Note of a meeting between Dr Mátyás Timár, President of the Hungarian National Bank and Lord Cockfield, Chancellor of the Duchy of Lancaster held at the National Bank, Budapest, on Monday 10 September 1984

After the opening courtesies Dr Timár touched on the excellent relations which existed between the Hungarian National Bank and the Bank of England. Lord Richardson had visited Hungary when he was Governor, and Dr Timár hoped he would be able to welcome the new Governor.

Lord Cockfield said that Hungary, like the UK, had had problems though they had been different from those of the UK. In Britain the Government's problem had been to get control of the internal economic situation and improve the working of the economy. The Hungarians also had had the problem of large foreign borrowing and the servicing costs which this entailed. Both countries had had to go through a period of economic adjustment. He asked Dr Timár for his assessment of the way the Hungarian economy was going. Were the targets for the remainder of this year and next year going to be achieved?

Dr Timár said that the biggest problems had been in 1982. The causes had been mainly external (Poland, Afghanistan). It had not been possible to borrow for a year. The result had been that despite some improvement in the Hungarian economy even in 1981 and 1982 there were liquidity problems. Then Hungary had obtained a bridge loan from the BIS in Basle with the help of Lord Richardson. Hungary had then joined the IMF and the World Bank. There had been, too, a change in the attitude of the commmercial banks towards Hungary.

Dr Timár said that Hungary was not responsible for the deterioration in relations between the US and the Soviet Union over Poland. The Hungarian economy was basically in order, the remaining problems being only of the day-to-day variety. Hungary had been asking only for normal treatment. The problem of liquidity had been tackled by stability since 1982 and by tough internal measures. The standard of living was declining by 1%-2% per annum. Inverstment was being decreased first of all in the non-productive sector. Budget expenditure had been cut, as had subsidies and subventions. A programme of energy rationalisation had been introduced. Imports had been restricted and the Hungarians had concentrated on export performance.

Dr Timár said that already by 1982 Hungary had succeeded in achieving equilibrium in its convertible balance of payments. There were no problems in the Socialist sphere. There had been an active balance of $100 m in 1983. There would also be an active balance in convertible trade this year, despite a drought.

Dr Timár said that tough policies would be continued in 1985 and 1986. There would be a minimal increase in living standards, and it would not be possible to increase investments. Effort would be concentrated on the competitive branches of the economy. There would be no increase in budget expenditure. There would be some liberalisation of imports since the restrictions in this area were temporary. The emphasis would be on efforts to further increase the level of exports. The general picture was one where the Hungarians could breathe a little more easily. The main period of stress was now over.

Dr Timár said the signs were that there would be a small recovery in 1985, but this was not being overestimated. The national economy had reacted slowly to increases in the price of raw materials, and despite the country's indebtedness things were getting into order. However there could be no easing up. The years which were lost after 1973 and 1974 had to be made up. The main target was the decrease in the country's net indebtedness. Hungary, however, did not want to achieve this by means of restrictive measures, but by better utilisation of resources, and by developing a management system for the economy. Dr Timár pronounced himself moderately optimistic. Recovery would come, though slowly.

Lord Cockfield commented that nearly all of the Western economies had reacted wrongly to the oil price crisis in 1973. Only the Japanese had got it right in realising that one had to improve one's efficiency to get the money to buy oil. They had, however, overdone it, with serious repercussions for other countries. The rest of the world had paid a heavy price for failing to get it right.

Lord Cockfield asked whether the decline in relations between the United States and the Soviet Union had had an effect on the economic situation. What had the repercussions been on exports, for example?

Dr Timár said that there had been an important negative effect on the Hungarian economy. He had already mentioned the financial effects which resulted directly from the international situation - the withdrawal of deposits and the lack of credit. This tightening up of financial relations had inevitably brought a tightening in commercial relations. Imports from the West had decreased by 20%. The Hungarians had increased their exports, but mainly to the developing countries rather than to the developed industrial countries. The restriction on imports from the West to the Eastern bloc had also affected the Western economies. Austria and Finland, which had maintained their traditionally high level of trade with the Eastern bloc had suffered less from the recession that the other Western countries.

Lord Cockfield said that the Western European economies were now beginning to recover. The UK had maintained a good rate of growth both last year and this year. All of this had an impact on international trade. In the end the recovery would result from the interaction of one economy with another.

Lord Cockfield said that efficiency was a crucial issue in the performance of the Hungarian economy. Were the Hungarians taking effective steps to improve the level of efficiency?

Dr Timár said that he was not entirely happy with the results, but there had been some success. There had been good results in the field of energy conservation. A decrease in energy consumption had been achieved at the same time as an increase in industrial production.

Dr Timár said that the aim was to develop the competitive branches of the economy. This had been fairly successful and quite considerable increases in exports had been achieved. Things were generally going well in energy, chemicals and heavy and light industry, but there were some exceptions.

Dr Timár said that he was unhappy with machine tools. With the exception of a small number of enterprises production in this area was not what it should be.

Lord Cockfield asked about the motivation and ability of Hungarian management. It was important that managers should be a driving force able to motivate the workforce. Were there problems in this area?

Mr Timár said that there were problems, but reform was under way and Hungary weas moving in the right direction; more initiative could be seen. He felt however that efforts to improve motivation in industry had not yet fully succeeded, though the position in agriculture was better.

Lord Cockfield asked about the provision of capital for investment. What if anything was being done to stimulate the supply of investment capital?

Dr Timár said that the main question had been how to ensure enconomic improvement. It had therefore been necessary to cut funds for investment, whether sourced by the budget or by the enterprises. However this had gone too far, and the managers of enterprises had been complaining. Their complaints were not unjustified. They should have been given more resources for intensification and development. The years to come were not years of large investment, but rather small-to-medium investment for intensification and the improvement of productivity. There was always the danger with a restrictive policy of managers losing the enthusiasm to invest. With foreign capital the main form was the financial loan. There were relatively few joint ventures, and they were mostly with Austria and West Germany. There were, unfortunately, very few joint ventures with the UK - only about 60, with only 20 really active. There were between 200 and 300 with West Germany.

On the supply of investment funds Lord Cockfield said that there were two sources in the UK; the retail banking system and personal savings. With the banks the system was that the individual deposited money which was then lent to industrialists. Whenever interest rates rose there was an outcry from industry. But the cash balances held by industry were almost as great as the borrowings held. Cash flowed through the bank to the borrower and provided enormous help to industry. What was the position in Hungary?

Dr Timár said that in Hungary the deposits of the population were used for credits given to the population and went into home-building. They did not provide additional assistance for production.

Lord Cockfield asked whether there were individual enterprises with surplus funds which could be used by others.

Dr Timár said that in the past the flow of cash had been vertical. The budget took away any surplus and gave to others. Of late, however, the Government had endeavoured to minimalise this and enlarge the horizontal movement of capital. This was done through the bank, but it was not on a very big scale. Because of restrictions the amount of free capital was not very large. There were also other forms of horizontal movement. The Hungarians had introduced bonds; and there were a number of joint ventures between Hungarian enterprises. It was generally acknowledged that the rôle of the banks would increase in the future.

Dr Timár said that the Hungarians were being a little cautious. Some people supported the idea of a double-tier banking system to separate the credit bank from the National Bank. Others however opposed the idea.

Lord Cockfield asked about the level of personal savings in Hungary. Dr Timár said that, including everyone in the population, the level was about £300 a head for individual savings, but this was expected to improve. The way in which it might be improved was a matter of dispute. An increase in interest rates on deposits had been proposed, but there was oppostion to this on the grounds that it would mean an increase in rates on loans for construction. And the question of who would and who would not benefit gave rise to political difficulties.

Lord Cockfield said that increasing the level of personal savings were crucially important for both Government and industrial finance. In the UK there was a great deal of institutionalised savings. But individual savings also provided funds for capital development. The problem in the UK was not a shortage of funds but rather a shortage of profitable ventures in to which those funds could be put. 30% of the UK GDP went into international trade. Unless capital was invested in profitable ventures it would be impossible to hold this level of exports.

After further courtesies the meeting closed.

A K GALLOWAY

September 1984

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