

Para 5 is in reverse. CONFIDENTIAL
Hungary ~~could~~ depend on the CMEA
at cost to her well being. *Stevie M. J. J. 1/4*
Mr C. R. Battiscombe, EESD
and much copy del.

Reference: *Mr Battiscombe*
I am not so sure that there is much news in all of this. What do you think?
2/20/6

ENH (8)
020/4

HUNGARY'S RELATIONS WITH THE SOVIET UNION AND THE WEST

1. During my visit to Budapest a senior Hungarian official took me aside, outside of the official discussions, to explain why Hungary was so concerned about 'détente' at present. What he said threw new light on Hungary's preoccupations.
2. Mr Cartledge knows who the official was and the circumstances of the encounter. He agreed that I should report what was said without further attribution as the official was directly concerned with the subjects he spoke about.
3. Several of the policy questions facing the leadership, the official said, touch on two of the most sensitive aspects of Hungary's relations with the Soviet Union - the nature of 'socialism' in Hungary and the extent of Hungary's economic involvement with the West.
4. The leadership, I was told, feared that unless there was real growth in the economy over the next couple of years there could well be a major political upheaval in Hungary. Hungary had exhausted the possibilities of developing trade with the Soviet Union. The only way in which the Hungarian leadership could 'deliver the goods' to the public was through developing trade with the West more rapidly than before.
5. Such a move, the official said, would be of considerable political significance. Hungarian trade experts have now come to the conclusion that Hungary can no longer depend on the Soviet Union as a trade partner. The Soviet Union seemed incapable of delivering the raw materials and other goods which it had already contracted to deliver. For example, in recent months it had fallen behind seriously in its delivery of chemical products, wood, coking coal, iron ore and iron and steel products. In retaliation Hungary has restricted its exports to the Soviet Union. The official said that he had recently had a lengthy discussion with a top Soviet economist from the Bogomolov Institute in Moscow. The economist had told him that the economic situation in the Soviet Union was much worse than generally believed. It would deteriorate further for some time to come. Dependence on supplies from other CMEA countries would be dangerous for the same reason. These indications had reinforced the leadership's belief that it must orientate its economic policy more towards the West.
6. But this is only part of the awkward decisions facing Hungary in its dealings with the Soviet Union. To regain economic growth Hungary must boost its exports to the West. To achieve this Hungary will have to continue with the reforms started within the framework of its New Economic Mechanism. Unless it does its economic gains will be eroded quickly. Hungary will have to continue to move towards a more profit orientated economy, with a close link between domestic prices and world prices, the establishment of a capital market in some form, a unified exchange rate and external convertibility for non-residents. In due course membership of the IMF and the World Bank may follow.

7. Personnel changes, which had taken place over the last year or so, the official said, had underlined the determination of Hungary's leadership to press ahead with its new economic mechanism. He cited in particular the fact that Hungary's former Ambassador to Moscow, Marjai, had been put in charge of Hungary's relations with CMEA and was being tough in his conduct of relations with the Soviet Union. The official also referred to the appointment of the former Ambassador to Paris, Mr Peter Veress, as Minsiter of Foreign Trade. Veress was someone who strongly favoured reforms in the Hungarian economy. Particularly important had been the elevation to the Politburo of Mr Havasi, in charge of Economic Planning. In the past he had had difficulties because of his enthusiasm for economic reforms.
8. The economic changes envisaged by Hungary clearly go well beyond what the Soviet Union has accepted before. A Soviet decision to permit such changes will be all the harder because they know that it is not just a question of economics, but a major social and political change as well. The wife of another senior official and party member told me that 'Hungary is going to become more like Austria and we have to have choice, not just in economic matters.' The Russians must be well aware of this type of sentiment.
9. The dogmatists in the party itself may strike back. They have lost much and may lose more. They are less well placed than they were. The failure of present policies, perhaps induced by a Soviet reluctance to let them run their full course, would help restore their fortunes.
10. There is little love lost between the Hungarians and the Russians. I was told, for example, that two years ago a Hungarian delegation sat through dinner with Mr Kosygin with bulging briefcases at their feet for fear that the Russians would learn their negotiating position. The situation is unlikely to be easier now. Relations between Hungary and the Soviet Union will not be short of bones of contention. For the time being the Hungarian leadership seems determined to pursue its present course. But as it takes one decision after the other, my contact said, reassurances of the West's interest in détente take on a particular significance. Hungary has a profound wish to see détente is re-established, even on the basis of a new 'realism', as this will help ease the tensions in Soviet-Hungarian relations.
11. I spent a lot of time in Budapest discussing Hungary's economic problems and policies, on which I have written a separate report. Nothing I heard led me to doubt what I have recorded above.

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18.15

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PA	MINISTRY
	Action Taken

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cc Mr Tait, CSCE Unit
Mr Banks, Research Dept.
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Mr Bull, Bank of England

Mr Atkinson, Budapest
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