveness. It is further worsened by the very high cost of live labour resulting from the withdrawals by the state, and furthermore net wages have continuously increased faster than productivity. Consequently, the efficiency of the Hungarian economy is below that of its fellow EU members'. The 'semi-peripheral' situation also suggests that technical development is 15-20 years behind that of the central countries, production is mostly done by imported technologies, Hungarian R&D costs amount to less than 1% of the GDP (Kozma, 1998).

2.5.3. Labour market and employment rate

In Hungary the unemployment rate shows an average or below average figure as compared with the other EU countries. The low rates of activity and employment pose a bigger problem than unemployment. In the last twenty years, the rate of activity has ranged between 58% and 61%. It is indicative of the fruitless efforts of central and local governments to solve this economic and social issue. We must note, however, that the number of unregistered employees is high and estimated at about one million. Three reasons might explain the inactivity rate of about 40%. Between 1990 and 1994 legal changes allowed for those losing their jobs to leave the labour market (retirements benefits, disabled pensions, etc.); more and more people are engaged in tertiary education postponing active participation in the labour market; an increasing number of mothers receive child care benefits of different types. These groups, however, make up only 87% of the inactive population. The remaining part can be explained by the hopelessness of a job hunt (based on Tárki 2003). The ratio of the economically inactive and active population has fallen back from 50 to 45% in twenty years, which improvement is the result of the gradual rise in the retiring age, but, still one employed person sustains 2.5 others on the average, of whom only 1.6 are not of an economically active age.

The population is continuously aging; within 20 years the percentage of the 0-19 age group per employee has fallen from 0.7 to 0.5 and the same percentage increased from 0.2 to 0.3 for the age group over 65. This may lead to the unsustainability of the pension system in the long run due to the narrowing down of the bread-winning social layer.

3. The Slovak economy from the change of regimes to our days

3.1. Change of regimes and the Mečiar administration

The Slovakian (Czechoslovakian) change of regimes, as opposed to the Hungarian one, is not the result of slow structural adjustment and negotiations by the political elite behind closed doors, but the outcome of a series of protests by the citizens. The attempts at reform, similarly to our country, had already started and in 1968 the negative results of the planned economy, voluntaristic economic management and social dissatisfaction lead to students' protests and the Prague Spring. The Czechoslovakian revolution expectedly met a fate similar to the Hungarian one in 1956; the troops of the Warsaw Pact entered the country and defeated the revolution. After that, Gustáv Husák got at the lead of the Czechoslovakian Communist Party, who, as opposed to the policy of consolidation adopted by János Kádár, followed a strict and dictatorial policy in order to maintain state socialism. This system was ended by the series of protests by the citizens in 1989, the so-called Velvet Revolution, and consequently, in Czechoslovakia, the transition to market economy was realised by an abrupt change, which shocked the community and the economy. The political, legal and economic conditions fitting in with the new system were created in three years and in 1993 Slovakia became independent of the Czech Republic.

The Slovak state although having become economically independent, its economic political institutional system had been left in Prague. Therefore it was forced to face the economic and social challenges without proper experts and experience. The realisation of the structural changes was further encumbered by that the government lead by Vladimir Mečiar did not always act democratically. The government followed a nationalistic, nonconformist Euro-Atlantic politics with the countries within the region then Mečiar, after his third election, recognised that this foreign economic policy could not be continued, and returned to the reform processes started in 1993-and interrupted later and showed more openness towards the European Union later on (Muraközy, 2007).

The independence of 1993 caused a sharp drop in the performance of the national economy, but this one-time effect did luckily not last long and Slovakia produced the largest growth and the lowest inflation rate in the year. This growth was mostly propelled by exports, but the trend changed in the later years and consumption and investment became the driving forces of growth. Between 1993 and 1996 the rate of inflation dropped from 20% to 6%. Consequent financial policy and structural reforms sustained growth and stabilisation. The improvement of macro level indicators faltered in 1996, however (Table 6).

One reason for deteriorating indicators was that in 1989, as the most significant element of structural changes and the change of regimes, privatisation was started. First in Czechoslovakia, then in the independent Slovakia, the system of 'voucher privatisation' operated. It meant that entrepreneurs and managers got the companies directly in exchange of the vouchers issued by the government. Later selling by vouchers was replaced by bond privatisation. The government thereby aimed to create a strong capitalist layer in the country. Still social tensions appeared. Bad morale meant only a minor problem; more damaging effects were caused by the lack of management know-how and capital on part of the new entrepreneurs so taking up foreign loans remained their only option. Consequently, public debt tripled in the middle of the 90s (Muraközy, 2007). The other reason was the fluctuation of Slovak demand in the first half of the 90s, which lead to a trade surplus and from 1995 a trade deficit. Household consumption increased by 7% annually and imports by nearly 20% and in parallel to this, the growth rate of exports slowed down due to stagnation resulting from the cyclicism of the Western-European economies and from weak competitiveness.

With the strict fiscal and monetary measures the budget reached a minimal deficit in 1995, then in 1996 the economic policy assumed an expansive character and in less than two years' the deficit to GDP ratio became 5%. Economic indicators also deteriorated because real wages increased more than productivity. Due to the increase in wages a high rate of unemployment of about 12-13% became constant, and furthermore more than half the unemployed were permanent . The government did not want and was unable to manage impoverishment and the high rate of unemployment. (IMF, 1998).

Table 6 - Slovakia's major macroeconomic indicators between 1994 and 1998

Description	1994	1995	1996	1997	1998
Growth rate of real GDP (%)	6.21	7.87	6.94	4.44	4.36
Consumer Price Index (%)	13.46	9.89	5.77	6.00	6.69
Unemployment rate (%)	14.60	13.70	12.60	11.88	12.61
State budget to GDP (%)	-6.10	-9.90	-6.30	-5.30	-7.40
Public debt to GDP (%)	57.80	53.70	48.90	45.80	48.10
Current balance of payments to GDP	4.30	1.95	-9.92	-8.54	-8.86

Source: IMF, eurostat

3.2. The age of change, the Dzurinda administration

In 1998 Mečiar lost the elections due to aversion to the anti-liberal and nationalistic regime. His place was taken up by Mikulaš Dzurinda, who launched a budgetary adjustment programme right away; he increased taxes and continued the privatisation and resold the assets distributed during the Mečiar era to foreigners. As a result of his strict fiscal policy the economic indicators of the country improved but before the elections year of 2002, the budget deficit soared again. After Dzurinda won the elections again, no further obstacles remained before the adjusting measures based on three key categories,

- The taxation system: a uniform rate of tax was introduced: the corporation, personal income tax and VAT were set a uniform rate of 19%. Minor tax types and personal income tax benefits were removed. This system complied a lot better with the principles of taxation: the system became simpler, more transparent and tax collection easier.
- Healthcare and social benefits: the two state-run insurers were joined by four private ones; hospitals were closed down and visit fees introduced. Unemployment benefits were cut by more than 30% and completely removed for people under 25. In a country struggling with a high rate of unemployment this caused enormous social tensions, in the less developed eastern part of the country even the army had to be called in.
- The labour market: they simplified the employment rules and reduced employers' administrative obligations. The unemployment rate reduced gradually and was also helped by the immense number of people finding
- employment abroad (Gyene, 2008).

Table 7 - Slovakia's major macroeconomic data between 1999 and 2005

Description	1999	2000	2001	2002	2003	2004	2005
Growth rate of real GDP (%)	0.04	1.37	3.48	4.58	4.78	5.06	6.66
Consumer Price Index (%)	10.45	12.20	7.16	3.50	8.43	7.47	2.80
Unemployment rate (%)	16.35	18.76	19.30	18.50	17.40	18.10	16.15
State budget to GDP (%)	-12.30	-6.50	-8.20	-2.80	-2.40	-2.80	-3.20
Public debt to GDP (%)	52.10	44.50	45.10	40.10	37.70	38.00	36.50
Current balance of payments to GDP	-4.79	-3.45	-8.27	-7.87	-5.93	-7.82	-8.49

Source: IMF and eurostat

The appearance of Dzurinda changed the attitude towards Slovak foreign policy too and sent the country along the path to European integration. At the Luxembourg meeting of the EU of 1997, where the concept of EU expansion was revealed, the countries wishing the join the EU were divided into two groups. Active negotiations were started with the first group while with the second group, including Slovakia, the EU could only move towards accession upon further positive changes. These changes did happen in 1998 and, in the following year, Slovakia could also start the specific negotiations on accession. In their attempts for integration the Slovak leaders were deeply hurt by being put into the second group and from 1999 they made every possible effort to join the other candidate countries both in terms of economic and social aspects.

3.3. The Slovak economy before and after the crisis

As a result of Dzurinda's measures the macro-level indicators of the Slovak economy got ever closer to the sustainable level. However, the social and welfare differences got deeper too and, in the elections of 2006, the society disillusioned with the right-wing reforms turned towards the leftist Smer.

Robert Fico's political rhetoric before the elections was about releasing the budget while, in reality, he continued the pragmatic politics of his predecessor and changes only happened in the field of healthcare; he abolished the visit fee and removed the uniform rate of tax for medicine. Fico continued Dzurinda's privatisation process. The Slovak economy improved buoyantly under Fico's leadership. On the improving dynamics of foreign investments industrial development also ran up, which bolstered the employment rate. Obviously the rate of unemployment deceased thereon but it was also helped by the fact that 170 thousand Slovak citizens found jobs abroad. In parallel to the increase in employment rate and wages, household consumption also increased while the rate of investments and state procurements slowed down. The expansion of domestic demand had an inflationary effect but it only appeared in the Slovak economy in the long run. On the output side of the GDP, the vehicle industry and electronics assembly became the engines of the economy and also influenced foreign trade. The slight current balance of payments deficit decreased year after year, exports expanded more than imports. The Slovak economy, because of its strengthening industry, mostly traded in machines and machine parts. Fico, despite the ideological foundations of the two nationalistic governing parties and his at times antidemocratic statements, paid close attention to strengthening the country's ties with the EU and introducing the euro as soon as possible. In this way, Slovakia got close to and has been maintaining the Maastricht criteria since its accession and therefore, of the ten countries joining the EU in 2004, having made up for its earlier shortfalls, has become a front-ranker in terms of nominal convergence.

The stumbling-blocks of the developmental strategy of the Slovak economic policy based on the vehicle industry became apparent as a result of the global economic crisis. Due to the high level of exports exposure, Slovakia's opportunities narrowed down in consequence of the international recession. Slovakia's exports primarily go to Germany and the fallback of the German economy had its effects in Slovakia too. The output of the machine, vehicle and plastic industries shrank by more than 20% in a year and therefore, annulling the achievements of several years' measures (the unemployment rate dropped back to 9.5% in 2008), the unemployment rate reached 12%. That year 110 thousand people lost their jobs and domestic demand consequently fell back so sharply that it caused a short period of deflation. The Fico administration introduced several fiscal programmes to mitigate the effects of the crisis, to increase internal demand and create jobs. In 2008 they introduced a rescue package of EUR 332m to retain workplaces, in March 2009 the scrappage programme totalling EUR 55m. They granted support totalling EUR 500,000 to formerly profitable companies that ran into debts due to the crisis.

These measures required major sacrifices from the budget: the deficit quadrupled in two years. Thanks to the rescue packages and the re-expansion of export opportunities, the Slovak economy entered the development path again; last year it realised an outstanding GDP growth of 4% while the unemployment rate is still very high, at 14% (Túry-Vida, 2010). The elections in 2010 were won by the right-wing coalition government of Iveta Radičová. Currently, the biggest challenge is implementing budgetary adjustment and fighting the nearly 8% budget deficit to GDP ratio. As part of stabilisation they wish to make sure that the extent of redistribution by state would not exceed the rate reached until that date, which is 34% of the GDP. They intend to increase incomes to allow for growth while they are planning to cut public sector salaries by 10% and then block wages and postpone more costly governmental investments. The are also planning to increase VAT by 1% and introduce the bank tax.

Table 8 - Slovakia's major macroeconomic data between 2006 and 2010

Description	2006	2007	2008	2009	2010
Growth rate of real GDP (%)	8.50	10.52	5.82	-4.78	4.02
Consumer Price Index (%)	4.26	1.89	3.93	0.93	0.70
Unemployment rate (%)	13.30	11.03	9.57	12.05	14.38
State budget to GDP (%)	-1.80	-2.10	-8.00	-7.70	-6.76
Public debt to GDP (%)	34.20	34.90	41.50	40.00	41.78
Current balance of payments to GDP	-7.84	-5.26	-6.62	-3.21	-3.46

Source: IMF and eurostat

3.4. The weak points of the Slovak economy

3.4.1. Unemployments

Of the countries joining the EU in 2004, Slovakia was the first to introduce the euro since it had fully complied with the convergence criteria.

The Council of the EU, however, are airing concerns about the high unemployment rate in their opinion on the Slovak convergence programme year by year. The unemployment rate currently stands over 14% in Slovakia and secular unemployment at 9.2%. Joblessness hits the unschooled layer most; this group can only find seasonal employment. The country's labour market is characterised by structural unemployment; on the one hand, we can see enormous differences between the regions, despite any effort, no government has managed to promote mobility significantly and, on the other hand, as far as qualifications obtained are concerned, the supply of and demand for labour do not meet (Lelkes, 2006). Disproportionate tertiary education may be blamed; there are 21 tertiary educational institutions with two military and one police academies and three musical and arts universities among them.

3.4.2. Backward regions

Slovakian regions show the most striking developmental differences in Europe; the relative variance in GDP per capita figures in 1995 was over 50%, employment and unemployment rates showed a relative variance of 8-13% between 1995 and 2008. The Slovak population was partly motivated to join the EU for this reason, since developmental supports have been available since 2002 in this way. Act no. 503/2001 on Regional Developmental Support defines aims to ensure Slovakia's balanced economic and social development, to mitigate and clear away the differences in economic and social development between the regions, to avoid the creation of regions with a low economic performance and standard of living, to ensure sustainable regional economic and social development. Utilising EU funds more efficiently is still an unsolved problem. Backward regions have been able to close up to a lesser degree only and their shortfalls are still enormous (Lelkes, 2006).

3.4.3. Economic openness

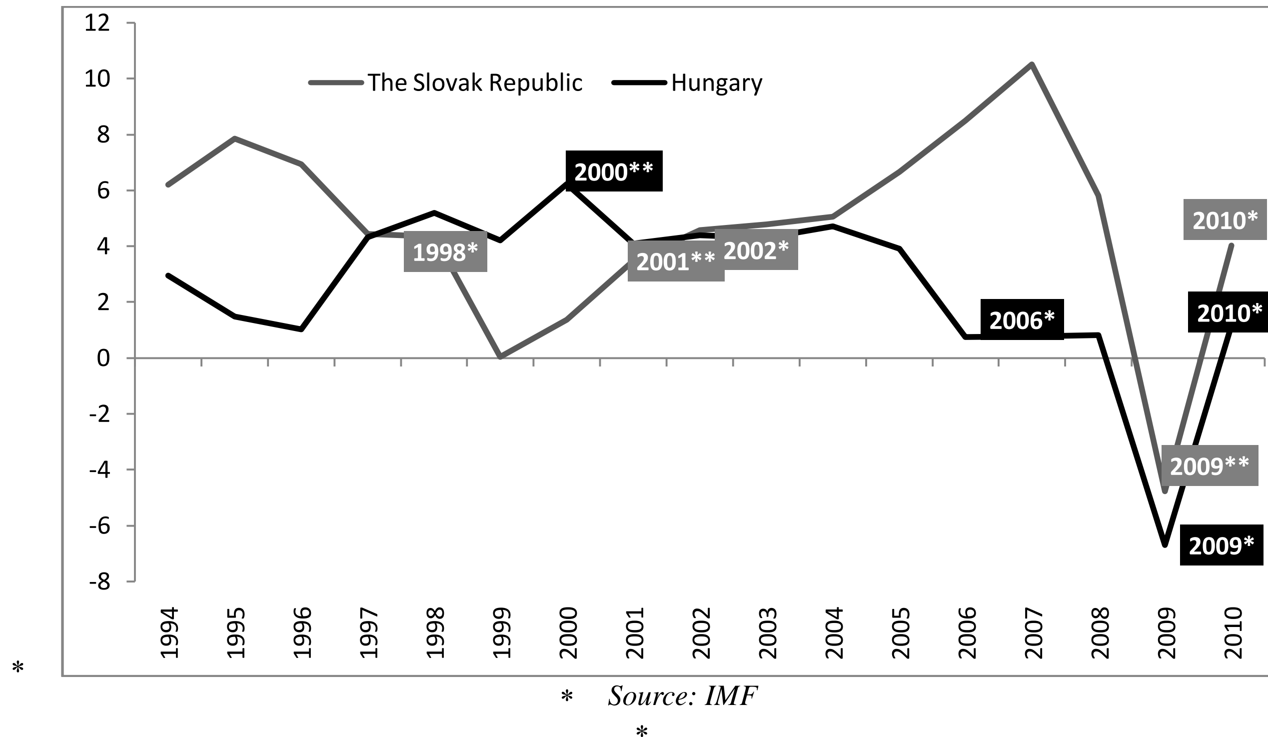
Slovakia is a strongly open country; both its exports and imports exceed 80% of the GDP. More than 30% of the exports go to Germany and Austria. Due to the high level of exports Slovakia is more exposed to the operation of the German economy and when it is hit by recession, the Slovak economy may also narrow down. This was evidenced by the crisis of 2008 too, when the country's exports dropped by 18%. It was mainly caused by the nearly EUR 2bn fallback in the exports of cars and other vehicles while the exports of oil and oil derivatives and vehicle parts reduced markedly too. The almost 5% fallback in GDP in 2009 was mainly caused by the significant drop in exports and industrial performance (of 15%).

4. Comparison of the performance of the two countries

The analysed countries followed completely different growth paths between 1993 and 2010 (Figure 1); we cannot find a correlation between the growth rates of the real GDP of the two national economies even if we take into consideration that Hungary can be considered as an independent market economy since 1991 and Slovakia since 1993. The main differences in the development of GDP are the following,

- In Slovakia, the investment activities have been more pronounced since 1993 than in Hungary, where household consumption takes up a much larger share in the GDP. Consumption-based growth carries dangers, as evidenced by the effects of the crisis of 2008, since household consumption, in case of a recession, public restrictions or the loss of jobs will stagnate or reduce and retrain economic development as a whole.
- In Slovakia, the industry's share in total output is higher than in Hungary due to the high level of investment activities.

Figure 1 - The growth rate of real GDP in the Slovak Republic and in Hungary



* *Source: IMF*

The chart shows that the growth rates of the two countries have developed in two different ways since 2004; while Slovakia was characterised by an unbroken growth, the Hungarian one lessened in each year. Up to 2004, Hungary was among the first-rankers in the region while Slovakia, after the EU accession shot out in terms of economic growth and convergence and our country has become a laggard. In the following part we are examining its causes.

4.1. The adaptation of economic policies to cycles

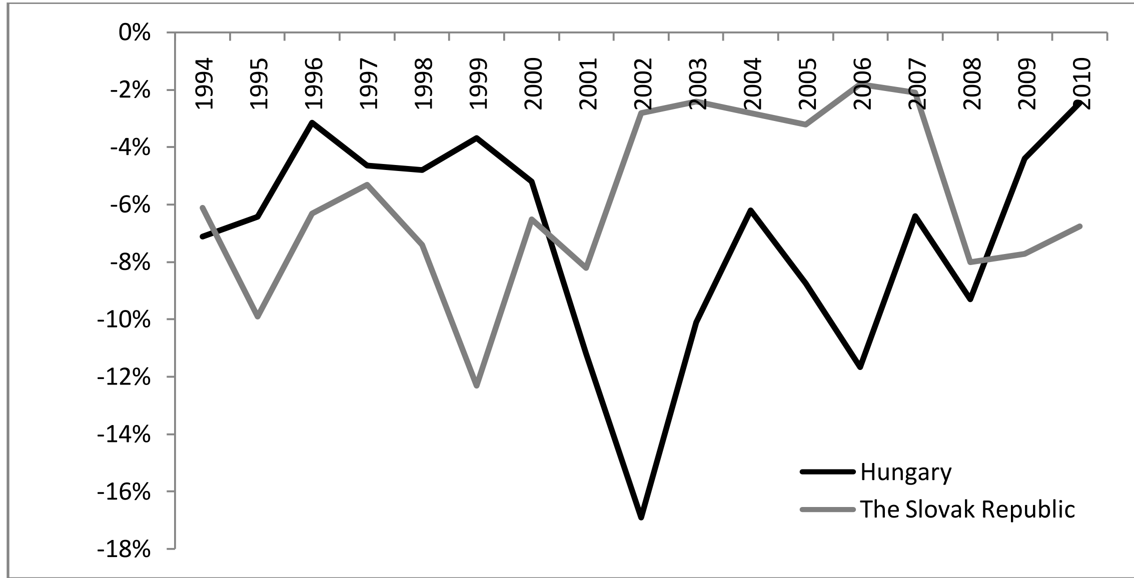
In the following figure we marked the major dates at which more significant economic political decisions were adopted in the given country; we marked restrictive interventions with a '*' and expansive ones with a '**'. The chart shows that against the falling performance Slovakia started to introduce economic restrains in 1998 and this process was stopped in year 2001 only, being a pre-election year. According to some economists the leaders of the country proceed in the right way if they follow a restrictive economic policy in the time of economic upswing thus accumulating reserves to fund the expansive measures introduced in time of depression (Greenspan, 2008). So the Slovak government did it right when they introduced the Dzurinda reform package as in the year following the economic crisis Slovakia already showed a 4% growth.

As opposed to this, in Hungary public spending lasted from 2000 to 2006 but failed to stimulate growth; consumption and investment increased at a slowing rate while the country's indebtedness increased. This process was not halted by the budgetary restrictions in force since 2006 either, which might be because the Hungarian economic policy did not adequately meet the economic expectations at the beginning of the 2000s. It is further evidenced by the fact that the economic management had a limited elbow room and range of instruments under the period of the financial crisis to minimise the impacts of the crisis as much as possible.

4.2. Joining the Euro Zone

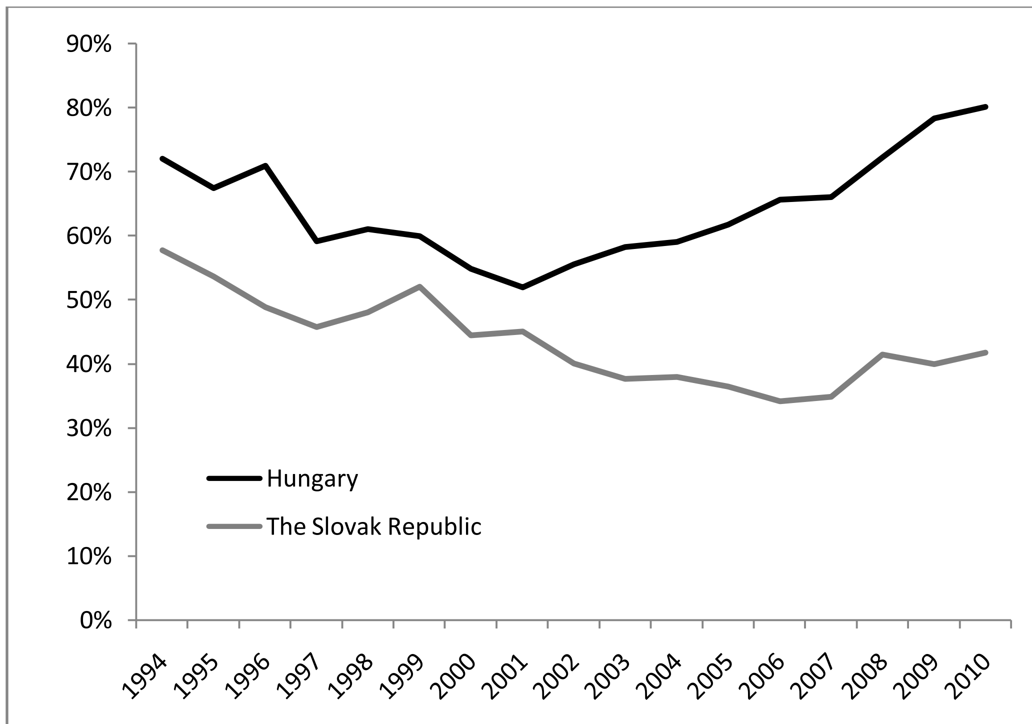
The success of Slovak economic policy and failure of the Hungarian one is best illustrated by that Slovakia has been part of the Euro Zone since 1 January 2009 while Hungary, after the continuous postponement of the target date, has not met the Maastricht Criteria to date. Figures 2 and 3 illustrate the development of the budget deficit and public debt in the two countries.

Figure 2 - Budget deficit in the two countries



Source: IMF

Figure 3 - Gross public debt in the two countries



Source: IMF

The figures show that Slovakia has complied with the two most difficult criteria since 2002; only the crisis management of 2009 caused the budget deficit to rocket. According to the forecasts of the IMF and the ECB, the figure is expected to decrease to 3.3% already in 2011. The public debt of less than 40% is of a sustainable rate.

In Hungary, unlike the countries joining the EU in 2004, the budget deficit has been near the expected 3% since 2006, but due to the indebtedness in foreign exchange and the continuous weakening of the Hungarian forint public debt gets ever farther from the sustainable level.

The budgetary shortcomings described in the former parts of the paper, the already highlighted defects in the system and the short-term thinking of the leaders influenced by election cycles only were the causes why Hungary has been unable to manage the twin deficit for 20 years. In Slovakia, the measures adapted soon enough, the simplification of the taxation system, the partial or full removal of social benefits and healthcare privatisation resulted in a sustainable economy.

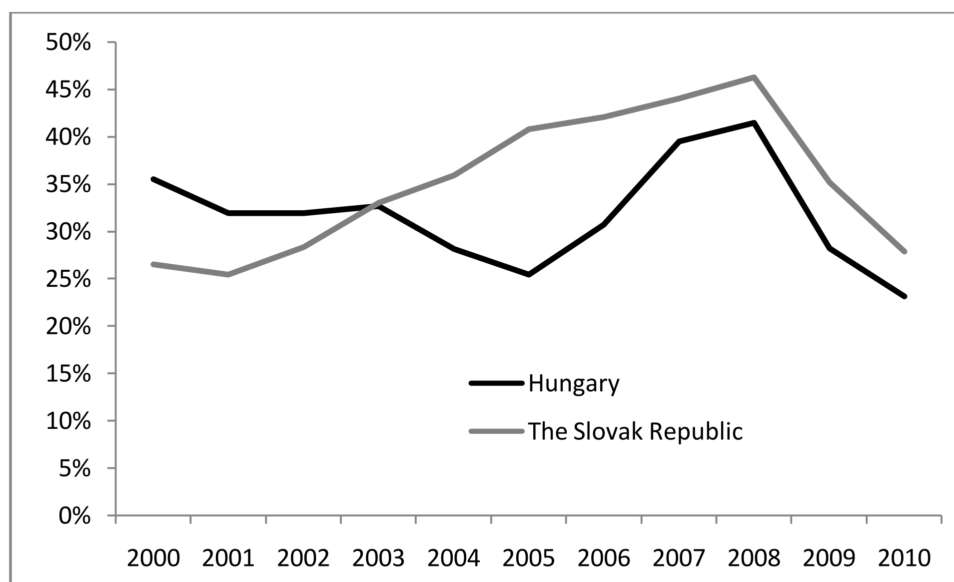
A further cause of this difference is the excessive redistribution so typical of Hungary, which Slovakia has been able to reduce over the years.

A common feature in the connection of the analysed countries with the EU is that, based on international declarations, both Slovakia and Hungary put a large emphasis on national economic policies, neither state is an unconditional follower of the idea of a federalist Europe. The difference is that Slovakia has been able to benefit from this way of thinking and Hungary has not; for Slovakia, rational state management was an aim to be reached in itself while our country laid the emphasis on accessing EU funds and only the crisis management year of 2009 focused the attention to the fundamental structural dangers of overspending and the importance of budgetary discipline.

4.3. Social disparities

The above-described facts prove that Slovakia has done everything possible in order to reach a fiscal discipline but the society made a huge sacrifice in order to ensure the sustainability of state indicators. Slovakia is one of the countries in which regional disparities are the largest but Hungary is just slightly better in this area. Figure 4 illustrates the relative variance of unemployment rate in the different regions of the countries.

Figure 4 - The relative variance of unemployment rate in Slovakia and Hungary

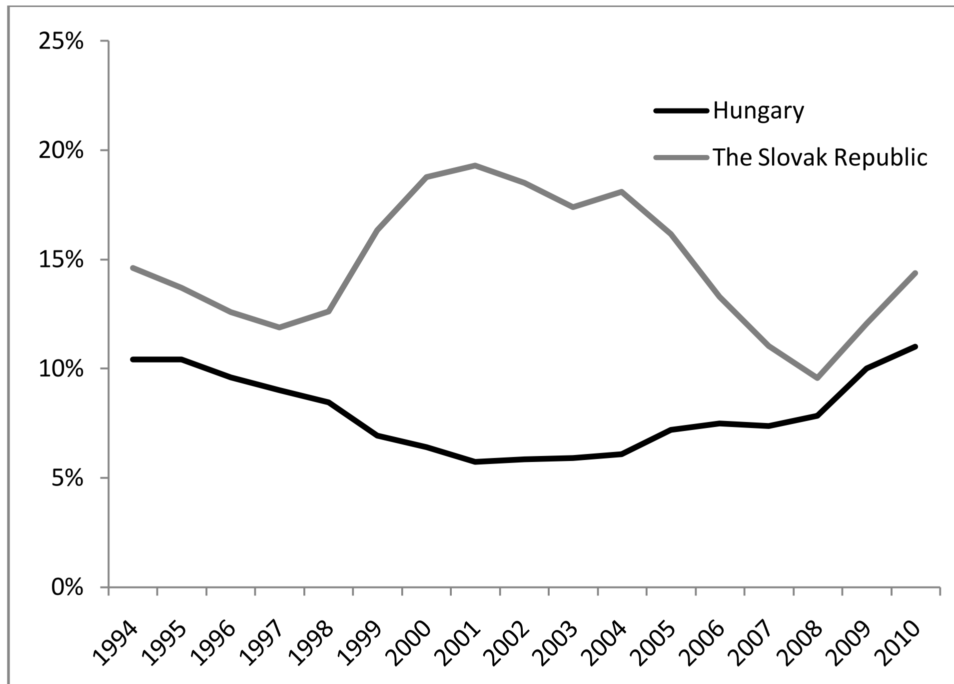


Source: Own calculation based on the data of the statistical offices in Slovakia and Hungary

The chart shows that regional disparities are of a very high extent in Slovakia and further worsened after the EU accession despite the developmental subsidies. In case of Hungary this indicator shows a fluctuation, and the differences between the regions visibly increased after 2005 while the developmental differences only reduced after the crisis.

A further problem for the Slovak economy, apart from the underdeveloped regions, is the unemployment hitting the whole country, which fact is illustrated in Figure 5.

Figure 5 - Unemployment in Slovakia and Hungary



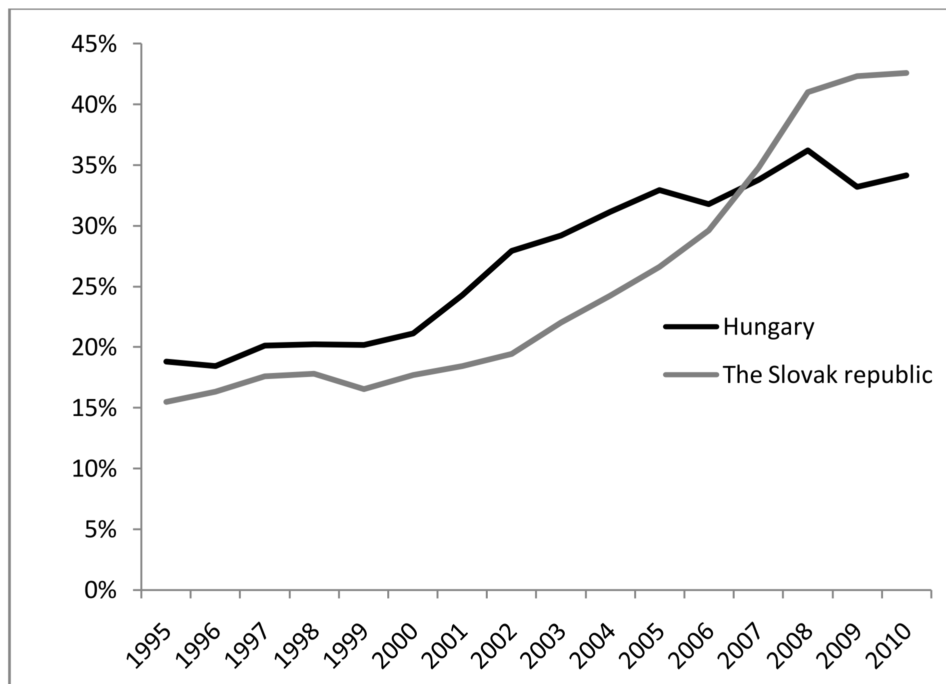
Source: IMF and eurostat

Before 2008 the Slovak unemployment rate was a lot higher than the Hungarian one but since 2009 the two figures have come close to each other. Structural unemployment, the discrepancy between professional training and the demand of the labour market and low-level mobility of labour are typical of both countries.

4.4. Closing up to the EU

In light of the data presented above the question arises as to what extent the restrictive reform implemented since 2002 has affected the Slovak society. Figure 6 shows GDP per capita figures to illustrate social well-being as compared with the average of EU15.

Figure 6 - GDP per capita in comparison to the average of the EU15



Source: own calculation based on eurostat data

The chart shows that the ratio increased in Slovakia dynamically between 1999 and 2009 and approached the average of the cohesion countries gradually, while Hungary has practically stagnated in this field for the past six years. These indicators properly illustrate that the price paid by Slovakia for the restrictions is slowly recovered, but in Hungary the 'wasted decade' typical of the budget still hinders the country's development and closing up with its more developed European fellow countries in the long term too.

5. Summary

We can arrive at several conclusions having reviewed the past twenty years of the analysed countries,

* As the indicator presented last illustrates, Slovakia is a good example for the importance and advantages of maintaining budgetary discipline. Unemployment and other regional social disparities suggest that the society has in fact paid too high a price for it. Still the data from 2010 and the increase in GDP per capita figures suggest that the measures introduced in 2002 have matured and born their fruit.
* The recognition that the reduction in the size of the public sector is fundamental to any efficiency consideration is also related to the conclusion above. The Slovak economic policy reregulated the large social supply systems, education, public administration and social security by specific measures and not by words only. Hungary is still to make these changes.
* Specific national features and adherence to them can be observed in Slovak economic policy too. This did not, however, rule out the possibility of adjustment to European Union norms or integration in the global economy.
* Hungary could also learn the lesson that the governments replacing each other continued the good measures and tools of their predecessors and did not sacrifice them for passing popularity.

The indicators chosen for the analysis do not provide a full and perfect picture of the two countries' situation but in light of the above-described it might become more understandable how the economic positions of the two countries were exchanged in the convergence process and how the Slovak economy has become one the front-rankers and the Hungarian economy has transformed from an 'eminent student' into a laggard

References

BALOGH, S. ed. (1985): Magyarország a XX. században. Kossuth Könyvkiadó, Budapest.

BÉKESI, L. (2010): A magyar gazdaság helyzetéről, kilátásairól, a gazdaságpolitika dilemmáiról és feladatairól. 'Élet és irodalom' Volume LIV Edition 9

CSABA, L. (2006): A fölemelkedő Európa. Akadémia Kiadó, Budapest

GÁSPÁR, P. – HALÁSZ, A. – LEPP-GAZDAG, A. (2004): Az államháztartás működési problémái http://www.icegec.hu/hun/_docs/publikaciok/egyeb/munkafuzet_3.pdf Downloaded on 21 September 2007

GKI Gazdaságkutató Zrt.'s forecast for 2011 (8 June 2011) http://www.GKI-Economic Research Institute.hu/sites/default/files/users/Szenczy%20D%C3%A1niel/sajtoanyag_honlapra_1106.pdf Downloaded on 14 December 2011

GREENSPAN, A. (2008): A zűrzavar kora (Kalandozások az új világban). HVG Kiadó, Budapest

GYENE, I. (2008): A tátrai tigris titkai. Méltányosság Politikaelemző Központ. http://www.meltanyossag.hu/files/meltany/imce/doc/ip-atatraitigris-081103.pdf Downloaded on 24 November 2011

IMF (1998): Slovak Republic – Recent Economic Developments. International Monetary Fund Staff Country Report No. 98/60 http://www.imf.org/external/pubs/ft/scr/1998/cr9860.pdf Downloaded on 26 October 2011

KOZMA, F. (1998): A félperiféria – Külgazdaság-stratégiai kiindulópont Magyarország számára az ezredvégen. Aula Kiadó, Budapest.

LELKES, G.: Területi egyenlőtlenségek Dél−Szlovákiában az uniós tagság tükrében. Fórum Társadalomtudományi Szemle 2006, no. 4

Magyar Köztársaság Kormánya (2009): Válságkezelés és bizalomerősítés – A válságkezelő kormány egyéves cselekvési terve. http://www.euroastra.info/files/Valsagkezeles_es_bizalomerosites_a_Bajnai_kormanyprogram.pdf Downloaded on 14 December 2011

MOMMEN, A. (2004): Magyarország neoliberális forradalma. A kapitalista globalizáció sikertörténete. 'Eszmélet' 2004, no. 63

MURAKÖZY, L. ed. (2007): Fecseg a felszín és hallgat a mély (Tudatok és tudatalattik a gazdaságpolitikában); Bokros, L.: Az állam alkati torzulásának eredete az átmeneti társadalmakban. A visegrádi országok esete, különös tekintettel Magyarországra. Akadémia Kiadó, Budapest.

TÁRKI (2003): Társadalomtudományi Intézet A gazdasági döntések hatásai a társadalmi szerkezetre középtávon, különös tekintettel az EU-csatlakozás folyamatára http://www.tarki.hu/adatbank-h/kutjel/pdf/a409.pdf Downloaded on 25 October 2006

TÚRY, G.-VIDA, K. eds. (2010): Monitoring jelentés 2010 Az Európai Unióhoz 2004-2007-ben csatlakozott Tízek teljesítményéről. http://www.vki.hu/ujd/Monitoring2010.pdf Dowloaded on 24 November 2011

TÚRY, G.-VIDA, K. szerk. (2011): Monitoring jelentés 2010 Az Európai Unióhoz 2004-2007-ben csatlakozott Tízek teljesítményéről. http://www.vki.hu/ujd/Monitoring2011.pdf Downloaded on 24 November2011

ZÁDOR, M. ed. (2010): Két válság között (A Magyar gazdaság wargabetűje– 1990-2010) ECOSTAT http://www.ecostat.hu/archiv/download/konyv/ecostat-konyv.pdf Downloaded on 2 November 2011