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Hungary and the CMEA

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Dear Peter:

Hungarian economists think of their country as part of the CMEA rather than as part of eastern Europe. The CMEA (which we call COMECON, and is formally known as the Council of Mutual Economic Assistance) was formed in 1949 to promote trade between the Soviet and East European economies. As one would expect, much of the trade within the CMEA is dominated by the Soviet Union. For example, 50% of the value of Hungary's agricultural exports go to the Soviet Union. In turn, the number one export of the Soviet Union to Hungary (and other CMEA countries) is oil and natural gas.

Soviet oil and gas sales to Hungary sparked a major controversy at the 8th U.S.-Hungarian Roundtable on Economics, which I attended in Budapest in December. The Soviet Union has been selling oil and natural gas to eastern Europe at lower-than-world market prices. These sales therefore have represented a subsidy to the oil importing countries of the CMEA, but the magnitude of the subsidy is debatable. Presumably the Soviets have received something in exchange, but the nature of the benefits they've received from trading with the other CMEA countries is another debatable point. Two Americans last year estimated the energy resource subsidies given by the Soviet Union to eastern Europe during the decade 1971-1980 at 80 billion dollars. They argued that in return, the Soviets have received a variety of political and strategic, but mainly non-economic, benefits. Hungarian economists at the Roundtable strongly objected to the idea that this trade had provided only non-economic benefits to the Soviet Union.

The Hungarians contended that contracts to sell industrial and food manufactures, in exchange for Soviet oil, had forced a restructuring of Hungarian industry and agricultural

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processing. Especially industry has been forced into producing goods of low quality, with technical specifications that make the products unsuitable for sale in western hard-currency markets. Several examples were offered of how industrial production has been distorted. One clear case was that of a fast, high pressure paint sprayer. This was a technically sophisticated machine, which the Hungarian manufacturer was required to depressurize to suit Soviet labor and technology levels. That alteration, in effect a benefit captured by the Soviet Union, had a cost to the Hungarians in that the machine was no longer technically competitive in western export markets.

The debate around the Soviet subsidization and mutual trade benefits was as much political as economic. The Hungarians are now engaged in negotiating new contracts for oil with the Soviet Union, and the subsidy arguments provide more justification for the Soviets to demand higher prices in the new agreements. Also, because the Americans had formulated the subsidy estimates, some Hungarians thought this would give the Soviets an additional edge at the bargaining table. They brought the subsidy issue up for debate on the first day of the Roundtable for the purpose of publicizing and raising questions about the validity of the subsidy estimates and how they were calculated. The evening reception that followed the debate did feature some new faces, which was perhaps an indication that the tactic was a success.

Apparent throughout the subsidy debate was a difference in approach between the American and Hungarian methods of economic analysis. The Americans analyze an economic event _ceteris paribus_, where all things other than that event are assumed to remain unchanged. In contrast, the Hungarians are inclined to take into account all the complexities surrounding an economic issue, including the political. Take the title of one paper by a Hungarian economist recently returned from 5 years in the Soviet Union: _The Realization of the Principle of Mutual Interests in the CMEA Member-Countries' Trade between Themselves and the Influence of this Principle on the Prospects of Economic Growth in Eastern Europe During the Eighties_. Obviously, greater complexity can also lead to confusion. On the other hand, a _ceteris paribus_ approach, while yielding quantifiable and concrete results, such as the estimated 80 billion dollar Soviet subsidy to the CMEA, may not be very realistic, or very politic.

The future of Hungary's agricultural trade with the CMEA, and especially with the Soviet Union, is another critical issue. Should the Soviet Union continue to be the major outlet for Hungary's agricultural exports? Hungary delivers about 60% of all Soviet apple imports, over half the canned vegetable imports, more than 40% of tinned fruits and brandy imports, and about 25% of the egg, fruit and wine imports. One quarter of the total Soviet meat imports come from Hungary. In addition, Hungary has been increasingly successful in exporting agricultural goods to the Soviet Union for dollars, rather than for rubles. These dollar exports to the Soviet Union, primarily for above-quota wheat and meat deliveries, may be as much as 46% of total (1982) Hungarian dollar agricultural exports. Thus, Hungary has come to rely on the Soviet market for agricultural trade surplus and for needed hard currency.

That market may be shrinking, however, depending upon how successful is the Soviet drive to increase food self-sufficiency. Although expectations vary as to whether or not the Soviet Food Programme really will result in greater food production and improved distribution, Hungarians realize that they must find other markets for their agricultural exports, particularly in the industrialized, western countries. Food production in Hungary is expected to increase by some 3% per year. Since domestic consumption is not expected to increase by much, the question is how to sell the excess. In selling raw agricultural products on the world market, Hungary has had to compete against the subsidized meat, grains and dairy exports of the EEC, the U.S. and Australia. Producing and exporting more processed food products may be one answer. Not only does processing add more value to the raw agricultural product, but there is also an effective demand for processed foods in high income countries.

Hungary has not had much success in exporting processed foods. Of the food that is processed (around 50% of total agricultural product,) most (80%) is sold on the domestic market. The poor export performance of processed foods is due partly to lack of market research. Hungarians have not searched out markets for processed foods because the Soviet market takes so much of their raw agricultural products. There are also quality problems in the food industry, as in other industries. No doubt the excellent canned sour cherries that Hungary does export could command a higher price with better labelling and, sad but true, with coloring and preservatives added to improve their dull and battered appearance. The food industry in Hungary is plagued by capital shortages, supply bottlenecks (e.g. shortages of bottles and cans at harvest times,) and low profits. With consumer food prices set low relative to producer prices it's difficult for food manufacturers to cover their costs and still produce a high quality product.

Although it may be true that agriculture in Hungary has succeeded without the help of domestic industry, as some at the Roundtable seemed to think, it's now clear that there must be more cooperation between agriculture and industry if more foods are to be processed for export. It's interesting that, as in the U.S., food industry and marketing issues receive less attention than do production problems, even though more of the production problems have been solved. There's certainly a need in Hungary, as in the U.S., for more marketing research.

Sincerely,

Lana Hall

Lana L. Hall

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