TITLE: HUNGARIAN AGRICULTURE AFTER SOCIALISM:
THE BIRTH OF A MARKET ECONOMY

AUTHOR: ANTHONY OBERSCHALL and ZSUZSA HANTO

THE NATIONAL COUNCIL
FOR SOVIET AND EAST EUROPEAN RESEARCH

TITLE VIII PROGRAM

1755 Massachusetts Avenue, N.W.
Washington, D.C. 20036
PROJECT INFORMATION:

CONTRACTOR: University of North Carolina, Chapel Hill

PRINCIPAL INVESTIGATOR: Anthony Oberschall

COUNCIL CONTRACT NUMBER: 810-09

DATE: September 25, 1996

COPYRIGHT INFORMATION

Individual researchers retain the copyright on work products derived from research funded by Council Contract. The Council and the U.S. Government have the right to duplicate written reports and other materials submitted under Council Contract and to distribute such copies within the Council and U.S. Government for their own use, and to draw upon such reports and materials for their own studies; but the Council and U.S. Government do not have the right to distribute, or make such reports and materials available, outside the Council or U.S. Government without the written consent of the authors, except as may be required under the provisions of the Freedom of Information Act 5 U.S.C. 552, or other applicable law.

---

1 The work leading to this report was supported in part by contract funds provided by the National Council for Soviet and East European Research, made available by the U. S. Department of State under Title VIII (the Soviet-Eastern European Research and Training Act of 1983, as amended). The analysis and interpretations contained in the report are those of the author(s).
Birth of a Market Economy:

Hungarian Agriculture after Socialism

Anthony Oberschall
University of North Carolina

and

Zsuzsa Hanto
Gődőllő Agrotechnical Institute

This paper was presented at the Society for Socio-economics in Geneva, July 14, 1996

We thank the National Council on Soviet and East European Research for supporting this research with a grant.
Table of Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Executive Summary</td>
<td>iii</td>
</tr>
<tr>
<td>Socialism and capitalism</td>
<td>1</td>
</tr>
<tr>
<td>The agrarian economy in 1980's socialism</td>
<td>3</td>
</tr>
<tr>
<td>The privatization laws</td>
<td>7</td>
</tr>
<tr>
<td>Bankruptcy</td>
<td>9</td>
</tr>
<tr>
<td>Creating private property</td>
<td>11</td>
</tr>
<tr>
<td>Markets: labor, capital, commodities</td>
<td>12</td>
</tr>
<tr>
<td>Adapting to a market economy: downsizing, decentralizing, incentives</td>
<td>14</td>
</tr>
<tr>
<td>Farm entrepreneurs: large, medium and small</td>
<td>18</td>
</tr>
<tr>
<td>Market coordination</td>
<td>21</td>
</tr>
<tr>
<td>The moral economy of system change</td>
<td>24</td>
</tr>
<tr>
<td>Conclusion</td>
<td>29</td>
</tr>
<tr>
<td>Bibliography</td>
<td>33</td>
</tr>
</tbody>
</table>
Executive Summary

Findings from a survey of 107 Hungarian farm enterprises that succeeded collective farms, and other related research, indicate that:

1. In the 1980s, collective farms undertook internal contracting and outsourcing to improve their productivity and to cut costs, with some success.

2. Loss of Eastern markets, an end to subsidies and price supports, and the depression of 1990-94 had devastating consequences: Farm output, employment, productivity, exports, and investment all declined; indebtedness increased; a quarter of 1,500 collective farms went bankrupt or had to be completely reorganized.

3. The farm privatization legislation on common property division, land privatization, and enterprise transformation shifted 90% of agriculture into the non-state, private sector. The goal of establishing a commercial family farm economy, as in Western Europe, did not succeed. Socialist agribusiness (huge collective farms) has become private-enterprise agribusiness (cooperatives owned by shareholders who are employees and retired workers). However, cooperatives have downsized, and many small farm enterprises have spun off or have started.

4. The privatization has been accomplished, albeit at considerable transaction costs and social costs (unemployment, forced retirement, loss of earnings, loss of social benefits). The surviving farm enterprises have downsized, increased incentives, and made internal changes for more productivity and profitability. In 1995, some enterprises were breaking even or showing profit for the first time since the late 1980s.

5. The greatest remaining problem for Hungarian agriculture is market coordination between large enterprises, the food industry, and one million small, part-time, family farming units (many worked by employees of the large farms). Uncertainty, volatile price changes, shortage of credit, and lack of coordination between producers and buyers result in shortages followed by surplus production, mismatch of quality supplied and demanded, underutilization of resources and duplication, and other inefficiencies in the farm economy as a whole (not due to inefficiency and incompetence in enterprise management).

In short, though a market economy has been created, it isn’t working well yet. When market coordination improves, new capital is invested, and market morality becomes widespread, the transition from socialism to capitalism will be complete.
Birth of a Market Economy:
Hungarian Agriculture after Socialism

The change from socialism to a market economy in Eastern Europe is an opportunity to compare socialist and post-socialist institutions, and how a market economy is created by human agency. Institutions don’t just happen, nor are they costless. They take time and effort to establish. There are winners and losers. They are judged on fairness and justice. Change may not create more efficient institutions. Looking at economic history, North writes that (1990, pp. 7-8) “Rulers devised property rights in their own interest and transaction costs resulted in typically inefficient property rights prevailing... [economic] actors frequently must act on incomplete information and process the information that they do receive through mental constructs that can result in persistently inefficient paths.” People have a limited choice about molding institutions. It is limited because international macroeconomic structures and national decisions by political parties and legislatures shape the outer contours of institutions; it is nevertheless a real choice because the local economic agents’ responses to national and international forces are varied and determine the inner configuration of new institutions.

We have studied Hungarian agriculture in the last years of socialism and the first years of post-socialism. The first question we raise is to what extent key dimensions of a capitalist economy such as private property of the means of production, competition, markets, free entry of entrepreneurs into economic activity, bankruptcy after business failure, job loss due to incompetence or labor redundance, were present in 1980’s socialism. A second and related question is what the differences are between socialism and a market economy, and why and for whom the transition proves difficult and costly. Last we ponder how economic actors - farm managers, new entrepreneurs, small family farmers, middlemen, farm workers - with imperfect information, imperfect mental constructs, and an imperfect understanding of a market economy none have experienced - create institutional change within constraints set by laws, policies and economic forces originating from national and international sources.

Socialism and capitalism

Capitalism is an economic system in which the means of production, distribution and exchange are in large measure privately owned and directed (Webster dictionary). For there to
be capitalism, there must be entrepreneurs and managers who have a stake in the profitability of their enterprises and assume personal responsibility for failure. Ultimately, that means bankruptcy results in a real loss. For Kornai (1990) the “soft” budget constraints under socialism, with the state ultimately bailing out failed enterprises, more than any other practice, blocked the evolution of a genuine market economy from “market” socialism. We must inquire to what extent private property and private entrepreneurs existed in socialist agriculture, whether there were bankruptcies in state and collective farms, and what changed in the 1990's.

Competitive markets are central in capitalism: labor markets, capital markets, land markets, commodity markets. Markets allocate scarce economic resources by responding to supply and demand. According to Max Weber, a market exists “whenever there is competition...for opportunities of exchange among a plurality of potential parties,” (quoted in Swedberg, 1994, p. 271). The integration of all these markets into a competitive economic system is what constitutes a market economy. In socialism economic resources are allocated centrally by state officials according to a plan, and not by markets. More concretely, Kornai (1990) demonstrated that allocation was by bargaining between state officials and state managers. We must inquire how resources were allocated in socialism and what was different in the 1990's.

A third dimension of the difference of socialism and capitalism are work incentives for ordinary employees. A frequent criticism of socialism and of state enterprises is the high job security of workers regardless of performance and of organization need, and the weak linkage of performance to wages and bonuses.

Closely related to work incentives is the organizational structure of an enterprise. Under socialism, planners and politicians created huge, multivillage collective farming enterprises which were difficult to manage centrally and which diluted personal responsibility. Williamson (1975) has shown organizations vary greatly on transaction costs. Some activities need no organization, only markets; others are best done in organizations; still others activities should be done by autonomous units within a decentralized organization. Under the competitive pressures of capitalism, the size and internal structure of an organization will change in response to transaction costs. We compare the internal organization structure and organizational configuration of agriculture under socialism and in post-socialism.
Private property rights are at the heart of capitalism. A common criticism of socialism is that without well-defined and secure property rights, people have no incentives to invest and that they devote their talents and energies to the small islands of private property that survived within socialism. We examine how managers and workers disposed of common property and user rights and what changed when private property was instituted.

Sixth and last, we look at the change from “redistributive integration” in the economy under socialism to “market coordination” under capitalism (Szelenyi et al., 1994). What integrated the agricultural economy in the 1980's and how did that change in the 1990's? A number of practices and policies, from taxation and price supports to subsidies and state loans, and a number of organizations from the food industry and wholesalers to collective farms and small family farming together shaped socialist agriculture production and exchange. What changed when privatization laws were implemented and macroeconomic policies were modified? Did these changes result in a market economy with market coordination? How well are economic actors responding to market signals, incentives, and opportunities?

The agrarian economy in 1980's socialism

Hungary in the 1980's had large farm enterprises (agribusinesses) and small plots cultivated by part-time farmers, and very little in between. The largest enterprises were state farms which were similar to large state industries except for what they produced, with an average of 950 employees on 7600 ha. The other large enterprise was the collective farm, with an average of 400 workers on 4400 ha., combining what used to be the agricultural resources of several villages under one management team. The collective was owned by the members, including numerous retired members. The land itself, by the late 1980's, was owned by the collective farm itself (about 2/3) and the members (1/3). Members could not withdraw their land or a share of other assets, nor could they sell their share, nor did they receive more than a nominal rent for land. Neither the land nor the members’ ownership of the collective was the same as private property in capitalism (Bell, 1984; Swain, 1985).

In the 1960's and early 70's Hungarian agriculture had mechanized and collective farms became agribusinesses. Management, professional staff, and some skilled workers (farm
equipment drivers and mechanics) were graduates of technical institutes and were employed in a national labor market, whereas semi and unskilled workers were mostly from the villages of the collective farm. Some nonlocal managers and professionals did not join the collective and were classified as employees. Those who did stay for several years tended to marry locally. Collective farms were highly stratified and specialized, which was reflected in the hierarchic structure and the salary and wage scale (Held, 1980; Swain, 1985). The higher one was in the structure, the more likely one was a year round, full time employee. Unskilled labor had only a minimum number of days per year work guarantee. On the other hand, job security was almost 100%, and children of members were guaranteed employment after a period of apprenticeship. Villagers stayed in the collective farm because it provided them important benefits. Villagers' strategy was to maintain one family member in the collective while others were commuters to a city in non-farm employment.

The most important benefit was the right to a plot of land, called a “household” plot, about 0.5 to 1 ha, which was joined to garden and houseplots and could be farmed by family members. They could also convert that user right into cash or grain, e.g. used for animal fodder. The collective offered to plow, supply fertilizer, and market the output. For unskilled workers, the earnings from small farming might be as much as the earnings from collective farm employment. Small farming was known as the second economy and produced an abundant supply of labor intensive farm products, vegetables, fruit, pork, eggs, etc. Many village families were selfsufficient in most of the food they consumed. In 1984, it was estimated that 62% of vegetable production, 59% of fruit, 57% of hogs and 44% of poultry were produced in the small farm sector (Kovach, 1988, p. 47).

There were other benefits of membership. Some collectives owned holiday facilities, paid a stipend for members' children's studies, provided transportation to a city hospital, allowed use of tools, equipment and building materials for house construction, and the like. Thus membership in the collective was a complex and fuzzy contract in as much as it encompassed family members and customary services in the village.

For the collectives' management, such a diffuse labor “contract” had advantages as well. The principal one was access to villagers' labor at peak farm work during the harvest. No matter
how mechanized, farm work has a fluctuating demand for labor. In many countries, migrant farm workers from underdeveloped countries supply it, at low wages. By providing the household plot and other benefits to members, managers had access to a pool of casual part-time village labor without obligation for year round work. By providing non-cash benefits, the payroll tax was reduced. There were some disadvantages. Villagers’ energies and priorities were for their own production, as when frost or flooding required their labor. Yet on the whole the non-wage benefits of collective farm employment were an ingenious adaptation by both managers and ordinary members to economic relationships and transactions under socialism.

Managers faced a labor surplus after the most busy months and solved it by diversifying into non-agricultural activities. The 1980’s collective farm usually had several divisions: one or two for the principal crops; one or two for livestock; one for machinery and repair; a dairy; a cannery or other food processing; a transportation branch; timber and sawmill; and increasingly also manufacturing, e.g. shoes and handbags, where unskilled female labor was employed. Some of these non-farm sideline activities were more profitable than farming, especially in marginal farm districts, yet there were limits to extending a collective farm into a non-farm business due to the policies of state banks, the food industry and state economic managers. Nevertheless, diversification was security against farm price fluctuations.

By the 1980’s, collective farm managers knew about the problems of large and diversified agribusinesses, and in particular the problem of incentives for managers and workers alike. Some created a decentralized enterprise giving more responsibility to division heads and holding them accountable for division performance, with bonuses matching performance. Within divisions, a contract might be signed by a team of workers with the collective under which a facility, e.g. a dairy, would be rented by the team and earnings beyond the contract amount kept as its profit. Another incentive scheme was “putting out”: the hog division would sign a contract with members and villagers for piglets they would raise to a weight with a buyback at a given price. It ensured labor-intensive care and a profit opportunity for those who would do such work. The risk for the piglets’ death - with a 10% mortality rate not negligible - was assumed by the contractors. Another common form of internal contracting was for fruit and other labor intensive crops. Families would sign a contract for picking cherry trees or raspberries to be sold to the
collective at a stated price. The collective might spray and market, the family would prune, pick and pack. The contracting family could make a profit, but also assumed risk of loss from frost or neglect.

To what extent these innovations made the collective farms more profitable is difficult to tell. Socialist accounting and the elaborate bookkeeping manipulations and “creative” accounting of managers to disguise real earnings, inflate production figures, reduce taxes, and maintain eligibility for subsidies, was one of the irrationalities of socialism. In our interviews collective farm managers openly talked about these practices since they were common knowledge. Some sources indicate that in the 1980's a third of the collectives were loss making and that half had accumulated large debts. If that is the case it suggests that socialist farming was caught up in the general malaise and economic slow down of the entire Hungarian economy in the late 1980's, indeed of the socialist economies as a whole.

At the margins of these large collective agribusinesses and several hundred thousand small family farms that collective members and other villagers cultivated both for subsistence and for market sales, there existed some 20,000 small to medium sized family farms which had broken with socialism (Szelényi, 1988). They made no use of state credit, employed only family labor, and retailed directly to consumers in farmers’ markets. These entrepreneurs often had impressive technical skills as in the case of a Békéscsaba hothouse pepper grower we interviewed who managed to produce peppers in the winter two weeks ahead of the competition. These small entrepreneurs were cramped for space but managed, in the absence of a land market, to lease some land from villagers, local government, or a collective farm. In the 1980's as the “putting out” system progressed in the collective sector, it was possible for family farm entrepreneurs to contract with collectives for poultry, geese, hog, duck, etc. farming on a large scale. Still until the demise of socialism, the expansion of such an independent farmer into crop farming was curtailed by lack of access to credit and land. According to Kovach (1988, p. 84), only about 15% of these farm entrepreneurs had the capacity for substantial commercial farming. In the aggregate, they were a small part of the total agriculture economy.
The Privatization Laws

The transition to a market economy, from 1989 to 1995, took place under difficult macroeconomic conditions, in a hostile political milieu for collective farms, and severe droughts in 1992 and 1993. Farm subsidies declined sharply, exports to East Europe and post-Soviet successor states were down, the domestic food market shrunk as real incomes fell and unemployment rose. Farm prices rose less than energy prices and farm inputs; capital equipment was not renewed; animal stocks were cut; fewer crop acreage was planted; employment in agriculture nosedived (AKII, 1995b). Banks lent at a prohibitively high 30-40% interest rate.

Economists and farm experts expressed doubt about whether technologically sophisticated socialist megafarming could be privatized into medium sized entrepreneurial farm enterprises (Pryor, 1990; 1991). It was not possible to divide common property into private property when much common and state property was immovable and non-divisible, e.g. a huge cold storage facility or a huge dairy, and when much farm equipment was too large for small-scale farming. The entire farm infrastructure from technical operating production systems to credit and marketing had been geared to large agribusinesses. Farm workers had become specialized and many had no knowledge of the spectrum of activities necessary for private farming. How was the debt of collective farms to be allocated among new owners? After a survey of collective farming in several countries, Pryor (1991, p. 3) wrote that “in certain historical situations, collectivization is not reversible so that any large-scale measures taken to return to individual farming are doomed to failure.” Though it is possible to make collective members and employees shareholders by a simple legal procedure, it leaves unchanged organization structure, incentives, management style, personal responsibility, and the economic environment of farms. Pryor suggested a two pronged institutional change to a market economy: first, the labor intensive small family farms would be totally privatized and gradually enlarged, and second, the autonomous teams working for profit would gradually acquire farm assets as private property until the collective shrinks and eventually self-destructs.

The first post-communist government intended to dismantle collective farms and to create in their stead a vigorous commercial family farm economy. To accomplish this purpose, three important pieces of legislation were passed in the early 1990's: a partial compensation law for
restoring land to pre-communism owners and their heirs; a common property division law for collective members and employees; and a collective enterprise transformation law. Land compensation (kárpotlás) partially restituted collectivized land to original owners and their heirs, as well as some land to employees and former employees, under a voucher scheme and local land auctions. By mid-1995, in some 21,000 auctions, 535 thousand people had gotten close to 2 million hectares land, about 40% of all arable land in Hungary, for an average four ha. land. The division of common property led to a further distribution of 1.3 million ha. to 1.5 million persons, which included many who had also been compensated (AKII, 1995a; Andorka et al, 1994). Together these two laws transferred 3.3 million ha. into private property, equivalent to 70% of all arable land. About half this land is farmed by small family farmers, many part-time; the other half is rented by farm enterprises that succeeded the collective farms (AKII, 1995b).

Under common property division (vagyonnevesítés) collective members had choices within broad guidelines for division. Members could take out a physical share, but less than 10% did because their share was insufficient for starting a family farm. It is estimated that 40% of assets in the form of shares passed to retired members, 20% to former members and employees, and 40% to current working members (Andorka et al, 1994). Shareholders have seen the value of their shares steadily decrease, most obviously in bankruptcies and liquidations, but more commonly when farm enterprises are downsizing, selling assets, and are unprofitable. There is no market in farm shares: in many places members are buying shares from “outsiders” and retired at 10% of nominal value. Although common property division legally created private property, for many its value turned out to be less than their user rights had been. Nevertheless, many farm managers have protected all shareholders’ interests.

The reorganization of collective farms (átalakulás) made them into cooperatives and limited liability companies. At the end of 1995, the 1300 collectives had become 2100 cooperatives and 3600 companies. These are much smaller than the megacollectives - the companies tend to have less than 11 employees whereas most of the coops are between 30 and 100 (AKII, 1995a). A large number of collectives and their successors have gone bankrupt, perhaps as much as a quarter, with consequences we will analyze. As a result of these downsizings and bankruptcies, employment in agriculture enterprises is down to 180,000 from
600,000 in the late 1980's. Some of those who are no longer employed are part-time farmers on the land they got under compensation, have retired, are unemployed, or work part time. A distinguishing feature of the transition from socialism to capitalism has been “privatization by bankruptcy”.

**Bankruptcy**

A crucial flaw in socialism is the absence of bankruptcy for state enterprises. Instead, under soft budget constraints, managers bargain with ministry officials and state banks for financial support when enterprises fail. Over time unprofitable and inefficient enterprises accumulate and the economy stagnates. Was this true for Hungarian collective farms?

According to Juhász (1990, p.11), “one third of Hungary's large scale farming operations became loss making for a lasting period [under socialism] and there were no mechanisms in the system which could make the necessary corrections.” Donáth (1980) wrote that in the 1968 economic reforms the debts of collective farms were canceled, and that 200-300 out of 1300 were subsequently loss making. There was an obvious problem with how to terminate or turn around failing enterprises under socialism.

From 1990 to 1993, a fifth to a fourth collective farms were in various stages of bankruptcy. In a nationwide survey of the newly organized cooperative farms, one third expected to go bankrupt (Varga and Toth, 1995). Bankruptcy was a new institution in post-socialism and not uncommon at that. These figures hide however some disguised bankruptcies under socialism and bailing out failed enterprises after socialism. Here are some instances of both.

The collective farm at Lövöpetri was forced by state officials to merge with a neighboring collective when it became hopelessly indebted in 1982. In the merger, jobs were terminated; offices, repair shops, a warehouse were closed; and all the farm equipment transferred. Lövöpetri was stripped down to a single grocery store, and farm workers commuted daily 15 km. to work. Although the change was termed a "merger", there were very real penalties to the collective and the inhabitants of Lövöpetri.

Another bankruptcy disguised as a "change" took place in Botpalád in 1986 after the collective farm was deep in debt. A group of seventy farmers made a deal with the creditors not
to auction its assets, but to let them restart as a downsized, "specialized" collective, for which they got an interest free loan from a ministry. In this "change", 130 workers lost their jobs as well as user rights to land. According to our informant, the new enterprise became profitable already the following year because "in the smaller group we understood one another and cooperated better, and we cut down on administrative overhead."

We don't know how common such disguised bankruptcies were under socialism. In the post-socialist 1990's, bankruptcies are frequent, but what in fact happened for some failed enterprises and their employees is that they lose most of their assets (but not land) and their jobs, and a nearby enterprise and/or a small team takes over the salvageable part, which is what occurred under socialism. In a 1995 interview, the president of Veszprémvársányi cooperative said it "took over" parts of the bankrupt Bakonyzentkirály coop, whose dairy would provide additional milk for its cheese factory. One third of the debt was written off by the creditor banks, one third was paid by auctioning assets, and the remaining third of the debt was assumed by a new company owned jointly by the two cooperatives. All this occurred, he said, "not without sacrifices", since many lost their jobs and the sale of assets reduced the failed coops' remaining farm and livestock operations. This 1990's takeover, which is reported as a bankruptcy, bears a close resemblance to the 1982 merger, which was not.

In Fehérgyarmat, in 1995, we were told of a reorganization after bankruptcy which was similar to the 1986 reorganization in Botpalád. A team of 25 former collective farmers formed a cooperative which made a deal with the creditors for renting farm equipment and sheds of the bankrupt enterprise, and continues farming in the locality. In Rozsály, the failed enterprise had to auction its movable assets. But the local government managed to get a low interest loan from a ministry to restart farming by a small team with newly purchased farm machinery. Without the team, the small family farmers of Rozsály would not be able to plow their land.

It is worth noting that under both economic systems a large part of the debt of a bankrupt enterprise ended up and keeps ending up in the national debt, which is one major cause of its growth. In the 1980's as in the 1990's, when a state bank "writes off" or forgives part of the debt - because it is uncollectible - it passes it on to a state ministry which then merges it into the national debt. This will go on for the foreseeable future since in a bankruptcy the state ends up
getting back a devalued asset it has created in the first place. It will take about a decade for agriculture assets paid by private, not state, investment to replace the current stock. This fact puts a constraint on the speed with which "hard" budget constraints can replace "soft" constraints. The mayor of Rozsály underscored this when he said that the collective farm members hadn't lost much when they went bankrupt. Over the years, they converted their earnings into improved houses and their own small farms, and had not invested in the collective because they counted on the state to do it. They still have their houses and small farms, and now they also own some land. What they lost in auctions was a lot of aging farm equipment, some livestock, a few buildings, and farm jobs that paid low wages.

Creating private property

There were three obstacles to the privatization of collective farm assets. Physical division of assets was either impossible without destroying a facility (a cold storage house) or much reduced the value of an integrated facility (when chicken are taken from a huge chicken coop). Much farm equipment was worth more than a member's share and there weren't enough movable assets to distribute among members. When only a few members wanted to exit, it was possible to provide physical assets without impairing viability of the enterprise. In fact, less than 10% of collective members exited singly or in a group. Pryor had been right: privatization by physical division of common property does not work in an agribusiness. There remained asset division by shares.

Share privatization may look good on paper and legally does create private property. Yet share values are worth only what an enterprise's earnings prospects are. With many farm enterprises going bankrupt and even the survivors struggling and not planning to pay dividends for some years, shares were either worthless or had very low market value. The shares that ended up in "outsider" ownership under the privatization law were being bought by coop members at 10% of nominal value. The president of Veszprémsársányi cooperative in fact told us 10% was a great bargain since in his view they should be worth 30% since he was getting profitable once again. But then how was anyone to know in the absence of agribusiness shares in the stock market and the information routinely provided to investors in a fully developed market economy?
Under socialism, a farm worker could not convert his share of common property to cash or some other movable private asset; in post-socialism, the same farm worker could not do it either. The value of private property is contingent on other market institutions: it is not just a legal fact.

The other main farm asset is land. What did land privatization accomplish? Under socialism there was no private property in land except on a very small scale. The collective farms had obtained land through political coercion for free. Villagers had their house gardens at their village homes, and many had user rights with membership in the collective to a "household" plot. It was impossible to put together a holding of 50-100 ha. for viable crop farming. Nor did collective farms sell or rent land to each other except for trivial boundary adjustments.

The land compensation law transferred about two-thirds of all arable land to over half a million new owners in some 20,000 land auctions, at a very low voucher price. Seventy percent of all farm land has become private property. A huge land rental market developed overnight because large farm enterprises are not legally entitled to own land, and many small farmers, the retired, and the non-resident owners don't farm their new land (or only part of it). Because the law put a five year moratorium on land sales to stop speculation in land, unregistered "illegal" sales are taking place and banks do not accept land as collateral for farm loans. Many have gotten land, but for some time will not be able to obtain a market price for it. In border districts, Austrian farmers are renting Hungarian farm land several times below Austrian rents. According to a county land registrar, land prices in the illegal market are a tremendous bargain since land sells at five times its rental value. Some new owners of small plots can't afford to survey and register their land; others have no access roads to it. All in all, land privatization has taken place, but as with other farm assets, further institutional changes are required for a well functioning land market. Private farmers can however rent now for commercial farming, and so can new farm enterprises. The state monopoly on land has been broken.

Markets: labor, capital, commodities

There has long been an agricultural labor market in socialism. The typical village family had both farm and non-farm workers, the latter commuting to nearby cities. The un-and semiskilled workers at collective farms were natives of the village. Unlike the earlier generation
of party cadres, the professional, managerial and technical workers by the 1980's were graduates of agrotechnical institutes and sought employment in a national market. The category "non-member employee" accommodated these workers, some of whom married locally and settled permanently in the district.

Two complaints were common: farm managers were burdened with redundant labor due to obligation to employ collective members, and were unable to dismiss unreliable, thieving, drinking, shirking workers. A farmer who quit his collective in 1992 said "the collective did not punish for bad work... I don't want to work with unproductive people... there is overstaffing." During privatization, all this changed dramatically as farm enterprises downsized employment to cope with the economic depression and to become efficient and increase labor productivity. In addition to the unmotivated and unreliable workers, many others lost their jobs, especially older workers and women.

Under socialism there was no capital market. Farm enterprises financed some capital from earnings, and for large projects and amounts bargained with ministries and state banks. Under this arrangement a fifth of collective farms became perennial loss makers. In the transition, socialist redistribution ceased yet no capital market took its place. Agricultural credit collapsed completely. The most usual problem in 1992 for farm enterprises was that wholesalers and food corporations were not paying their debts to the producers, yet producers had to buy fuel, fertilizer and other necessities for cash, not to mention their payroll. At 35-40% short term interest rates, it was ruinous to borrow. Meanwhile the vice-president of a large bank told us that "the banks had gone to the limit of their willingness to loan in farming." Faced with this credit squeeze, farm enterprises sold and slaughtered livestock on a large scale, reduced fertilizer use, repaired aging equipment instead of buying new machinery, and reduced their labor force. In Szolnok county, according to an agriculture official, the 1989 harvest had taken 10 days, whereas 1991 took 16 days, because aging combines kept braking down. It was the same all over the country.

In 1995 there was still no capital market, at least not for farming. Many agricultural enterprises had gone bankrupt; the survivors had made many changes (to be described in the next section) to stay solvent. A few enterprises managed to raise capital from foreign partners, but potential farm entrepreneurs were for the time being staying out of farming. No rural banks like
the French Credit Agricole had appeared on the horizon nor marketing cooperatives that would
make low interest loan to their members. The economist Csaba Csaki underscored in an interview
(March 1996) that a market economy in agriculture cannot function without a rural banking
system for continuous financing of farming activities. Some successful farm enterprises had
created an internal banking scheme of a central financial and administrative unit making low cost
short-term loans to operating units. But this worked only for viable enterprises and for modest
amounts. Capital markets don't just happen; they have to be created, and no one had.

**Adapting to a market economy: downsizing, decentralization, incentives**

In the 1990's transition, farm enterprises took many measures to cut costs and increase
efficiency. Some measures were rooted in the 1980's enterprise reforms; others were novel.
Cutting the labor force was universal. Very common as well was the splitting of huge, multi-
village collective farms into village enterprises. In the process, one or more parts of
the megabusiness would go bankrupt. In Réde, the largest unit inheriting 46% of assets went
bankrupt because of a lack of experienced, competent management, according to our informants,
whereas another smaller unit at Bakonyszombathely prospered. The new president there told us
he made efficiency gains from shortened travel time, reducing idle farm equipment, and fewer
administrative and supervisory costs, a statement echoed by another coop president at Nagykőrösi.
Both of them underscored the advantage of fewer employees: "if we were 100 workers instead of
220, we would do the same amount of work, perhaps even more," and "having a lot of workers is
a greater liability than having a lot of debt."

Division and downsizing went against socialist mentality and practice, even though one of
the principal architects of collective mega farms had been puzzled about the lack of relationship
between size, productivity and efficiency (Donáth, 1988, p.408ff): "neither profit nor capital
accumulation nor personal incomes of workers are higher on large than on small farms, despite
the tax advantages and higher subsidies for large farms." In the 1990's, though there were huge
efficiency gains from splitting, there were also some losses, as at Rábacsanákk where one village
cooperative was left with a huge repair facility now used for crop storage and another had an
excess capacity for feed storage and livestock. Penyige, a small cooperative, formed a company
with three other cooperatives to share a dryer, silos and to market jointly. New farm enterprises are discovering what the appropriate scale is for various farm operations.

Downsizing is ubiquitous. In a national sample of 104 cooperatives, Varga and Toth (1995, p.50) found that the average workforce declined from 377 to 142 in four years, and keeps shrinking. Here are the detailed findings:

<table>
<thead>
<tr>
<th>Year</th>
<th>Cropland (ha)</th>
<th>All Land (ha)</th>
<th>Workforce</th>
</tr>
</thead>
<tbody>
<tr>
<td>1989</td>
<td>331,441</td>
<td>478,480</td>
<td>39,227</td>
</tr>
<tr>
<td>1993</td>
<td>236,034</td>
<td>331,667</td>
<td>14,744</td>
</tr>
</tbody>
</table>

These figures show the effort made to cut costs and increase efficiency. These aggregate figures agree with our case studies in 1995. In Táp, as an example, the cropland - worker ratio increased from 20.8 in 1991 to 28.6 when we restudied it in 1995. These ratios are also interesting because farmers everywhere said a family farm needed 50 ha. land to be viable, and counting two family workers, the ratio comes to 25 ha./worker, which is just about what the cooperative farms are now achieving.

Cutting the workforce was done in many cases with early retirement, which, according to the president of Cibakháza coop, "saves half the cost per person." Many were put on the unemployment rolls, and some rehired part-time while unemployed. We were told of some who were classified as "disabled" with the collusion of the local physician. Everywhere a freeze was put on hiring, which ended the custom of automatically hiring the children of members after schooling. Rural people tried to cope best they could with the impact of such massive loss of employment. As for those who were still employed in farming, their real wages fell. One manager expressed it thus," great sacrifices had to be made... I lift my hat to the vast majority of the workers." Other cost cutting measures included selling or terminating some units, such as industrial branches, or leasing.
After downsizing, the most common cost-cutting and efficiency enhancing measure was decentralization of the enterprise. Decentralization into autonomous accounting units under socialism was not uncommon. In Marcali, in 1990, production had been decentralized to thirteen teams of six to twenty workers, each signing a yearly contract with the collective. They had the right to hire workers, keep the profits, and borrow money from the collective. The director hoped to change "thirty years of employee mentality" by giving farm workers more autonomy, incentives and responsibility. In our 1990 and 1991 fieldwork farm enterprises had implemented various forms of decentralization called "önszámoloegység" and "működőegység". According to a farm survey, some 30% of large farm enterprises practiced one or both in 1989 (Toth and Varga, 1995, appendix 5). Such internal contracting to teams of workers was combined with "putting out" of production to farm families in the village, as with hogs. Putting out created quasi-private property because workers assumed risk when accepting responsibility for common property and enjoyed the profit opportunities.

In the post-socialist transformation, decentralization was continued into a total corporate restructuring with the formation of limited liability companies attached to a central cooperative. Just how a large privatized agribusiness operates in the 1990's market economy is best explained with a case study from 1991 and 1995 at Veszprémvarsányi. In 1991 it was a huge eight village, 7000 ha., 1500 cows and 1200 hogs, collective farm. It was just introducing a computerized payroll and bookkeeping. It had 17 John Deere tractors, a profitable hog farm which delivered high quality meat to Pápa meatpackers, and was experimenting with bottling and marketing milk because dairy corporations were not paying their bills for milk. In 1995, after the three privatization laws, the collective had transformed into a cooperative, covered still the same eight villages, lost all its land and rents 70% back from the new owners, 40% of its assets are owned by non-resident "outside" shareholders. It carries out the same farming and livestock activities, but under a new ownership and management structure.

Realizing that such a "mammoth" and diverse farm enterprise could not be managed efficiently from one center and destroyed cost consciousness and incentives for workers, the cooperative decided on major restructuring. Six production entities were made into limited liability companies: two crop and livestock companies, a hog farm, horticulture, two repair and
service companies. Each was made the responsibility of an independent management team who hire and fire workers, set wages, make production decisions, and increase their earnings with profitability. No team came forward to claim the sawmill, an apparel plant and another workshop. These were leased to their former managers. Forestry and construction could not be sold or leased and remain for the time being under cooperative management. The cooperative became a holding corporation that owns most of the six companies’ shares, and provides financial and other business services to them for a fee. Company managers had to buy company shares and workers are advised to do the same. Company employees are also shareholders in the cooperative; thus cooperative managers sit on the company boards and company managers are represented on the cooperative board.

At start, 60% of coop assets were assigned to the companies, including some cash reserves, and debt was also allocated in similar proportion. Each company leases assets from the coop, and returns 70% of profit to it. The coop’s earnings are used to repay debt, put into an investment fund, and will eventually pay dividends on shares. The companies have started paying some dividends with their profit, but most goes into investment. The coop keeps close watch on its companies. It loans to them far below the commercial 35% interest rate. Restructuring, downsizing and more efficient management turned the losses of 1991 and 1992 into a modest profit in 1994 and an even better profit was anticipated 1995. The cooperative has been successful at vertical integration into the cheese industry, though not by bottling and marketing its milk. With 25 million Ft. worth of vouchers received for land lost to compensation it bought a nearby cheese factory, which it modernized. Other attempts at vertical integration were blocked by the State Privatization Agency.

Like other collective farms that made a successful transition, Veszprémvarsányi cooperative created a central cooperative linked to satellite operating companies that was a continuation of the autonomous accounting units under socialism. What was novel was the addition of private property in the form of shares and shareholders and greater responsibility for assets. For the time being, shares pay no or negligible dividends since management uses profits for investing in capital equipment (much needed after some years’ neglect) and bolstering wages (that fell behind the cost of living). Nor did the companies create significant new capital since
managers and employees had little spare cash to invest. For the longer run, as Pryor (1990, p.12) foresaw in his privatization plan for socialist agribusiness, the satellite companies can buy a majority of their shares from the coop and form a separate, independent, privately owned farm enterprise. Such a gradual "buyout" is in fact what the director of the cooperative anticipates some years hence.

In contrast to Pryor's and the director's view of a future with numerous medium sized privately owned agribusinesses, the communist intellectual Donáth (1980, p.427-437) had foreseen a socialist future of industrial mega-farming collectives and state farms organized about a "system center" that introduce new technologies, handle credit, provide equipment services and training, and collect data. In this organizational and human relations utopia, manual labor would become almost totally obsolete. Donáth proposed this scheme despite his own data that showed "unit costs rising and profitability stalling" in large industrialized agriculture. As for commercial family farming and medium sized private farm enterprises, communists had relegated them to the dustbin of history, or so they thought. The 1990's privatization laws had made them possible once again.

Farm entrepreneurs: large, medium and small

The Schumpeterian entrepreneur of classical capitalism is both owner and manager of the family business. Under socialism, with large state and collective agribusinesses on one side and small family farms unable to burst the bounds of the second economy on the other, the few commercial family farms were exceptional (Kovách, 1988; Szelényi, 1988). Juhász (1990) estimated in the late 1980's about twenty thousand such farms in a sea of 1.5 million small farms. How are they now faring in post-socialism? Could they become the spearhead for Western Europe type commercial family farming in Hungary?

In 1990 we interviewed a few of these commercial farmers. Rudi, a graduate of an agrotechnical institute, and his family had raised egg-laying hens and pigs in his garden plot for years, like many others in the second economy; then he quit his job as quality inspector for a food corporation, rented a larger plot, built a big chicken coop and pig stalls for 1500 hens and 200 piglets, all with family labor. In 1995, he had got land from compensation, grows the feed he
used to buy, and had expanded somewhat. In the same city a hothouse pepper grower in 1990, with family labor, transplanted, fertilized, prepared beds, harvested, trucked and sold peppers in wholesale markets and directly to food processors. When they needed money, they raised small loans from friends and business associates, never from a state bank. This business as well had survived the 1990's depression, but it hadn't expanded.

Other entrepreneurs were staying out of farming, both in 1990 and in 1995, choosing other types of business until farming becomes profitable. Béla lived on the Tisza and opened an ice cream parlor at his home close to a recreation area; he built a holiday cottage to rent; he made jam and liquor from the plums in his orchard; he did a lot of smuggling across the Ukraine border, but farming he dismissed as a waste of time. That was in 1990. Five years later he was still pursuing many ventures, his two automobiles had become more expensive, and he hadn't bothered about land compensation: "too much paperwork," he shrugged. Some others who did get land and added to it by purchase (with vouchers bought from others) had not entered farming either. Gábor had been a collective farm manager and had for years raised hundreds of chicken, like Rudi. When his family received lots of land in compensation, and after the collective disbanded, he is still a chicken farmer, grows corn for feed, but rents out most of the land. He owns the village grocery store and holiday and hunting cottages next to his house, but won't get into crop farming for the time being. Tivadar, a highly qualified farmer who still is the president of his cooperative, has put his savings and energy into a small winery though he owns 300 ha. good cropland. It is not lack of land or farming skills that inhibits them, but the low profitability of farming and the high cost of outfitting with equipment and farm buildings.

We did locate a few new farm entrepreneurs. They had gotten land through compensation; they had mechanical skills from previous jobs in collectives; they bought farm machinery at auctions cheaply and repaired them; they are a family enterprise; a few are in animal husbandry, e.g. raising geese. All were struggling. According to farm statistics, the total number of crop farmers on the 100-200 ha. scale hadn't changed since the late 1980's despite privatization (Harcsa, Kovách and Szelényi, 1995).

There are new successful entrepreneurs, but they enter farming on a much larger scale, with more capital, as a corporate organization, with non-family employees, and not by incremental
growth of a family enterprise. They compete with cooperatives and other large farm enterprises by having privileged access to capital, finding a special market niche, and possessing unusual human capital. A young German-speaking lecturer at an agrotechnical institute received 70 ha. land compensation with his family, and formed a corporation with three German partners he knew through professional contacts. They put up 90% of the capital. With it the corporation bought the most up-to-date German farm equipment, rents 2000 ha., hired five operator-mechanics, and most important, sells crops in the German and Italian markets through the German partners at well above domestic prices. With 300 ha. per worker, this enterprise has a labor productivity about ten times that of the commercial family farms we observed. Other new corporate farm entrepreneurs have a similar story: access to foreign capital, special marketing niche, vertical integration into the food industry, few but highly skilled and motivated employees. In the aggregate these enterprises are few.

As for the several hundred thousand small family farms which formed the second economy under socialism, most have become owners of cropland as a result of land compensation, but lack the tools, equipment, farm buildings, and access to credit to break out of part-time into commercial farming. Many rent some land to large farm enterprises and purchase farm services, e.g. ploughing. According to a nationwide survey of small farmers in 1993 (Varga and Szijjárto, 1994), sixty percent farm out of necessity and for lack of other opportunity for making a living: they lost their jobs when cooperatives downsized or went bankrupt, though 20% are part-time employed in coops. They do sell some crops and livestock in the marketplace. A majority is over 40 years old and uncertain whether another family member will continue farming. Half of those who farm on a commercial scale (50 ha. and more) still maintain a non-farm job, though in this group one finds farmers who want to expand, rent or buy more land, employ non-family labor and sign contracts with wholesalers. Some are going to grow into medium sized farm enterprises when business conditions improve. Yet the survey demonstrates that the small farm sector after privatization is mostly a continuation of the socialist second economy. Landownership and rental are new, but haven’t made a difference. Privatization has disrupted market coordination in Hungarian agriculture, especially for the small farmers.
Market coordination

The change from socialist redistributive integration to capitalist market coordination has been chaotic and is far from over. In the 1980's most agricultural commodities were sold in the market place. For vegetables, fruit, wine, eggs, poultry, pork, price was set by thousands of producers dealing with consumers in farmers' markets, with wholesalers, food processors, the AFESZ consumer cooperative. Other crop and livestock prices were set by contracting between 1500 state and collective farms and state exporters, wholesalers and food corporations. Collective farms were barred from exporting and had limited storage capacity, making for weak bargaining position. Milk and some grains had controlled prices, and farms in poor soil districts received state subsidies. Because land was free, the price of food did not include its value. Supermarkets in border towns were full of Austrian shoppers buying Hungarian food at bargain prices. Despite such anomalies, market prices were dominant under 1980's socialism.

Two forms of integration had developed over the years, neither organized by state planners. The highly competitive small farm sector, referred to as the "second economy", was embedded in the "household" plots and putting-out system of the collective farms. Production and marketing decisions in the second economy were made in contracts and bargaining between hundreds of farm managers and thousands of small farmers. The second integration stemmed from state agribusiness introducing, selling and managing high yield crop technologies and livestock systems to collective farms: In the late 1980's such integration extended even to the commercial private sector. In 1990, in Békéscsaba, an association of private pig farmers had contracted for organically raised lean hogs with a state enterprise which supplied a special breed of piglets, feed, credit, and marketed the pigs in Western Europe.

The integration of small farming, state and collective farming and the food industry created contract certainty: all could calculate what and how much to produce at stable prices, and what costs would be. Exports to communist countries were secure.

In the early 1990's everything in agriculture became uncertain and problematic: landownership, jobs, credit, export markets, prices, costs, privatization politics and legislation, not to speak of the drought. In our 1991 interviews, the most common complaint of farmers was that wholesalers and the food industry had stopped paying their bills for the farm produce they had
received. Meanwhile producers had to purchase fertilizer, fuel, and other inputs for cash, and had to pay their employees. International transactions with the Soviet Union (later the Ukraine and Russia) were reduced to barter by the truckload and smuggling. Other markets were disrupted. In Szolnok county in 1991, fruit growers managed to sell only when German and Austrian truckers drove up and the entire village picked fruit for the next three days. Without cold storage and juice presses and with chaos among wholesalers, villagers considered themselves lucky. Prices stopped being useful signals for decisions. Faced with a sudden drop in egg prices, an egg growers association urged its members to sell the hens; shortly the price doubled but the members were now short of hens. And so it went.

In the second economy, small farmers had lost access to the "household" plots and farm services once provided by the now defunct collectives. The nationwide small farm study found that 76% had no contract for their produce, 47% decided what to grow before they had any idea about prices and who to sell to, and 50% of those who had contracts reported problems with contract enforcement (Varga and Szijjarto, 1994). Just as telling, nine of ten said their situation had not improved or worsened in the past two years, and eight of ten did not expect improvement. Another report a year later showed that agricultural markets were still disorganized, especially for small farmers (AKII, 1995a): the food industry was unable to purchase sufficient amounts of the products usually grown by small farmers, despite higher prices, and had to import some. Quality was below its standards and it was costly and uncertain to collect small quantities of produce from large numbers of small farmers. The researchers concluded that "there is no linkage between supply and demand".

In contrast to small farming, conditions for market coordination in large enterprise agriculture were positive: large enterprises had downsized but doubled in number, and had privatized; food corporations and wholesalers were also smaller, more numerous, largely privatized, and had benefitted from massive foreign investment. Still, contract uncertainty had gotten worse. The 1994 survey of cooperatives reports (Toth and Varga, 1995, p.57):

"the transformed cooperatives can choose today among more market participants to sell their output than 5-8 years ago. But that does not mean that equitable economic relationships have developed. To the contrary the market ...has made for deviant behavior: there is lack of trust, verbal commitments are unreliable,
payments are late and even defaulted, there is uncertainty and no reliable market information."

The economist Csáki similarly stressed in an interview that a well functioning market needs rules, institutions and a legal framework. Privatization does not automatically create these; in Hungary, they are yet to be made.

Is the market becoming coordinated? There are three possibilities: the food industry coordinates the market; the cooperatives do; new farm entrepreneurs and medium sized corporations that split from cooperatives do it. The food industry has become profit making and can raise capital from foreign investors and banks (AKII, 1995a). It has an interest in assuring a steady flow of suitable inputs from thousands of small producers and the larger commercial farm enterprises. It might organize and finance a network of county cooperatives for small farmers. It could distribute seed and fertilizer and provide some farm services through these cooperatives, sign contracts for large purchases and exercise quality control. That would be no different from the way multinational corporations deal with small farmers in many countries.

The second scenario assumes a cooperative-small farmer alliance which is not so odd if one remembers that many small farmers are the employees, members, kinfolk and retired members of the coop. In this alliance, the labor intensive crops and small animal husbandry would be handled by the small farmers and the large scale grain farming and livestock would remain with the cooperative and its satellite companies. The coop distributes seed and fertilizer, advances small loans, exercises quality control and markets the output. Collective farms had performed these functions in the second economy under socialism.

Cooperatives are still the heavyweights in farm production. Though they reduced their input into the small farming sector, the cooperative survey of 1994 reports that 80% still perform important farm services to small farmers in their locality (Toth and Varga, 1995, pp.59-60). The confrontation of large and small farming was a temporary artifact of the political climate of the early 1990's, and cooperation can resume. In the words of the president of the Veszprémvarsányi cooperative:

"We are not the enemies of small farms, on the contrary...small farming is an integral part of our economy. One should not split the two. There is work to be performed exclusively in small farming, labor intensive, high price, high cost
products, whereas extensive large scale farming should be done in large enterprises. The division between the two can be decided best without political intervention; politics has worsened our relationship. What we are doing now is first and foremost for our members and employees. We give them land and help them produce hybrid corn and sugarbeet; that way they get higher earnings. For others, we are willing to buy their output...we dry their produce with our dryer... I believe such integration is steadily expanding. For us it is counterproductive to suppress the small farmer. On the contrary, we have to keep them alive...when their production increases, we collect and market their output, we can both profit from it."

What is telling about the president's statement is that his cooperative is coordinating the "second economy" that had become disrupted in the early 1990's.

The third possibility, and more of a longshot than the previous two, is for more of the cooperatives to go bankrupt, downsize and divide, with the satellite companies becoming independent, while many small farmers sell more and more of their land to commercial family farmers and farm enterprises. In that case, medium agribusinesses will come to dominate production, and hire unskilled farm labor seasonally for labor intensive tasks. These agribusinesses will form strong interest groups and will be large enough to have bargaining power in contracting with wholesalers and the food industry. One way or the other, market coordination will be achieved, but it will take trial and error, and time.

The moral economy of system change

The economist Kenneth Arrow (1974,p26) has written that "the principles of ethics and morality...are agreements, conscious or, in many cases, unconscious to supply mutual benefits...which are essential to the survival of the society, or at least contribute greatly to the efficiency of its working." With 15% of Hungary's assets targeted for privatization in agriculture - the nation's farm land, livestock, farm machinery and buildings - and hundreds of thousand farm jobs in doubt during a depression, how was the problematic and contentious change from socialism to a market economy accomplished? Did people weigh justice, not just interest, equity, not just efficiency, in decisions?

Collective farms were huge, hierarchic, stratified agribusinesses. Though democratic in their constitution, the collectives were controlled by agromanagers. There was no work place
The farm workers had an "employee mentality" and thought that administrators had soft jobs for high pay (Bell, 1984, chapter 6). They put their energies into small family farming in the "second economy". Solidarity was strong among kin and friends, with limited commitment and loyalty to the collective farm, as was true also for industrial workers in state enterprises (Andorka, 1993).

Nevertheless there was some solidarity binding villagers and the collective farm: the collective provided many social and economic benefits - day care, holiday camp, school lunches, subsidized fuel, home repair assistance, the household plot and associated farm services. According to the head of the national farmers' association (interview, 1995), by the 1980's most farm managers were the sons of middle peasants persecuted under communism, and a reconciliation had taken place between villagers and agromanagers. In the early nineties some politicians and the news media tried to open old wounds with the pejorative term "green barons" - a reference to their alleged management style and lifestyles. In our field work we discovered no large gap in the standard of life of agromanagers and employees. Managers lived in houses and drove autos not noticeable larger and more luxurious than many villagers'. They wore clothes suitable for getting about the farm and not suits. They worked long hours. The manager of a very large agribusiness, with 9600 ha. and 630 employees, put it this way: "I earn more from my six hectares of peppers than from my salary." When the time came to elect the heads of the new cooperatives, most of the managers who decided to stand were reelected.

Some managers had abused their position, e.g. making employees work their private farm on collective time. Employees in turn stole farm supplies and freely used equipment for their own private purposes. Hard, competent and honest work was not properly rewarded and shirkers and incompetents not sufficiently sanctioned. Morality about state and private property was fuzzy and ambiguous. Even in the second economy, villagers contracted and bargained within a small circle of familiar faces, and few had the experience of transacting business in impersonal markets. In dealing with state planners and officials, managers concealed and falsified information. Trust was low all around. Andorka (1993, p.320) writes that "a modern society is an open society...[it requires] the development of certain civic virtues, values and norms, or the mentality essential to
the functioning of a market economy and political democracy." Socialist morality was a poor preparation for a market economy.

The privatization laws opened and accentuated old social divisions and created new ones. For land, most rural people wanted a "land to the tiller" property settlement. Instead much land was gotten by non-residents, some of them the children of village folk who had long ago severed their village ties and had no interest in farming. The rent they are getting is looked at as an undeserved, politically engineered, windfall. It certainly is a continuous cash transfer from rural to urban people. The fragmentation of land ownership into small plots is not efficient, not even for small family farms. Surveying, delimiting and accessing such plots has huge costs.

The division of common property was surprisingly consensual. Without the land, the remaining farm assets on an average per capita basis, after subtracting debt, were worth 318,000 Ft (about $3000), less than the cost of a used tractor and certainly not enough to outfit a small farm (Andorka et al, 1994). Collective members well knew the losses from privatization by physical division. They agreed on privatization by shares, and voted to allocate shares proportional to years worked, sometimes adding one or more lesser factors such as last five years' average earnings. The division favored the retired members who in many places were a majority. It was a concession to the elderly who, had they insisted on physical division, would have gained some quick cash at the cost of destroying the agribusiness. But favoring the retired was also considered equitable. Eventually the middle aged cohort would inherit these shares, and in the meanwhile it was assured of a livelihood.

The privatization law however mandated that former employees - most long gone from the district - were also entitled to shares (though not voting rights in the new cooperative). These "outsider" shares were described as a "political payback" and a "second compensation" (land to outsiders was the first one) designed to ruin cooperatives. Consequently, for the whole country, members got shares worth 41% of assets, the retired got 39%, and "outsiders" got 20% (Andorka et al, 1994). Because of the state of farming, members are buying outsider shares at 10% of nominal value. As the retired and elderly die, many of their city children inherit both land and farm enterprise shares in a drain of village resources that will continue a good twenty years. As with land compensation, farm workers had no choice but to conform to national law.
Bankruptcies and the transformation law put village solidarity and morality to a great test. In some places it has resulted in unnecessary hardship, due to greed and dishonesty. Elsewhere farmers handled the conflict of generations and between skilled and unskilled workers in a cooperative manner. Under the law, a new cooperative no longer had an employment obligation, and could terminate the household plot and social benefits. To save on costs and for greater efficiency, cooperatives downsized, leaving thousands without a job. Most of the unemployed were unskilled workers, older workers, and women. As for the retired, though some gained land and rental income from land compensation, they lost household plots, free farming services and other benefits. For many, small farming is more expensive and difficult than under socialism. Having made the transition of agribusiness from socialism to capitalism possible with their votes in the cooperatives' general assemblies, the older generation ended up with a diminished and vulnerable economic position.

Cooperatives varied in the degree to which those who saved their jobs and continued to farm protected the financial interests of other members. At one end, as at Veszprémvarsányi, a new corporate structure was created with income producing assets owned by all shareholders. Management fully intends to protect share values and to pay dividends as soon as the agribusiness profits are resumed. At the other end, at Ököritofülőpös, cooperative management gradually sold off assets then transferred the rest, minus debt, to a company owned by a small clique, and left the cooperative bankrupt. The majority of members, including all the retired, have got nothing. "Wild West conditions prevail in some districts" is how one agromanager phrased it in an interview. Bankruptcy by design has also occurred. In it, some run down an enterprise by selling off assets and converting what they can into salaries; when bankruptcy inevitably follows, they buy some of the remaining assets at local auctions at bargain prices and start a private farm.

The moral flaws in human nature become exaggerated when many are trying to salvage a share in a diminishing pie. Unfortunately in the 1990's the pie has been shrinking, political and social restraints on unethical and illegal behavior was weak, and accountability ineffective. The difference between ethical and unethical privatization depended on village solidarity and the honesty of farm managers. Fortunately many villages had both.
In dressing a balance between relative winners and losers from privatization, those who got more property in the legal sense did not end up as the winners. The elderly and the retired received the largest land compensation and the most in cooperative share values. Without well-functioning land and shares markets their property cannot be transformed into resources for living. User rights to land, farm services and social benefits under socialism were more useful to them than private property. The well-being of the older generation depends on family, neighborly relations and village solidarity as much as, if not more than, before. Unskilled workers and many women had low human capital and social capital limited to the village economy. They received little land and few shares, and lost their farm jobs. Low on human and social capital and with little property, these categories are the greatest losers in privatization. Agromanagers did not get more than the average villager in land and enterprise shares, but they were knowledgeable about running an agribusiness and possessed translocal business networks. They have cash savings for buying land and for starting a private business. Cooperative agribusinesses could not continue without them. When they did quit, they became wholesalers, specialized service providers, consultants, heads of small companies that hived off the large enterprise. For them lack of private property was no barrier to good jobs and earnings after privatization. Skilled farm workers, drivers, repairers, and technicians possessed human capital in short supply and useful to start a private business or farm. They got plenty of land and enterprise shares. Many continue working in the privatized agribusiness. The greatest winners are new entrepreneurs, still few in number, who got lots of land in compensation, possess human capital and social capital, and have managed to access financial capital, as the young agronomist-lecturer did with professional links to some German investors.

Some analysts have described the consequences of privatization as the "pauperization" of rural Hungary and the accumulation of land and assets by an agromanagerial elite (Harcsa, Kovách and Szelenyi, 1995). No one doubts that in an economic depression and with high unemployment much of the population is worse off than earlier, in cities as well as villages, in fact throughout Eastern Europe. But is this an irreversible trend? There are no signs of pauperization in villages. Unemployment support, part-time work, private farming, farm services to the retired, two-earner families, public works projects, have all cushioned the impact of the depression.
There are signs in 1995 that the depression has bottomed out in some counties. Villagers own land: even when not enough to farm commercially, they grow their own food and get a small rental income. It is premature to describe these folk as a new agrarian proletariat.

As for a new agromanagerial elite based on private property, there are no indicators of recently accumulated wealth either. However common property was privatized, no one has managed to appropriate anything like an oil well. What they got was aging farm equipment and buildings, some livestock, some land, a struggling farm business they have to share with some others, which will need a lot of hard work and investment before it makes anyone rich.

Conclusion

Now that we have described how agriculture was organized under socialism and what changes occurred with privatization in the early 1990's, we return to the analytic questions about socialism and capitalism that we started with. Were the seeds of a market economy present in the 1980's in socialism? Has a market economy become institutionalized? Why was the transition painful, and for whom? How do agents create new institutions?

The seeds of a market economy existed before the downfall of socialism, but the seeds had produced some trees and not a forest. Prices were set by market forces. Enterprise decentralization, internal contracting and putting out resembled outsourcing, subcontracting and enterprise division autonomy in capitalism. State policy and enterprise practice supported a thriving second economy based on the private property and family labor of hundreds of thousand villagers. With extreme failure bankruptcy did occur. All of these were requirements of a market economy. At the same time, redundant and incompetent labor could not be fired, and most loss making enterprises continued to be subsidized. There was no land market. Private commercial farming was limited, and private investment in agriculture discouraged. The state was the main source of capital. State officials and policies interfered in enterprises, as on favoring large agribusiness over small. As long as capital formation and allocation was by the state, there were limits to marketization. That is not to take away from the successes of Hungarian agriculture under socialism. It provided the country with abundant food and lots to spare for export, and it had raised rural living standards to urban levels.
Has a capitalist market economy been institutionalized in agriculture? There is no longer any common property and very limited state property in land and other farm assets; private property has replaced them. Bankruptcies are frequent and not disguised. Enterprise management has taken many steps to cut costs and to become profitable by reducing the workforce by two-thirds. Private entrepreneurs are free to enter farming, and do. With imports from Western Europe competition has increased. State officials have stopped intervening in enterprises. State subsidies have stopped. Unlike industry and banking, there is no blurring of private and state property and no interlocking directorships and share ownership between agribusinesses and state banks (Stark, 1996). In agriculture there exists a fully capitalist market economy. But why isn't it working well?

Institutions, as North reminded us, are not created overnight by enacting laws. People have to learn new knowledge, new ways of thinking, new habits of conduct and norms of transacting, new forms of social control. All of these are costly and take time. Institutions have to be coordinated and synchronized. Bankruptcy is the ultimate guardian of enterprise efficiency under capitalism, as Kornai underscored. For some time to come in Hungarian agribusiness the farm assets lost in bankruptcy will have been created in part by the state, and not by private investors and managers. Bankruptcy does not have the same force yet as in capitalism. Prices are the most important market signals in a market economy, but they don't signal well yet, especially to small farmers, and won't until market coordination is established. Contract certainty is most likely when businesses are in the market for the long haul, benefit from a lasting reputation and are profitable. In Hungary, many enterprises in the market are new, transient and failing. Contract certainty will improve with settled business conditions, but these haven't come yet. It is impossible to make capitalism work without capital. When the state withdrew from agriculture, it created a capital vacuum. It will take time for a capital market to emerge.

It is instructive to examine private property in the new market economy. Pryor (1991) was of course right that a socialist agribusiness could only be changed into a capitalist agribusiness, and not into commercial family farms. Farmers became share owners, but share ownership does not yet confer the same benefits in Hungary as it does in Western countries. In the absence of a market in shares, one cannot exercise the "exit" option (Hirschman, 1970). All
analysts of socialist collective farming concurred that despite the democratic charter of collectives, they were run by an oligarchic agromanagement (Swain, 1985; Bell, 1984). The new right of hiring and firing has increased management's power in the cooperatives. Members may well own most of the shares, but without exit they have no influence over management. It will take time before a market in agribusiness shares gets going, i.e. when agriculture becomes profitable. Until then, shares will remain a weak form of private property. In socialism, managers had user rights in common property; in the new market economy, for some time to come, they continue to control farm assets, though it belongs to others.

Why has there been so much pain in the transformation from socialism to capitalism? The pain has two sources: Hungary lost an export market worth 30% of its agriculture output in two years, and state subsidies were terminated. Had the economy been capitalist, such a huge loss in such a short time would have inflicted just as much pain. The pain is not evenly shared. As we have seen, those with human and social capital have done relatively well, and those without have not. Private property has not made much difference. In socialism, the labor market was segmented and the work force was stratified by schooling, skill and gender into higher and lower paid, full-time year round and part-time employees (Swain, 1985). In capitalism, segmentation has increased and stratification continues, but it wasn't capitalism that created them.

Last, how do people create the institutions they live with? Rural people experienced many aspects of the privatization laws as inequitable and inefficient for farming, in particular the huge transfer of assets to urban folk, but they had to live with that. The common property division and enterprise transformation laws left much scope for decision by farmers, individually and collectively, to make their own futures and the institutions they would live with. Considering the high stakes of such an undertaking, with most everybody's jobs, earnings, and life chances on the line as resources diminished, the rural people of Hungary acted in a remarkably cooperative fashion. Millions of hours were spent in meetings listing and valuing assets and calculating each member's share, reading, debating and explaining the complex details of the privatization legislation and rules; debating and voting in general assemblies of cooperatives; electing and working on land commissions that designated compensation land and rated soil quality; conducting the land auctions themselves, and engaging in land exchanges and consolidation.
Bankruptcies and reorganizations too were implemented. All this was an enormous outpouring of human effort, and it is not over yet. We don't know enough about the way in which efficiency was weighed against equity in collective decision, and how individuals and groups used power, connections and information to advantage. We have some research in progress on these questions. This much for the time being: had the older generation pursued a narrow, short term interest, it could have destroyed the economic foundations of agribusiness in Hungary. It did not. Had the agromanagers pursued a narrow, short term interest, they would have privatized more farm assets for own private farm businesses and would have destroyed the cooperatives. They did not. Despite differences, a majority of rural people cooperated to keep agriculture viable during a very trying time, and they have succeeded.
Bibliography


Kovách, Imre, 1988. Termelők és Válalkozok, Budapest, TDJ.


