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**Working Paper**

## The "Chinese style reforms" and the Hungarian "Goulash Communism"

IEHAS Discussion Papers, No. MT-DP - 2009/3

**Provided in Cooperation with:**

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*Suggested Citation:* Csanádi, Mária (2009) : The "Chinese style reforms" and the Hungarian "Goulash Communism", IEHAS Discussion Papers, No. MT-DP - 2009/3, ISBN 978-963-9796-51-5, Hungarian Academy of Sciences, Institute of Economics, Budapest

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MŰHELYTANULMÁNYOK

DISCUSSION PAPERS

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MÁRIA CSANÁDI

Discussion papers  
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Institute of Economics, Hungarian Academy of Sciences

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The „Chinese style reforms” and the Hungarian „Goulash Communism”

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March 2009

ISBN 978 963 9796 51 5  
ISSN 1785 377X

# **The "Chinese style reforms" and the Hungarian "Goulash Communism"<sup>1</sup>**

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## **Abstract**

Similarities and differences will be demonstrated between Chinese and Hungarian party-state systems. We define the role of reforms in the self-reproduction of both party-states. We shall demonstrate how different patterns of power distribution lead to the implementation of different reforms. We shall describe how these different reforms have created the Hungarian "Goulash communism" and the "Chinese style" reforms. We shall also explain the conditions that have lead "Goulash communism" to political transformation first in Hungary accompanied by economic crisis, and "Chinese style reforms" to economic transformation first in China, accompanied by macroeconomic growth.

**Keywords:** reforms, transformation, party-state systems, goulash communism, Chinese style reforms

**JEL:** B52, D85, N10, P2, P3, P41, P52

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<sup>1</sup> This is the background paper of the presentation given at the conference "China's Three Decades of Reform and Development: Global Perspective" organized by the East Asian Institute at the University of Singapore in November (7-8), 2008. The paper will be published as a book part of the conference volume in early 2009. We are grateful to the National Scientific Fund of Hungary for financing the project.

# **A "kínai típusú" reformok és a magyar "gulyáskommunizmus"<sup>2</sup>**

MÁRIA CSANÁDI

## **Összefoglaló**

A cikk a kínai és a magyar pártállamok közötti hasonlóságokat és eltéréseket mutatja be. Meghatározzuk a reformok szerepét mindkét pártállam újratermelődésében. Bemutatjuk, hogy milyen módon vezetnek az eltérő hatalmi eloszlások eltérő reformok alkalmazásához. Leírjuk, hogy ezek a reformok hogyan teremtették meg a magyarországi "gulyáskommunizmust" és a "kínai stílusú" reformokat. Elmagyarázzuk azokat a feltételeket, amelyek között a gulyáskommunizmus folyamatából először a politikai átalakulás bontakozott ki és azokat, amelyek között a kínai stílusú reformok először gazdasági átalakuláshoz vezettek.

**Tárgyszavak:** reformok, átalakulás, pártállami rendszerek, gulyáskommunizmus, kínai stílusú reformok

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<sup>2</sup> Ez a cikk a 2008 novemberében (7-8), a University of Singapore East Asian Institute által szervezett "China's Three Decades of Reform and Development: Global Perspective" című konferencia előadásának háttéranyaga. A kutatást az OTKA finanszírozta.

## INTRODUCTION

Hungarian reforms that started in the early 1960s providing relatively high living standards were outstanding among party-states. No wonder Hungarian economic system was nicknamed as „Goulash communism”. „Goulash communism” however, ended up in system collapse in 1989 and transformation accompanied by economic crisis, similar to all Eastern European and Soviet party-states. Chinese reforms started in late 1970s demonstrating an uncontested economic growth. The system survived the Tiananmen Square tragedy that occurred at the same time when system collapse swept all over Eastern Europe. Moreover, economic growth even accelerated some years after the political shock. Reforms that caused that exuberant development were viewed as strictly connected to wisely pursued Chinese economic policy, thus nicknamed worldwide as “Chinese style reforms” that do not seem to follow the same tendency as those of its European counterparts.

Was there anything in common at all between the Hungarian and the Chinese reforms? Tracing back in time to find the motivations of reform and their structural background we arrive to one very important common factor: both countries were operating in a Stalinist centralized system in the 1950s and both countries suffered transitory system collapse that pre-empted reforms.

The character and motivation of these system collapses however was different. In Hungary, it was a sudden, abrupt event, initiated bottom-up, due to the destabilization of the system and the weakening of the Hungarian Muscovite leadership in the aftermath of Stalin’s death in 1953. The collapse, marked by the 1956 revolution, was short-lived due to its clamp down by Soviet military intervention and fast system restoration. In China a series of transitory collapses were initiated top-down due to Mao’s internal power struggles that ended up in two major nation-wide mobilizing and decentralizing campaigns. These campaigns temporarily paralyzed the operation of the system to stabilize personal power against potential competitors. Differences occurred also in the motivations of the restoration and stabilization of the system in a modified power structure. In Hungary, restoration of the structure was based on the bitter experiences of an over-centralized power concluding in revolution and thus, there was a strong drive to balance power to prevent another de-stabilization. This motivation ended up integrating crucial economic interests in the centralized decision-making process. In China, motivation was to decentralize the power-structure toward provinces by integrating them in the decision-making process in order to inhibit the de-stabilization of Mao’s personal power by central power struggles.

Different patterns of power distribution however had several common traits: both diverged from the centralized Stalinist structure of the 1950s; both involuntary integrated strong resisting capacities to central interventions and resource attracting capacities in the decision-making process; and both were based on the same basic system characteristics.

In the next chapters, through the application of the Interactive party-state model (IPS)<sup>3</sup> we shall first detail the common system characteristics, and second, the structural basis of different patterns of power distribution. We will show that these different patterns will attract different kind of instruments of resource extraction and distribution provided by the reforms, in order to reproduce the system. Next, we shall demonstrate that these different ways of working will end up in different ways of transformation. Conclusions will follow that dissimilarities of reforms are not the result of different strategic choices but have a structural basis within which strategic choices have the room for maneuver while interacting with the structure.

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<sup>3</sup> Maria Csanádi, *Party-states and their Legacies in Post-communist Transformation* (Cheltenham, UK, Northampton, Ma, US: Edward Elgar, 1997); Maria Csanádi, *Self-consuming Evolutions: A Model on the Structure, Self-reproduction, Self-destruction and Transformation of Party-state Systems Tested in Romania, Hungary and China* (Budapest: Akadémia Kiado, 2006).

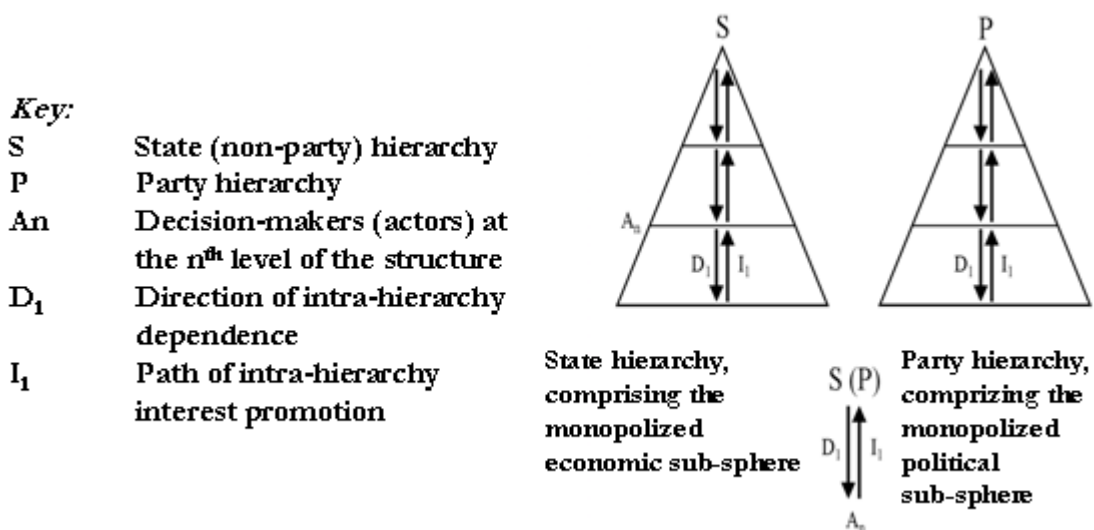
## 1. SELF-SIMILARITIES OF PARTY-STATES

The IPS model is based on the decision-making process and the relationship of party-, state-, and economic-decision-makers during this process. The model defines three overlapping and intertwined layers of relationship among decision-makers during the decision-making process that form the party-state structure:

(1) First of all, there are two hierarchies: the party hierarchy monopolizing the political sub-sphere and the state hierarchy with the state-monopolized economy that allows for the monopolized extraction and distribution of resources (see Fig. 1)

*Figure 1.*

### First layer: the formal hierarchies of the party-state structure





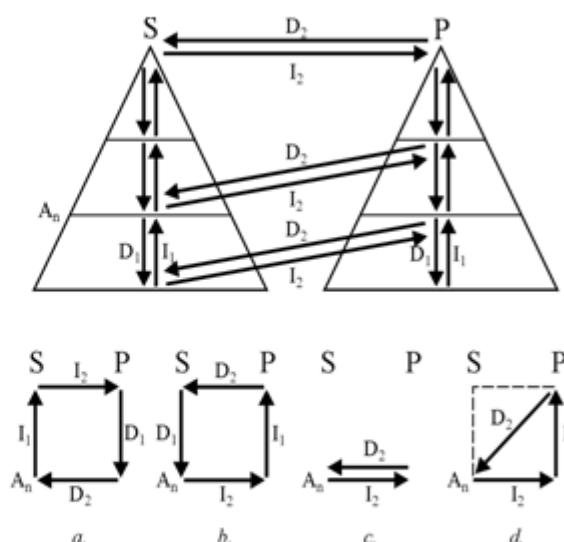
(2) The two separate hierarchies are interlinked by the party's instruments of power that infiltrate the boundaries of non-party institutions and overlap the decision-making process through positional structure, activity structure, and organizational structure and through individual decision-makers upon their party discipline<sup>4</sup>. These interlinking dependency lines at the same time allow for the interest promotion of those embraced by them, introducing an inequality of interest promotion among decision-makers attached to, and deprived of these lines (see Fig. 2).

Figure 2.

### Second layer: the interlinking threads

**Key:**

S	State (non-party) hierarchy
P	Party hierarchy
An	Decision-makers (actors) at the n <sup>th</sup> level of the structure
D <sub>1</sub>	Direction of intra-hierarchy dependence
D <sub>2</sub>	Direction of cross-hierarchy dependence
I <sub>1</sub>	Path of intra-hierarchy interest promotion
I <sub>2</sub>	Path of cross-hierarchy interest promotion



<sup>4</sup> These instruments of party power are for example: the well known nomenklatura system that infiltrates non-party institutions and overlap decision-making process through the positional structure; the subject-matter responsibility system of the party that overlaps decision-making process through activity structure; the instructor system that overlaps the decision-making process through the organizational structure and the party discipline of individual party members, that overlaps decision-making process directly through individual decision-makers.

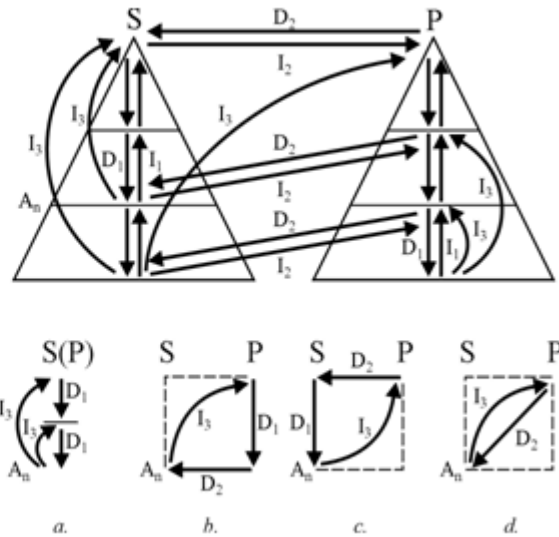
(3) The decision-making process for some actors may be short-cut both within each hierarchy and also across state-to- party hierarchy by having the chance to directly or indirectly participate on higher level decision-making. Short-cuts form a structural feedback loop through either intra-hierarchy or cross-hierarchy dependency lines. Through feed-backs a new structural inequality of interest promotion is introduced for those privileged by them, since actors at one level may meet decision-makers of higher levels whom otherwise would never meet, thus, have access to information, are able to influence decisions, accumulate new short-cuts and prepare to unavoidable impacts (see Fig. 3).

Figure 3.

### Third layer: the shortcuts (feedbacks)

**Key:**

S	State (non-party) hierarchy
P	Party hierarchy
An	Decision-makers (actors) at the n <sup>th</sup> level of the structure
D <sub>1</sub>	Direction of intra-hierarchy dependence
D <sub>2</sub>	Direction of cross-hierarchy dependence
I <sub>1</sub>	Path of intra-hierarchy interest promotion
I <sub>2</sub>	Path of cross-hierarchy interest promotion
I <sub>3</sub>	Direction of feedbacks

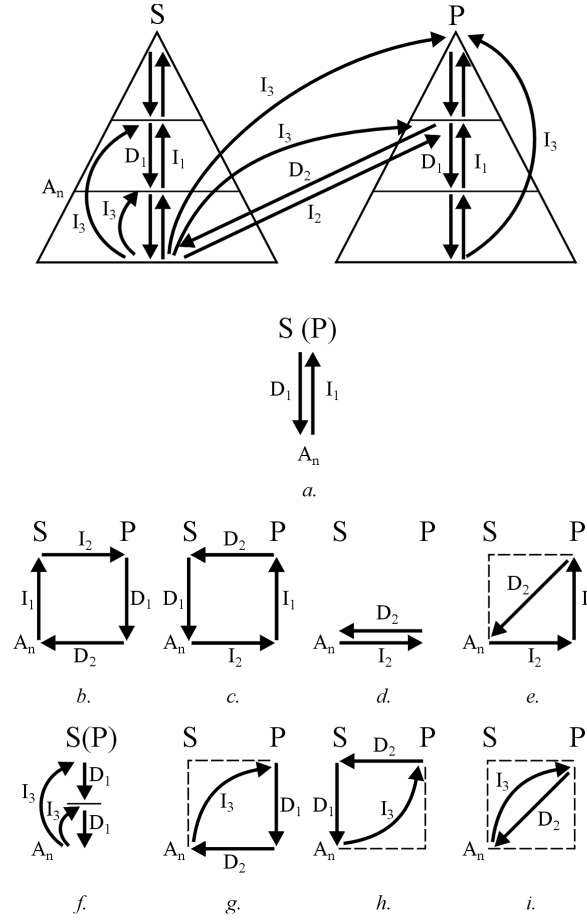


The two hierarchies with monopolized political sub-sphere, and monopolized economic sub-sphere, the interlinking lines and the feedbacks are the main elements of the party-state structure. These elements appear in three intertwined layers that will form the party-state network. The structure reveals its principles of operation: since all actors hold hierarchical dependency lines but only actors in the party hierarchy hold dependency lines interlinking decision-makers in all other sub-spheres, dependencies, interest promotion and resource extraction and allocation are directly or indirectly politically monopolized.

Consequently, the party, originally as one entity in one sub-sphere (political), through its power instruments permeating and monopolizing other subfields and defining its internal inequalities, develops into a monopolized power network that *functions as a social system* (Fig. 4.)

Figure 4.

### The complex network of party-states as a social system



Structural and operational characteristics will provide the dynamics of self-reproduction. Within this complex social structure actors are in dual position: they are simultaneously *holders of and captured by* dependency lines, thereby incorporating two functions simultaneously: distributors and pleaders in *one single entity*. The dual functions will be fuelled by dual structural motivations:

- As monopolistic holders of the lines, they are able to intervene the decision-making process, and simultaneously forced to intervene since there are no alternatives to intervention and thus, restraining from intervention, they would lose positions to other actors who will intervene

- As embraced by these lines they are exposed and simultaneously interested in keeping and multiplying monopolistic dependency threads for interest promotion and accommodate to expectations of those who intervene. Without alternative ways of interest promotion, non-applying actors will lose bargaining position and chances for interest promotion to those who apply

Consequently, capacity and force, exposure and interest together ensure the politically rational motivations of behavior for actors to reproduce bargaining status-quo and thereby the cohesion and reproduction of the whole network.

Owing to actors' dual position and function, the capacity for self-reproduction is *complex*: one single actor as holder of the lines (intervener) has resource extracting and redistributing capacity, while as embraced by those (pleader), it has resource attracting capacities and resisting capacities to interventions. These factors together will provide the *constraints* of the capacity for self-reproduction of an actor.

However, constraints of this capacity are *not uniform* to all actors, since positional differences due to built-in inequalities – interlinking lines ( $D_2$ ,  $I_2$ ) and feedbacks ( $I_3$ ) – will forge *selective chances* (capacities) for resource attraction, extraction, allocation and resisting interventions. Consequently, this will lead to *selectively soft or hard* constraints of self-reproduction according to the actors' structural bargaining capacities.

The above features are self-similar in time, in space and in different aggregation levels and induce self-similar behavior and interest for selection, allocation. Characteristics of self-reproduction are leading to self-similar traps of self-consumption of the system. These self-similar characteristics form the basis of comparison of the Chinese and Hungarian party-states despite so many individual specifics connected to size, historical, cultural, economic, geographical, geopolitical differences.

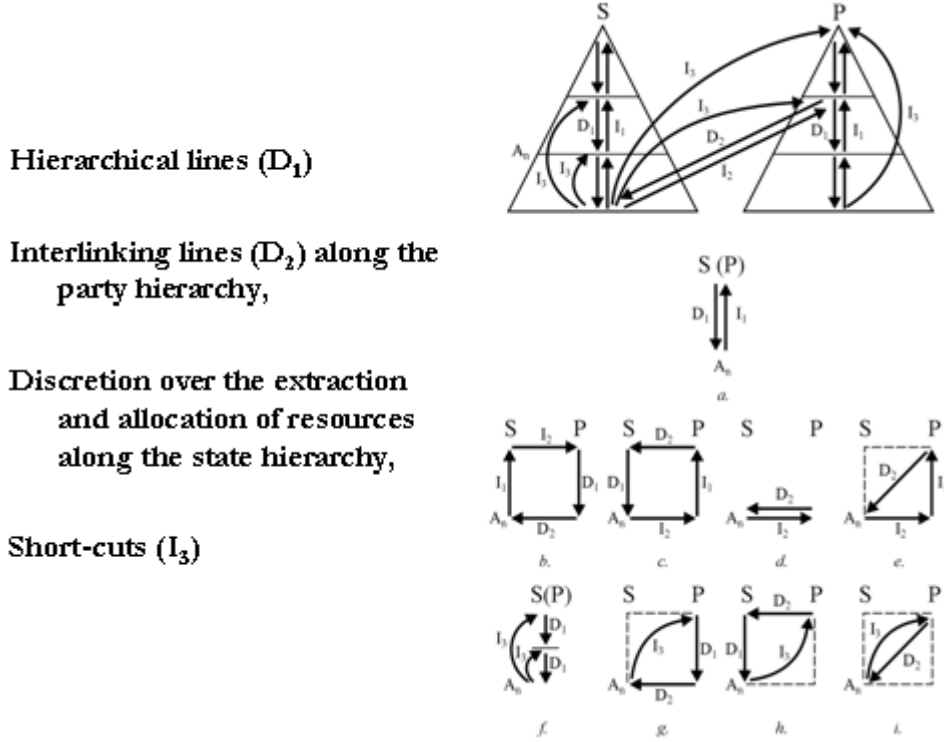
## **2. STRUCTURAL BACKGROUND OF THE DIFFERENT OPERATION OF PARTY-STATES**

Despite of self-similarities, party-states operate, reproduce themselves and transform *differently*. The IPS model offers a structural explanation of those differences. The structural background of differences is produced by the combination of the variations of constructing elements while keeping principles of operation unharmed. That is, (1) the strictness of decisions within the hierarchies, (2) the level of centralization or decentralization of discretions over extraction and distribution of resources along the state hierarchy, (3) the level of centralization or decentralization of the discretion of holding interlinking dependency lines along the party hierarchy, its density, its outreach and its depth in the place of outreach, and

finally, (4) the origin, the target, the density and the accumulation of feedbacks, be they within and/or across state-party hierarchy.

Figure 5.

### Structural background of variations



The combination of these varieties will provide the *different distributions of power* within the network, and, at the same time, define the scope of the space outside the net. These wide-ranging power distributions may be grouped into three characteristic patterns. Pattern specifics are defined by the above factors (discretion over extraction and allocation, discretion in holding interlinking lines and accumulating feedbacks). These three patterns will have characteristic distributions of power that define resisting and resource attracting capacities within the structure, characteristic instruments for reproducing the power structure, and finally, characteristic ways of transformation. The Hungarian and Chinese party-state structures belong to two different patterns. Let us see the three patterns in detail.

(i) *The self-exploiting pattern*: this pattern is the original type institutionalized by Stalin in the USSR, served as a blueprint to all party-states from the end of the World War II until mid-late 1950s, to several European, Central Asian republics still by the end of 1980s and presently to North Korea. In this pattern, the distribution of power is such that both the extraction and allocation of resources and the interlinking lines are centralized, and there are weak or none

economic feedbacks. These latter will mean weak resisting and attracting capacity within the network. In this case, the whole structure has unconstrained extracting capacity, in other words, its *reproduction constraints are soft*. Softness evolves and persists due to the fact that forced resource redeployment (extraction and reallocation) may be repeated without meaningful resistance. Forceful restructuring will result in forced redeployment of resources or that of directly resourceful targets (subjects). We shall not detail this pattern, since this was characteristic to the Hungarian and Chinese structure in the 1950, which is not our present concern.

The following two types of patterns describe the differences in the distribution of power in Hungary and China, that both stabilized after a transitory collapse of the former – Stalinist – structure. The process of institutionalization went on from 1957 to 1963 in Hungary and from 1957 to 1976 in China.

(ii) The second pattern will be called *self-disintegrating* which is characteristic to the Hungarian pattern of power distribution after the transitory collapse caused by the 1956 revolution. Learning from the violent consequences of the overly centralized power and high speed of industrialization to the detriment of consumption, the new leadership wanted to have an upper hand over strategic economic interests that could destabilize the system. Both managers of larger enterprises and newly organized and merged agricultural cooperatives were integrated into the decision-making process. Yet, this move did not only allow the authorities to keep strategic interests under control, but also built up stronger bargaining capacities through feed-backs. In the stabilized distribution of power interlinking threads were overwhelmingly centralized, and so were extraction and distribution of resources, but with strong economic feedbacks within the net. Consequently, forced resource redeployment efforts *become form-fitted* to specifics of power relations according to resisting and resource attracting capacities and the system ran more frequently into hardening reproduction constraints.

When and where forced resource redeployment does not work, reforms become instruments to reveal and extract resources and to recreate the structure's lost cohesion through new allocations. Let us call resource-mobilizing reforms those direct or indirect resource-revealing actions that remain within the confines of the net.<sup>5</sup> With these instruments, resources formerly hidden may come to surface or units formerly passive become active.

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<sup>5</sup> For example, resources are mobilized within the net by decreasing the state's administrative role through the introduction of normative, macro-measures: a quasi- world market price system, revenue-sharing constructions, or income-taxation system, enterprise revenue system, reducing the role of compulsory planning, decentralizing decisions over input, output and commercial partners, over investment, import, export etc. Resources may be mobilized by *narrowing* the circle of selective allocation (e.g. narrowing the number of those privileged, altering the ratios of revenue sharing, increasing tax rates. It will render similar results if the attracting and resisting capacity of sub-units is *decreased*. For example, this happens by abolishing of branch (line) ministries that mediated enterprise interests, or by depriving these latter of their interest promoting capacities and functions. Another way to reach that goal is the decentralization of the nomenklatura and appointment rights of enterprise managers to lower

However, owing to the strong attracting and resisting capacity of those fed back within the net, mobilized resources will be allocated invariably on the basis of politically rational criteria. Repeated direction of allocation contributed to the maintenance of fixed paths and the further strengthening of those privileged. Vicious cycle is developing through escalation of reforms<sup>6</sup> there is no capacity to abandon forced paths and political priorities of continuously increasing living standards that gave the legitimacy of the party since 1957.<sup>7</sup> Meanwhile, reform escalation occurs without creating alternative resources and alternative rationality of behavior outside the net. The recurring drives for sustaining self-reproduction with reforms gradually disintegrated the net<sup>8</sup>. When no further resources may be attracted or extracted in the given power structure, decentralization of interlinking threads accelerate, extracting discretion is partially decentralized and drives to get rid of burdens increase. Simultaneously, efforts to create resources outside the net or attract from above strengthen. By that time though, in this structural pattern the condition of the structure deteriorates to such extent that cohesion may not be regenerated and system collapse takes place. Thus, Goulash Communism was created by the demands of the power structure and the same represented the traps that have lead to the loss of party legitimacy and political transformation.

(iii) The third type of pattern will be called self-withdrawing which refers also to the present Chinese pattern of power distribution. This pattern developed and stabilized during the frequent decentralizing-centralizing campaigns of Mao from the end of the 1950s to the end of his power in 1976. It meant the decentralization of decision-making power over resource extraction and distribution, supported by the decentralization of subordination of state-owned enterprises. Decentralization followed size and administrative rank: the smaller the enterprise the lower the rank of the administrative level under which the enterprise was subordinated. By the time Deng Xiao Ping took over and decided on decentralizing reforms, the new pattern with decentralized distribution of power was institutionalized, and interests towards decentralizing reforms that would increase decision-making power of local administration had a firm background. On the other hand, strong resisting capacities towards the center had evolved due to the alternative resources to central distribution and selective integration of provinces into the higher level decision-making process.

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levels of the administration. Similar results may be achieved by weakening the bargaining capacity of the sub-units themselves by disconnecting their feedbacks.

<sup>6</sup> The continuous drive for revealing and exploiting further resources to distribute may be accelerated further by the hardening of reproduction constraints from above or from outside the net.

<sup>7</sup> Csanádi, *Party-states and their Legacies* p. 229; Edward S. Steinfeld, *Forging Reform in China. The Fate of State Owned Industry* (Cambridge: Cambridge University Press. 1998), p. xiii-xv, 3 and pp.18-21; Roger H. Gordon. and David D. Li. "Government Distributional Concerns and Economic Policy During the Transition from Socialism" *Transition Economics*, N. 1662 Discussion paper series. Centre for Economic Policy Research, London (1997), p. 2.

<sup>8</sup> Growing difficulties will arise in maintaining traditional control through interlinking lines ( $D_2$ ) reaching out to the multitude of organizations, activities and positions. Moreover, the activity of using the net will decrease, since there are no expectable allocations through it while few alternatives emerge.

Therefore, in this pattern interlinking threads are partially decentralized, so are resource extraction and allocation capacities, while there are strong economic feedbacks from several dimensions of the network for some enterprises and provinces. There is an increased resisting capacity to resource extraction and alternative to central resource distribution within the given pattern. Under these circumstances neither forced resource-redeployment, nor resource-mobilizing efforts within the network are sufficient for the self-reproduction of the whole structure. During 1979-1992 overwhelmingly decentralizing (resource revealing) reforms within the net were implemented in China mirroring those in Hungary. During this period one may detect overheated local investments, inflation and advantages of resource extraction of provinces to the detriment of central sources. As a reaction, one may perceive almost yearly repeated central retrenchments to halt the economically disadvantageous consequences of decentralization. Retrenchment and resource centralization fuel efforts to get rid of allocation burdens by continuously decentralizing allocation responsibilities (both expenses and targets of allocation). Besides decentralization, drives develop to leap out of the net for new resources to extract by allowing the increase of the economic field outside of the net. This was the process that is dated from Deng Xiao Ping's round trip in south China in 1992. The round-trip took place in the aftermath of the last retrenchment in 1989-90 combined with the bitter experiences of the Tiananmen square events that has slowed down the economy. Reforms directed to the creation of new resources were twofold: on the one hand, measures were taken to encourage foreign and domestic investments outside the network, on the other hand, a tax reform was introduced in 1994 that shifted the ratio of local and central taxes to the advantage of the center. Complementing these ones, several other instruments were applied within the net allowing for resource centralization.

Let us call resource-creating reforms those measures through which decision-makers partially or completely "leap" out of the net, or let the field outside the net grow in order to acquire new resources<sup>9</sup>. This process increases the alternative field to the net (alternative behavior, activity, organization, property resources and rationality) that makes the net relatively retreat<sup>10</sup>, but it will retreat absolutely too from the economic sub-field (see later). Thus, it was the structural specifics of power distribution that brought about the "Chinese Style" reforms keeping the legitimacy of the party by macro-economic growth and rising living standards while ending up in economic transformation first.

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<sup>9</sup> For example, extractable resources are created by allowing increases in the number of resourceful units outside the net and the creation of the institutional conditions for this process. For example, letting the exchange of over-the plan products on market prices, to increase revenues outside the net, to enhance conditions for domestic and foreign private ventures, enhance private plot cultivation, to abolish collectives and cooperatives, setting up domestic private enterprises, encouraging the settlement of foreign funded enterprises. Allowing the "entrance" of resources from outside the net, by attracting FDI for creating joint-ventures, transforming SOEs into shareholding enterprises for foreign and domestic private capital infiltration, lifting up barriers to labor mobility, price setting and product and capital flow etc.

<sup>10</sup> Naughton calls the relative growth of non-state sector as "growing out of the plan" in John McMillan and Barry Naughton, "How to Reform a Planned Economy: Lessons from China." *Oxford Review of Economic Policy*, Vol. 8. Spring (1992), pp. 130-143.



Concluding the above, we have seen that pattern specifics will bring about pattern-conforming instruments of resource extraction and distribution serving self-reproduction that reflects the distribution of power within the system. This is how the pattern that evolved in Hungary during 1957 and 1963 brought about the decentralizing and resource-revealing reforms within the network with growing living standards called “Goulash Communism”. On the other hand, the pattern that evolved and stabilized between 1957 and 1976 in China induced, besides decentralizing reforms, the development and dominance of resource creating reforms accompanied by growing living standards that acquired the name of “Chinese-style reforms”. Both dominant reforms and the acceleration of their implementation willingly or unwillingly paved the way of the different sequences of system transformation: political transformation first in Hungary and economic transformation first in China. How could such different transformation occur?

### **3. THE DYNAMICS OF TRANSFORMATION**

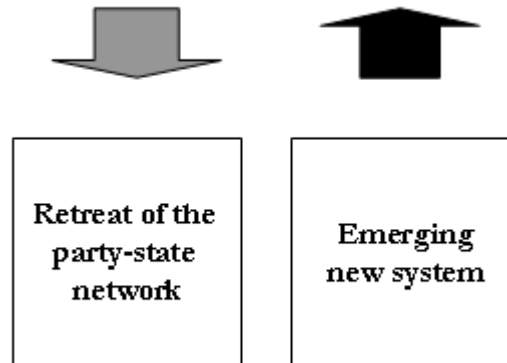
Dynamics within the net are not independent from that outside of it. External factors have a substantive impact on the conditions of self-reproduction. These factors or their absence influence transitory or definite restructuring within the net. The impact of external factors and response to those depends primarily on the pattern of power while strategies are secondary. This is because the room for maneuver of strategies is constrained by the possibility, interests and conditions within the pattern, though interacting with it. If structural constraints are met and resources from higher aggregation flow poorly, reproduction constraints within the pattern become hard and exposure to external factors arise. In those cases the importance of the constraints exerted from outside the net emerges.

Hardening reproduction constraints from within and hardening budget constraints exerted from outside the network if occur simultaneously, adaptive drives intensify, pattern-conforming measures accelerate and pattern-conforming transformation process will take place.

Based on the above, we may now define in more detail the disparities of transformation in the model's approach. We shall focus on the following questions:

Figure 6.

### What does transformation mean?



The definition of transformation in the analytical approach of the model is the following: the party-state network is *retreating* as a social system from monopolized sub-spheres, while outside of the net the sub-spheres of a new social system are *emerging* (Figure 6). The nature of these two tendencies may be different. It may involve *absolute and relative retreat of the network*. Absolute retreat occurs when elements of the network, their functions and their impact decline. Relative retreat evolves in relationship to the higher speed of development of the emergent sub-sphere compared to that of the network.

However, both retreat and emergence are *pattern-dependent* that influence the characteristics of the transformation process. Specifics of such path-dependency evolve in several dimensions: (1) according to the differences *among* patterns; (2) the disparities of power distribution *within* patterns; (3) the different interplay among intertwined patterns (similar or disparate) of different levels of *aggregation*. Intensity of influence will depend on the density and depth and extent of centralization or decentralization of intertwining lines of dependence, the distribution of power of higher and lower level aggregations. These characteristics may mutually speed up or slow down the process of retreat and emergence; (4) Finally, path-dependency is also the result of the combination of the actual importance of different composing factors of the process of retreat and emergence.

All of the above four characteristics of pattern-conforming path-dependency will influence where, how and with what sequence, speed, conditions and outcome will pattern-dependent

transformation occur. The interplay of the above pattern-conforming characteristics with local individual traits will jointly define the concrete outcome of the process of transformation. Pattern-characteristics will also influence the adapting capacity of actors during the transformation process. Next we shall detail only two of the above four specifics that are crucial for our present arguments focusing on the differences between the transformation of Chinese and Hungarian party-states.

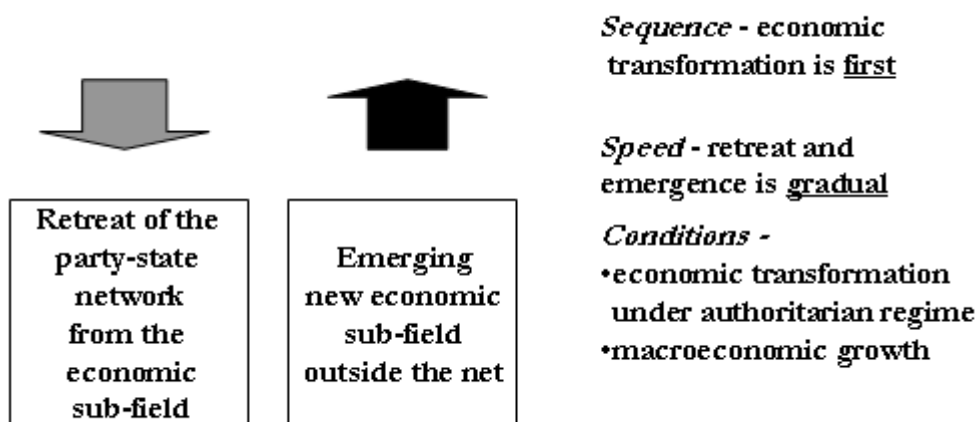
#### 4. IMPACT OF PATTERN DISPARITIES ON THE TRANSFORMATION

The IPS model suggest that path-dependency will emerge due to the different pattern *dynamics* resulting (a) in the different *sequence* of transformation of political and economic subfields, (b) in the different *pace* of the retreat of the net from monopolized sub-fields and emergence of the field outside the network, concluding in (c) the different political *conditions* of economic transformation and different economic conditions of political transformation.

In the Chinese case, pattern-conforming characteristics of transformation due to the impact of resource-creating reforms outside the network are the following: economic transformation comes first, either followed or not by political transformation. The retreat of the net and the emergence of the new economic sub-sphere is gradual, economic transformation occurs under authoritarian political regime, accompanied by macroeconomic growth (essentially due to the economic field outside the net) (Figure 7.).

Figure 7.

#### System transformation in China: transformation of the economic sub-field first



Due to the *authoritarian political conditions* the retreat and emergence in the economic subfield is accompanied by the following phenomena: In the stretched out transformation process intensive traffic of actors and capital in- and out of the net prevails. There is a potential threat of the long-term stabilization of rent-seeking behavior, corruption and a steady stripping of the public values of the net through capital, manpower, elite and organization flight. This process might also enhance a network-selected and dependent private sphere on short-term interests. Authoritarian conditions also encourage the infiltration and institutionalization of criminal networks and organized crime. These activities benefit the monopolized closed channels of interest promotion of the party-state network. Institutional and horizontal organizations to control changes are lacking. Labor force is exposed, chances for institutional voicing are lacking, both in the state and the concurrent private sector. Thus, open mass grievances due to corruption or other economic and social reasons increase in number, scope and mass.<sup>11</sup>

However, the same stretched out process under authoritarian conditions provides the opportunity to smoothen the retreat of the net, keep overall political stability. Gradual transformation provides also an opportunity for a gradual economic and political pluralization within the network. Pluralization is caused by the infiltration of private capital in the state owned sector and capitalists in the network. There is a steady macroeconomic growth, overwhelmingly due to the emerging field outside the net owing to the constant infiltration of foreign capital and increasing domestic capital investments. Meanwhile, there is a selective economic decline within the network chances for bailing out larger loss-making SOEs narrow. Thus, prospects of massive and concentrated lay-offs strengthen, revenue disparities at several dimensions widen, the party's mass and economic basis in SOEs and joint ventures is narrowing. However, until macroeconomic growth is secured party legitimacy is kept. But as soon as growth declines, economic and social tensions may sharpen and legitimacy may suffer.

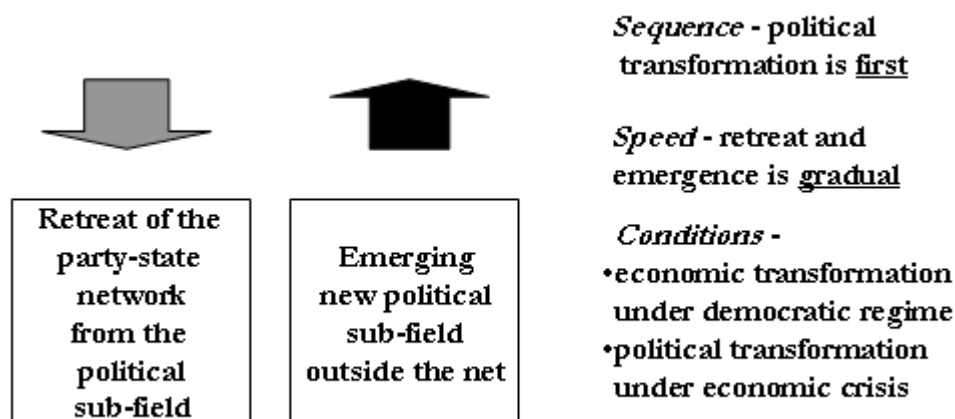
In the case of Hungary, political transformation comes first owing to the loss of party legitimacy due to the inefficiency of resource-revealing (decentralizing) reforms and exhaustion of foreign resources (see Figure 8.). Economic transformation follows political transformation, thus, this latter occurs under democratic political regime. The retreat of the net and the emergence of the new political sub-sphere is gradual.

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<sup>11</sup> Yongshun Cai, "Power Structure and Regime Resilience: Contentious Politics in China", *British Journal of Political Science*, Vol. 38, No. 03. (2008), pp. 411-432

Figure 8.

# System transformation in Hungary: transformation of the political sub-field first



Sequence also determines economic conditions during political transformation: There is a steady economic decline, indebtedness, and growth of the volume of loss-making enterprises. Restriction spiral that de-legitimizes the communist party despite accelerating decentralizing reforms makes the network retreat gradually from political sub-sphere. Horizontal organizations and new parties form under conditions of macro economic imbalances. Since decentralizing reforms within the net did not create private sphere, domestic private capital is lacking. There is no domestic economic force that could equilibrate incomes, introduce alternative capital, behavior and interest, provide new workplaces, decrease budget deficit and form electoral base for newly emerging parties. The fluidity of the political, economic and social structure is general:<sup>12</sup> institutions, functions, positions, parties, horizontal organizations, rules and laws are frequently changing. Fluidity enhances cumulated uncertainty. There are social grievances, regionally concentrated mass unemployment due to the close-downs or privatization of loss-making large enterprises that increase political conflicts. Frequently changing institutions, functions, internal distribution of tasks and staff hinders information and transparency during privatization and FDI inflow, attracts short-term interests. Meanwhile, former elite's positional advantages the preservation of fragmented but steady networks contribute to the insiders' information and wealth acquisition.

Critical economic conditions, cumulated uncertainty during transformation, volatile electorate and, inexperienced elite are aggravating political transformation. These factors are adding to the weaknesses and to political swings of elected parties and governments. Several

<sup>12</sup> Valerie Bunce and Maria Csanádi. "Uncertainty in the Transition. Post-Communism in Hungary," *East European Politics and Society*, Vol. 7., No. 2. Spring (1993), pp. 240-275.

party splits occur due to the initial phase of their formation. Governments and programs are changing relatively frequently due to economic crisis. Thus, governing parties soon lose social trust and popularity, due to economic crisis, unrealistic hopes, uncontrollable fast changes, frequently modified decisions and frequent policy swings.

Based on the above approach, we could define why “Goulash communism” owing to pattern-specifics of self-reproduction and external pressure of expiring Western loans ended in political transformation first. We have shown under what economic conditions this occurred and how political conditions of the newly emerging political sub-field influenced the subsequent economic transformation.

## **5. FACTORS WITHIN THE PROCESS OF RETREAT AND EMERGENCE**

The ingredient factors of the process of retreat and emergence and their different combination will influence the ways the transformation occurs *within* each pattern. Similarly, the processes of transformation of a given subfield raise similar problems and incite similar solutions (Csanádi, 2006). However, the scale of impact will be strongly influenced by pattern specifics, the sequence, speed and conditions of system transformation and the combination of the variety of the composing elements of retreat and emergence as well as individual characteristics. The different combination of the inherent factors of the transformation will interact and thus reinforce or slow down mutual dynamics.

Let us see the components of the economic transformation through the absolute retreat of the network from economic sub-field and the emergence of a new economic sub-field outside of it at the example of China (Figure 9. and 10.).

Figure 9.

### Components of the process of retreat of the network in China

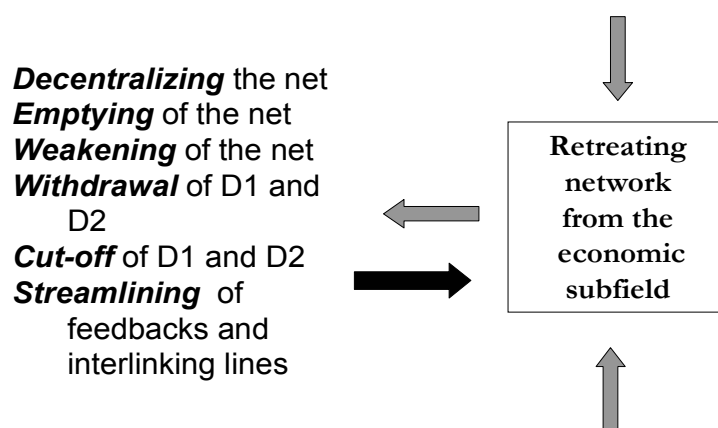


Figure 9. reflects the factors of the absolute retreat of the net. These factors will characterize the transformation since they may strengthen in different sequences, or simultaneously, or in different combinations. Due to frequently hardening reproduction constraints of the network in China decisions over allocation, price, investment, extractions are decentralized while revenues and revenue sources are siphoned away. This process may occur directly, by deliberately withdrawing interlinking- and hierarchical lines (for example, the withdrawal of the net from below county level through semi-free governor elections on township level in China.<sup>13</sup> The network may be withdrawn also by abolishing former distributive functions and organizations dealing with resource distribution and decisions over allocation and allowing investments or by elevating the threshold of administrative (official) consent for investments. Thus, hierarchical lines of command are shortened and lines interlinking functions and organizations are also withdrawn. Another reason for the absolute retreat of the net is the attractiveness of the alternative options of resource acquisition outside the

<sup>13</sup> Hairong Lai, "Development of Competitive Elections since mid 1990s on Township Level in Sichuan Province in China.", *China Perspectives* (Hong Kong), Vol. 51, January-February (2004), pp. 13-27.; Ding Shuhfan, "The Party-state Relationship in China, 1978-1986.", (Dissertation submitted to the Graduate School of the University of Notre Dame, in Partial Fulfillment of the Requirements for the degree of PhD, Dept. of Gov. and International Studies, UND. June 1987), p.32, fn. 18

net. Options will motivate decision-makers to partially or definitely exit<sup>14</sup> the network, vacate the rigid structures and to leave burdens within the net that incites further decentralization.<sup>15</sup> Burdens may be get rid of by cutting them off the net. This event occurs when the economic units embraced by hierarchical and interlinking lines disappear from the end of the through bankruptcy and close-down or privatization of SOEs<sup>16</sup> and TVEs. The network may also weaken by attracting resources from outside the net (such as FDI<sup>17</sup>), integrating alternative interests, alternative behavior and capital that will decrease the political influence through the hierarchical and interlinking dependency lines.<sup>18</sup> The network – both hierarchical, interlinking lines and feedbacks – were streamlined for purposes of rationalization that weaken their density and accumulation declining the capacity for interest promotion.

These actions have several consequences: they decrease the number of sub-units attached to the net and in exchange, increase the amount of redistributable resources to the remaining sub-units within the net, and also may provide the unit with resourceful entities outside the net. Moreover, because of available alternative resources, the intensity of using the net also decreases.

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<sup>14</sup> This may occur either individually: Gordon, and Li, *Government Distributional Concerns* p.1-2 and 23), or as an organization Yingyi Qian, "Enterprise Reform in China: Agency Problems and Political Control" *Economics of Transition*, Vol. 4 N. 2, (1996), pp. 427-47, p. 430, Russel Smyth, "Recent Developments in Rural Enterprise Reform in China: Achievements, Problems and Prospects." *Asian Survey*, Vol 38. N. 8, (1998), pp.784-800 and p. 798.

<sup>15</sup> E.g. in the form of daughter enterprises which than found joint ventures with private ones). Qian, "Enterprise Reform in China", p. 431

<sup>16</sup> According to the utilization of resources earned from privatization, resources may be re-deployed if used for the subsidization of remaining SOEs, or social causes, and may end in resource creation if invested in joint ventures or infrastructure or shares in private enterprises. Meanwhile, privatization decreases subjects for resource extraction within the net.

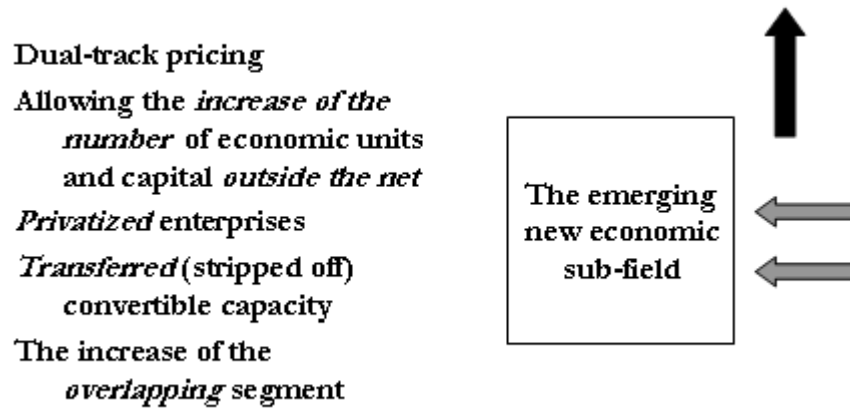
<sup>17</sup> Yanrui Wu, (ed.). *Foreign Direct Investment and Economic Growth in China New Horizons in International Business*, (Cheltenham, UK: Edward Elgar Publishing Ltd. 1999); Yasheng Huang, "Internal and External Reforms: Experiences and Lessons from China." Part I. *ChinaOnline News*. Sept. 20, (2000).

<sup>18</sup> Margareth M. Pearson, *China's New Business Elite. The Political Consequences of Economic Reforms* (University of California Press: Berkeley, L. A. London, 1997)



Figure 10.

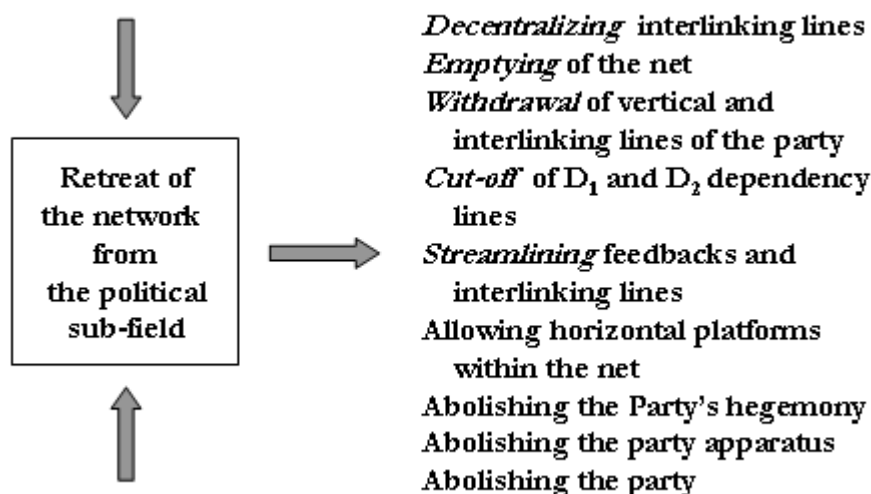
### Factors of the process of emerging new economic subfield in China



How did relative withdrawal of the net, that is, the emergence of the new economic sub-field occur? The higher is the expectations for harder reproduction constraints within the net the more intensive the pressure to decentralize and to leap out of the net. This drive will cause the escalation of resource creating reforms. Emergence of the economic sub-sphere outside the net occurs as a result of allowing over-the plan production to be sold at market prices both in the industrial and agricultural spheres. The increase of the number of economic units and capital outside the net was allowed. Growing number of enterprises prior attached to the network now privatized. The results of the increase of the transfer (stripped) of convertible capacity (manpower, capital, organization, production) from the net outside of it. This drive is reinforced if chances for resource attraction through the network decline. The scope of the overlapping segment of the network and the emerging field widens through joint ventures or joint-stock companies with private majority share.

Figure 11.

### Factors of the process of retreat of the network in Hungary



Tables 11. and 12. show the elements of political transformation that occurred in Hungary. Hardening reproduction constraints of the system have driven decision-makers in the party to get rid of burdens by decentralizing the discretion over interlinking lines in the party that reached economic decision-making processes. The party itself weakened its influence within economic units by abolishing full-time position of party secretaries and subordinating them to enterprise managers by nominating them part-time. Declining influence and legitimacy of the party enhanced the emptying of the structure: growing number of party members quit the party due to disillusion, declining privileges and alternative options; also staff members are quitting party positions to public or private spheres; not only actors leave but also the interactivity through network gradually vanishes due to the declining capacity of resource distribution. There was a clear withdrawal of vertical and interlinking lines due to the introduction of multi-candidate elections in several fields: at local governments, in the nomination of enterprise managers, to the parliament and to the party central committee membership. Towards the end of 1988, the interlinking threads were already incapable of "covering" the economic sphere, let alone the social and political spheres. In response to all these changes, pressures and instability, in October 1988, the Politburo displayed increasing tolerance towards emerging new political and economic interest groups. It set very easy criteria for the acceptance of alternative movements by the party and allowed party members to join these

movements.<sup>19</sup> Indeed, the Hungarian Socialist Workers' Party (HSWP) even offered them political alliance.

At its meeting in early February 1989, the CC made an historic admission: it declared that it regarded the events of 1956 as a popular uprising, not as a counter-revolution, in which the forces of democratic socialism were also present.<sup>20</sup> This announcement retrospectively called into question the legitimacy of the system, given the bloody repression of the 1956 uprising with the help of Soviet military forces. At this mid-February meeting the CC recorded that the HSWP had renounced its claim to being in a leading role, and had declared that it wished to be a political party. In March, the Budapest PC suggested the total abolition of the nomenklatura system.<sup>21</sup> In April it had also publicly defended the developing horizontal organizations of the various kinds of reform groups within the party,<sup>22</sup> though these were incompatible with the principles of hierarchy. This also led to the reluctant acceptance of the principle of competing platforms which had been rejected outright earlier.

In May 1989, the CC initiated the total abolition of the nomenklatura system. It declared that it wanted to practice its jurisdiction over party positions only. It also called for the reversal of its earlier decision on the party leadership over the workers' militia — which was its armed force established in 1956.<sup>23</sup> With these steps the legitimacy of party groupings within organizations was further weakened, as was that of the workers' militia funded in 1957. The suggestion to shift the headquarters from enterprises to territorial organizations, however, still faced resistance. The greatest — and well-founded — fear of the party organizations in shifting the scope of membership registration from enterprise to territory was that in the event of territorial organization, they would lose a large proportion of their membership. As a result of the process of retreat, Party as a social system was withdrawn from political and economic subfields, abolished as a hegemonic party and reborn as a political entity in a de-monopolized political sub-field.

Parallel to the gradual retreat of the network from the political sub-sphere, a new political sub-field was emerging outside the net (Figure 12).

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<sup>19</sup> "The October 4, 1988 meeting of the HSWP PC", in *Népszabadság*, 5 October 1988.

<sup>20</sup> "The February 10-11, 1989 meeting of the CC", in *Népszabadság*, 13 February 1989.

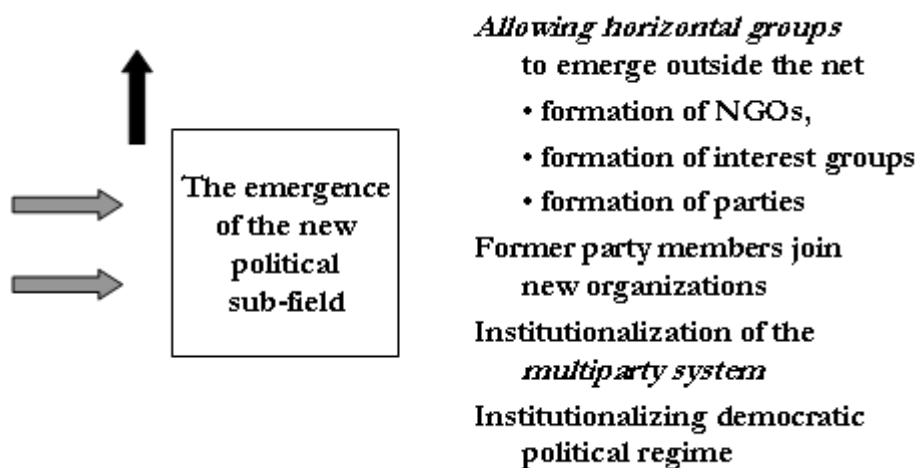
<sup>21</sup> "Interview with the First Secretary of the Budapest PC", in *Népszabadság*, 18 March 1989.

<sup>22</sup> Arguments about political initiatives, criticism, freedom of opinion, intra-party debates, and the freedom of platform formation. Party Debates, (HSWP CC Department of Propaganda and Canvassing, 1989, No. 3).

<sup>23</sup> "The May 3, 1989 meeting of the CC", in *Magyar Nemzet*, 10 May 1989.

Figure 12.

### Factors of the process of emerging new political subfield in Hungary



Growing number of horizontal groups outside the net was allowed to form: first NGOs of various kinds emerged with non-political scope. Formation of various interest groups was allowed to organize both on economic, public and political subfields. In unison with its meeting in early February 1989, when the CC accepted the need for political pluralization and a *multiparty system*, interest groups were transformed into parties. Former communist party members, who quit the party joined the new interest groups and later new parties. At the behest of the increasingly vocal opposition groups and the internal opposition of the HSWP itself, negotiations began in May 1989 between the government and the new political groups. The talks gained increasingly more weight, and legitimacy gradually shifted from Parliament to the scene of these negotiations.<sup>24</sup> Within weeks, the agreements reached here became important items on the Parliament's agenda. No longer could Parliament debate bills without these having first been passed and/or amended by this extra-Parliamentary forum. Noteworthy among these were the amendments to the constitution and the so-called crucial laws formulated through tough negotiations: the freedom of information law, the party law, the electoral law, and many other important amendments to current laws.<sup>25</sup>

<sup>24</sup> The participants of the National Round-Table Conference were: 1) The HSWP, 2) The new opposition parties, 3) The trade unions, together with old and new social organizations (Vigh, 1989).

<sup>25</sup> Report on the June 27-30 1989 session of Parliament, in dailies *Magyar Nemzet* and *Népszabadság*, July 1 1989.

Following the agreements, the remaining threads holding the structure together became strikingly contradictory to the accepted changes. During the first eight months of 1989, 68,000 people left the HSWP, whereas only 2,600 entered, leaving 725,000 party members out of the 790,000 of the previous year.<sup>26</sup>

Political transformation with the formation of new parties, the emptying and withdrawal of the HSWP and the introduction of the new political structure went rapidly and smoothly given the pre-empting gradual weakening and disintegration of Party power. The HSWP congress voted for the transformation of the Party into a political entity, and with the active support of the reformist wing it dissolved itself. The last party congress was held in early October 1989. The delegates recognized and declared the end of the monopolized power relations, and disassociated themselves from the former methods of management, power, and control. On the fourth day, the reform wing of the delegates or, more specifically, reform communist leaders succeeded in convincing the participants on issues of reform. The reform platform pushed through the democratization of the party rules of organization, the approval of a short, socialist-inspired party program, the abolition of the HSWP and its apparatus, and the formation of the Hungarian Socialist Party (HSP) as its official (legal) successor. The distribution of Party property was also put on the agenda and free election was put in process.

Free elections were held, and six parties succeeded in joining the parliament.<sup>27</sup> The conservative left, overwhelmingly formed by the aged members of the dissolved HSWP did not achieve the minimum quota (four per cent) to enter the parliament. The reform communists became a small parliamentary opposition party after free elections. The first government was formed by the conservative right wing of the former dissidents.

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<sup>26</sup> *Népszabadság*, October 4 1989.

<sup>27</sup> These parties were the conservative Hungarian Democratic Forum, two traditional parties that had historical background in pre- and post-World War II period, the Smallholders and the Social Democrats, the successor Socialist Party, and two liberal parties, the Young Democrats and the Free Democrats.

## CONCLUSIONS

Chinese and Hungarian party-state systems, despite their huge individual disparities in size, in geopolitical location, economic structure, cultural and historical traditions etc. may be compared based on their common systemic characteristics demonstrated by the IPS model. The common traits interact with different characteristics of the pattern of power distribution and individual specifics. They will jointly determine the varieties of the structure, operation and of system transformation in time and space. Disparities in the pattern of power distribution bring about different resisting capacities to resource extraction. This will require the implementation of pattern-conforming, instruments of self-reproduction (extraction and allocation) of the system. Such were the decentralizing reforms from above within the network in Hungary, and the decentralizing and resource creating reforms within and outside the network in China. „Goulash Communism” in Hungary, which meant a steady increase in living standards combined with decentralizing reforms in the economy should be dated to the period of pattern-conforming self-reproduction of the Hungarian party-state system until the second half of 1980s, when economic crisis, retrenchment spiral and the exhaust of foreign loans together exerted pressure for adaptation and decreased party legitimacy. „Chinese style reforms” became characteristic from early 1990s, when resource creating reforms outside the network accelerated, contributing to macro-economic growth and party legitimacy. Characteristic operation and instruments within patterns do not change substantially in time even under adaptation pressures. Instead, they escalate with the growing pressures from within and outside the network. Thus, while supporting the self-reproduction of the system they simultaneously contribute to its transformation. Transformation will be pattern-conforming: it will define the disparities in the sequence, speed and political conditions of economic transformation and economic conditions of political of transformation. These characteristics explain why Hungarian „Goulash Communism” ended up in declining legitimacy of the party and political transformation first accompanied by economic crisis, while economic transformation occurred second, under democratic regime while we find the specifics of the „Chinese style” in economic transformation first accompanied by macroeconomic growth under authoritarian regime, with political transformation second in the waiting. Choices of sequence and conditions are structurally constrained. Differences in the combination of composing elements of the process of retreat of the network and the emergence of the new system’s subfield will contribute to the differences.

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