Transition and monetary policy

Katalin BOTOS

Theoretical and practical experts often raise the question why the methods and aim of monetary and fiscal policy remained unchanged after the political transition in Hungary. The simplified answer is because of the IMF conditions. But only a more detailed analysis could answer a wide range of other emerging questions:

Couldn't it have happened in another way? If so, why not? Why was monetary restriction unavoidable in the period of the hidden system-transformation? What is the relation between economic growth and monetary-fiscal policy? What foreign exchange policy was necessary to create balance of payments equilibrium? What is the influence of FDI on the economic growth of the country and the balance of payments? What kind of challenges do we face in the state household in the period of EU accession? Which kind of support does economic policy need from monetary policy at the beginning of the 3rd millennium? These are the main issues the study tries to answer.

Key words: monetary policy, systemic transformation, EU accession, capital inflow, public finance

Working capital investments and investment stimulation in Hungary

Katalin ANTALÓCZY

Hungary played a significant role relating to working capital investment per capita during the transition period in Central and Eastern Europe. After privatisation has been finished domestic working capital inflow entered into a new phase in the last third of the 1990's which was characterized by stagnating capital inflow of approximately 2 billion US dollars annually, a growing importance of owners' credit, significant amount of profit reinvested and slowly extending volume of capital export.

In our study we look a domestic system of investment stimulation currently working and compare it to the practice of the European Union. Following this, I investigate the possibilities of distinguishing between the differently motivated investor groups and then the chances of their success. The most important conclusion of the study is that Hungary needs first of all export-oriented network building, the domestic connections, forward placing, growing value producing investors based in the current fundamentals and the desired course of development.

Key words: working capital inflow, investment stimulation, market and export-oriented investors, investment matrix

Some lessons from growth theory for catching-up countries

István DEDÁK

The evolving revolution dating from the second half of the 1980's has brought extraordinarily accurate and precise analysis of developing processes of national economies to the theory of economic evolution and has also led to consistent theories with empirical data. As a consequence, modern growth theory offers many examples for countries with emerging economies and also contains guidelines about macroeconomic areas to which economic policy must pay additional attention. Special relevance is given to the theoretical contexts of economic catching-up by the fact that in most Eastern European transition states economies have started a dynamic growth in the middle and in the second half of the 1990's after the recession and transformation. In spite of the ongoing growth many uncertainties and questions have risen regarding the transition process. Problems have been connected mainly to the durability of growth, the possible time of catching-up and to the real extent of the growth rate of catching-up. In our opinion, deductions connected to the time of catching-up and the growth rate are formulated that in many cases lack economic reality.

In our study we make an effort to summarize some of the most relevant lessons of evolutionary theory without totally covering the field and we will present some macroeconomic problems of the domestic growth process.

Key words: economic emerging, growth rate, rate of savings, public debt

Financial policy, saving and public choice

Péter CSILLIK

The globalizing world in the revolution of electronics gives a chance again to Hungary to transform from a country of the semi-periphery into a country of the semi-centre by intelligent cooperation. To cooperate efficiently with multinational companies in the long-run we must build a strong supplier background. To achieve this, adequately high interest rates are a pre-requisite for stimulating domestic savings (adjusting to the course of economic growth and accumulated wealth) which slows down growth in the short-run. We don't know for sure which political coalition views sustainable development as more fundamental than fast growth we only know for sure that people will cast their vote on this in 2002. We don't know who will participate in the elections but we can suspect that their financial contribution to the public sector, the size of the sociological group they belong and their degree of education will play a role. Even less do we know which political party the elector is going to vote for but we do know that his position on a scale of power reflects whether

he is interested in transfers or tax reduction, birth or mortality control and what his general attitude is towards short term sacrifices if the burdens are mainly paid by others.

In this study we concentrate on 2 things: in the first part we'd like to point out how savings depend on interest rates in a fully developed and in an emerging economy and why is it essential to adopt a sustainable growth-maximizing and not a short term growth maximizing economic policy. In the next part we will examine using the theory of public choice which of the competing economic policy conceptions get priority in political elections in democratic countries.

Key words: transformation and transaction costs, model of savings, public choice, welfare expenditures

Challenges of economic policy and the state-bond market in respect of joining the European Union

András NEMESCSÓI – Zsolt WERMESER

The establishment of Economy and Monetary Union (EMU) and the introduction of the euro have led to fundamental economic changes both on the national and global levels. The authors give an overview of the effects and challenges of this economic and political conversion, particularly in the field of the monetary and fiscal policy as well as debt management, with reference the Hungarian economy. The authors divide the discussed space three theoretical parts. The first period has started with the signing of the Hungarian – EC Agreement on Association and lasts till our accession to the EU. The second theoretical part of the study deals with the period starting with our EU-accession, while the last part deals with the era coming after Hungary joins EMU.

Key words: EMU, convergence, government securities, debt management, Balassa-Samuelson effect

Fiscal transparency – without index numbers?

Gábor P. KISS

One of the main findings of the study is – depending on the aim of the survey – that there is a need for more fiscal index numbers at the same time. Parallel to this it draws attention to the need to know the theoretical background of different index numbers. Only then can we decide which index number to use in a given case and how to alter existing index numbers. Furthermore according to statistical standards it compares the advantages and drawbacks of index numbers made for analysing. Statistical index numbers - in spite of their apparent advantages - often don't meet the

requirements either of comparability or simplicity. This has as a consequence that the mechanical use of statistical rules ensures only formal comparability. The precondition for comparing the content is to define adequate alternative index numbers for economic analysing. You can read in the study the main analysing index number (SNA deficit) applied by the Hungarian National Bank illustrating how to characterize fiscal policy in the 90's regarding demand impact.

Key words: transparency, deficit, net financial asset, ESA, GFS

Inflation and exchange rates or inflation and exchange rate policy?

János VINCZE

In the past decades pegging nominal exchange rates was frequently regarded as the safest way to control inflation in (small) open economies. After a number of frustrating episodes the opposite view developed, also. According to the latter the nominal exchange rate has a negligible role in the determination of inflation. This study reports some basic facts about the relationship between exchange rates and prices. Then it turns to explanation and inferences. The main conclusions can be summarized as follows: 1. Nominal exchange rates have had a very important role in the determination of inflation in Hungary, both directly and indirectly. Although, we might have a different impression. 2. Prices are influenced both by current and expected exchange rates. 3. Changing the exchange rate regime might alter the nexus between exchange rates and prices, at least in the short term, by making it more noisy at present.

Key words: inflation, nominal exchange, real exchange, exchange rate policy, small open economy

Costs and benefits of macroeconomic policy strategies

András SIMON

In a country where external debt is high the level of interest rates is a crucial element of the interest cost burden. However, high interest rates are an important tool of monetary policy to fight against inflation. How can the two targets, low interest costs and disinflation be reconciled?

The answer relies on the fact that the rate of disinflation depends not only on the interest rate but on the expectations of the market. Inflation expectations depend largely on the credibility of policy focusing on the health of the economy: maintaining or approaching low levels of indebtedness, and demonstrating a history of steady improvement in the inflation rate and exchange rate. In such an economic environ-

ment investors are willing to finance economic growth at a lower interest rate. Such a policy cannot be successful without the cooperation of a prudent fiscal authority but if it obtains the support of fiscal policy, the costs of the disinflation process can be minimized. The present Hungarian economic strategy is based on these considerations.

Key words: disinflation, exchange rate regime, financial stability, sterilization, yield curve

Regulating capital requirements for credit risks: the past, the present and options for improvement

György KOVÁCS

The practice of banking regulation has undergone constant changes during the last decade in Hungary in the context of which laws on financial institutions and then on credit institutions and connecting lower-tier regulations attempted to alter existing rules in accordance with the practices of banks and the requirements of international regulations, respectively. The key element of international and national regulation as well became recommendations or orders on capital requirements, like the capital adequacy ratio of 8% which has had an international career in the last 12 years. This study attempts to introduce the changes in Hungarian regulatory practices regarding capital requirements of credit risks and draws attention to problems of the existing regulation. Some new ideas are also formulated regarding the possibility of enhancing regulation according to international recommendations.

Key words: warranted capital, credit risk, capital adequacy, diversification, risk weighting

Liquidity, solvency, prudency

Katalin BOTOS

Finance is surrounded by mystery although it's a profession. What's more it's a profession in which credit is built upon trust. Banking Supervision and other money and capital market supervisory organs as well have the task of forcing, keeping and helping this trust and prudent behaviour. The right way of circulating money is a Bank Management comprising of trustworthy, reliable people. Prudent banking operations require prudent bank officials. Bank crisis have always been linked with improper management. Actors in business create their own environment. Surveillance cannot be a substitute governance.

Key words: financial policy, Banking Supervision, bank qualification, bankruptcy