

B. CSIKÓS-NAGY

NEW PRICE SYSTEM IN HUNGARY

In January 1980 pricing has been put on a new basis. Its guiding principle is that domestic prices should reflect relative world market prices thus making international competitiveness the main criterion of economic efficiency in enterprise activity. The price system, as a whole, will become more elastic in order to orient towards rational economic decisions more consistently.

The system of controlling income and finance has considerably changed in Hungary with 1980. Parallel with this a *general price revision* took place, covering both producer and retail prices. New industrial producer prices and freight tariffs were introduced. In agriculture new state procurement prices are valid in animal husbandry with January 1st 1980 and in plant growing with the turn of the economic year 1979/80. The price system has changed in the building industry, too. Estimates for investments in process have to be repriced by the application of indices specifically determined for this purpose.

In harmony with the adjustment of producer prices *retail prices were partially modified* already with July 23, 1979. Prices of certain foodstuffs, fuels, electric energy, building materials, shoes and furniture were raised. This measure increased the retail price level by round 9 per cent, from which 6 per cent were compensated by complementing earnings. Modification of the producer prices affects in 1980 retail prices naturally in other fields, since nearly half of the total commodity turnover, the majority of products put into circulation are realized at free prices. But these latter price changes are implemented by the trade gradually, adjusted to the character of individual products. This was the case also in 1968 when free prices were introduced in a wide domain.

Basic principles of the new price system

The Central Committee of the HSWP determined the *guidelines of the perspective development of the price-system* in April 1978. Introduction of retail prices proportionate to value, re-establishment of the two-level price system (i.e. that the level of producer prices should be lower than that of retail prices), an organic connection between foreign trade and domestic prices as well as an increasing elasticity of the price mechanism were formulated as long-term requirements. The desire was expressed that these guidelines should serve as a basis already for the 1980 price modifications taking into consideration urgency as well as the possibilities.

The measure of July 23, 1979 may be considered as an important step from the viewpoint of progress towards *retail prices proportionate to value*. This was first set as an

aim by the 1968 economic reform in Hungary. As it was formulated at that time: everybody should pay for products what they really cost. Of course, this has never been interpreted as a mathematical equation. According to central intentions, a relatively low price level (compared to inputs) of products and services satisfying basic cultural, health and social needs will be maintained in the long run, and so will the prices formed through higher than average taxation being aimed to secure budget revenues and to restrict the increase of personal consumption. To this latter sphere belong price deflections aimed at curbing a too rapid rise in the consumption of certain luxury articles, alcoholic drinks and tobacco and, recently, motoring.

Price preferences proposed for elimination were divided into *two groups*. The first one includes those concerning *only Hungarian citizens* like housing rents, travel facilities or certain services. Into the second one were grouped those *more closely connected with foreign trade* or with invisible exports as, for example, tourism. Here energy, fuel, chemical products and foodstuffs are of greater importance. The opinion has developed that in the framework of a general price revision the – at least partial – elimination of those price preferences should be endeavoured where the interplay into foreign trade is considerable. As against this, the modification of subsidized prices affecting only Hungarian citizens may be postponed.

The main and novel feature of the new price system introduced in 1980, deviating from the previous one, is *adjustment to world market prices*. This means that

- in the domestic valuation of *natural resources* (primary energy and raw materials) adjustment to the prevailing most expensive purchase prices;
- and in the domestic valuation of *finished goods* produced in competitive industries adjustment to export prices in convertible currency are taken for basis.

In the sphere of natural resources basing the economic calculations on world market prices means application of the principle of the more expensive import source. When world market prices are rising, purchasing from the West is the more expensive source for Hungary, since in the CMEA contractual prices follow the movement of world market prices with a lag, being an average of the previous five years' prices. Practically this amounts to a revaluation of energy and raw materials against the average inputs and it has to play a role in introducing more rational energy and material management than the previous one.

In the new price system the relative price of energy increased by 65 per cent and that of materials by 35 per cent in comparison to prices of finished goods. The change is even more conspicuous if the new price relations are compared with those before the explosion of oil prices. In comparison to 1973 the relative rise in prices amounts to 110 per cent with energy and to 60 per cent with materials. Accordingly, in harmony with the changes in international value relations the conditions of production technology, product pattern and business organization were made stricter under which the energy- and material-intensive products are realizable at a profit.

Interestedness in manufacturing products which are profitably saleable at every market in the world is promoted by *changing the prime-cost-type price system into a*

competitive one. In such a price system profit and loss reflect the position of the firm in international competition; and enterprise efficiency is an indicator of international competitiveness.

Naturally, introduction of the competitive price system was possible only in *competitive sectors*. When valuing the finished goods produced in competitive sectors, adjustment to the export price in convertible currency is based on the application of the export efficiency indicator. In Hungary, since the economic reform of 1968, it is regularly examined in each industry and in each enterprise participating in exports, how many forints of input are necessary to produce one unit of foreign exchange. A simple mathematical formula is applied: the numerator is the expenditure calculated in domestic currency and the denominator the foreign exchange receipts for export. On this basis the producer price level can be determined. The idea is that the producer price level would be determined for enterprises by the price level of exports, but the relative prices of products by the domestic demand and supply relations.

In the competitive sectors adjustment of the producer price level to the export price level is the condition that the profit (or loss) of sectors (enterprises) should express their real position in the international competition; i.e. the hierarchy of rates of profits should reflect that of efficiency. It is in this manner that a producer price system that is an indispensable element of a structural policy, keeping rationality in view, may be established. At the same time, the producer price system is to be directed towards such retail price policy which ensures equilibrium, i.e. which considers the domestic demand and supply relations. This is why the relative prices of products should be adjusted to the domestic conditions of demand and supply.

The idea was raised that not the *export*, but the *import price* should be the regulator of price level. This conception was based on the fact that under the Hungarian development policy enterprises were founded and industrial sectors were established many times with the purpose of saving imports. Under such conditions however, when the *price gap* between the import and export price of a product is considerable, it is of fundamental importance in principle, that *the export price should be the general regulator of the price level*. The new price system should orientate first of all towards a structural policy economically expanding the export potential. Moreover, such procedures of production development and sales policy are to be adopted which allow the assertion of reasonable export prices.

The division of social production into competitive and non-competitive sectors depends on whether they manufacture such products, provide such services which may be subjects of foreign trade (export or import) or not. If classification of production is made on such a basis, we think only of visible trade (foreign trade), i.e. disregard the invisible trade (e.g. tourism). Namely, the invisible trade dissolves this distinction, because in that case the foreigner is confronted with the total domestic assortment of commodities; he is not excluded from anything, only from the social benefits ensured by law for Hungarian citizens.

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From the viewpoint of the price revision of 1980 it was a novel task to examine in which branches the competitive price system might be introduced as well as applied. *Agriculture had to be excluded* from the branches designated with this purpose. In a competitive price system the level of state procurement prices of agricultural products could not have been raised; what is more, even a modification of relative prices ought to have been made in favour of plants and at the expense of livestock. As against this, (a) the level of state procurement prices increased by 11 per cent, but ought to have been raised by round 30 per cent to eliminate the budgetary dotation of means of production (chemical fertilizers, plant-protectives, etc.), as well as (b) relative prices were changed in favour of animal husbandry and not of plant growing.

This was required to maintain the interestedness of producers in the intensive development of agriculture. The latter is realized throughout Europe by means of protectionistic agrarian policy, since the world market price of agricultural products is regulated partly by extensive ways of inexpensive cultivation overseas and partly by the production conditions of industrially developed countries producing at low specific costs.

Since a competitive price system covers only a part of social production, stress was laid upon examining *how inclination to waste materials and energy could be eliminated* or at least diminished in the formation of prices based on costs in the non-competitive industries. That is why a *price formation based on proportionate prices* has been decided upon. This is a principle of price formation applicable in the sphere of goods substituting for or related to each other. This method had already been applied in Hungarian price policy also previously and is generally characteristic in the sphere of retail prices, since, in the case of related articles, trade cannot disregard what price surplus the consumer is willing to acknowledge in the case of a new product, which is better because of its qualities than the products serving the same purpose and already on the market.

The method of proportionate prices is not new in the sphere of producer prices, either. E.g. in transportation the individual branches compete with each other. Therefore, when determining the tariff levels of branches we must not disregard the conceptions of transport policy and that the consigners should use the different transport vehicles in adequate proportions on the basis of interestedness. In a competitive price system it can be assumed that demand for those means of production which are in substitution relationship is governed by the principle of cost-minimization if there is a possibility of choice in productive consumption.

Finally, the price re-arrangement of 1980 established a *price system with three centres*. Formation of competitive prices covers approximately 35 per cent, "proportionate" price formation about 40 per cent and traditional price formation based on costs about 25 per cent of social production. It was, however, easier to agree on the fundamental principles than on their implementation. This is understandable if we consider that the change in the price system was urged in Hungary by the need to restore the equilibrium of the balance of trade and not by the domestic market conditions. Therefore, in a certain sense, *price relations best serving economic efficiency under Hungarian*

conditions had to be stimulated. This is the essence of the problem, because the new price system can meet the requirements only

– if it can be ensured on the one hand that the orienting function of price towards rational economic decisions is not restricted to the day of the price revision, but is *enforced continuously*, complying with the changes in external economic and domestic market relations of the national economy; and on the other hand,

– if the restrictions with which the accepted principles of price formation could be introduced will gradually disappear and, parallel with this, the normative character of financial regulation will become more pronounced in the national economy.

It is not easy to realize all this and, obviously, such price relations cannot be “reproduced” regularly without an adequate market background. Therefore, it is useful to underline that the comprehensive modification of the control system and the related new price system are based on the dual hypothesis that

– disequilibrium is reflected in the balance of international payments and deficits can be eliminated without a sharpening domestic disequilibrium; what is more,

– equilibrium between demand and supply will be consolidated through more and more deliberate restrictive financial policy.

Problems of functioning

Adjustment of the industrial producer price level to that of export prices in convertible currency raised some problems. How can the price level of an industrial sector or an enterprise be controlled, if price movements affecting only an insignificant part, perhaps not even 10 per cent of the value of output are considered? How can the general price level of the industrial sector and of the enterprise be reconciled with that of exports in view of the different product patterns and the fact that there are enterprises selling certain products only on the world market, but not at all on the domestic market? These problems are more severe in industries where the assortment of goods produced may amount to several thousands and the change of products is fast.

By means of the indicator of the cost of foreign exchange earnings the level of enterprise producer prices could be reconciled with that of export prices and the initial profit rates of enterprises for 1980 could be determined. At the same time, *export efficiency* measured by the cost of foreign exchange earnings could not be made the basis of controlling the level of producer prices. In this case we ought to have reckoned with the following problems. Enterprises would become very much interested in increasing the efficiency of exports which can be attained also by diminishing the volume of exports through elimination of uneconomic exports. The improving profitability of exports would entitle them to calculate higher profit rates also for domestic sales. The enterprise might concentrate its technological and organizational measures on the export-oriented activity and the price consequences of improved efficiency achieved in such a way with 5–10 per cent of output would be automatically enforced for the remainder of output.

In the early 1950s enterprises had to divide production into comparable and non-comparable parts in the interest of checking the fulfilment of plan targets concerning the reduction of prime costs. In connection with this much experience accumulated concerning the possibilities of enterprises in grouping their costs at discretion, a regulation of producer prices relying on the costs of foreign exchange earnings may revive also this practice.

This is why the opinion was formed that the movement of producer price level should depend partly on *profits realized in exports*, and partly on the export price level, though the information basis of the latter is not satisfactory. Competitive price formation should be developed in the future in such a way that the control of domestic prices through export prices should be adequately asserted without moderating, however, the interestedness of enterprises in increasing the efficiency of production for domestic purposes.

It seemed to be expedient to apply competitive prices in a wide domain, wherever there is a possibility for attaining international competitiveness within 4–5 years by means of reconstruction, changes in technology, modernization of products, modification of the product mix and, last but not least, through improvement of enterprise marketing policies. The permanent and temporary elements of tax refunds will be applied accordingly in exports.

Hungarian industrial enterprises compete on the world market with companies whose taxation rules allow them to offer their products on external markets at lower prices than at home. This is achieved in such a way that the value added tax (so-called net turnover tax) adjusted to the individual phases of production is reimbursed from the budget in the case of exports. In Hungary enterprises pay a 24 per cent tax on wages costs and this is calculated in producer prices. This is of the same type as the value added tax. Moreover, it is a characteristic feature of the new Hungarian price system that energy and material costs are determined for enterprises by the purchase from the most expensive source; the price difference resulting from less expensive sources of purchase is drawn away by the budget. This is naturally a disadvantage in international competition which can be compensated only by tax reimbursement.

It seemed to be expedient to introduce such a tax-reimbursement system in exports which furthers the modernization of production. A two-channel system of tax reimbursement was established keeping these considerations in view:

- a generally 10 per cent linear tax-reimbursement on the basis of export returns converted at the rate of exchange and
- subvention for the modernization of production adjusted to the particular conditions of enterprises.

The general tax-reimbursement is *permanent*, but subvention for the modernization of production is *temporary*, the process of its reduction was announced beforehand. This is how the reimbursement system influences the modernization of production, structural transformation and, finally, the attainment of international competitiveness.

It is assumed that improving economic efficiency will compensate for the reduction of the subsidy on modernization of production.

Price formation keeps the requirement of *proportionality* in view both in agriculture and in *transport*. Relative prices of the individual branches (products, services) are regulated in both sectors by their utility as judged by consumers. Of course, the situation is not fully identical in the food industry and in transport. Food economy is an important export industry as regards both its volume and proportion. In view of this, in those branches of the food industry which are important for export, relative prices were developed depending on export prices.

It should not be forgotten that both in agriculture and transport actual inputs have an important role in the development of the general price level or at least in the formation of "demand" for the price level. It is difficult to push into the background the routine thinking which *attributes losses not to bad management, but to obsolete prices*. According to this way of thinking price cannot be the critique of management, but has the only task to ensure conditions of self-financing for cost levels created by decisions on development, technology and work organization made independently of prices.

More attention should be paid to this problem in the future than previously. In the 1970s increasing material and technical supply had a too great part in the relatively rapid quantitative growth in agriculture, while improving efficiency had only a smaller one than would have been desirable. In transport trends developed, still prior to the 1973 explosion of oil prices, and dependence on cheap hydrocarbon and expensive solid fuel can still be observed.

In agriculture and transport official prices are enforced in a wide domain. There is considerable budgetary subvention in both sectors. Agriculture can obtain profits only with preferential prices and through budgetary subsidies of the means of production making the application of up-to-date agrotechniques possible. Under circumstances when we are changing over to competitive prices in the industry and wish to further the improvement of efficiency through degressive tax-refunds, it is justified to raise the question whether the introduction of similar mechanisms, complementing the price system, should not be examined also in the agricultural and transport sectors.

In the *building industry* (investments) the negative effects of the price system based on prime costs are seemingly neutralized by the normative system of costing. Costs of building are determined on the basis of cost-norms, additional costs stated by price authorities and normative profit margins. It is well-known, however, that because adaptation to individual circumstances is allowed, and for other reasons, even this price system does not enforce a rational behaviour despite all efforts.

The price system of the building industry (and even more of investments) has changed in some relevant respects. The new price system introduced in 1980 applies more unambiguous definitions in regard of surplus costs of construction works carried on under special circumstances, and makes the interestedness of the building industry independent of material costs. This is realized in such a way that cost-estimates are made in so-called

two-tier system. They contain the material and freight costs separately and no profit can be calculated after them.

However, a comprehensive reform of the price system of investments could not be realized. Though this would be needed because the present price system developed under such historical circumstances when investments were characterized by excess demand, building without plan documentation (designs), as well as by laxity in technology and working discipline. The price system of the building industry has to be further developed in 1980–1983. Introduction of a uniform system of norms, more organically connecting costs estimates with building methods, will mean considerable progress. In coming years measures should be taken independently of this in order to *strengthen the enterprising character of investments*. Gradual elimination of excess demand for investment will create more favourable conditions than previously and this may allow a more extensive use of the system of tenders in price formation already in the first half of the 1980s.

Preparation and introduction

Three phases were established for the price re-arrangement. The first was price modelling, started in 1978 and lasting until the middle of 1979. The second phase started following this and ended with the introduction of new producer prices at the end of 1979. This was the phase of actualization. The third phase – the so-called adjustment – will last till the autumn of 1980.

In the *modelling phase* attention was concentrated on three questions:

1. Determination of the principles of price formation. The three-centre price system was established at that time.
2. Determination of changes in price and cost structures. Most relevant measures in this regard were the following:
 - a) Elimination of the charge on assets engaged.
 - b) Elimination of the wage-tax imposed on wages paid by the enterprise.
 - c) Regulation of the technological development fund.
 - d) Standpoint on the revaluation of fixed assets.
 - e) Regulation of normative profits.
3. Modelling of the main framework of the new price system, taking 1977 world market prices of materials and energy for basis, and using a 36 Ft/US \$ exchange rate.

The main deviations of the *actualization phase* from the first one can be determined as follows. 1. In the modelling phase principles of price formation of different sectors and within them of the individual branches were determined in general terms. But in the second phase already a concrete application of these principles to the individual branches (enterprises) had to be carried out. 2. In this phase 1977 world market prices of energy and materials had to be replaced by prices developing by 1980. Taking the inflation on the world market between 1977 and 1979 into consideration, the 36 Ft/US \$ rate of exchange was reduced to 34 Ft/US \$ in the actualization phase. This had to be done lest

the inflation of world market prices expressed in US dollars should bring about a similar inflation in forints. 3. Model computations were made mostly on macro-level. Actualization could be made only with the participation of enterprises. The main feature of the second phase was precisely this transposition of macro-models to micro-models.

In the second phase most problems were raised precisely by the transposition. Computations with indices of changes in input-output price levels of enterprises made at the National Planning Office, the Ministry of Finances as well as the National Office for Materials and Prices revealed "price adjustment deficits" of several 10 thousand million forints. These "price adjustment deficits" indicated that enterprises built into their cost-calculations non-existing costs when they formed the new prices. The enterprises – with a few exceptions – overestimated input costs and established the initial prices for 1980 on the basis of production costs increased in this way, to which then normative profit margins were added.

This is not a new trend and is reckoned with also in other socialist countries. But the situation is relatively simple in such a system of economic control and management where profits are drawn away by the budget and the interestedness in profit of enterprises is based on the fact that a part of profits, the so-called "rest" is left with them. In Hungary profits belong to the enterprises on which a tax is levied by the state. That is why an *about 3 per cent reduction of the producer price level* had to be ordered in the manufacturing industry, the building industry and trade in the actualization phase, assuming that the 1980 initial producer prices would reconcile the price level with normative profit rates in this way.

At present the *third phase*, i.e. adjustment, has come to the fore. Reduction of the producer price level carried out in the second phase may not mean a final solution just for two reasons. Firstly, because micro-computations made in intersectoral relations still indicate some "price adjustment reserves". Secondly, because price adjustment errors are obviously not linear. We are interested in two issues. Firstly, that industrial enterprises left out of the system of competitive price formation may not get into better positions than those of progressive industries. Secondly, that the criteria of normative profits formulated in the price system should be enforced.

Profits have economic contents in the new price system. In industries where competitive price formation is applied, the initial profit rates have to be regulated by export efficiency. Therefore, if this was based on wrong computations, the errors have to be corrected. In agriculture and transport and, in general, where profits are regulated by budgetary subvention, this subvention has to be corrected, should it turn out that profitability is higher or lower than planned because of the subvention. Corrections are to be made on the basis of enterprise balance-sheets referring to the first quarter and first half of 1980, respectively.

At present, it can already be seen where world market prices were wrongly forecast. In the case of some materials it was already known in the second phase of the price reform that world market prices would be higher by the beginning of 1980 than the initial prices. These deviations may have cyclical reasons, but also lasting ones. In the

latter case they might express merely inflation on the world market, but might also indicate changes in relative prices. Regular examination of these price movements and adaptation to changes in the international price structure cannot be disregarded.

The "maintenance" of the new price system is a new task, though the problems themselves are not, and one could get familiar with them in connection with partial price adjustments made since the 1973 explosion of oil prices. It is justified therefore to characterize the price revision as a measure having founded a new course of price policy and not simply as the introduction of new prices.

The new price and financial systems recently introduced as well as the elements and functional mechanism of the system of economic conditions jointly created by the price and business situation on external markets still contain some uncertainties. There is no adequate experience about the functioning of the price and financial system as a whole, but first of all about enterprise reactions. What is known is that *fundamental changes are needed in approach and attitude* at both macro and micro levels. The problem to be solved is too serious for a solution to be sought after by usual excuses instead of self-examination.

Besides, there are some issues where a uniform economic policy attitude should be determined under more settled circumstances than those prevailing at present. This refers, for example, to the *exchange rate policy*. Towards the exchange rate policy such requirements are raised as the improvement of the state of equilibrium, currency stability, rational protection of the price level, strengthening of normativity as well as the elimination of budgetary subventions — which are often contradictory. The right solution ensuring a balanced economic development should be found through a joint examination of all these effects.

НОВАЯ СИСТЕМА ЦЕНООБРАЗОВАНИЯ В ВЕНГРИИ

Б. ЧИКОШ-НАДЬ

В январе 1980 года в Венгрии была проведена реформа оптовых цен на базе новых принципов ценообразования. Ей предшествовала в июле 1979 года частичная реформа розничных цен, приблизившая цены на некоторые пищевые продукты, топливо и горючее, электрическую энергию, строительные материалы, кожаную обувь и мебель к уровню затрат на их производство. В результате этого пересмотра общий уровень розничных цен возрос на 9%, из которых 6% компенсировались населению за счет доплат из госбюджета.

В оптовом ценообразовании был осуществлен переход к ориентации на цены мирового рынка, привязке внутренних оптовых цен к внешнеторговым ценам, чтобы критерием экономической эффективности хозяйственной деятельности предприятий стала их международная конкурентоспособность. В соответствии с этим во внутренней оценке природных ресурсов (энергосителей и сырья) определяющим фактором становится импортная цена, уплачиваемая при закупках из наиболее дорогостоящего источника импорта. Оптовые же цены на готовую продукцию определяются экспортными ценами на нее в конвертируемой валюте. Такой принцип ценообразования применим лишь в так называемых конкурирующих производственных отраслях, значительная доля продукции которых поступает на экспорт, оплачиваемый в конвертируемой валюте. Основой ценообразования на продукцию таких отраслей служит показатель рентабельности экспорта (затраты в форинтах/экспортная выручка в свободной валюте). Применяя этот показатель

рентабельности, предприятия устанавливают оптовые цены и на продукцию, поступающую на остальные рынки. Таким образом, конкурентоспособность и рентабельность продукции данного предприятия в оценке мирового рынка становятся основополагающими и в калькуляции его оптовых цен на внутреннем рынке. В неконкурирующих производственных отраслях оптовое ценообразование строится или на принципе пропорций замещения (субституции) потребительских стоимостей (исходя из цен на продукцию конкурирующих предприятий) или на себестоимости отечественного производства.

Таким образом, реформа оптового ценообразования 1980 г. создала систему цен, строящуюся на трех ценообразующих принципах: на принципе конкурирующего ценообразования (эта сфера охватывает 35% общественной продукции), на принципе пропорций замещения потребительских стоимостей (распространяющемся на 40% общественной продукции) и на базе себестоимости (охватывающей 25% общественной продукции). Цель реформы ценообразования — усилить ориентирующую роль цен в принятии рациональных хозяйственных решений, служащих восстановлению внешнеэкономического равновесия венгерского народного хозяйства путем усиления конкурентоспособности его продукции.