Be on your guard! Cyclically adjusted budget deficit

Gábor P. Kiss and Gábor Vadas

Cyclically adjusted budget deficit (CAB) is a concept widely cited and used in evaluating fiscal situations. The key idea behind it is to separate temporary and/or non-discretionary effects on budget deficit from the underlying balance and/or effects of discretionary measures of fiscal policy. Computation of CAB is based on identification of the potential level of economic variables. In this paper, it is demonstrated that composition matters in the case of both real and nominal variables. The European Commission and the European Central Bank have each proposed methods for measuring CAB, but these are not fully capable of satisfying all requirements. Besides, results show that aggregated and disaggregated approaches provide different estimations, to the benefit of the latter. The paper presents an alternative method, able to incorporate the advantages of both approaches. Combining output gap from production function and constrained multivariate HP filter induces a theoretically motivated disaggregated approach that also exploits the implication of production-function parameterization. Taking into account the nominal features, for example, nominal elements of the tax code or deflators directly affected by the government, the more precise definition of discretionary measures became also important.

Indexed options based on the underlying price

Márton Radnai

Indexed options are ones that can only be exercised at a profit if the yield of the stock concerned exceeds the yield of a certain index. The article shows that structures published so far, in which the call option is indexed to the exercise price of the instrument, does not filter out all index risk. A proposal is made for a new type of indexed option, indexed to the price of the underlying product, so that all index risk is eliminated. The valuation relations of these options are provided and it is shown that they can be used not only for executive remuneration, but in stock-market trading as well.

Recalculation of the first Hungarian bankruptcy-prediction model using neural networks

Miklós Virág and Tamás Kristóf

The article attempts to say whether the latest bankruptcy prediction techniques are more reliable in Hungary’s case than traditional mathematical/statistical ones. Simulation experiments carried out on the database of the first domestic bankruptcy-prediction model
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show clearly that neural-network models possess greater classification accuracy than the models based on discriminant analysis and logistic regression analysis elaborated in the 1990s. The article presents the main results, analyses the reasons for differences, and draws up constructive proposals for further development of domestic bankruptcy-prediction practice.

Unilateral or mutual dependence? The economic relations of Taiwan and the People’s Republic of China

Gyula Jordán

The economic relations of Taiwan and China, in terms of trade turnover and investments of operating capital, have been developing very rapidly since the early 1990s. Taiwan’s export dependence has exceeded 20 per cent. Its investments of operating capital are estimated at around $100 billion and major Taiwanese production capacity has been transferred to the mainland. Nonetheless, the paper argues against the common view that Taiwan is entering a situation of unilateral dependence and vulnerability and in favour of growing mutual dependence. A violent move against Taiwan would jeopardize the fastest developing export-oriented sector of the Chinese economy and the country’s own economic development strategy. Taiwanese firms have built a network of economic and social ties not only with Chinese firms and officials, but with multinational firms operating in China. Several other factors (such as WTO membership) are also strengthening the mutual dependence.

Thoughts on the susceptibility to analysis of the market-force problems found on the Hungarian electricity generation market

Péter Gordos

The study sets out to present the constraints on analysing the market-force problems of the Hungarian electricity generation market by using a Cournot model. The author’s thoughts are designed to draw attention to the problem rather than be critical, to decide the extent to which sometimes oversimplified models in economic analyses and the results obtained with them can have practical uses in devising an effective regulatory environment. The study (which follows from Paizs and Mészáros 2003) places less emphasis on questioning the analytical methods of those authors and the results of them than on presenting the possibility of result distortions deriving from model assumptions that simplify reality.