

Hungary

Status Index (Democracy: 5.0 / Market Economy: 4.7)		9.7	Management Index		6.7
System of government	Parliamentary Democracy		Population	10 Mio.	
Voter turnout	70.5 % (2002)		GDP p. c. (\$, PPP)	12,340	
Women in Parliament	8.3 %		Unemployment rate	6.5 %	
Population growth	-0.2 %		HDI	0.837	
Largest ethnic minority	4 %		UN-Education Index	0.93	
			Gini-Index	24.4 (1998)	
<small>Figures for 2001 – if not indicated otherwise. ^{a)} Annual growth between 1975 and 2001. Sources: UN Human Development Report 2003. Electionworld.org 2002. OECD 2002. European Commission 2002.</small>					

1. Introduction

This report on the status of Hungary's economic and political transformation during the last five years deals largely with the administration of the conservative Hungarian Civic Party (FIDESZ) led by Viktor Orbán. The report concludes that the right-wing conservative victory in the 1998 parliamentary elections resulted in the stagnation of development and even some tendencies that were detrimental to democracy. This must be viewed as a failure in cementing democratic consolidation.

During his term in office, the head of government, Viktor Orbán, divided Hungary's political elite and its citizens with his inability to compromise and cooperate and his unbridled ambition for power. He sidelined the parliament and, as part of this strategy to concentrate power, neutralized the institutional checks and balances that countered the executive branch. He served nationalist resentments and returned, at least in part, to a statist economic policy.

Only the Constitutional Court remained a strong, independent authority and saved Hungarian democracy from suffering any serious damage—despite many clashes with the administration in the years from 1998 to 2003. Within its first months in office, the social democratic government under Péter Medgyessy, which was elected in 2002, reversed much of the damage that had been done under Orbán. Hungary still has stable institutions and close ties to established Western democracies. However, deep rifts remain within Hungarian politics and the economy and within Hungarian society. In the medium term, the transformation process and the new administration's political work will certainly be shaped by efforts to overcome these fissures. In this respect, the Orbán administration must be seen as a—albeit reversible—step backward in what was otherwise an advanced process of transformation.

2. History of transformation

Hungary's switch to democracy took place after forty years of communist rule. Unlike its neighbors, Hungary had “liberalized” its single-party socialist rule relatively early, after a period of Stalinist totalitarianism that followed the 1956 uprising. As early as the 1960s, a more consumer-based communist economic system began to emerge under the leadership of the Kádár regime. By not politicizing all spheres of social life, partially liberalizing private, economic and social life, and allowing the dynamic development of the hidden economy, Hungary experienced a period of social calm and modest contentment in the 1970s in what became known as “Goulash Communism.”

However, the rising standard of living—the communist leadership’s primary legitimizing factor—was short-lived. A lack of industrial output had to be compensated by extensive borrowing from the West, which meant increasing external debt. By 1982, Hungary already owed some \$9 billion to foreign creditors. At the end of the 1980s, Hungary's “socialist market economy” was on the brink of bankruptcy, with external debts of around \$20 billion. This was the price Hungary paid for opening its economy so early. But the early opening not only laid the microeconomic groundwork for competitiveness, it also prepared significant parts of the Hungarian population for the demands of transformation.

The democratic transition was initiated by reform communist elites. Against the backdrop of political change in Moscow and the desolate economic situation at home, these forces were prepared at least to allow a limited degree of liberalization and pluralization in the political arena. János Kádár, who had been the leader of the Communist Party since 1956, was ousted in the spring of 1988 and replaced by communist reformers Károly Grósz and Miklós Németh. Accelerated political and economic reforms strengthened the opposition to the regime and ultimately led to the abandonment of the single-party system. In 1989, Round Table discussions were established after the Polish example. They were supposed to fundamentally change the political system and its constitution, but given the prevailing circumstances—a demobilized and apolitical society—the talks had an exclusive character and resulted in a compromise negotiated by the elites. The compromise consisted of the agreement to have free elections in 1990 and the necessary constitutional amendments. The process of changing the system in Hungary was largely run from above by old regime elites.

In the years that followed, Hungary was able to establish a democratic political system that was cemented by several successive democratic governments. The administrative system was decentralized and made more effective. Local self-administration was established as early as 1990. Middle levels of self-administration followed as the motor for a regional development policy. Democratic transformation brought with it a restructuring of the economic system.

The democratically elected governments of the 1990s privatized state-run companies, liberalized foreign trade and helped increase the privately held share of all productive property from 35.2 % (1992) to 72 % (1997). During the same period, industrial relations were reformed in Hungary; unions as membership organizations were established, as were employer and trade associations. Different platforms, such as the “tripartite” committees, were established to enable interest groups to participate in the processes of the formulation of political demands and objectives. Democratic transition and economic transformation spurred economic growth, which increased greatly from 1996 onward.

3. Examination of criteria for democracy and a market economy

3.1 Democracy

Hungary has made progress in its political transformation. Democratic institutions and processes based on the rule of law were consolidated more quickly than in almost all of the other transition countries of post-communist Central and Eastern Europe. This rapid consolidation of democratic institutions based on the rule of law prevented the Orbán government’s polarization strategy (1998-2002) from doing any permanent damage.

3.1.1 Political regime

(1) *Stateness*: There are no problems of stateness that could threaten the process of democratic consolidation in Hungary. The state’s monopoly on the use of force is uncontested. Defining citizenship and who qualifies as a citizen is not a politically volatile issue. The Hungarian constitution defines the national and ethnic minorities living in Hungary as constitutive elements of the nation. Hungary has a sensitive, active minority policy. Church and state are separate. The political process is secularized. Public administration has been further professionalized and modernized—a reform process that is almost complete at the central level.

Territorial institutional decentralization has made only slow progress. Shortcomings are especially great at the local level, where a lack of resources is impinging on the autonomy and performance of local self-government. Particularly after 1998, many administrative positions were awarded to Independent Smallholders Party (FKGP) or FIDESZ sympathizers. It is questionable whether the local governments will be able to adequately perform the new tasks resulting from Hungary’s decentralization and EU accession.

(2) *Political participation*: There is universal active and passive suffrage in Hungary and elections are conducted correctly. The parliamentary elections in

April 2002 were free and fair, as were previous elections since 1990. They met the international standards and requirements for democratic elections. At 71 %, voter turnout was the highest it had ever been since the regime change. The elected government has effective power to govern. There are no vetoing powers or political enclaves in the hands of churches, state security forces or the military. The government respects the principles of free political organization and expression.

Trade unions represent more than 30 % of Hungary's workers and there are more than 60,000 non-governmental organizations registered in Hungary. The Constitutional Court declared a bill unconstitutional that would have limited the freedom to report critically on public figures. Since May 2002, the government and opposition once again have equal representation within the Board of Trustees for public media. Under the FIDESZ administration (1998-2002), only party adherents were appointed to these bodies, which resulted in the over-representation of the ruling parties in public radio and television, especially during election season. This problem was resolved when the new government took office in 2002. The change of government had a positive effect on the quality of democracy and political culture in Hungary, both of which had suffered under the polarizing politics of the Orbán administration.

(3) *Rule of law*: Hungary has an extensive system of checks and balances. However, from 1998 to 2002, the FIDESZ government put all of the balancing institutions—and the constitution—to the test. It managed to neutralize the Central Bank, the supervisory bodies, the judiciary and the competition authority in its push to concentrate power in the executive branch. In addition, the opposition was sometimes completely driven out of all important committees and prevented from participating in inquiry commissions.

Since the election of the social-democratic government in April 2002, democratic practices have made a complete comeback in parliament. The new government has also announced that it will reinforce the rights of the opposition, even by way of constitutional amendment. But even in the years from 1998-2003, judicial rights of supervision and inspection were not completely circumvented. Constitutional and statutory guarantees for the independence of the courts work well.

However, the judiciary's financial dependence on the government is problematic. For instance, the FIDESZ government (1998-2002) restricted the Constitutional Court's finances. Yet related attempts to restrict the courts' jurisdiction were unsuccessful. The Constitutional Court had acted as a strong, independent authority since 1990, despite all clashes, and this did not change between 1998 and 2003. In August 2002, under the new social democratic administration, a bill was introduced to parliament that would eliminate the judiciary's financial dependence on the executive.

Though corruption in politics and in public administration is a problem in Hungary, it is also subject to criminal prosecution. The immunity of elected officials entrusted with the authority to exercise government power was much more narrowly defined as part of a long-term strategy to fight corruption. In addition, the Criminal Code was tightened, disclosure requirements were expanded and the process of awarding public contracts was placed under stricter supervision. However, the public is not yet satisfied with these and other measures. Some areas of the public sector are still considered to be open to bribery. On the whole, civil liberties are respected in Hungary. Human and basic rights are guaranteed.

The constitution establishes equality before the law and the judiciary is considered to be non-partisan. Freedom of religion is codified in the Hungarian constitution and to date there have been no difficulties in implementing and guaranteeing it. Hungary is pursuing a sensitive minority policy and focusing primarily on remedying the insufficient integration of the Roma. The lack of uniform anti-discrimination legislation warrants criticism. There is also no comprehensive system for enforcing existing bans on discrimination. The new administration has drafted a bill to address existing problems in this area.

3.1.2 Patterns of political behavior and attitudes

(1) Institutional stability: Hungary has stable institutions that guarantee democracy and the rule of law. However, the parliament was pushed to the sidelines under the Orbán administration. Days of session were cut and debates about government policy were limited to such a degree that even MPs from the ruling party complained. With respect to the rule of law, the FIDESZ administration's efforts to concentrate power resulted in the temporary restrictions mentioned earlier. Generally speaking, public administration is effective at the level of the central government. Exceptions included the FKGP-run ministries of agriculture and environment under the Orbán government. There are, however, considerable deficiencies at the local level, particularly with respect to decentralization and EU accession.

Hungary's judiciary is independent and the autonomy of the courts is effective. Legal proceedings are generally reasonably speedy. Most trials in the courts of first instance are concluded within a year. In order to relieve the backlog of cases before the Supreme Court, Regional Courts of Appeal were established in early 2003. Some 6000 appeal proceedings will be immediately transferred from the Supreme Court to the new Regional Courts of Appeal. This and the safeguarding of the judiciary's financial independence are key steps toward increasing the effectiveness of this branch of government.

(2) *Political and social integration*: While the majority of the post-communist states experienced—and continue to experience—extreme fractionalization and an incomprehensible series of divisions, alliances and re-establishments of parties in the years following the founding elections, Hungary's party system is astonishingly stable. However, the right-of-center political camp has not yet stabilized; solid party bonds and loyal voters have not yet been established. Ideological polarization is moderate, although the Orbán government made efforts to intensify it from 1998-2002. The Hungarian Justice and Life Party (MIÉP) was neither part of the opposition nor part of the governing coalition in the four years of Orbán's government, but is to be classified as radical right-wing and anti-Semitic. Observers have differing views on whether the party has the potential to gain more than the 4.3 % of votes it won in the 2002 elections. There are no other anti-system parties in Hungary's party landscape.

The 2002 elections resulted in a concentration of the political camps and a moderate increase in polarization. The election campaign pitted a traditional, national-populist camp—which included the ruling FIDESZ—against a cosmopolitan, social democratic camp and poisoned the public debate in Hungary more than ever before since the system change in 1989. Premier Viktor Orbán's FIDESZ party was primarily responsible for this, although the socialists and liberals also did their fair share of demagoging. During this period, the parties tended not to focus on recognizing and resolving conflicts but rather on spreading the political and cultural differences of the elites into the voting public. Therefore, it must be the duty of the new Premier, Péter Medgyessy, to heal the political and economic wounds that the campaign created.

The party-independent public, which could act as a mediator between the two camps, is still too weak in Hungary. The trade unions have lost much of their influence and privileged political position in the last few years. Their plight is marked by plummeting memberships and waning legitimacy. Political participation is below Western European levels. There is a trend toward the alienation of the government and the people. Indicators of satisfaction with and confidence in the democratic regime dropped sharply in the first half of the 1990s and continue to fluctuate at a relatively low level. Intermediary political institutions at the meso and micro levels are rare. Many of the 60,000 non-governmental organizations, like Hungarian civil society as a whole, are more focused on market-based services than on actively reinforcing participatory democracy.

3.2 Transformation to a market economy

Hungary has made continued progress in transforming its economic system and, after a long transitional stage, is now taking a leading economic role among the reform states of Central and Eastern Europe. This is particularly true with respect to business, the services sector and the use of advanced technologies. Yet Hungary's attractiveness to foreign investment has recently suffered and a loss of macroeconomic competitiveness has become evident in the past few years. In addition, stability-oriented fiscal and debt policies have very recently been loosened again.

3.2.1 Level of socioeconomic development

The key UN indicators show a high level of development in Hungary in an international comparison. The level of development as measured by the HDI grants adequate freedom of choice and opportunity to a growing number of citizens. The inequality of income as measured by the GINI index is exceptionally low and the level of education as measured by the UN education index is high. The UN gender development index does not suggest that gender-specific discrimination in Hungary exceeds the OECD level (see Table 1). (Relative) poverty is also not widespread. Many households whose incomes dropped below the poverty line during the recession (1991-93) have since recovered. However, a study conducted by the World Bank (2001) shows that poverty is prevalent in rural areas that are not well connected to industry, and even more pervasive among the Romany minority, and threatens to become firmly established.

3.2.2 Market structures and competition

The foundations of free-market competition are safeguarded. The economy is largely privatized. However, some re-nationalization rather than privatization took place under the FIDESZ government. For example, the Postabank and the Hungarian Development Bank were put back under state control. Orbán's statist intervention in the economy led analysts to conclude that the socialists' election platform would be more in line with market requirements than the practices of conservative FIDESZ. One of the FIDESZ administration's failures was that it dragged its feet on necessary reforms in public administration and regional, health and educational policy at a time when the macroeconomic situation was favorable for such reforms. In the case of pension reform, the government even actively hampered the reforms.

There are no significant restrictions on entering and exiting the market in Hungary. Since mid-2001 all foreign exchange restrictions that had existed until then have been lifted, allowing for the complete convertibility of the Forint, the

Hungarian currency. Foreign trade is more than 90 % liberalized. There are no export duties. At the end of 2000, all import duties on industrial goods from within the EC were eliminated. Antitrust laws meet European standards in the key areas. The competition authority is doing a good job. In addition, Hungary has a system of law that includes rights that can be enforced through legal action (e.g. property). Hungary's banking system is stable and efficient. Capital resources and profitability are satisfactory. The share of bad loans has dropped steadily since 1998 and was down to just 2 % in 2002. Hungary's financial and capital market has become increasingly transparent and secure in the past few years.

3.2.3 Stability of currency and prices

During the period under study (1998-2003), Hungary has pursued consistent inflation and exchange rate policies. After 2001, direct financing of the public sector through the central bank was abolished. Thus, the central bank's independence is safeguarded in accordance with EU standards. The price increase rate was reduced to around 6 % in 2002 after having fluctuated at a high level in the years before (the average between 1997 and 2001 was 12.1 %). The necessary abandonment of the "crawling peg" had no negative impact on the stability of the Forint. The government's fiscal and debt policy was stability-oriented and successful until mid-2001. Net new debt and aggregate budget debt were reduced. Even external debt could be reduced thanks to the strength of the Forint. But a recession and campaign promises that were pushed forward resulted in a loosening of fiscal policy from mid-2001 and a marked increase in new debt in 2002. To avoid endangering the stability of the currency and prices and to keep debt policy from going off course, the new social democratic government pursued a restrictive fiscal policy in 2003.

3.2.4 Private property

Hungary has a functional private sector, which generated about 80 % of the country's GDP in 2002. Private property rights are transferable and clearly defined in law. In Hungary, private ownership is now the most widespread form of ownership.

3.2.5 Welfare regime

There is an established social safety net in Hungary to offset poverty and protect citizens against other social risks. There is disability and unemployment insurance, welfare, and a state program for disabled persons. In the last few years there have been efforts to fight the poverty that has become firmly established in rural areas and among the Romany minority by means of rehabilitation and

reintegration programs. A quarter of Hungary's population depends on the statutory minimum wage, and although the monthly minimum wage was increased by 25 % to €200 it is still far below the EU standard, while inflation, in comparison, is higher. Hungary's pension system underwent far-reaching reforms beginning in 1997 and by 2002 it was on a solid, sustainable footing.

In contrast, the healthcare system is in bad shape. Compared with Western Europeans, Hungarians are in poor health, which suggests poor performance on the part of the healthcare system. Healthcare financing is also deficient. Inefficiency and a lack of incentive to cut costs have left healthcare coffers chronically empty in the last few years. By law, equality of opportunity is well established in Hungary. In addition to a constitutional guarantee of equal treatment, a number of mechanisms are in place to promote ethnic minorities and disabled persons and there are discrimination bans stipulating that women must receive equal pay for equal work. In reality, however, there are problems.

A large portion of the Romany population is still at the very bottom of the social strata. Their situation is characterized by poor education, long-term unemployment and, as a result, poverty. Women are grossly underrepresented in parliament and on Hungary's labor market. In reality, the principle of "equal pay for equal work" is not sufficiently put into practice. However, this is true of most of the EU member states. With respect to government integration efforts, only the program for disabled persons seems to be truly successful.

3.2.6 Strength of the economy

Hungary's economic growth rates are stable. At 5.3 % in mid-2002, unemployment is far below the EU average. The debt situation is easing slowly. Foreign direct investments continue to flow into Hungary, but dropped steadily during the period under study. However, this is due in part to the fact that more and more investments that were originally foreign investments are now being refinanced with profits generated in Hungary. Through mid-2001, fiscal policy resulted in the stabilization effects mentioned earlier. Along with the Czech Republic, Hungary has taken the economic lead among the reform states of Central and Eastern Europe. (GDP per capita in 2000/EUR: Czech Republic 13,500; Hungary 12,400; and Poland 8,700).

3.2.7 Sustainability

Hungary has made remarkable progress in the area of environmental protection in the last few years. In 1998, Hungary adopted a comprehensive environmental protection program. Between 1998 and 2000, considerable investments were made in environmental protection, and administrative capacities for the effective

monitoring of environmental regulations were expanded. As a result, water and air quality have improved, nature reserves have been expanded and good progress has been made with respect to waste management. Popular indicators rate Hungary's educational system very highly, without exception. Education spending, literacy rates and rates of participation in the respective levels of education are comparable to the EU member states. Schooling and adult education are well developed. The share of university graduates, the net entry rate to university education and enrollment rates all rose steadily in the last few years, indicating that Hungary should be able to remain competitive in the future. However, the current stagnation of university funding is standing in the way. Low wages for research and teaching personnel at the universities could result in a gradual "brain drain" from tertiary education in the medium term. This is a burden for the future that is weighing heavily on the Hungarian educational system, and in fact, all of Eastern and East-Central Europe.

4. Trend

4.1 Political regime

Even before the period under study (1998-2003), the following criteria were fully safeguarded in Hungary: the state monopoly on the use of force, the definition of who qualifies as citizens, and the secularization of the government. And they have been maintained. The same is true of free and fair elections and the democratically elected authorities' effective power to govern. Freedom of choice and civil liberties were and still are guaranteed in Hungary. There have been progressive tendencies in the upper levels of public administration, particularly the central government. Over the past four years the central government administration has been professionalized and modernized and its reforms appear to be nearly complete.

Regressive tendencies and shortcomings with respect to freedom of expression, freedom of the press and the system of checks and balances, which arose from the FIDESZ administration's efforts to concentrate power in the executive (1998-2002), were remedied by the new social democratic administration (from mid-2002). The fight against corruption has stagnated. Despite a long-term anti-corruption strategy, some areas of the public sector are still considered to be open to bribery. The reform of local administrative structures in Hungary has also made no further progress, despite early successes. Persistently deficient funding of local self-government is compromising their effectiveness and their autonomy.

4.2 Democratic consolidation

The basic constitutional institutions were stable before the period under study and have remained so. The Constitutional Court played a positive role in the power structure in Hungary. It continued to act as a strong, independent authority and proved its enforcement power in all its conflicts with the FIDESZ government. Developments in the areas of political and social integration must be rated poorly. The 2002 election campaign had a negative impact. During the campaign, the parties dragged the voting public into their conflicts and did not adequately fulfill their function as the representative and aggregation of society's interests. They poisoned the public debate and created rifts within politics and the economy. They polarized what had been a rather passive population. Independent civic groups that could have played the role of intermediary were and still are grossly underdeveloped in Hungary. But even the bitter election campaigns could not jeopardize the population's fundamental acceptance of democratic norms and practices.

4.3 Level of socioeconomic development

For the period under study, the fundamental indicators of development show a slight improvement in what was already a high level of development. The same applies to sustainability indexes and the GINI index, the latter of which shows a slight reduction in income disparities.

Table 2: Development of socioeconomic indicators of modernization

	HDI	GDI	GDP index	Gini index	UN education index	Political representation of women ²	GDP p.c. (\$, PPP)
1998	0.817	0.813	0.77	25.3	0.91	8.3	10,232
2000	0.835	0.833	0.80	24.4	0.93	8.3	12,416

²Percentage of female members of parliament following the parliamentary elections. Sources: UNDP, Human Development Report 2000, 2002

4.4 Economic system

Between 1998 and 2003, Hungary continued to develop its organization of the market and competition. There was some statist intervention that impeded the privatization process in a few, isolated areas, such as the re-nationalization of companies. Foreign exchange restrictions were completely lifted and foreign trade was further liberalized. Antitrust laws were reformed and now correspond to

Western European standards. The capital and banking systems remained stable and effective despite the poor economic situation. Bad loans declined steadily since 1998 and the transparency of the financial and capital markets increased during the period under study.

4.5 Economic performance

Overall economic development was stable and successful during the period under study. Progress was made in inflation and exchange rate policy, and the rate of price increases has been reduced significantly since 2001. On the flip side, the Hungarian government's fiscal and debt policy ceased to be stability-oriented after mid-2001. Since then, the loss of tax revenues and an increase in government spending have led to rising new debt, particularly in 2002. The increase in primarily consumptive government expenditures is reflected in the current account. The current account deficit was at about 4.7 % of GDP in 2002. For the next few years, a return to tight fiscal policy will be essential, particularly with regard to Hungary's prospects of joining the European Economic and Monetary Union but also in order to get the budget deficit under control.

Table 3: Development of macroeconomic fundamentals (1998-2002)

	1998	1999	2000	2001	2002
Real GDP growth, in %	4.9	4.2	5.2	3.8	3.3 (est.)
Exports of goods, in \$ billions	19.7	21.8	25.4	28.1	31.0 (est.)
Imports of goods, in \$ billions	22.1	24.0	27.5	30.1	34.1 (est.)
Inflation	14.2	10.0	10.0	9.1	5.3 (est.)
Unemployment, in %	8.9	6.9	6.6	5.7	5.9 (Q4)
Budget deficit or surplus, in % of GDP	-7.0	-4.3	-3.5	-3.3	-9.5(est.)
Current account balance, in \$ billions	-2.3	-2.1	-1.5	-1.1	-3.1(est.)

(est.): estimate based on the last 3 quarters.

Source: European Commission 2002; Dresdner Bank 2002; Bank Austria 2002.

5. Transformation management

5.1 Level of difficulty

Transformation in Hungary has been smoother than in most other post-communist European countries. Politically and economic speaking, the baseline conditions were favorable. Even under the communist system, some free-market structures had emerged. The level of economic development was relatively high as compared with the other Eastern bloc countries and the development structure was balanced. Further early advantages to Hungary's transformation included a solid level of education, a wealth of well-educated and well-trained workers, secure borders and the absence of violent conflicts. In addition, Hungary's society is ethnically homogeneous and the intensity of ethnic, religious and social conflicts was low. Only the situation of the Romany held a certain potential for conflict. However, parliamentary democracy was only weakly rooted in Hungary's civil society after the collapse of the communist regime.

When Orbán took office in 1998, a stable democracy was in place, and for the second time since 1994, a smooth transfer of power to a new government through changed parliamentary majorities ensued. Basic rights and minority rights were safeguarded; the three branches of government respected each other and worked together constructively. At the time, fighting corruption and reforming the judiciary were on the agenda. On the economic front, the Bokros Package was bearing its first fruits when the FIDESZ administration took office. The package was an economic stabilization program launched by the previous, social democratic government. It was a necessary move, yet unpopular because it involved substantial cuts in welfare spending. For the reasons mentioned above and despite the deteriorating economic situation between 1998 and 2003, the level of difficulty for continued democratic and free-market transformation is to be rated as low.

5.2 Reliable pursuit of goals

The Orbán government's strategic priorities lay in completing the system change that began in 1990 and that the FIDESZ viewed as having been interrupted by the social democratic government of 1994-1998. At the same time, the FIDESZ wanted to create a new social elite and establish a firm foothold for it in politics, the economy and society. During the FIDESZ administration and the election campaign, reform policy was focused entirely on EU accession. All economic and institutional reforms were measured against the aim of accession until mid-2001. In essence, Orbán carried on the previous administration's rigorous reform policy, setting new macroeconomic directions by abandoning the crawling peg exchange rate regime while pursuing a successful anti-inflation policy.

However, in terms of economic policy, the administration was certainly tempted to pursue a platform of national statism, for instance by favoring Hungarian business and discriminating against foreign investors when awarding public contracts. This “populist economic nationalism” was intensified by the re-nationalization of some companies. Orbán’s administration continued the reform of the judiciary and adopted a long-term anti-corruption strategy. In terms of social policy, it also continued to reform the pension system. However, it repeatedly postponed a much needed thorough reform of the healthcare system and then completely tabled it. It also announced numerous infrastructure measures but only partially implemented them.

As part of the election campaign the incumbent FIDESZ government also abandoned its restrictive, stability-oriented budget policy in favor of a loose, populist spending policy despite the loss of tax revenues. Despite the institutional reforms that were completed, Prime Minister Orbán’s idea of democracy resulted in an about-face in the relationship between the government and the opposition. The election campaign caused rifts in politics and the economy and undermined the basis of mutual trust and reliability of expectations.

5.3 Effective use of resources

The FIDESZ government favored statist economic policies that tended toward populist redistribution. Their stability and economic policy reforms were largely based on the 1995 Bokros Package introduced by their socialist predecessors. Orbán’s domestic and social policy lacked consistency and creative drive. Instead of carrying on with the reform policy, he relied on the status quo. Although the judiciary and the central government’s administrative structures were reformed, reforms to the healthcare system, the education system and local administrative structures largely failed to materialize—despite favorable economic fundamentals. The same is true for the infrastructure, where rail, road and bridge projects were announced but then rarely carried through. Shortcomings in social services have not yet been remedied.

The government did take up the fight against corruption by adopting a long-term strategy. A new legal framework was created for this strategy. Yet many areas of the public sector are still considered corruptible. Although the FIDESZ took office in 1998 with the aim of restoring the citizens’ trust in government, the Orbán administration also awarded numerous lucrative government jobs and contracts to its favorites. There are civic traditions in Hungary, but they could only be put to use for parliamentary democracy to a limited degree between 1998 and 2002, as in the years following 1990.

Instead, Hungarians were divided into two more or less equal camps. Civic groups that could act as intermediaries by stepping into the debate are still too

underdeveloped. Traditions of the rule of law, which were revived by the first moves toward liberalization, made Hungary an attractive location after the regime change. Secure framework conditions attracted a high influx of foreign direct investment after 1989—something that still characterizes the Hungarian economy today. However, this status was significantly weakened by the Orbán government's lack of political credibility between 1998 and 2002.

5.4 Governance capability

On the whole, Viktor Orbán had enough parliamentary authority during his term in office to implement reforms. He did not always sufficiently respect the constitutional checks and balances in his actions as head of government. Management achievements between 1998 and 2003 must be viewed critically, from both a democratic and an economic point of view. The key players during the FIDESZ administration can hardly be described as being flexible or capable of learning. Nation, Catholicism, family and strict anti-communism were the touchstones around which the thoughts of Viktor Orbán, László Kövér, József Szájer and János Áder revolved. There were no truly innovative reform policies, but there was a universal claim to leadership that was exercised through a strategy aimed at concentrating power, a command economy, and the reduced role of municipal governments. The result was the misallocation of economic resources through re-nationalizations and re-privatization attempts and through public contracting practices.

As regards economic transformation, the key fundamentals for 1998 through 2002 indicated that reform policies were successful. Economic growth and successes in stabilization were more the result of measures taken by the previous government than Orbán's policies. The change of course on budgetary policy as part of the election campaign was also detrimental. In macroeconomic terms, it was neither prudent nor clever and it pushed Hungary closer to the days of double deficits that it had experienced before 1997 in both the federal budget and current account. On the domestic front, the return to nationalism and Orbán's "majority rules" concept of democracy when dealing with the opposition was problematic and testified to the unreadiness to learn with respect to participatory, minority-sensitive and consensus-oriented practices within a democracy.

5.5 Consensus-building

Building a market-based democracy was not called into question by the key political decision-makers between 1998 and 2002. Influential anti-democratic veto players are not active in Hungary. However, there are segments of Hungarian society that are susceptible to nationalism and xenophobia. The FIDESZ government's ability to moderate political conflicts in order to prevent them from

widening existing rifts must be rated as low indeed. Even in the 1994 election campaign, Orbán compared the social-democratic government with the old socialist nomenklatura. The campaign dragged the voting public into the conflicts of the elites and resulted in divisions within the economy and society. Parliament was sometimes pushed to the sidelines, and the work of the opposition was hampered. Rather than seeking compromise, the government sought to trammel and neutralize the institutional checks and balances to executive power almost to a point of unconstitutionality. Yet direct conflict was avoided. Under the new social-democratic government, all of the democratic traditions of parliament have been revived and the new Premier, Medgyessy, is making a concerted effort to use integrative policy to heal the rifts that were created during the election campaign.

5.6 International cooperation

Hungary entered into its first trade agreements with the European Community in 1989 and has since steadily expanded its foreign trade with Western Europe. Hungary became a member of the WTO in 1995, joined the OECD in 1996 and NATO in 1999 under Orbán. In 2004/2005, the unwavering policy of Western integration will climax when Hungary becomes a member of the EU. The World Bank and the EU's Phare Program are making an important contribution to the modernization of Hungarian society. At the government level, cooperation programs with Canada, Switzerland, Germany, Austria, the Netherlands and France are playing an important role in the training and retraining of administrative workers and economic officials.

Hungary has become an important, reliable international partner that is helping to promote economic reform and stabilize the security situation in the region. Immediately after joining NATO in 1999, Hungary participated in the air assault on Yugoslavia by allowing NATO to use several of its airports and its airspace. In its foreign policy toward its neighbors, the Orbán administration advocated national interests more strongly than its predecessor had. Political initiatives launched by FIDESZ and comments made by Orbán tainted Hungary's relations with Romania, Slovakia, Serbia, Ukraine and the Czech Republic. This is because Orbán constantly criticized the situation of ethnic Hungarian minorities in these countries. The neighbors feared that Orbán would actively support the breaking away of areas inhabited by Hungarians.

Orbán remarked that the Czech Republic could hardly become a member of the European Union if it did not annul the Beneš Decrees, a comment that led to a series of diplomatic imbroglios and weighed heavily on the two countries' relations.

6. Overall evaluation

(1) *Baseline conditions:* The baseline conditions for continued transformation between 1998 and 2003 are to be rated as very positive. Functional and efficient free-market structures existed even before this period. Problems of stateness that might have jeopardized the consolidation process did not exist. Democratic institutions were stable; the three branches of government shared mutual respect and worked together in a constructive manner. Civic traditions and traditions based on the rule of law contributed to the security of basic and minority rights. Reforms that were necessary for the sake of stability but nevertheless unpopular had already been carried out by the previous government and had begun to show their first positive results at the time the FIDESZ took office.

(2) *Current status and evolution:* On the whole, the development of democracy and a market economy stagnated between 1998 and 2003. The system of checks and balances suffered under Premier Viktor Orbán's sometimes authoritarian concept of democracy. The Constitutional Court functioned as an effective check in this stage of the concentration of executive power. While other institutional counterweights were neutralized and sidelined, the Constitutional Court proved to be a strong, independent authority in its run-ins with the administration.

Within months of taking over after defeating Orbán in the April 2002 parliamentary elections, the new social democratic government eliminated many of the deficiencies caused by its predecessor. It brought democratic practices back to the parliament, respected the constitutional role of the opposition, established the financial independence of the judiciary from the executive, and ensured that supervisory committees of public radio and television were put together in a less partisan manner. The FIDESZ government cannot be accused of making any severe macroeconomic mistakes between 1998 and 2003, although the abandonment of stability-oriented economic policy and the re-nationalization of some companies was a step backward in terms of reform policy. Moreover, no truly significant reforms were launched during the FIDESZ' term in office despite favorable economic fundamentals.

(3) *Management:* The verdict on the Orbán administration's management is negative. Politically, Orbán's government practices were detrimental to democracy. Economically, Orbán based his policy largely on the reforms made by the previous administration and failed to implement more far-reaching reforms himself. The FIDESZ government was incapable of handling political conflicts in a manner that would prevent divisions. Internationally, Orbán consistently pursued a policy of Western integration that would culminate in Hungary's accession to the EU in 2004/2005. His nationalist gestures toward Hungarians living in neighboring countries tainted Hungary's political relations with its immediate neighbors.

7. Outlook

The FIDESZ administration was time lost for Hungary's further transformation to a consolidated democracy and market economy, but it does not seem to have done any lasting damage apart from the polarization of the political arena. Its defeat in the 2002 election resulted in the third democratic change of government following 1994 and 1998. It showed that Hungarian democracy is working well. The close vote gave expression to the fact that the FIDESZ government's heavy involvement in business and industry, the media, and daily life would not be tolerated. Péter Medgyessy and his new government have slim majorities in parliament, but his first months in office show that the new social democratic administration has enough strength to push forward more reforms and to heal the rifts in Hungarian society.

Steps taken under Medgyessy have already remedied some of the ills of Hungary's democracy that were created under Orbán. Now, what is needed now are a continued strengthening of an independent civil society, reforms of the local administrations and the continued fight against corruption. In addition, Hungary needs a renewed healthcare system and a return to consistent, stability-oriented fiscal and economic policy. Although the years from 1998 to 2003 have to be seen as years lost, Hungary is still leading the way toward reform among the post-communist countries of Central and Eastern Europe.