



THE ECONOMICS
AND POLITICS OF TRANSITION
TO AN OPEN MARKET ECONOMY
EGYPT

BY
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DEVELOPMENT CENTRE STUDIES

THE ECONOMICS
AND POLITICS OF TRANSITION
TO AN OPEN MARKET ECONOMY

Egypt

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DEVELOPMENT CENTRE
OF THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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Foreword

This study was carried out under the Development Centre's research programme entitled, "Major Regions and Large Countries", as part of a project to analyse the political preconditions for the success of economic policy reform in transitional and developing economies. Other studies in the same series have been carried out on China, Colombia, India, Russia and Viet Nam.

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Preface

During the 1990s, the number of countries which have embarked on fundamental economic policy reforms leading to open, competitive market economies has grown dramatically. Centrally planned economies in Eastern Europe and East Asia, as well as countries with highly interventionist policy regimes such as India or Brazil, have been eager to reduce government involvement in economic decision making, to ensure macroeconomic stabilisation, and to open up to international trade and capital flows. Based on these experiences, a considerable amount of knowledge about critical reform ingredients and the timing of their implementation has been accumulated.

Experience has also shown, however, that reforms are not always carried through, or are stalled during the reform process, due to opposing political interests. Economic reform always creates winners and losers, and frequently the losers include politically powerful groups. In 1996, the OECD Development Centre launched a research project to analyse the political preconditions for the success of economic policy reform in transitional and developing countries. The objective is to study the interplay between economic necessities and political challenges during the implementation of policy reform, thereby generating recommendations for dealing with political opposition to reform.

The project focuses on the experience of six countries: three large economies, China, India and Russia, and the smaller Colombia, Egypt and Viet Nam. The distinction between large and small countries was made because the regional dimension adds to the problems of reform in large countries, while outside influences may play an important role in small economies. The case studies, each of which is being published separately, will be complemented by a synthesis volume identifying common experiences and summarising the major policy conclusions for countries which are latecomers in implementing reform.

Egypt was chosen as an example of a country exposed to considerable and continuous external interference because of its geopolitical location. The objective of the study is to trace the impact of external involvement on the direction and the pace of the reform, as well as to evaluate the potential contribution of outside support for policy reform. This analysis will not only be important for reforming countries, but also for the bilateral and multilateral donor community.

Jean Bonvin
President
OECD Development Centre

July 1998

Introduction

The following case study on Egypt is part of a research project initiated and sponsored by the OECD Development Centre on the economics and politics of transition to an open market economy. Economists — even if they have been involved in policy consulting — tend to avoid the politics of economic decision making and to leave the subject to political scientists. The latter, with a few exceptions, tend to focus on specific policy aspects and to leave economic technicalities to economists. Thus, the political economy of economic transformation is most often not addressed by either profession.

In addition to the frequent deficiencies of statistics in developing countries, the process of economic transformation is often accompanied by further deterioration of the data base. As part of the decline of the old public-sector structures, statistical offices at all government levels, and in parastatal organisations — such as federations of industries, chambers of commerce, labour unions, professional syndicates and banks — previously geared to top-down national planning may not be able to document the turbulent economic and social change. The Egyptian economy has reached a level of complexity which makes it difficult to compile even most elementary data such as GNP, economic growth rates, and demographic statistics, let alone reliable information on unemployment and social indicators. In its presentation of the *Human Development Report for Egypt*, the Institute of National Planning — a remnant of the Nasserist heritage — underlined that “there are enormous problems in even the most basic indicators in Egypt” (Institute of National Planning, 1995). The USAID Privatization Project reiterated “...that a large amount of current important data and information is not available. This data covers a wide scope from the private sector’s share in investment and trade, to the unemployment rate and average wage rates in the different main sectors of the Egyptian economy. Despite the importance of this data, very few attempts were actually carried out to obtain for policy makers and other parties these important sets of data. Thus, our analyses are based on partial and incomplete data in an attempt to discuss trends and identify important policy issues” (International Business & Technical Consultants, Inc., Quarterly Review of July–September 1996).

Large bilateral donors like USAID collect data on their own. Even the World Bank and IMF have differed widely in their estimates of annual real GNP growth, with figures ranging from less than 1 per cent to between 3 and 4 per cent for the early 1990s. Such controversial estimates served as benchmarks for donor conditionality

and were subject to heavy disputes between the Egyptian government and its donors during the various phases of the painstaking reform process. When delineating the political dimension of economic transformation, the authors had to draw on published sources reflecting these conflicts and using the data available at the time in the then current debates. Since the mid-1990s, most of the earlier estimates have been subject to revision. The Annex presented in this study gives a fairly consistent overview of the major economic and social indicators during the period under consideration from the *ex-post* perspective of 1996–97, often diverging from the earlier estimates of the same, or of competing sources which had been subject to political debate month-by-month during the continuous struggle over a suitable pace of reform. The authors held that it would not have made sense to correct all figures which had been used in the contemporary sources during the early years of the Economic Reform and Structural Adjustment Programme (ERSAP) and to replace them with the revised *ex-post* data. As a result, the figures quoted in delineating the ongoing political struggle over ERSAP — particularly in Chapter 4 — are not always in line with the Annex, largely following the revised estimates of a major donor organisation. Generally, concepts of statistical accuracy and reliability become questionable when dealing with turbulent economic and social change. *Pattern recognition* appears to be a more relevant perceptual category than *hard data*, all the more so since data in Egypt have been deliberately manipulated to fit performance criteria, to affect restructuring and privatisation strategies, and to tamper with the valuation of public business assets. Information is being used as a weapon, or as a scarce commodity for sale in bits and pieces by a mushrooming skein of consultants demanding extraordinary fees. Research in this type of environment requires massive and time-absorbing information networking.

Particular difficulties arose in documenting the political decision-making process linked with ERSAP. The major consecutive moves to overcome the legacies of Nasser's Arab Socialism on the one hand and Sadat's Open Door Policy on the other are well explored (in particular by Hinnebusch, Richards, Springborg, and Waterbury). For the 1990s, the period under special consideration in the present study, similar comprehensive works do not exist. There is no easily accessible methodology for dealing with these issues. Apparently, high-ranking political decision makers cannot be addressed by standard empirical interviews. Nor do they disclose their day-to-day political moves to a broader public audience in writing, except — eventually and much later — in their memoirs. As a result, there is usually no first-hand empirical evidence on the considerations and particular political pressures which really motivated, for example, a decision to keep the exchange rate stable, to raise tax rates and electricity tariffs, or to reduce non-tariff barriers for specific import items. The only sources available to the outsider are scattered hints in published and “grey” economic papers and background sources which rarely address crucial political factors in detail. The authors tried to review whatever had been written on the Egyptian transformation process and to extract eventual glimpses of respective political considerations, both on the Egyptian side and among the donor community. During two extended field research missions in spring and autumn 1996 and a third one in the spring of 1997, the authors drew on Egyptian TV and radio, on Egyptian and foreign newspapers,

professional journals, and the helpful documentation compiled by *Egypte/Monde Arabe*, The Economist Intelligence Unit, the Bundesstelle für Außenhandelsinformation, as well as on donor agency sources, as far as they were accessible and not subject to confidentiality. Other sources were standardised and half-standardised interviews with Egyptian professionals related to the macroeconomic policy process, managers in public and private enterprises, representatives of business associations, chambers of commerce, professional syndicates, staff of universities and research institutions. A number of congresses, conferences, lectures and various Egyptian economic policy forums related to economic policy issues provided additional valuable insights. Thus, the authors tried to reconstruct the sequence of major political events related to the reform process, for example, a meeting of President Mubarak with the US President, Mubarak's subsequent press conference, and his meeting with the Director General of the IMF the day after, followed by a striking softening in the Fund's stand as to conditionalities and benchmarks; or the links between "wild-cat" strikes in large state-owned enterprises followed by wage concessions to public-sector employees, and the postponement of cuts in subsidies on butane gas for cooking purposes of the urban poor.

The authors had to deal with the problem of transforming such insights into the political dimension of reform decisions into a text. It was easier to draw up a fairly illustrative picture on the *micro* level of enterprises and other actors. As to the political aspects of the *macroeconomic* process, the authors chose a chronological form emphasizing major political events linked to the transformation process rather than a sectoral or problem-oriented presentation (e.g. of monetary and financial policies, trade regime decisions, etc.). Due to its limited empirical accessibility the political process *per se* appears rather between the lines of identifiable events (for example, the timing of a visit of President Mubarak to the United States and the outcome in terms of IMF concessions, or the EU Barcelona initiative, French President Chirac's visits to the Middle East, and adaptations of the Egyptian trade regime). Rather than tracing the various political aspects of sectoral or problem-oriented conflicts over Egypt's reform performance, the text tries to capture the full complexity of the continuous struggle, the impact of donor pressure, its considerate restraint with a view to preserving Egypt's political stability, the "low profile" approach preferred by the Europeans, and the Egyptian decision makers' reluctance to proceed with privatisation because of its high political risks. Without access to internal files, the chronological presentation of essential events, rather than a sectoral or problem-oriented order, reveals the painstaking, stop-and-go process — although the authors are aware that this documentation may be no easy reading.

The study follows a general outline which emerged from a round of elucidating discussions in the OECD Development Centre with its Director, Ulrich Hiemenz, Jeffrey Sachs, and various authors of the other country case studies in April 1996 in Paris. Chapter 1 briefly explains the pre-reform conditions, Chapter 2 the macroeconomic crisis which initiated the reform process. Chapter 3 deals with the lacking dynamics of earlier reform initiatives and outlines the new programme since 1990. Chapter 4

explores the macroeconomic political process. Chapter 5 documents the political economy of reforms on the enterprise level. The reasons for the unsatisfactory performance are explored in Chapter 6 dealing with the weakness of civil society in Egypt, Chapter 7 on the role of the donors, Chapter 8 on the impact of ideology, and Chapter 9 on institutional obstacles to a reform-oriented political decision-making process. Random influences such as the murder of President Sadat, the collapse of the Soviet Union eliminating Egypt's "second option", the Gulf war of 1990–91, the intricacies of the Middle East peace process and the Barcelona initiative of the European Union are analysed in Chapter 10. Chapter 11 summarises the core reasons of Egypt's privatisation impasse, and Chapter 12 draws five major conclusions and presents some other lessons learned.

Readers may wish to take shorter paths depending on their limited time budget and their particular interests. All readers should cover Chapters 3 and 11. Here aid administrators will find a comprehensive overview of the reform programme and its political background. Professionals mainly concerned with the macro- or microeconomic dimension should look at Chapters 4 or 5 respectively. Readers mainly interested in the web of political institutions, in issues of civil society and ideology may benefit from Chapters 6, 8, and 9. Scholars will find extensive references to published material in the footnotes.

It is clear that this type of research is deeply indebted to an extraordinary amount of assistance from a wide variety of individuals and institutions. A large number of Egyptian and foreign colleagues have helped the authors to grasp the political dimension of the economic reform process and its inherent parallelograms of political forces. In particular, the authors gratefully acknowledge many informative background discussions with Omar El-Shafei, Fatima Farag, Sonja Hegazy, Ahmad Kamaly, Eberhard Kienle, and Samir Shehata. James Exelby supplied most helpful support in a number of difficult research activities and the arrangement of interviews. Abdel Meguid Amer, Burghard Claus, Martin Dorschel, Andrew Dowell, Alan Eames, Norbert Eder, Christian Glosauer, Ernst Herb, Steven Joyce, Essam Montasser, and Thomas Scheben shared their longstanding experience and helped to identify additional sources of information and to establish further contacts. The authors cannot name the large number of interview partners, particularly of business executives in public and private enterprises who were willing to spend their time to answer a wide range of questions, quite often including sensitive ones. The authors' understanding of the intricacies of the political economy of the Egyptian reform process has been greatly enhanced by many of these seasoned professionals who managed to survive under consecutive economic and political regimes. Many labour leaders, academics, consultants, bankers, and administrators gave freely of their time, consented to interviews and provided valuable insights. The study could not have been carried out without their help and co-operation. Space — and sometimes confidentiality — precludes our acknowledging each one individually.

Naturally, a large number of widely diverging views and judgements were expressed during the interviews. The conclusions presented in the following chapters are exclusively those of the authors, and all errors of fact or interpretation are their own.

Last but not least, the authors wish to acknowledge the tremendous effort of compiling large amounts of publications and other background materials by Verena Dommer and Penelope Winterhager. Particular thanks go to Karin Bösche, Elfriede Gottschalk, Hendrik Schneider, and Uwe Tigör for typing innumerable excerpts and repeated drafts, and for maintaining reliable links of research communication between Cairo and Berlin over many months.



The boundaries and names shown on this map do not imply official endorsement or acceptance by the OECD.

K. Smith

Pre-reform Conditions

Historical Background

The military coup by a group of Egyptian army officers on 23 July 1952, led by Lieutenant Colonel Gamal Abdel Nasser, was supposed to open up a new era of economic well-being, social justice, human dignity and national pride for the impoverished people of the Nile valley country. Arable land, the major resource, was extremely unequally distributed until King Farouk's feudal rule had been overthrown. A majority of smallholders, tenants and landless labourers were living in an age-old system of semi-slavery, open or concealed¹. The group calling themselves Free Officers were inspired by a social and political mission, and one of their first steps was to carry out an agrarian reform, which was enthusiastically received by the people. When the West refused *inter alia* to finance the Aswan High Dam, to provide water for the large land reclamation projects in the desert in 1956, Nasser, now president, nationalised the Suez Canal as a profitable source of foreign exchange. This was followed by the military intervention of Britain, France and Israel in the canal zone, and Egypt's subsequent orientation towards the Soviet Union and major Eastern-bloc donors². In the industrial field the government opted for an inward-looking, import-substitution strategy with its inherent weaknesses.

By 1960 Egypt had turned to full state planning. It tried to promote capital-intensive industrialisation with unsatisfactory results. Banks, insurance companies and industrial plants were nationalised. Russian and Eastern European military and economic advisers helped to draw up a clumsy centralised planning system geared to import substitution, trade protection, heavy industry and an extensive military-industrial complex, which enjoyed special privileges. The growing public sector supplied jobs for those who had finished their schooling (with guaranteed employment for all university graduates) and remunerative management positions for former army officers. The public sector became an important instrument for preserving power, although with poor economic results³.

Nasser established a system of increasingly centralised presidential rule. From the 1960s, Egypt's nationalised economy lost touch with the dynamics of the world economy, which would be skilfully exploited by other newly industrialising countries, particularly in the Far East. The defeat in the 1967 war with Israel led to widespread Egyptian demoralisation. Nasser died in 1970 and was succeeded by Vice-President Anwar al-Sadat.

Egyptian politics and economics did not regain momentum until 1973. The surprise attack on Israeli positions on the east bank of the Suez Canal (occupied by Israel since 1967), the stabilisation of this partial military success by US Secretary of State Henry Kissinger's Middle East diplomacy and the regained Egyptian self-esteem enabled President Sadat to proclaim an "Open Door Policy"⁴. A turn towards economic liberalisation and a market economy, and a political reorientation towards the west and the United States in particular led to the peace treaty with Israel.

Enthusiasm for economic reform, however, faltered after the first year. A huge bureaucracy with weaknesses inherited from Ottoman times and the public sector defended their vested interests. President Sadat and a small number of reformers failed to impose their reform agenda. Sadat declined to carry out unpopular measures at home while being lionised abroad (an address in the Knesset, the Camp David accord, and a Nobel Peace Prize). Nevertheless, partial economic decontrol and the introduction of relatively free markets in some segments of the economy permitted tangible GNP growth rates⁵ until the mid-1980s. However, these achievements were accompanied by increased inequality in the distribution of income and wealth, continuing population pressure⁶, rising unemployment, and discontent, particularly among the educated youth who were no longer guaranteed automatic employment in the state bureaucracy or the public sector. The public was indignant over corruption on an unprecedented scale. A class of *nouveaux riches* emerged which exploited inconsistent reforms and remunerative niches opening up as a result of the opaque co-existence of markets and bureaucratic regulations. The new private entrepreneurs were mainly engaged in import trade financed by the inflow of foreign funds. Scandalous patterns of conspicuous consumption added to the erosion of the social consensus.

As a critical Ministry of Planning strategy paper of 1977 put it, the Open Door Policy was trying to combine eastern and western elements of economic order without adopting their respective management systems: capitalism without market mechanisms, but with excessive luxury consumption, and socialism without effective public control. "The end result is a society lacking discipline or supervision: distribution without production, promises without obligations, freedom without responsibility⁷." Considering the macroeconomic problems and the emergence of a new class society with its inherent potential for political conflict, the authors held that "crisis is always imminent"⁸. Radical Islamic movements were on the rise, paradoxically often among the students of science and technology departments, who were outraged by widespread corruption and moral decay, and yearned for social order and cultural identity. On 6 October 1981 President Sadat was assassinated by young, radical Islamist officers during a military parade. Vice-President Hosni Mubarak, a former air force officer, became his successor.

Resources

The economic geography of Egypt is conditioned by the narrow, fertile Nile Valley and the delta between the Eastern and Libyan Deserts with a tradition of centralised water management and bureaucratic control — a “hydraulic society” (Wittfogel) — ever since Pharaonic times. The country has always been dominated by Cairo. The traditional resource base consists of irrigated land and abundant unskilled peasant labour. Long-fibre cotton has been the major cash crop since the 19th century, enjoying high international esteem for its superior quality. Other important sources of income are the Suez Canal, tourism exploiting the heritage of the ancient monuments, crude oil exports, and since the boom in the Gulf states, the remittances of up to four million Egyptian migrant workers abroad. Textile and other unsophisticated industries established by an emerging national bourgeoisie since the 1920s and the industrialisation efforts under three presidents since the revolution of 1952 have not been able to absorb the abundant Egyptian labour supply, with some 500 000 new entrants on the labour market annually. Egypt has been exporting people rather than manufactured goods and sophisticated services.

Geopolitical Considerations

After the opening of the Suez Canal in 1869 Egypt acquired vital strategic importance as a link in the passage to India, eliminating the need to circumnavigate Africa. Following the financial collapse of the Khedive administration in 1876, the Commission on the Public Debt was established, and Egyptian revenue and expenditure were placed under the supervision of British and French controllers. In 1882 Britain sent an expeditionary force to the Suez Canal, and Egypt was turned into a British protectorate until 1922.

Cairo hosted the headquarters of the Allied Forces in North Africa during World War II. Egypt was drawn into the subsequent Cold War conflict and was involved in repeated military confrontations in the Middle East (Israel, Yemen, Kuwait). Western support for Israel contributed to Egypt’s orientation towards the Soviet Union until President Sadat’s strategic shift after the 1973 war with Israel. Western and especially US strategic interests in the region and in secure oil supplies have led to closer US–Egyptian ties (Camp David Accord, anti–Iraqi coalition during the 1990–91 Gulf War, US support of Egypt’s position in western donor and creditor forums such as the IMF and Paris Club). Control of the Suez Canal and the Suez–Red Sea–Mediterranean (SUMED) oil pipeline and contiguity with Libya, Sudan, Israel, the Palestinian Gaza Strip and the Gulf states, give Egypt a unique position to claim a substantial geopolitical rent in the form of grants, concessional loans and trade concessions.

Notes

1. Lacouture and Lacouture, 1956.
2. Wippel, 1996.
3. Weiss, 1964; Waterbury, 1978.
4. Arab Republic of Egypt, Ministry of Information, 1974.
5. Average annual real growth rate of the GNP per capita during 1970-80 was 5.6 per cent; cf. *World Bank Atlas*, 1983. GNP per capita at market prices was \$250 in 1973, \$280 in 1974, \$260 in 1975, \$280 in 1976, \$340 in 1977, \$340 in 1978, \$420 in 1979 and \$500 in 1980; cf. *World Bank Atlases*, 1975–83.
6. The population's growth rate during 1970–80 was 2.4 per cent.
7. Arab Republic of Egypt, Ministry of Planning, 1977.
8. *Ibid.*

Initiation of Reform

Lagging Reforms in the 1970s and 1980s

By the mid-1960s it had become obvious that Egypt's Arab Socialism was not delivering the promised results. Major achievements in supplying inexpensive social services, which put a heavy burden on the budget, were not matched by dynamic innovations in industrialisation. The plans aimed at physical output targets rather than at increasing business efficiency, labour productivity and value added. Agricultural and industrial exports were oriented towards Soviet and eastern European markets with low quality requirements under barter agreements. As a result, managers in Egypt's public sector were not exposed to the challenges of rapid international technological change and sophisticated marketing requirements.

The unsatisfactory performance continued through the second half of the 1960s, particularly after the shock of the 1967 defeat and Israel's occupation of the Sinai. The general sense of despair only lifted after Egypt's surprise military attack of 1973 and its reorientation towards western countries since 1974. National enthusiasm and regained self-esteem were channelled into domestic political support for the change of international orientation and for the Open Door Policy (*Infitah*), which promoted liberalisation, exports, and a major role for private and foreign investment.

It turned out that the economic reform programme was poorly implemented from the beginning. Whereas the government continued to affirm its new political credo, few operational measures were adopted to put a new economic policy into practice. The political leadership was preoccupied by the major issues of foreign policy, particularly the Camp David negotiations. The domestic political elite had no experience in handling *macroeconomic* policy instruments. High-ranking civil servants were familiar with *microeconomic* intervention on the project level rather than with the indirect techniques for steering an internationally competitive market economy. The

huge state apparatus, with its proverbial lethargy and inertia, and the public sector enterprises, with their sinecures for retired military officers, were putting up effective resistance to reform.

Bilateral¹ and multilateral² donors drew up a comprehensive reform programme, but only partial steps towards liberalisation were implemented in areas where urgent changes seemed to be unavoidable and public resistance (e.g. to phasing out subsidies) would not threaten the government's stability. Restrictions on the private sector were partially lifted. Steps towards profit-oriented management practices in the public sector were hesitant and did not go far enough, mainly because of the political risks of dismissing excess employees in the overstuffed enterprises, a result of earlier guarantees of employment for all people finishing school. The most far-reaching reforms were adopted in the modern services sector (banking, trade, professional services). The core problem of population growth continued to be neglected.

In spite of attempts at stabilisation, the fiscal deficit grew, mainly as a result of rising subsidies and the deficits of the public enterprises. The partially liberalised trade regime offered opportunities for a new class of merchant entrepreneurs. They were mainly engaged in import trade and amassed spectacular profits. Another shocking phenomenon in the new speculative business environment was the rise and fall of the Islamic investment companies³ in the 1980s, which had attracted large amounts of savings from workers' remittances by promising profit sharing (interest being prohibited according to Islamic law) with returns of 18 to 34 per cent annually. The alleged dividends were mostly paid from the influx of newly attracted savings deposits. The "snowball system" collapsed after 1988 when it became clear to the larger public that investment opportunities with such exceptional returns did not exist in Egypt or abroad. By the time the Islamic investment companies were finally closed down by the government, hundreds of thousands of migrants had lost the fruits of years of hard work in the Gulf countries.

The initial boom after the proclamation of the Open Door Policy subsided by the second half of the 1980s. GNP growth fell from an average 7.5 per cent in 1975–82 to 5 per cent in 1982–87 and 1.9 per cent in 1987–89⁴. During the Gulf crisis of 1990–91 it declined to 1 per cent. The share of manufacturing in the GNP amounted to 12 per cent in 1975–82 and 5.8 per cent in 1982–87.

The Crisis of the Late 1980s

The current account deficit rose from an annual average of \$5 billion in fiscal years 1983–84 and 1986–87 to \$6.7 billion in 1987–88 and \$7.5 billion in 1988–89.

Egypt's foreign debt reached \$50 billion in 1990, with an annual debt service of \$6.6 billion and a debt-service ratio of 56 per cent⁵. Import capacity was drastically reduced. From 1987 the government was no longer able to sustain its expansionary policies as in the first half of the 1980s. Distorted macroeconomic signals had been

set. The real exchange rate of the Egyptian pound against the US dollar increased by 38 per cent from 1982 to 1985 as a result of differing rates of inflation and a rigid exchange rate regime. Non-oil exports declined with the exception of textiles and clothing. Domestic manufacturers benefited from high import duties and quantitative import restrictions. The price distortions, including negative real interest rates and low domestic energy prices, encouraged capital- and energy-intensive subsectors such as metallurgical industries, basic chemistry and transport equipment rather than investments in food processing or textiles. Comparative advantages such as the agrarian potential and the inexpensive labour force were not being exploited. Agricultural production was impeded by low administered purchase prices. Manufacturing remained dependent on imported raw materials and did not make use of export opportunities, e.g. to neighbouring Arab Gulf countries. A structural adjustment programme was undertaken in 1986 but was not fully implemented. A stand-by agreement of 1987 with the IMF failed.

During the 1980s, Egypt had not adjusted sufficiently to the negative external shocks of the decline of world market prices and the increase in international interest rates. Budget and current account deficits and increasing debts led to an unsustainable macroeconomic imbalance. Egypt was no longer able to service its foreign debt by the second half of the 1980s. Capital inflows decreased, arrears piled up, and GDP growth dropped, whereas inflation accelerated to more than 20 per cent and open unemployment rose to more than 10 per cent. A number of social indicators showed the erosion of the standard of living of the majority of people. For example, real per capita consumption of the lower income strata during the 1980s decreased by 50 per cent. Acute malnutrition rose from 2.3 to 7 per cent, and anaemia among pre-school children increased from 38 to 52 per cent⁶.

The Economic Reform and Structural Adjustment Programme of 1990

In 1990 the Egyptian government decided to embark on an economic reform and structural adjustment programme. It aimed at macroeconomic stabilisation (budget, trade balance, inflation), structural adjustment and correcting social policies, especially by targeting subsidies to those population groups which really needed them, as well as by establishing a social safety net for the most vulnerable poor. A 1991 stand-by agreement with the IMF supported the macroeconomic stabilisation programme, while the World Bank approved a \$300 million structural adjustment loan in June 1991. The World Bank also established a Social Fund for Development financed by IDA, the European Union and various bilateral donor countries.

In May 1991 the Egyptian government entered into an 18-month IMF stand-by agreement amounting to 234.4 million SDRs (34.6 per cent of quota). The IMF support was conditional on the World Bank's judgement that the structural adjustment programme was being implemented satisfactorily.

The Paris Club granted debt relief of 50 per cent in May 1991 after Egypt's participation in the anti-Saddam Hussein coalition during the 1990–91 Gulf War. This debt relief was also linked to the Egyptian government's reform performance under IMF arrangements and was provided in three phases. The first phase provided a 15 per cent reduction of the present value of the debt service and was implemented in July 1991. The second phase, also 15 per cent of the present value of debt service, was to be implemented by December 1992, and the third phase with a further reduction of the present value of debt service by 20 per cent was scheduled for September 1993.

The economic reform and structural adjustment programme took a comprehensive approach towards Egypt's unsustainable macroeconomic situation, the dramatic changes in the international economic environment after the collapse of the Soviet Union and a worldwide tendency towards market-friendly regimes. The targets were ambitious, although it was clear from the beginning that increasing social tensions in Egypt and internal security problems, i.e. terrorism by Islamic fundamentalist groups, would continue to set limits to effective and forceful implementation. A cautious approach to reform had already emerged during the 15 years of President Sadat's Open Door Policy before President Mubarak had taken office in 1981. A general pattern emerged in which verbal support would be given to comprehensive reform, but implementation would be hesitant because of unacceptable social costs for the lower income groups⁷.

President Mubarak's main concern was the maintenance of political stability, a vital interest of the Egyptian political establishment, which was shared by foreign policy makers in the United States, the European Union and the Arab world, but it was also obvious that the international donor community would be unable to supply ever-increasing aid funds to a country whose population will approach 70 million people by the turn of the century and which has practically no international competitiveness in its manufacturing and service sectors, and a very limited traditional export potential to pay for rising food imports. Egypt is the world's second largest importer of wheat, accounting for one fifth of its total imports. Its major suppliers are the United States and France. Finally, Egypt can no longer rely on alternative donors since the collapse of the Socialist bloc.

Hence, at least initially because of a very limited traditional export potential, Egypt had no choice but to tackle all major components of an unavoidable reform process:

- Macroeconomic stabilisation in view of inflation, current account and budget deficits, restoration of creditworthiness, and the establishment of a macroeconomic policy framework conducive to efficient and competitive business activities.
- Restructuring and privatisation of public enterprises, reform of financial relationships between public enterprises, the banking system and the Egyptian government; elimination of the soft budget constraint; full managerial autonomy; and the liquidation of unviable public enterprises.

- Domestic price liberalisation and removal of distortions: decontrol of prices in the public and private agricultural and manufacturing sectors within three years. Oil, gasoline and kerosene prices were to be gradually increased to international levels, and transport and electricity tariffs to their long-term marginal costs.
- Foreign trade liberalisation, promotion of import competition and international competitiveness of exports through the removal of government-imposed distortions in the incentive system. Most non-tariff barriers on imports and exports were to be phased out within two years. The high customs tariffs were to be reduced and restrictions on exports were to be eliminated.
- Private sector reform was geared to promote competition, to enable easier market entry and exit, and factor mobility for both capital and labour. Many investment and production controls were to be abolished, government monopolies were to be dismantled and private sector discrimination in the purchase of inputs from public sector companies was to be phased out.
- The Social Fund for Development was to ease the social consequences of the reform process, particularly for the surplus employees in the public enterprises to be laid off during the reform process (employment programmes, retraining schemes, loans for the establishment of small enterprises etc.)⁸.
- Whereas the IMF took care of the macroeconomic elements of monetary, foreign exchange, and fiscal and tax policies including income, stamp and value added taxes, the World Bank supported and monitored price and trade liberalisation, public investment, public enterprise reform and privatisation, regulatory reforms, financial sector reform, and the strengthening of the social safety net.

Notes

1. Cf. Möller, Billerbeck, Heimpel, Hillebrand, Taake and Weiss, 1980.
2. Waterbury, 1978.
3. Wippel, 1994.
4. *World Bank Atlas*, 1990.
5. Semich, 1990.
6. Cf. World Bank, 1991.
7. Posusney, 1996.
8. Elsaied, 1995; Weiss, 1992*b*.

The Missing Dynamics of Reform

Overview

It was clear from the beginning that the government's room for manoeuvre was limited in view of the vested interests of the state bureaucracy, of the public companies and the government-controlled labour unions¹. Even private entrepreneurs have not been fully committed to reform since they could take advantage of protection from international competition, closed insider networks and clientele, comfortable market niches, and benefits from foreign aid flows.

From the 1952 revolution to the collapse of the Soviet Union, Egypt's unique geopolitical position enabled the ruling elite (mainly recruited from higher army ranks, the civil service and professional groups such as engineers and lawyers) to play off one donor against another and to capture a geopolitical rent. There was a lack of long-term strategic outlook translated into operational concepts. Egyptian capabilities for formulating and implementing policy have been relatively undeveloped. In policy recommendations to President Sadat, for example, a German economic advisory mission, headed by former Finance Minister Möller, stressed that "development requires, firstly, a well-functioning, performance-oriented development administration which is able to translate political goals into well-formulated policies, sectoral programmes and projects. Development requires, secondly, consistency of planning and financing, i.e. the incorporation of plan targets in the budget structure... A crucial task is the improvement of the decision-making structure"². The mission stated that "a stronger development commitment on the part of Egypt, improved planning and organisational efficiency of the administration, and the formulation of medium-term guidelines for development, would be viewed by the donor countries as a sign that the Egyptian Government is raising its own contribution"³.

A major bottleneck in the political economy of reform since President Sadat's announcement of the Open Door Policy in 1974 had been the difficulty in mobilising the power of the political leadership for essential strategic economic policy decisions,

translating the decisions into operational macro and sector policies, and linking policy directives with their implementation via short and effective lines of communication, control, feedback and monitoring. Hence, the Möller mission noticed that “a surprising fact by international standards is the little use made of the budget for the formulation and implementation of policies... The budget structure enforces the concretisation and articulation of the political process, necessitates the clarification of intended policies through budget item specification, provides the funds for their implementation... This process only occurs partially in the Egyptian administration”⁴.

It is well known that decisions are often a “scarce commodity” in government systems, all the more so in heavily centralised administrations with a notorious information overload at the top level. “The urgent drives out the important” (Kissinger). As a result, pending economic policy issues are not being resolved if other policy issues concerning foreign policy, internal security, etc. demand time and attention. *Ad hoc* or selective stop-and-go measures tend to respond to short-term considerations, e.g. appeasing domestic and foreign pressures or meeting donor conditionalities.

After the economic reform and structural adjustment programme (SAP) was undertaken, in 1993 the World Bank felt the need to establish a special Structural Adjustment Monitoring Programme within the Egyptian cabinet structure in order to assist and monitor the reform performance⁵.

On the other hand, donor pressure had to take into account Egypt’s entitlement to a strategic rent based on its vital role in the Middle East peace process and related issues.

As a result, Egyptian policy makers and the international donor community both pursued reform cautiously. The bilateral donors tried to avoid the diplomatic costs of a direct confrontation and preferred to rally behind the World Bank and the IMF. The multilateral organisations were, in turn, not free from institutional self-interest. As a result, the reform objectives were subject to substantial constraints, both on the donor and the recipient sides, and the outcome was far from satisfactory.

Macroeconomic Distortions

In spite of the liberalisation measures during President Sadat’s Open Door Policy, Egypt’s economy was still constrained by a tight network of controls at the end of the 1980s. Customs duties for a number of products were more than 100 per cent, and large areas of domestic production were fully protected by quantitative import barriers. The exchange rate regime had two different rates: one for government trade in “strategic” goods and one for other items of international trade. The domestic market was subject to a strict system of price controls.

Subsidies on basic necessities, e.g. bread, edible oil, kerosene for household cooking, electricity, bus and rail transport, etc., brought their prices far below international production costs or domestic long-term marginal costs of production. Subsidies were not targeted to the really needy. Higher income groups shared the benefits of subsidised basic necessities and enjoyed additional benefits such as low gasoline prices for their automobiles.

In the sphere of production, most prices for inputs and outputs were regulated. Agriculture benefited from low prices for seeds, fertilisers, and pesticides. On the other hand, farmers were ordered by the state to plant specified percentages of their land with “strategic goods”, such as cotton, sugar cane, wheat, etc., to be delivered to public purchasers at prices far below world market levels. Other crops would have yielded higher net returns to the farmers.

Industrial producers were caught in a system of regulated input and output prices. For example, fertilisers had to be delivered at low prices to farmers, leading to losses by the fertiliser enterprises, irrespective of the efficiency of their manufacturing operations. Such losses were covered by the public budget. Administered prices for other “strategic” goods such as steel or cement used at the beginning of many inter-industry linkages distorted the accounting system of the whole economy and failed to supply adequate signals for an efficient allocation of resources.

The Egyptian economy’s isolation from international production and consumption prices led to a loss of awareness among the decision makers about the country’s real comparative advantages and disadvantages. During periods of rapid price fluctuations in the international crude oil markets Egyptian administrators changed the prices of their oil exports too slowly and thus missed opportunities for substantial windfall gains. High-quality long-staple cotton could have reaped high returns in the world market. Instead it was distributed to domestic public spinning and weaving companies at much lower prices to produce low-quality grey cloth exported under barter agreements to eastern European countries in exchange for low-quality machinery or military equipment. Egyptian decision makers in government and industry were largely unaware of the overall developmental impact of their activities in a distorted system setting wrong signals.

Therefore, the reform efforts had to focus on a liberalisation of the domestic price system, and of the foreign trade and exchange rate regimes; the reform of public finance; and a thorough reform of the supply side, i.e. the public enterprise sector.

Sequencing of Macroeconomic Reform Measures

Lack of Political Will in the 1970s

Since the October 1974 Working Paper which initiated the Open Door Policy⁶, hesitant reform steps had been taken within the limits set by risks of social revolt and political destabilisation. The government had learned a lesson when in January 1977 there were mass street protests against the cuts of bread subsidies requested by the IMF. This had led to a price increase of the local bread loaf from one to two piasters⁷. Order was restored by a withdrawal of the reform measure, and bread then became so cheap that it was used to feed livestock.

In spite of all sorts of subsidies, the standard of living for the low income groups deteriorated. At the same time, the Egyptian people experienced the emergence of a class of *nouveaux riches* engaged in import trade, real estate speculation and various forms of arbitrage favoured by a transitional regulatory system between state control and free markets that offered many remunerative opportunities. Partial and inconsistent reforms and the collapse of the previous patterns of social control opened up (partly illegal) niches for amassing wealth. New dimensions of corruption and conspicuous consumption added to social unrest and the rise of political dissatisfaction.

When the “bread riots” of 1977 flared up in Cairo, Western donors who had stopped their aid transfers a year before because tangible Egyptian reform measures were not forthcoming, rushed in with new assistance. These events taught lessons to the donors and the Egyptian government. The latter recognised that the potential for chaos in Egypt could be considered as an asset. All stakeholders learned that due to its unique geographical and political position Egypt was entitled to a geopolitical rent.

The Camp David accord created a special relationship with the United States. The price Egypt paid was diplomatic recognition of Israel. Moreover, the European Union and its member states were becoming increasingly sensitive to events at the southern edge of the Mediterranean, especially in Algeria, and were concerned about oil supplies, rising immigration into the EU, and security considerations. Hence they were willing to contribute their share to Egypt’s political stability.

The rising Islamist movement in Egypt reflected a growing sense of social frustration. Tight political control and restrictions on civil rights limited channels of political expression. President Sadat moved cautiously, and even tried to use the Islamist movement against the left in the domestic power equation. The reform agenda ranked below the primary concern of preserving power. The World Bank, IMF, EU and bilateral donors tried to accelerate the pace of reforms, but were faced with a government which lacked the political will to take large risks.

In addition, the Egyptian administration was unable to design a comprehensive and consistent reform package. Sectoral policies lacked co-ordination and cohesion. Links between global goals and sectoral targets, institutional reform measures, project implementation and budgetary impact were often absent⁸. In May 1977 President Sadat called for an “administrative revolution” that was never carried out.

The 1978–82 Five–Year Plan drew a stark picture of the Open Door Policy: inflation, balance–of–payments problems, insufficient investment and labour productivity, high population growth, price distortions, the burden of subsidies, the emergence of a new class society, inefficient administration and the dilemma of the public sector⁹. The authors held that the administrative apparatus was out of touch with reality and was absorbed with the satisfaction of short–term needs instead of envisaging long–term solutions. They called for a new “social contract between the people and the government”¹⁰ as the government’s political base was contracting.

Economic reform was not on top of the government’s political agenda. It was absorbed by the great issues of foreign policy and stabilisation of the domestic balance of power. In 1981, before the government fully faced the issues of economic reform, President Sadat was assassinated by Islamic terrorists.

Patchwork Macroeconomic Stabilisation in the 1980s — Conflicting Legacies

Former air force officer Hosni Mubarak who succeeded Sadat as president in 1981 was the heir to a conflicting legacy¹¹. From President Nasser’s era there was populism, the public sector and an inward–looking economy oriented towards import substitution. Furthermore, a new private business community geared more to the import trade and to speculation, than to internationally competitive industrial production, had arisen during the era of his immediate predecessor. Growing disparities in income distribution and wealth, and the re–establishment of a class society led to increasing social tensions and erosion of the social consensus.

The donors kept pressing for macroeconomic stabilisation and structural adjustment. The new government implemented a number of reforms related to the budget deficit such as cuts in subsidies and tax reforms, the unification of the exchange rate regime, a partial relaxation of price controls, etc.

Since the overall economic performance during the first half of the 1980s had been fairly satisfactory and a major crisis could be avoided, the government did not seriously embark on a comprehensive reform programme. The piecemeal measures were not parts of a coherent approach and were not implemented with determination. There were repeated conflicts with the World Bank and the IMF. A stabilisation and structural adjustment programme undertaken in 1986 was not implemented vigorously enough, and a programme with the IMF lapsed in 1987 because of Egypt’s failure to meet its targets for reducing the fiscal deficit and unifying its exchange rates¹². Egypt succeeded in mobilising its strategic rent and postponed moves towards a painful overhaul of its economy. There was no tangible progress in privatising the public

sector. No serious steps were initiated to lay the foundations of an internationally competitive productive apparatus in manufacturing and sophisticated services able to support a rising population. Food imports accounted for 70 per cent of Egypt's domestic consumption, largely financed by aid funds rather than by the country's own export earnings.

The economic situation became unsustainable during the second half of the 1980s. GNP growth fell from 7.5 per cent in the 1975–82 period to 1.9 per cent in the 1987–89 period. This drop and continuing population growth of about 2.4 per cent per annum led to a fall in per capita income. A number of economic indicators also deteriorated. The current account deficit amounted to some \$5 billion annually in 1983–84 and 1986–87. It rose to \$7.5 billion in 1988–89. By 1990 the foreign debt amounted to \$50 billion, and the annual debt service reached \$6.6 billion with a debt–service ratio of 56 per cent. Inflation accelerated to more than 20 per cent in 1988–90, and open unemployment increased to more than 10 per cent. After various half–hearted reform steps, the old, unfulfilled agenda was still topical: adjustment and stabilisation, a more rational exchange rate policy, more effective incentives for private investment, liberalisation of foreign trade (including export barriers), deregulation of the price system, public sector reform, less public spending and reduction of the money supply.

It is clear that Egypt's foremost task is building technological and innovative productive capacity. The educational system needs a complete overhaul, including its basic values, before Egypt can become internationally competitive, especially in view of the growing number of Third World players. Otherwise the rising population cannot be sustained. The Western and Arab donor community will not permanently subsidise Egypt.

Long–term perspectives, however, rank second behind short–term considerations of preserving power. As long as the majority of the Egyptian electorate earns an income from the civil service or public sector employment, and benefits from low cost social services, basic reforms will not gain general acceptance. Repeatedly, the Egyptian government has deliberately adopted reforms after the closure of parliamentary sessions to avoid public debate. The Egyptian government and the donors both have reservations about moving faster towards democratisation. Both prefer not to put the precarious political status quo at risk. Basically, the donor governments accept Egypt's arguments for restraining the pace of reforms. Repeatedly, the US government has used its weight in the IMF executive board in favour of easier terms for Egypt. The EU countries and the Commission of the European Communities have been careful not to cause strains in diplomatic relations with Egypt. President Mubarak has been a regular visitor to Germany. Britain, France and Italy have special interests in the area. Spain considers that its historical heritage of eight centuries of Arab occupation of the Iberian peninsula makes it a privileged mediator, and it hosted the Madrid Middle East peace conference of 1989 and the Barcelona conference of November 1995. The latter initiated the EU concept of a Euro–Mediterranean Free Trade Zone by the year 2010.

The Commission and the European governments avoid more vigorous pressure for reform because of their short-term interest in the political survival of the Egyptian government. On the other hand, the donors are aware that the slow pace of reforms brings Egypt closer to incalculable future risks.

The New Reform Programme since 1990

By 1990 the overall situation had become unsustainable. Budget and current account deficits had piled up, and Egypt was no longer able to service its debts. The payments crisis led to the adoption of the economic reform and structural adjustment programme supported by a World Bank adjustment loan and an IMF stand-by agreement, as mentioned.

Strict Conditionality

In light of the Egyptian government's hesitancy towards reform and the failure of the 1987 stand-by agreement with the IMF, the donor community insisted on a strict conditionality, linking the World Bank structural adjustment loan and the IMF stand-by agreement of 1991 with debt relief by the Paris Club.

For the IMF stabilisation programme, the following indicators were chosen:

- fiscal deficit in percentage of GDP,
- the rate of monetary expansion,
- the increase of credit to the public sector,
- the size of public investment as a share of GDP.

Progress in the structural adjustment programme of the World Bank was measured in terms of:

- trade reform: by domestic production covered by import bans, levels of maximum and minimum import tariffs, removal of tariff preferences, reduction of export bans and quotas, and elimination of prior approvals;
- public enterprise reform and privatisation: by the amount of asset value brought to the point of sale and the actually completed sales;
- private sector development: by the increase in the share of private sector companies in trading, cement and fertilisers (previously strictly controlled "strategic goods"),
- price liberalisation: by the adjustment of prices of petroleum products to international levels, the increase of cotton prices paid to the farmers to world market levels, the rise of electricity prices to long-run marginal costs, the

reduction of budget subsidies for fertilisers and pesticides, and the increase of railway rates to attain the targeted improvement in the Egyptian National Railways' revenue coverage ratio.

Major Macroeconomic Results

The implementation of the macroeconomic stabilisation programme was satisfactory. The fiscal deficit was reduced from 20 per cent of the GDP in FY 1990–91 to 1.3 per cent in FY 1994–95 (Table 10) and less than 1 per cent in 1997. The rate of growth of broad money supply (M2) declined from 15 per cent in FY 1991–92 to about 10 per cent in FY 1995–96. The foreign exchange market was unified ahead of schedule and restrictions were eliminated. A flexible exchange rate system was adopted.

Inflation slowed from over 21 per cent in FY 1988–89 and 1991–92 to about 7 per cent in FY 1995–96 (Table 10) and 6 per cent in 1997. Interest rates were liberalised at the beginning of the reform, and declined from about 20 per cent on 90-day Treasury bills to about 11 per cent in FY 1995–96. However, as a result of high interest rates set by the Egyptian Central Bank for its Treasury bonds, the Egyptian pound remained stable at LE 3.38 to 3.40 per US dollar (Table 2). This was meant to attract, as it did successfully, substantial inflows of foreign capital, particularly from Egyptian migrant workers and Arab investors. Real interest rates turned positive and adjusted to real international rates by FY 1994–95.

The current account of the balance of payments, including official transfers, improved from a deficit of \$2.6 billion in FY 1990–91 to surpluses of \$3.7 billion in FY 1991–92 and \$2.2 billion in FY 1992–93, and then declined to a \$200 million surplus in FY 1995–96. Major factors contributing to the improvement were the debt relief granted by the Paris Club and bilateral creditors in 1991 following the Gulf War, and increased foreign exchange earnings from tourism, workers' remittances, and Suez Canal tolls. The international reserves held by the Central Bank increased to \$18 billion, equivalent to 17 months of import requirements.

As the foreign debt to GDP ratio declined from over 150 per cent before the Gulf War to about 49 per cent in FY 1995–96, Egypt's creditworthiness improved substantially. The debt service ratio declined from 49 per cent in FY 1988–89 and 23 per cent in FY 1990–91 to 13 per cent in FY 1995–96 (Table 8), mainly as a result of international debt relief and debt restructuring.

Foreign Trade

Before the economic reform and structural adjustment programme some 37 per cent of trade in agricultural and manufactured goods was protected by import bans in accordance with Egypt's import-substitution policy. The range of tariffs on imports was 5 to 100 per cent (200 per cent for luxury items) with many exceptions. By February 1993 the coverage of the import bans had been reduced to 10 per cent, meeting the

conditionality of the structural adjustment loan, down from 23 per cent of all traded goods and services in 1991. The range of tariffs was reduced to 5–50 per cent. Egyptian military imports and various other items continued to be exempted from tariffs.

The number of tariff preferences was reduced as well as the list of items which needed prior approval of the Egyptian administration. Export bans and quotas were eliminated. The foreign exchange quota system for public enterprises and the requirement of prior deposits for imports were also abolished. In some domains where there was no major domestic political opposition the Egyptian government went beyond the programme's original targets.

At the end of the first Structural Adjustment Monitoring Programme¹³ the Egyptian government had eliminated almost all non-tariff barriers. The non-tariff barriers on textile imports will be phased out in accordance with the Uruguay Round Agreement. The quality control system on imports became more transparent and less discriminatory. Duty drawback and temporary admission procedures for exports were streamlined.

Private Sector Development

In spite of Egypt's Open Door Policy since 1974, the private sector continued to struggle with major obstacles in the regulatory framework; numerous restrictions on investment and production, and on access to physical and financial assets when competing with public enterprises; and from being in a weak position with respect to state monopolies. Under the economic reform and structural adjustment programme, the government was committed to changing this business environment. Nevertheless, many obstacles for the private sector persisted, particularly in manufacturing.

The government liberalised the prices on cement and fertilisers, removed quantity restrictions on private sector sales with regard to special groups of customers and regional distribution. Previous restrictions on private sector investment in many fields were abolished, as well as restrictions on access to bank credit and foreign exchange. Previous investment licensing procedures of the General Organisation for Industrialisation were reduced to a function of registration except for a reduced negative list of products.

Social Conditions

The situation of the poor strata of the population is deteriorating as measured by economic and social indicators, such as basic health¹⁴. The reform of the social safety net is an essential part of the reform package. Instead of untargeted subsidies of foodstuffs, infrastructure (rail travel, electricity, etc.) and social services, emphasis should be on providing income, employment opportunities and access to social services for the most vulnerable groups and those who are particularly exposed to the negative effects of the reform programme.

The World Bank and the Egyptian government established a Social Fund for Development (SFD) of \$613 million. From that fund, \$221 million was earmarked for programmes such as small, labour-intensive public works with local contractors in regions with high unemployment, for example for the repair of irrigation canals, rural road construction, rehabilitation of schools and health stations, the planting of trees, cleaning of urban slums and historical districts in the old city of Cairo. Furthermore, loan and training schemes for small and micro enterprises were to receive \$77 million; retraining and job replacement programmes, \$51 million; and improving implementation of the SFD (project identification, monitoring, evaluation), \$5 million¹⁵.

Disputes between donors and the Egyptian government on management, appointments, adequate qualifications and sluggish disbursements led to substantial delays in starting the operations. By November 1993 the SFD had committed \$184 million and had disbursed \$72 million. An additional \$343 million was in the project pipeline.

A 1993 mid-term review of the SFD came to the conclusion that progress was broadly satisfactory, except for the labour adjustment programme. In this field the SFD started to promote technical and financial assistance services, but only two enterprises were being supported by 1993, and three more were about to receive SFD funds for a total of about 13 000 workers.

Obstacles to Implementation

A crucial aspect of implementation was the conditionality which linked debt relief by the Paris Club with Egypt's performance in reforms. Weaknesses remained at the level of formulating and implementing policy. It took the World Bank considerable time to set up a monitoring unit for the structural adjustment loan as a technical secretariat to the Council of Ministers to co-ordinate the reform programme across sectors. The effective start of the structural adjustment loan was delayed by eight months after approval by the board of the World Bank because of the Egyptian government's reluctance to increase cotton prices. This and other institutional problems led to a delay in releasing the second tranche of the structural adjustment loan. In March 1993 the World Bank finally considered Egypt's implementation as satisfactory. Hence, the Paris Club agreed to put the second phase of its debt relief programme into effect in October 1993.

During the next two years Egypt's reform performance slowed down due to the improving foreign exchange position which prevented an immediate balance-of-payments crisis, though without creating the basis for an internationally competitive economy. Islamic fundamentalist terrorism absorbed the attention of the Egyptian leadership. At the time, several hundred million dollars in structural adjustment and stand-by loans did not provide the incentive to speed up the reforms. The only leverage left to the donor community was the third phase of the Paris Club debt relief. After

considerable delay, Egypt finally received the debt relief of \$4 billion near the end of 1996, after renewed commitment to reform had been demonstrated since the beginning of 1996 under a new prime minister, Kamal al-Ghazouli.

Meanwhile, falling real per capita incomes and rising unemployment aggravated the social and political crisis. Terrorist activities led to tightened security measures and further restrictions on civil rights.

The deepening of trade reform met increasing opposition among private and public enterprises alike, which felt threatened by the exposure to international competition.

Credibility Gap

Credibility is the key to successful reform programmes¹⁶. The ambiguous commitment to reform created a credibility gap. In its Letter of Development Policy of September 1993, the Egyptian government underlined that “the main thrust of these reforms would be in those areas that would elicit a quick and sustainable supply-side response from the private sector in order to accelerate economic growth and the pace of employment creation”¹⁷. “The government’s vision of the economic future of Egypt is a rapidly growing private sector operating in a competitive and stable environment”¹⁸. As stated during the Consultative Group Meeting of 1994, “the ultimate risk of the program would be if the private sector fails to respond strongly and rapidly to the structural reform and the more stable macroeconomic environment”¹⁹.

Thus far, domestic and foreign private investors have been reticent²⁰. The results of the reforms have done little to create the foundations of a viable, internationally competitive economy. In spite of various improvements of the overall macroeconomic regulatory system²¹, the incentive framework remains insufficient to stimulate a private investment boom. Very few industrial subsectors have reached international competitiveness. Human capital development is still being neglected in the fields of primary, secondary and tertiary education. The prevailing domestic climate hardly encourages intellectual curiosity, creativity or criticism.

Summary

The multilateral donors held that the pace of reform had been sporadic and generally slower than envisaged. However, important progress had been made towards fiscal adjustment. Inflation came down to 6 per cent, and a more decentralised, market-oriented and open economy began to emerge. Real GDP growth continuously declined from 5.1 per cent in 1987–88 to 1.9 per cent in 1992. It recovered to 4.9 per cent in 1996 (Table 3)²² and 5 per cent in 1997.

After considerable conflict over the Egyptian reform performance, the Paris Club finally put the third phase of its debt relief into effect in October 1996. After the elections of November 1995, President Mubarak reshuffled the cabinet and made a renewed commitment to reform. Kamal al-Ghazouli, the new prime minister, announced new initiatives to speed up the process of privatisation.

Under pressure from the IMF executive board, the staff drew back from its demand for a devaluation of the Egyptian pound through a reduction of interest rates on Central Bank Treasury bills, and shifted its focus to a faster pace for structural reforms²³. A new two-year stand-by loan through September 1998 was to replace the last Extended Fund Facility that had expired in September 1996. Emphasis was on broadening and stepping up privatisation, deregulation, trade liberalisation, fiscal and financial sector reform, and energy price adjustment, in a bid to stimulate outward-oriented growth led by the private sector.

Key structural weaknesses persist, however, somewhat obscured by a comfortable foreign exchange position. The latter was due to the Central Bank's attractive interest rate, and not to a competitive export performance. Egypt is far from being ready to meet the new challenges and opportunities arising from the Middle East peace process, the Uruguay Round agreements, and the Euro-Mediterranean Free Trade Zone, with countries such as Morocco, Tunisia, Malta, Cyprus or Turkey being much more internationally competitive.

Notes

1. Posusney, 1996.
2. Cf. Möller, Billerbeck, Heimpel, Hillebrand, Taake and Weiss, 1980.
3. *Ibid.*
4. *Ibid.*
5. Established as a technical secretariat.
6. Arab Republic of Egypt, 1974.
7. 1 LE = 100 piasters = approximately 1 US dollar at the time.
8. Weiss, 1979.
9. Arab Republic of Egypt, Ministry of Planning, 1977.
10. *Ibid.*
11. Hinnebusch, 1993.
12. Posusney, 1996.
13. The \$300 million World Bank structural adjustment loan had been approved in 1991 and complemented by the IMF stand-by loan. The first tranche of \$150 million was disbursed. In view of an improved foreign reserves position, Egypt had no need for the remaining \$150 million of the second tranche and requested that the second tranche be cancelled. As a follow-up to the structural adjustment loan, Egypt and the World Bank established a Structural Adjustment Monitoring Programme (SAMP) which complemented the IMF's Extended Fund Facility (EFF). It focused on trade and financial sector liberalisation and privatisation. The World Bank's formal review of progress relative to SAMP targets of December 1993 indicated that Egypt's performance was largely satisfactory.
14. Cf. World Bank, 1993.
15. Weiss, 1992*b*. Approved projects were distributed as follows: 26 per cent for public works, 54 per cent for an enterprise development programme, 17 per cent for community development, 2.1 per cent for labour adjustment, and 1.3 per cent for institutional development.
16. Hiemenz and Funke, 1994.

17. Government of Egypt, Letter of Development Policy, 1993.
18. *Ibid.*
19. Consultative Group Meeting, Paris, 25–26 January, 1994.
20. World Bank, 1994.
21. Handoussa, 1995.
22. Lower figures are estimated by other international sources. The Egyptian authors of the *Human Development Report* for Egypt attached to the Institute of National Planning, previously the think tank for socialist planning, state: “A major concern is related to the accuracy and reliability of data. Some claim that most data are accepted at face value without scrutiny, revision, or comparison with data available from other sources. This concern relates mainly to data on economic growth, education and unemployment... The basic concern is that there are enormous problems in even the most basic indicators in Egypt. The Institute of National Planning (INP) team is working behind the scenes to improve the situation, but the basic issue is that serious conceptual, data collection and transparency problems remain in basic national data, such as the rate of economic growth, the rate of inflation, the level of unemployment, basic literacy rates, and so forth.” Cf. Institute of National Planning, 1995.
23. Economist Intelligence Unit, 1996.

Chapter 4

Chronology of the Politics of Macroeconomic Reform

1990–91: Pressure for Reform and International Support

The unsustainable macroeconomic situation in 1990 due to budget and current account deficits and the burden of foreign debt made comprehensive reform necessary, but a coherent decision making process geared to consistent objectives, a realistic assessment of constraints, and institutions for effective implementation were all lacking. High officials, including the president, prime minister and some cabinet members sent contradictory signals to calm the apprehensions of the Egyptian people while trying to ease the negotiations with the World Bank and the IMF¹.

On 3 January 1990 Prime Minister Atif Sidqi still denied that the government envisaged any new price increases, but on 30 January the cabinet discussed an increase in taxes, levies and prices for public services to reduce the budget deficit². At the same time, progress was being made in the negotiations with the World Bank on a structural adjustment loan in February 1990.

The negotiations with the IMF were difficult. On 12 January President Mubarak declared that no agreement with the IMF had been reached “because Egypt refused to impose new burdens on the poor”³.

After a meeting between Egyptian officials and IMF representatives on 19 January, President Mubarak emphasised five major topics of disagreement with the Fund, in particular rejecting a devaluation of the Egyptian pound and a reduction of the domestic interest rate. He told the press that the reforms could not be carried out in a period of less than five years, and that he appreciated the “positive attitude of the US government”, supporting Egypt in its negotiations with the IMF. The United States said on 27 January that in spite of moves in Congress to cut foreign assistance Egypt would receive some \$2.1 billion of foreign assistance “because of Egypt’s vital role in the Middle East”⁴.

The IMF kept pressing for a floating exchange rate, cuts in subsidies, privatisation of the public sector, and a reform of the wage policy in exchange for rescheduling of \$12 billion of debt and \$3 billion of new loans⁵.

In March 1990 President Bush confirmed that the United States was prepared to forgive Egypt's debts. Thus right from the beginning of the economic reform and structural adjustment programme, Egypt could count on firm US support, motivated by strategic considerations, with some \$2 billion of military assistance and \$850 million of development aid per year⁶. Foreign Minister Boutros-Ghali, referring to US support during a Paris Club meeting on debt relief, observed that "Egypt has been able to benefit from the international weight of the United States. This also constitutes a clear recognition of Egypt's importance and its regional credibility"⁷.

The Egyptian side could assume that the US government had a predominant interest in Egypt's political stability for the sake of the Middle East peace process, and would support Egypt in its dealings with the demands of the international donor organisations⁸.

First Hesitant Steps towards Reform

On 10 March 1990, an agreement with the World Bank was signed. Supply-side structural adjustment was on top of the agenda. Implementation began in the tourism sector. Tourism Minister Fouad Sultan was a fervent advocate of privatisation, and attractive and profitable properties were available for sale to the Egyptian and foreign investors without touching issues such as "strategic sectors" or the dismissal of large numbers of employees. In April 1990 the hotels Meridien and El Nil were the first to be offered for sale⁹. The Hotel Ramses in Abu Simbel was leased to a private company. There was also no political opposition when in September 1990 the minister of agriculture offered 27 000 contracts covering some 37 000 feddans¹⁰ of agrarian reform land owned by the state to the actual tenants¹¹. In manufacturing the sale of company shares at reduced prices to their respective employees was being considered.

Prime Minister Atif Sidqi delineated the basics of public sector reform: sales of hotel companies, of residential buildings, of state land, of government shares in mixed (public-private) enterprises, of public enterprises (usually small and medium sized) belonging to the Governorates¹², and selling equity in public companies by inviting participation by private investors¹³.

Even within the cabinet there was no consensus on the general approach¹⁴. Advocates of privatisation were confronted by adversaries like the minister of industry who bluntly denied in public that there were any preparations for the sale of public sector enterprises¹⁵.

On 1 May 1990 President Mubarak proclaimed his "Programme of 1 000 Days" in the People's Assembly. To avoid political opposition, the planned reforms have never been published in their entirety. In his speech the President referred to the IMF

as the “International Misery Fund”, and promised a healthy recovery, but the top Egyptian policy makers were aware that Egypt had no choice but to accept donor conditionality¹⁶. In public the Egyptian side expressed scepticism about the reforms, being aware of the unpopularity of a programme which would alter existing patterns of consumption and production, job security, public sector careers, and paths to status and prestige. As late as May 1990 the minister of planning announced a large new investment programme of LE 10 billion for the public sector for 1990–91.

The IMF insisted on basic stabilisation measures in monetary and budgetary policies and price liberalisation. Electricity, for example, then cost 34 per cent of average international prices. President Mubarak admitted the necessity of rationalising consumption since subsidies for basic necessities amounted to LE 3 billion annually.

The first steps towards implementation were taken without public announcement. Prices for pharmaceuticals, meat and textiles rose by 20 to 100 per cent. The price for a package of tobacco was raised from 15 to 20 piasters¹⁷. On 1 July 1990 the Egyptian pound was devalued from LE 1.10 to LE 2 against the US dollar¹⁸.

The IMF demanded the total elimination of subsidies within four months, higher taxes and interest rates in addition to the measures already adopted which had led to a rise of prices of various basic necessities of 40 to 100 per cent. After political unrest in various towns, the minister of the interior created special police forces to control prices in the local markets¹⁹. The price increases seriously affected the standard of living of the poorest people²⁰.

Blocked Channels of Political Expression

The reform process was impeded by a political system that did not fully allow for free expression of opinions, eventually paving the way for a viable compromise. The fragility of civil society increased the risk of riots, revolts and terrorism. There was a degree of domestic pluralism, but it has not been allowed to pose a serious challenge to presidential power²¹. The political participation of the people is still limited. The state of emergency since the 1967 war against Israel has never been lifted.

Repeated strikes in factories over the years — as in the Helwan Iron and Steel Works — were met by a drastic reaction of the security forces. Clashes with Islamists have escalated since the second half of the 1980s. Unemployment among school leavers is on the rise, adding to the general sense of frustration.

The restraints on political expression led elements of the authorised opposition (Wafd, Labour Party, Muslim Brotherhood, Liberals) to boycott the election to the People’s Assembly in November–December 1990, complaining about unfair practices and unequal access to the media. The National Democratic Party was credited with 79.6 per cent of the vote. An Egyptian observer complained: “Since 1952, the legislative elections have not brought any change of power, they are characterised by unanimity, interference by administrative bodies — if not the police — and the

(low) real percentage of voters which defies any mathematical logic of ‘national representativeness’²². Hence, the Egyptian government had reasons for being apprehensive of public protests and moving cautiously on the reforms.

1991: Gulf War Windfall Gains

The Gulf War of 1990–91 and its aftermath provided unexpected debt relief. Despite conflicting views in Egyptian public opinion, the government firmly sided with the anti–Saddam coalition. Some 30 000 Egyptian troops took part in the defence of Kuwait and demonstrated Egypt’s position as a close Middle Eastern ally of the United States. An immediate reward was US forgiveness of Egypt’s \$7.1 billion military debt in October 1990 and US support for the Paris Club’s November 1990 decision to cut Egypt’s \$50 billion debt burden by 50 per cent²³.

Thus Egypt was relieved of immediate pressure to reform. The debt crisis which could have been conducive to serious and painful reform had been suspended²⁴. Short–term considerations of political survival again were given precedence over long–term economic viability.

Prime Minister Atif Sidqi quickly put forward Egypt’s claims for war indemnities. In his January 1991 presentation of the government programme to the People’s Assembly, he declared that Egypt had suffered a decline in foreign exchange inflows of \$8 billion resulting from losses of workers’ remittances (\$2 billion), receipts from tourism (\$1 billion), Suez Canal fees and exports (\$6 billion), which were only partly offset by a \$1 billion increase in crude oil sales. Losses of property of Egyptian migrant refugees from Iraq and Kuwait who had left their possessions behind were estimated at \$18 billion, and the costs of their reintegration into the Egyptian labour market at \$5 billion²⁵.

Privatisation and Labour Union Concerns

The prime minister also stated that every public company was to be privatised, apart from a limited number of enterprises designated as “strategic” or of “national character”. A new law (Law 203) of June 1991 shielded the public companies from direct ministerial interference. They were regrouped under several dozen holding companies whose government–appointed board members were expected to manage their portfolios according to market principles²⁶.

Moreover, Sidqi promised that there would be administrative reform in accordance with the World Bank’s doctrine: limitation of the state to activities which it could deliver efficiently and which individuals could not provide by themselves²⁷. Two bills on the reorganisation of the administration and the public sector were greeted coolly by the state–sponsored labour unions (tightly supervised by the Ministry of Labour since the Nasser era). Representing some 3 million members, their major concerns

were higher wages and pensions, job security, health and accident insurance schemes and the right to collective bargaining on wages and working conditions, and eventually the right to strike. They rejected an immediate privatisation²⁸ as “a bomb threatening social peace and stability, which will lead to serious social explosions”²⁹.

Social Issues

The prime minister said that liberalisation did not mean that the state was abandoning its social obligations, and that the protection of people with low incomes was not incompatible with economic freedom³⁰. The state would continue to subsidise basic necessities such as food, kerosene, electricity, popular textiles, pharmaceuticals, bus and railway passenger transport, and to supply inexpensive social services. Public health and education would remain free or be delivered at very low fees.

It was obvious that the envisaged reforms would lead to rising prices, unemployment and a further decline of the standard of living for the majority of the people at least during a transitional period if the state were to reduce its number of employees³¹. There would be little room for manoeuvre in implementing the reform agenda while maintaining social and political stability.

Therefore, the World Bank and the government had agreed to establish the Social Fund over a period of three years to ease the social consequences of the reform. Surprisingly, the Egyptian side was not concerned with its speedy implementation. It took almost one year before the presidential decree was signed and a director was appointed³².

Under IMF pressure prices for railway tickets were raised by 40 per cent, electrical batteries by 12 per cent, bus tickets from 10 to 25 piasters, and school fees by one LE. The Planning and Budget Commission of the People’s Assembly recommended the elimination of free secondary and university education, and of subsidies for low-cost housing³³.

On the other hand, the government was concerned with maintaining the purchasing power of the civil service and the public sector employees. Since 1987 it had paid an annual social bonus of 15 to 20 per cent of wages and in addition a seasonal bonus to compensate for inflation. The IMF agreed that government expenditure for wages, education and health should not be reduced as their real value had gone down during the past 25 years, and that the social insurance system could be extended.

Liberalisation of Credit

An essential step towards a free market economy was taken in 1990 by introducing banking secrecy to attract the savings of Egyptian migrant workers in the Gulf states and of other Egyptian expatriates. As a result, deposits in the Egyptian banking system in 1990 increased by \$1.7 billion over the previous year to \$13 billion³⁴.

All loan regulations were eliminated. Officially, public enterprises lost their privileged access to credit, although old practices were not completely eliminated. Interest rates were decontrolled. The Central Bank took on a surveillance function for the banking system, and the capital market was strengthened by a reorganisation of the stock exchange.

The Central Bank issued Treasury bills to finance the fiscal deficit in a non-inflationary way, with interest rates at some 20 per cent, also setting a signal for the money markets. They became an effective incentive for the “dedollarisation” of the Egyptian economy, and helped to support the Egyptian pound against the US dollar. The exchange rate regime was unified³⁵.

Foreign Trade Liberalisation and the Impact on Domestic Industry

Whereas credit liberalisation did not encounter opposition, the trade regime was critical for an Egyptian business community largely unprepared to face international competition. Entrepreneurs organised in the Union of Chambers of Commerce were accustomed to high tariff and non-tariff protection, and were anxious to be consulted before major decisions on the liberalisation of imports³⁶. Export firms demanded the elimination of export quotas³⁷.

The prime minister indicated the new priorities to the People’s Assembly: emphasis on exports of semi-finished products rather than of raw materials, priority of the private sector, focus on specific export markets (e.g. leather goods to the EU; textiles, foodstuffs and pharmaceuticals to the Arab world; cotton clothing to the Netherlands and Japan), the establishment of export promotion boards linking producers, exporters, transport, packaging and marketing firms, and a simplification of export regulations. The private sector’s share of exports had increased to 36 per cent by 1990. The public sector still had a monopoly on exports of crude oil, cotton and rice³⁸.

However, the prime minister still believed that Egypt’s dependence on foreign machinery and intermediate goods must be reduced by domestic production³⁹. In line with such patterns of inward-looking economic thought, the Committee on Industry and Energy of the People’s Assembly called for bailing out a paper factory and a cement factory, which were close to bankruptcy after a sudden change in demand⁴⁰.

Nevertheless, considerable structural adjustment had already taken place since the Sadat period. Some 1 270 small and medium-sized producers out of a total of 1 600 in the textile city of Mehalla el Kobra in the Nile Delta had collapsed and had dismissed some 30 000 employees. The remaining firms had been working at 50 per cent of their capacity due to competition from inexpensive Southeast Asian products entering Egypt through the free zone of Port Said. Other obstacles were the migration of qualified labour to the Gulf, a six-fold price increase for yarn and dyestuffs, and shortages of special yarns. The enterprises had fallen victim to inconsistent liberalisation measures and a continuing state monopoly of the General Organisation of Textiles⁴¹.

Private entrepreneurs complained that 122 small private hotels and pensions had been closed down by decree of the Ministry of Tourism. They had been unable to comply with regulations requiring that a certain percentage of their turnover be in foreign exchange and that their capital be increased. They also suffered from various bureaucratic obstacles and excessive information requirements in addition to increased interest rates, electricity tariffs, prices of flour etc. Unemployment in the tourism sector rose to more than 20 000⁴².

IMF Stand-by Agreement

After protracted negotiations, a stand-by agreement with the IMF was concluded in principle on 4 April⁴³ and was ratified on 17 May 1991 for 278 million SDRs (\$372 million) for 18 months to support the economic reform and structural adjustment programme of the World Bank⁴⁴. IMF Director General Michel Camdessus referred to the negotiation period of almost three years: “Rather than coming to a rapid but evasive result open to all sorts of misunderstandings, we have preferred to dot our i’s to base our cooperation on a clear basis”⁴⁵. The agreement opened up Egypt’s access to a total of \$500 million of structural adjustment loans from the World Bank, the African Development Bank and the European Investment Bank, and paved the way for the negotiations on Egypt’s public debt with the Paris Club, and its debts to private creditors with the London Club.

On 25 May the member states of the Paris Club signed an agreement cutting 50 per cent of Egypt’s public debt and rescheduling the remainder. This reduced the annual debt service by some \$1.2–\$1.5 billion during three years (Table 8). The precedent of debt forgiveness for Poland and the US intervention in favour of Egypt after the Gulf war were instrumental in determining the exceptional terms: reduction by 15 per cent of the debt held by member countries of the Paris Club on 1 July 1991; another 15 per cent 18 months later on 31 December 1992 on condition that the IMF approved Egypt’s reform performance and would sign a subsequent agreement; annulment of the additional 20 per cent in July 1994 and rescheduling of the remaining 50 per cent would depend on Egypt’s fulfilment of the IMF’s macroeconomic conditionality.

Egypt’s subsequent unsatisfactory performance became subject to a continuing struggle over the second and especially the third phase of debt relief⁴⁶. The latter debt relief was only approved in October 1996⁴⁷.

World Bank Structural Adjustment Loan

On 24 June 1991 the World Bank approved a structural adjustment loan of \$300 million, with repayment over 20 years, including a five-year grace period, and a variable interest rate (then 7.73 per cent), depending on the Bank’s own borrowing

rate, to be disbursed in two equal tranches. The agreement was signed on 22 November 1991. The second tranche was to be disbursed 18 months after the first tranche subject to satisfactory implementation of the IMF conditionality on macroeconomic reforms.

Budgetary Policies

One of the cornerstones of the macroeconomic stabilisation programme was the reduction of the fiscal deficit as a share of GDP. Here Egypt was very successful. The deficit which still amounted to 17–21 per cent of the GDP in 1990–91 was reduced to 6.6 per cent of the GDP in 1991–92, even lower than projected by the IMF (10 per cent)⁴⁸. The IMF target for 1992–93 was 6.5 per cent.

One of the first IMF recommendations, partly implemented in April 1991, was the introduction of a value added tax of 10 per cent⁴⁹ as a general sales tax replacing the previous consumption tax⁵⁰. It was supposed to yield more than LE 1 billion of additional receipts⁵¹. It became subject to harsh criticism because of its hasty and inaccurate implementation. The resulting increase in consumer prices was intended as part of the IMF austerity programme⁵².

In order to increase budgetary receipts, in May 1991 the government substantially raised customs duties, by up to 20 per cent in the higher brackets, conflicting with the target of foreign trade liberalisation. On the other hand, in June 1991 new import legislation reduced the number of goods subject to import prohibitions from 210 to 105. The list was to be revised every six months. The previously required foreign exchange deposits for each transaction were reduced to 20 per cent of the value for traders and 10 per cent for producers. The private sector was authorised to import and export all products including cotton, wheat, tea, coal and crude oil (previously reserved for the public sector)⁵³.

Price Increases and Falling Living Standards

In line with IMF demands for ending subsidies and adjusting prices to their world levels, in May 1991 the government raised gasoline prices by 33 per cent, kerosene and diesel fuel by 100 per cent, fuel oil by 14 per cent and butane gas — a basic necessity for cooking in low-income households — by 66.6 per cent⁵⁴. This meant a substantial decline in the purchasing power of the lower income groups, and social tensions were on the rise, but, apart from Islamic movements, an effective political opposition did not materialise.

Consultative Group Meeting

The Consultative Group for Egypt held its third meeting at the Paris office of the World Bank on 8–10 July, the previous meetings having been held in 1976 and 1981. The membership⁵⁵ indicated the political weight attributed to Egypt in the Middle East. A precondition of the meeting was the agreement with the IMF of April 1991.

The head of the Egyptian delegation, Vice Premier and Planning Minister Kamal al-Ghazouli, asked for assistance of \$3.2 billion per year for three years (totalling \$9.6 billion) and addressed Egypt's entitlement to a geopolitical rent: "The fact that all these states and institutions have accepted the invitation that was extended for them to attend the meetings, and the fact that none of them were absent is of major significance, as it demonstrates the high degree of international interest, and support for Egypt's internal and external policies. It underlines the support for Egypt under President Hosni Mubarak's leadership and his adherence to principles of legitimacy during the Gulf crisis"⁵⁶. Egypt was particularly interested in the establishment of four special aid funds:

- a Social Fund, already mentioned;
- a fund to support social security and pension schemes;
- a fund for the protection of the environment and the restoration of historical monuments; and
- a fund for the support of privatisation, particularly to supply public companies with additional capital before sale.

Only the first was accepted, but \$8 billion was pledged for the years 1991–92 and 1992–93⁵⁷, greater than the level of aid before the Gulf War.

Special Relationship with the US

In July 1991 the Pentagon announced the sale of Hawk anti-aircraft missiles to Egypt for \$146 million, and in December the sale of military telecommunications equipment plus training for \$70 million. The first M-1 Abrams tanks arrived by the end of June 1991. They were intended to train Egyptians who were supposed to assemble them in the future. In a first stage, 52 tank components were to be manufactured in Egypt, and 100 per cent of the parts by 1998⁵⁸.

Under the aegis of the Egyptian Businessmen's Association, the Egyptian-American Business Council began to promote investment by small and medium-sized US entrepreneurs in Egypt, and organised seminars in New York and Boston with the participation of US businessmen of Egyptian origin⁵⁹. By 1990 total US investment in Egypt had reached \$1.7 billion, of which 82 per cent was in the petroleum industry. Thirty-two companies were operating in the manufacturing sector, and eight in banking⁶⁰.

Unification of the Exchange Rate

The exchange rate regime was unified in October 1991⁶¹ by the Minister of Economy, four months in advance of the timetable agreed with the IMF. This was made possible by the debt relief provided by the Paris Club and the Egyptian pound's stability against the dollar as a result of the inflow of foreign exchange from savings of Egyptian migrant workers and of other expatriates. They responded to interest rates of 19 to 20 per cent on LE deposits as compared to 5 per cent for dollar accounts. Public entities were allowed to hold foreign exchange deposits and to use their hard currency assets freely except for the three "strategic" export products of cotton, rice and crude oil⁶². Tourists no longer had to exchange a minimum of \$30 per day and could freely resell their Egyptian pounds for foreign currency when leaving the country. Egyptians could leave with foreign currency up to \$5 000 without any declaration (as compared with \$500 before).

Issue of Treasury Bonds by the Central Bank

Following an IMF recommendation, the Central Bank had been issuing six-month Treasury bills since October 1991 after a previous successful issue of three-month bills. Interest rates were raised from 14.2 per cent in the beginning to 19–20 per cent⁶³. The monthly issues were supposed to provide non-inflationary financing for the budget deficit, absorb excess liquidity, and provide a reference for the emerging capital market.

Further Price Increases

The IMF kept pushing for an adjustment to world prices. Petrochemicals were to reach world market prices by June 1995. In January 1992 the price for one litre of kerosene and gas oil had risen from 20 to 30 piasters (9 cents), for fuel oil from 18 to 27 piasters, e.g. by 50 per cent, except for power stations. On 18 January the petroleum minister declared in the Industry Committee of the People's Assembly that President Mubarak himself had decided to postpone the increase of the butane gas price by six months with an annual reduction of budgetary receipts by LE 836 million, contrary to the agreement with the IMF. President Mubarak preferred not to respect the government's commitment in order to avoid social risks.

The military factories were ordered to rush in with an additional 1 million gas bottles and preparations were made even to import butane gas if necessary⁶⁴. The situation was both politically sensitive and economically untenable, with the consumer price fixed at LE 2.5 and the production cost at LE 7, the difference being subsidised.

Climate for Private Foreign Investment

Foreign investment had been solicited ever since Sadat's Open Door Policy of 1974, but there was still an intimidating regulatory framework, especially for medium-sized enterprises. "Undoubtedly Egypt is a market. But it is also, and perhaps mainly, a state of mind"⁶⁵. There were general risks related to administrative culture such as clumsiness, tardiness, lack of competence, corruption, a general reluctance to make decisions and to adhere to them, lack of delegation of power, delays in answering letters, etc. The authorisation of a company took at least 18 months to two years although legal regulations prescribed a maximum of 60 days. The whole administrative environment was far more complicated than in Maghreb countries or in Turkey, which compete for private foreign investment. A major problem consisted of delays in the administrative rules concerning implementation of laws. Tax provisions changed rapidly⁶⁶. Other difficulties arose when a foreign enterprise wanted to import raw materials which are manufactured in Egypt, although at lower quality. Planning and budgeting with Egyptian business partners often encountered difficulties when the western partner expected strict implementation. Labour productivity was still lower than in other Mediterranean countries⁶⁷.

As a result of the uncompleted reforms, substantial parts of the Nasserist regulatory framework still existed. It requires special services of Egyptian lawyers and business consultants who know how to cope with such obstacles⁶⁸. As to larger foreign investments, domestic political resistance to a "sell out" or "foreign dominance" had to be taken into consideration, especially from the Nasserist old left.

1992: Reform Delays

Current Account Balance

Between 1990 and 1991 the trade deficit was reduced by 25 per cent (Table 1) as a result of an increase in exports largely due to the crude oil price boom, and a decline of imports following economic adjustment. Tourist receipts rose by 15 per cent. Interest payments on foreign debts declined by one third (Table 8) due to the Paris Club arrangement. In addition, Egypt received grants from the Gulf countries amounting to \$3.4 billion⁶⁹.

Thus the government would have been in an exceptional position to pursue its reform programme, but it preferred to avoid painful decisions. The leverage of international aid organisations was reduced since Egypt did not need the structural adjustment loan of \$300 million⁷⁰. The first drawing of \$60 million occurred in March 1992. Egypt was not interested in the approval of the second tranche of \$150 million envisaged for July 1992 since it did not need the loan and had only implemented a

small part of the reform programme. In particular, the sensitive subject of public sector privatisation was not being pursued. Government officials argued that the Letter of Development Policy had not mentioned a time schedule.

The government was more concerned with the next Consultative Group meeting, which was to give its approval to the second phase of debt relief by the Paris Club. This decision was subject to the conditionality of a second follow-up agreement between Egypt and the IMF. If Egypt did not obtain the second debt reduction, debt service of the order of \$1 billion per year (as compared to \$3 billion before the Paris Club agreement in 1991) would remain unchanged until mid-1994. The comfortable foreign exchange position, however, allowed the Egyptian government to proceed more hesitantly with its reform policies, particularly in the field of privatisation with its clear risks of unemployment and political destabilisation.

The Geostrategic Rent

Egypt received \$32 billion in aid from 1975 to 1990. Major donors were the United States (\$15 billion), the European Community and its member countries (\$8.3 billion), the Arab Gulf countries (\$3.3 billion), the World Bank (\$3.5 billion), and various other international and regional organisations (\$2 billion). Egypt received another \$5.6 billion in 1991, including \$3.6 billion to compensate for the Gulf War. Thus Egypt had become the largest recipient of official development assistance, averaging \$2.3 billion per year, which was greater than India (\$1.8 billion) and Israel (\$1.5 billion). In July 1991 the Consultative Group for Egypt had pledged another \$8 billion for fiscal years 1991-92 and 1992-93.

These large amounts of aid have not contributed to obtaining a serious government commitment to sustainable policies for Egypt's economic future in which, besides the problems of the domestic economy, the country will have to face the challenges of the Middle East peace process and the Euro-Mediterranean Free Trade Zone promoted by the EU. Instead, the government is concerned with maximising the international rent for a minimum of concessions towards reform.

Evaluation of Structural Adjustment by the World Bank

The evaluation of the reform in February 1992⁷¹ was a condition for the release of the second tranche of the structural adjustment loan. A number of administrative formalities with regard to Egyptian and foreign investments had been simplified. Prior authorisation had been abolished as well as former feasibility studies to be presented to the General Authority for Foreign Investment (GAFI), special permits to apply for bank credit, GAFI import licences for equipment, and export approvals. Profits could now be transferred within 72 hours. The GAFI was to be transformed into a service organisation for investors. By April 1992, 1 950 foreign investment projects with a total value of LE 5 billion had been authorised⁷².

Budget Policies

In May 1992 the People's Assembly adopted the new Five Year Plan for 1992–93—1996–97 and the budget for its first year. President Mubarak had already signed both documents on 29 April, and the parliament was simply legitimising decisions which had already been made elsewhere.

According to the IMF schedule, the budget deficit was to be reduced to 7 per cent of GDP in fiscal year 1992–93. Receipts were to increase by 33 per cent as a result of a 28 per cent rise in petroleum earnings and a 30 per cent rise in Suez Canal receipts. Expenditure was supposed to grow more slowly due to a 10 per cent decline in public investment. On the other hand, wages and pensions were to rise by 20 per cent to compensate for inflation, whereas subsidies for consumer goods were to be reduced by 40 per cent⁷³. Organised opposition was expected to develop more easily in the civil service than among the unorganised population. Security measures were tightened to clamp down on any unauthorised opposition, in particular the Islamists.

New Banking Law

The People's Assembly passed a new banking law to strengthen the control of the financial system by the Central Bank which previously had been subordinated to the Ministry of Economics. Initial opposition since the first half of 1991 was overcome when President Mubarak intervened in May 1992 in favour of the law, following the recommendations of the World Bank except its demands for private banks, and especially the (public–private) joint venture banks⁷⁴.

Guarantee for US Private Investment

Egypt and the United States concluded an agreement to guarantee private investment in May 1992. A delegation of the New York–based Egyptian–American Businessmen's Association, with some 100 US businessmen of Egyptian origin, was received by President Mubarak in the same month. Special efforts were envisaged to sell Egyptian products in the US market⁷⁵.

Growing Pressure from the Washington International Institutions

The government's lack of commitment to reform provoked harsh criticism, particularly by the IMF. In the summer of 1992 relations with the international aid institutions became strained. The main conflict arose over the 1992–93 budget. The IMF demanded a LE 3 billion reduction of the budget deficit from increased receipts and cuts in defence spending as a condition for renewing its agreement with Egypt after the expiration of the current agreement in November 1992. Its renewal was a

condition for the second 15 per cent reduction in Egypt's foreign debt by the Paris Club. Meanwhile, however, Egypt had accumulated \$12 billion of foreign exchange reserves which weakened the IMF's leverage on Egyptian performance.

Furthermore, Egypt was strongly supported by the United States on the IMF executive board. Washington shared Egypt's predominant interest in political stability. The IMF Resident Representative in Egypt, Pierre van den Boogaerde, spoke out in *Business Weekly* of July–August 1992 “that as an economist I believe that the faster Egypt moves toward reform the better, but it is not my opinion which counts. A political decision has been made to proceed at a certain rhythm”⁷⁶.

After advice from the United States not to overplay its position with the international donors, the Egyptian government promptly turned to negotiating a compromise. Four Egyptian ministers and the governor of the Central Bank tried to repair the situation with the IMF on the occasion of the annual meetings of the IMF and World Bank on 18–27 September in Washington. Egypt's position improved in September when Abdel Shakar Shaalan, an Egyptian who was former director of Middle East Affairs in the IMF, was elected to represent the Middle Eastern countries as an IMF executive director for the next two years. Immediately after assuming office in November 1992, he said that the IMF was in a position to prolong its present agreement with Egypt by two or three months.

The IMF had made available 278 million SDRs in May 1991 (then \$372 million), i.e. 60 per cent of the Egyptian quota, but, because of its accumulated foreign exchange reserves, Egypt had drawn only 147.2 million SDRs by September 1992. In view of the unsatisfactory performance on reforms an IMF mission to Egypt in June 1992 decided to postpone the evaluation by three months. This evaluation was a condition for the release of the remaining 130.8 million SDRs of the stand-by loan. The disbursement of the structural adjustment loan was also postponed. Egypt had drawn the final \$90 million in August 1992 from the first tranche of \$150 million. The release of the second tranche was planned for July 1992 by the World Bank, but the conditions, particularly with regard to privatisation had not been met. Again, the government was not anxious to use the structural adjustment loan because of Egypt's comfortable foreign exchange position and the loan's relatively high interest rate as compared to other sources of foreign assistance⁷⁷.

A lack of precision on privatisation in the structural adjustment programme allowed the government to evade a more serious privatisation effort, very much to the discontent of the World Bank. Law 203 of 1991 had shifted emphasis from privatisation to the possibility of 49 per cent participation by the private sector in public sector companies. Minister of Industry Mohammed Abdelwahab, an ardent supporter of a leading role for the public sector, declared that “privatisation means encouragement of Egyptian investors and savers to raise the private participation in the public enterprises in order to make use of all resources of the private sector. The Ministry of Industry has been doing this for years. This shows that we are in complete harmony with the programme of economic reforms”⁷⁸.

Financial Market Reform

In August 1992 Prime Minister Atif Sidqi announced that priority would be given to the sale of minority participations of the government up to 7–8 per cent of the capital in the joint ventures via the stock exchange. Following recommendations of the World Bank, Law 95 was adopted in June reorganising the financial market. Various taxes and fees were abolished, and a capital market surveillance authority was established⁷⁹. A number of foreign financial institutions from the United States, Europe, Hong Kong and Singapore expressed interest in trading in Cairo.

Promise to Avoid Dismissals

It was clear that massive dismissals in the privatised companies would launch a political upheaval. This basic problem was at the root of the government's stratagems to reconcile two conflicting aims: complying with donor conditionalities on the one hand, and preserving power and domestic political stability on the other. President Mubarak declared in September that "no worker will be released by the restructuring of the public sector", its reform being "a long-term process"⁸⁰. The state enterprises employed 1.1 million people. The public sector as a whole had 4.2 million employees out of an active Egyptian population of 12 million⁸¹.

Import Liberalisation

In August 1992 the number of prohibited imports was reduced from 105 to 78 in line with the IMF's stipulation to abolish all import restrictions by the end of the year. Tractors, tobacco, soft drinks, meat, fruits, perfumes, radios, refrigerators and cement could now be imported. International competition, however, was buffered by tariffs, although at reduced rates. A number of tariffs were still higher than the maximum of 80 per cent accepted by the GATT. Manufacturers and traders no longer had to make deposits of 10 and 20 per cent of the value of imports⁸².

Agrarian Reform Measures

After adoption by the government and approval by the parliament, President Mubarak signed a new agrarian law in July 1992 amending the old Agrarian Reform Law 178 of 1952, the main heritage of the Nasser period and the core of its social commitment to the Egyptian peasantry. Originally, the maximum size of the farms had been set at 200 feddans⁸³, later reduced to 100 feddans in 1961 and to 50 feddans in 1968. The Nasserist law had fixed the land tenure and had made tenancy inheritable, but it had also caused a continuing fragmentation of the holdings. It had blocked the sale of land and the modernisation of Egyptian agriculture. Meanwhile the size of the

holdings had often become so small that they could no longer support a family. The new law wanted to revalue real estate and to allow for a consolidation of arable land and for profitable private investments, a modernisation of agricultural technology and an increase of production.

Tenancy contracts had to be renegotiated before the end of the 1996–97 season. Rents were to be increased by 315 per cent. Previous rents amounted to LE 200–300 per feddan. Many tenants were unable to pay the increased rents and had to leave their plots. The social and political impact could only be substantial. On the other hand, it had become clear since the 1980s that the changing economic conditions were no longer compatible with the old regulations.

The new law had been supported by Wafd and the Socialist Labour Party of the opposition. Only the Nasserists had opposed it. In 19 hours of debate in the People's Assembly during four sessions the discussions mainly focused on the compatibility of the bill with Islamic law rather than on the massive socio-economic consequences⁸⁴.

Elimination of the “Negative List” for Foreign Private Investment

One of the World Bank's conditions for disbursing the second tranche of the structural adjustment loan originally scheduled for June 1992, was the elimination of the “negative list”⁸⁵ which prohibited private foreign investment in various subsectors. Since the government no longer needed the structural adjustment loan, the GAFI could afford to postpone the elimination of the negative list for more than a year. Only after the intervention of World Bank President Lewis Preston during his visit to Cairo on 18–21 July did GAFI Vice President Mohammed Abdelfattah Mongi announce the abolition of the list. However, permission from the local authorities was still required with regard to environmental impact⁸⁶.

Social Impact

The contraction of macroeconomic demand, a central objective of the stabilisation programme, had an impact on the standard of living of the majority of the people. The consolidation of public finance led to a drastic reduction of social services. The Nasser government had considered social distribution as one of its main sources of legitimacy (besides industrialisation and its firm stand with regard to Arab unity and Israel). This source of legitimacy was being eroded under the economic reform and structural adjustment programme. Cuts in subsidies and adjustments of prices to world levels or to long-term marginal costs of production had been especially affecting low income groups. Moderate wage increases in the public sector, opposed by the international donor organisations, had been insufficient to compensate for the rising cost of living. Real incomes had declined⁸⁷. The government was apprehensive of mass political dissatisfaction and eventual “bread riots”, and tried to shift the responsibility for the

social effects of the economic reform and structural adjustment programme to the Social Fund. The latter was never meant to assume such a comprehensive task, and lacked the financial and organisational resources.

Rising poverty had become especially acute in the more remote rural areas of Lower and Upper Egypt. Detailed studies showed that poverty had been increasing since the mid-1970s. Annual per capita household expenditure in 1981–82 amounted to LE 277 in urban areas and LE 188 in rural areas, as compared to LE 266 and LE 186 respectively in 1990–91 at constant 1981–82 prices⁸⁸. Annual per capita expenditure of the poorest 10 per cent of the urban households amounted to LE 98 in 1974–75, LE 133 in 1981–82 and LE 119 in 1990–91⁸⁹. Poor households⁹⁰ spent up to 64 per cent of their income for food and suffered from the large price increases. The economic burden of sending children to school had gone up relative to the household budget⁹¹. The unemployed and the elderly in urban areas were particularly hard hit⁹². In regional terms, poverty was worst in the Governorates of Fayoum, Sohag and Assiut in Upper Egypt⁹³ where education⁹⁴ and health services had also been neglected. Since the end of the 1980s they had turned into areas of political violence and Islamist terrorism.

International Earthquake Relief and Islamist Attacks on Tourists

An earthquake shattered large parts of the old residential quarters of Cairo on 12 October 1992, causing 561 deaths and leaving some 9 990 injured. The Egyptian government was able to mobilise exceptional international relief funds amounting to some \$285 million⁹⁵. Abdel Shakar Shaalan, an executive director of the IMF, declared in November 1992 that the Fund would prolong the current agreement, expiring in the same month, because of Egypt's additional burden following the earthquake. Egypt also stressed the sharp decline in tourism after terrorist assaults since the summer of 1992, which led to losses in tourist receipts of \$200 million per month⁹⁶. The renewed support of the Egyptian government by the newly elected Clinton administration also would help to postpone reforms⁹⁷.

Fourth EU Financial Protocol

On 9 November 1992, the fourth EU Financial Protocol for the 1992-96 period was signed. It supplied 258 million ECUs of grants and concessional loans from the EU budget and 310 million ECUs from the European Investment Bank, totalling 568 million ECUs (\$784 million). This meant an increase of 26.5 per cent as compared to the previous protocol. During a meeting of the Egyptian–EU co-operation committee in Brussels on 25 November, the Commission also abolished tariffs on agricultural imports from Egypt three years ahead of schedule and raised Egypt's import quotas⁹⁸.

**Box 4.1. Social Decay and Islamist Revolt:
The “Islamic Republic of Imbaba”**

By official count, some 700 shantytowns have sprung up in or around Egypt’s major urban centres since the 1970s. In 1995 their total population was estimated between 10 million and 12 million. Western Munira is one of them. Located on the north–western edge of Imbaba in Greater Cairo, it is less than three kilometres across the Nile from the upper–class district of Zamalek. At two square kilometres, that is less than one–fifth of the size of Zamalek, Western Munira has nearly one million residents, ten times the population of Zamalek. With nearly 50 times the population density of Zamalek, residents of Western Munira had no schools, hospitals, sewage system, public transportation, or police station within walking distance. For many years, Western Munira represented a world run by thugs, criminals, and drug dealers. “With no state presence, Western Munira was also used as a hideout for many Islamic militants on the run. In the late 1980s, one of them, Sheikh Gaber, felt safe enough to operate in the open. He preached and recruited followers. In a very short time, he emerged as a community leader. He began to weed out the vice lords, impose order, veil women, arrange marriages, and collect ‘taxes’. The Egyptian state did not take note of him until a Reuters reporter filed a story with the provocative title, ‘Sheikh Gaber, the President of the Republic of Imbaba’. Angered and embarrassed, the Egyptian authorities ordered the Reuters reporter out of the country and staged an armed expedition to arrest Sheikh Gaber. By official count, some twelve thousand armed security forces laid siege to Western Munira, then stormed the place. The operation took three weeks before Sheikh Gaber was arrested and six hundred of his followers were killed, wounded or arrested.”

Source: Ibrahim, 1996. Cf. *Al Ahrām Weekly*, 10–16 December 1993.

1993: Renewal of International Donor Agreements and Egypt's "Announced" Reforms

Second Tranche of the Structural Adjustment Loan and Another IMF Grace Period

On 25 February 1993 the Egyptian government and the World Bank signed a Letter of Intent releasing the second tranche of \$150 million (50 per cent of the structural adjustment loan of \$300 million approved in November 1991). Originally the disbursement had been scheduled for July 1992, but Egypt had not met the conditionality for the structural adjustment loan, and had not been eager to obtain the funds because of its comfortable foreign exchange position. The Letter of Intent followed from the Egyptian announcement of a programme of privatisation and foreign trade liberalisation after several months of painstaking negotiations and considerable tension with the international donor organisations⁹⁹.

Privatisation Measures

After many excuses, on 5 February 1993 the government stated that eight public and mixed banks had been authorised to sell the state's participation in 16 enterprises¹⁰⁰. On 26 February Prime Minister Atif Sidqi announced the privatisation of 85 public or joint venture enterprises by June 1997.

Meanwhile a number of partial privatisations had taken place through the sale of shares at the stock exchange¹⁰¹. The National Bank of Egypt and the Bank of Alexandria started to sell their participations in a number of companies. Generally, the state remained the majority owner.

The new government announcements of further privatisations partially satisfied the World Bank which released the second tranche of its structural adjustment loan. With respect to the IMF agreement of May 1991, concluded for 18 months in October 1992, the prime minister announced its renewal for November, then, on 11 November for January 1993, and on 2 February 1993 for the end of that month. At an IMF board meeting on 18 March, the major points of disagreement with Egypt's reform performance were the budget deficit, obstacles to private investment, liberalisation of housing rents, fiscal reform, and delays in implementing the Social Fund.

President Mubarak met with IMF Director General Michel Camdessus on 5 April in Washington after seeing President Clinton. This was to pave the way for the renewal of the agreement.

The IMF had granted a first grace period after the Cairo earthquake of October 1992 until the end of February 1993. These prolongations automatically postponed the second phase of the Paris Club's planned debt reduction, linked to the IMF conditionality. Egypt had no balance-of-payments difficulties due to its foreign

exchange reserves which had accumulated to some \$15 billion. Finally, the World Bank and the IMF decided that Egypt's reform performance was by and large satisfactory¹⁰².

Budget Deficit, Treasury Bills and the Exchange Rate

According to IMF estimates, the budget deficit had declined from LE 19.7 billion in 1990–91 to LE 7.6 billion in 1991–92, i.e. from 20 to 6.4 per cent of GDP. An essential part of the IMF programme was a non-inflationary financing of the deficits via Treasury bonds instead of the previous recourse to social insurance funds or Central Bank credit.

This policy shift was in fact successful mainly due to the initial high interest rate on Treasury bills of around 20 per cent which also attracted large amounts of Egyptian savings abroad, resulting in the “dedollarisation” of the economy and the stabilisation of the pound at an exchange rate that was considered to be overvalued by the IMF. The latter kept arguing for a devaluation via a decrease of the interest rate on the Treasury bills which served as a signal for the banking system as a whole. In fact, the Ministry of Economy in February 1993 announced a reduction of the interest rate from 17.5 to 15.5 per cent. Inflation was estimated at 10 per cent. By February 1993 deposits in the banking system had risen to LE 159 billion, of which 60 per cent were in Egyptian pounds, an increase by 50 per cent in 6 months¹⁰³. The pound had remained stable against the dollar after the reduction of the interest rate, but the Central Bank had to intervene with \$300 million during the first two weeks of March 1993 to defend the pound¹⁰⁴.

In 1992–93 the budget deficit was 6.8 per cent of the GDP. The deficit would be reduced to LE 9.1 billion, i.e. 6.5 per cent of GDP, according to the planned 1993–94 budget. A major expenditure was the 17.5 per cent increase in wages and pensions in July 1993 for 10.5 million active and retired public employees (which was supposed to be 3 per cent above the rate of inflation), whereas subsidies on basic consumer goods declined by 6.2 per cent¹⁰⁵.

The sales tax that had been introduced in 1991–92 yielded LE 7.3 billion in 1992–93. It reduced profit margins of entrepreneurs and consumption. The sales tax replaced a consumption tax which yielded only LE 3.6 billion. The sales tax had been levied on manufacturers, importers and certain services, and was to be extended to retailers in 1995–96. In line with the agreement with the IMF, an amendment was introduced in July 1993 by presidential decree establishing a tax of 20–30 per cent on luxury items and a tax of 25 per cent on electrical appliances. A number of services (express couriers, cleaning, personal security, car hiring) were taxed at 10 per cent.

In line with the Egyptian commitments to the IMF scheduled for the end of 1993, the People's Assembly on 31 December passed a unified income tax law after long and heated debate¹⁰⁶.

Foreign Trade Liberalisation

Three decades of import–substitution policies had left their mark. Between 1977 and 1989, exports made up only some 5 per cent of GDP, whereas imports amounted to 28 per cent. In 1989 the export to GDP ratio was almost three times greater in Turkey and five times greater in South Korea¹⁰⁷. Egyptian exports financed less than one–fifth of imports. Food accounted for 24 per cent of imports, followed by capital goods and industrial inputs. In 1990–91, major imports were foodstuffs (24 per cent) and capital goods (20 per cent). The main exports were crude oil and petroleum products (51 per cent), textiles (14 per cent), and aluminium and chemical products (12 per cent).

Aluminium production was subsidised by low electricity rates. Egypt does not have a comparative advantage in capital–intensive chemical industry under free trade. Exports have been discouraged by taxes and numerous administrative obstacles to maintain secure domestic supplies¹⁰⁸.

Since May 1991 the structural adjustment programme had aimed to eliminate customs and non–tariff barriers on imports and exports and to expose the Egyptian economy to international competition. In March 1990 before the programme began, 76 per cent of domestic production was protected by non–tariff barriers and 12 per cent of local production was subject to non–tariff export barriers. By June 1991 these figures were 26 per cent and 4 per cent respectively. Private importers and exporters were permitted to trade in product groups previously monopolised by the public sector.

To meet the conditionality for the second tranche of the structural adjustment loan in February 1993 (eight months behind schedule), the government agreed to reduce the number of items subject to import prohibition to 30 per cent compared to March 1990. In August 1992 the number of banned import products was reduced from 105 to 78, with an average tariff of 25 per cent.

Four product groups out of 18 which still required import permits in May 1991 (compared to 55 in March 1990) were freed from this obstacle by August 1992. Excessive quality controls of imported products were to be eliminated, as well as preferential customs treatment of 27 imported products out of 90. Special foreign currency allocations to the public sector were abolished. Customs tariff variations were to be reduced to a range of 10–80 per cent (except for some basic foodstuffs and luxury items) compared to 5–100 per cent at the beginning of the reform programme. This was implemented by March 1993, although with a 5–80 per cent range which was accepted by the World Bank.

Egypt was supposed to raise export quotas by 15 per cent annually for the last products subject to these regulations, namely raw wool, wool waste, cotton and paper. In March 1990, the export of 20 products had been prohibited, and 17 products had been subject to export quotas. In June 1992 the People’s Assembly had approved the establishment of an Egyptian Export Insurance Company by the Export Development Bank of Egypt (EDBE), the National Investment Bank and three insurance companies.

In October 1992 a GATT committee examining Egypt's liberalisation policy had noticed that a great number of quantitative import restrictions still existed, that the tariff system lacked transparency, and that many tariffs were excessive¹⁰⁹.

By the end of July 1993 two decrees further liberalised the foreign trade regime after the IMF had considered earlier steps as insufficient. Import tariffs on 44 raw materials and intermediate products were reduced to encourage local manufacturers. Customs duties were abolished on 53 locally manufactured products such as lorries, buses, tractors, motorcycles and bicycles; import bans on 52 articles were lifted, including that on automobiles, which aroused particular public interest. Trade protection was maintained on textiles made from synthetic fibres. Only 4.8 per cent of Egypt's agricultural and industrial production remained subject to import prohibition, compared to 36 per cent the year before. Furthermore, the variation of tariffs was reduced to a range of 10–80 per cent (with higher tariffs for high-powered automobiles, cigarettes and alcohol), compared to 5–80 per cent before. Preferential tariffs for public enterprises were abolished and the need for prior approval of exports was ended. Private companies were allowed to deal in public sector imports. Overall protection was reduced to 20–4 per cent as compared to an international average of 7–12 per cent.

New Union Law

In February 1993, the People's Assembly approved a new law for professional union elections. Islamist-controlled unions denounced the legislation as a blow to democracy. The purpose of the law was to prevent the mainstream Muslim Brotherhood from maintaining control of the governing councils of professional syndicates. The law made a 50 per cent turnout of voters mandatory in the first round at any syndicate elections if they were to be valid, and that they must not be held on Fridays and official holidays. The most vigorous opposition came from the syndicates of engineers, lawyers and doctors, all dominated by the Islamists¹¹⁰.

Human Development

Private consumption declined with the loss in purchasing power. Wage increases did not compensate for the inflation. The *Human Development Report* of 1993 stated that Egypt had declined from position 114 to 124 (out of a total of 160 countries) in the human development index, based on per capita income, level of education, and life expectancy¹¹¹.

Social Fund

Established in 1991, the Social Fund did not begin functioning before February 1992¹¹². By April 1993 it had allocated LE 368 million for various loans, i.e. for the "productive families" programme (LE 68 million), literacy programme (LE 20 million),

Nile river bank works (LE 75 million), primary health care (LE 8 million), handicrafts (LE 100 million), small and medium-sized industries (LE 41 million), rural infrastructure (LE 54 million) and re-employment of workers dismissed by the El Nasr Company for Foundries¹¹³. LE 450 million was allocated to Egyptian banks in order to subsidise loans to small entrepreneurs¹¹⁴, especially those who had emerged from the restructuring of public companies, of which LE 21 million went to the Industrial Development Bank, LE 40 million to Bank Misr and the Alexandria Businessmen's Association, and LE 50 million to the National Bank of Egypt.

Fencing with Donors

The government carefully tried to preserve political stability and avoid hurting powerful domestic vested interests. Effective structural reform was not at the top of its political agenda. Instead, the rent seeking approach prevailed. The new Clinton administration's support during President Mubarak's 6 April 1993 White House visit immediately influenced Egypt's bargaining position with its donors and slowed down reform, particularly in the highly sensitive domain of privatisation. President Mubarak told the press that he would ask President Clinton to maintain present levels of US aid for three years, and to re-examine the level of assistance thereafter. He also asked for US support in Egypt's dealings with the IMF, meeting with Michel Camdessus the following day¹¹⁵.

On 1 May 1993 President Mubarak announced the continuation of reforms, without referring to the expiring IMF agreement, with emphasis on improving public services and infrastructure, on fighting unemployment and regional imbalances, and on encouraging investment. He promised that not a single worker would be dismissed, and the economy would not be exposed to "undue foreign influence".

Extended Fund Facility of the IMF

Egypt's position was strengthened by US support and had an immediate impact on the negotiations with the IMF. The latter had accepted a prolongation of the agreement (expired in November 1992) until the end of May 1993 as a signal to the Paris Club that Egypt had by and large abided by the conditionality but, contrary to the statements of various cabinet members that the Egyptian government did not put emphasis on renewal of the agreement with the IMF, negotiations continued. This allowed the Egyptian government to maintain contacts and save face in spite of serious differences, especially with regard to the budget deficit, trade protection and privatisation¹¹⁶. The chief negotiator was Minister of State Youssef Boutros-Ghali, a former IMF staff member and nephew of the then UN secretary general¹¹⁷.

An agreement with the IMF was finally reached in September¹¹⁸. Egypt could draw on an Extended Fund Facility of 400 million SDRs (\$569 million), representing 59 per cent of its quota in half-yearly tranches until the end of the agreement in

September 1996. Thus Egypt entered into a second phase of the reform programme. The second evaluation of the first agreement had been scheduled for June 1992, but the government had asked for a postponement because it had not yet met the performance criteria with regard to budgetary and adjustment issues. The Fund had accepted a postponement of the evaluation to November 1992, and had prolonged the agreement to March 1993. In January 1993 the government had asked for another prolongation to May 1993, which was accepted after the evaluation was considered satisfactory. The World Bank released the second tranche of the structural adjustment loan linked to the IMF programme in March 1993¹¹⁹.

Political Manoeuvres

After his meetings with President Clinton and IMF Director General Camdessus in April 1993, President Mubarak decided to speed up the reform process while negotiating the softest possible conditions¹²⁰. Backed by reaffirmed US geostrategic support, President Mubarak ordered the prime minister and cabinet members with economy-related responsibilities to reach a new agreement in June 1993, only after the grace period of the IMF agreement expired and the World Bank expressed harsh criticism¹²¹. After a month of negotiations, Egypt accepted IMF demands. To ensure that the IMF executive board would ratify the agreement in principle in July, the government immediately started to implement the measures suggested in its Letter of Intent. It was transmitted to the IMF in its final form on 18 August after the parliamentary session, to avoid embarrassing discussions in the People's Assembly. On 20 September the IMF accepted the letter and renewed the 1991 agreement. Since Egypt did not formally sign the agreement, the prime minister could tell critics accusing him of having submitted to another "IMF dictate" that the government had signed no agreement¹²². As usual, no technical details were published in the press¹²³.

The new agreement followed the previous schedule of half-yearly evaluations of the progress of reform. Meanwhile, Egypt's foreign reserves reached \$14 billion. Egypt had already told the IMF at the beginning of 1993 that it would not draw on the last tranche of 130.8 million SDRs (at the relatively high interest rate of 7 per cent). A major function of the new agreement was to pave the way to the second instalment of debt relief by the Paris Club. It ran from 1 July 1993 to 30 June 1996, and listed precise reform measures with emphasis on public finance, monetary policy, financial markets, restructuring and privatisation of the public sector, private sector promotion, customs tariffs, and the foreign trade regime¹²⁴.

Egypt had obtained the second instalment of debt relief from the Paris Club without fully abiding by the original conditionality. The stabilisation policy was by and large implemented, but the essentials of structural adjustment were not. By stressing the danger of social turmoil, Egypt was able to get the IMF to accept reform at a slower pace in the domains of monetary control, fiscal reform, public sector wages, administrative overhaul and performance of the Social Fund. The main reason was the IMF's reduced leverage as a result of Egypt's improved foreign reserves position.

Concerning the crucial issue of privatisation, the newly appointed Public Sector Minister Atif Ebeid reiterated in November 1993 that not a single worker would lose his job¹²⁵.

Political Weight of the Private Sector

For the first time Egyptian businessmen were allowed to meet with an IMF delegation. They expressed particular concern about the IMF's target of decreasing the maximum tariff to 50 per cent and the increased exposure to international competition. Other demands of the business community were for minimum prices for all imported articles, with customs duties levied accordingly, and for import quotas for each product group¹²⁶.

After President Mubarak's re-election in October 1993, a number of new ministers were appointed. The private sector business community deplored that no representative of their group was invited to join the cabinet, and complained that this indicated that there was a credibility gap¹²⁷. At that time the private sector accounted for one-third of the Egyptian GDP.

US Aid

On 30 September 1993, President Clinton signed a law on US foreign assistance for the fiscal year (beginning in October) which provided \$2.3 billion for Egypt, of which \$815 million was in grants. Until then, Egypt had received \$18.1 billion in US aid since 1975, after President Sadat had initiated an Open Door Policy. Annual grants of \$1.3 billion in military aid were given to the Egyptian army to accelerate the Americanisation of its (formerly Russian) military equipment. Forty per cent of the aircraft, 70 per cent of anti-aircraft weapons, 45 per cent of the tanks and armoured vehicles, 85 per cent of the guns and 50 per cent of the warships were still of Soviet origin. Defence Minister General Tantawi expressed the Egyptian Army's desire to strengthen the US-Egyptian relationship so that it would match US-Israeli relations.

A \$3.2 billion programme was supposed to support the assembly of 524 A1-M1 Abrams tanks in Egypt's military factories until 1998, with a rising percentage of Egyptian-made components. However, costs rose far beyond initial estimates and were considered to be prohibitive by the US General Accounting Office¹²⁸.

Second Instalment of Debt Reduction

On 12 December 1993, a protocol was signed in Cairo during an IMF mission on the first steps of the new reform programme¹²⁹. A second agreement was signed on 22 December after a World Bank mission delimited Egypt's future borrowing in terms

of the size of its reimbursements. Egypt had declared that it would not use the second tranche of \$150 million of the structural adjustment loan in view of its own foreign reserves, consistent with the non-utilisation of the IMF loan¹³⁰.

The Paris Club agreed to the second instalment of 15 per cent debt relief for Egypt, amounting to some \$2.5 billion linked to the renewal of the agreement with the IMF. On 13 December 1993 Prime Minister Atif Sidqi said that he expected the third instalment in July 1994, but it only materialised in October 1996¹³¹.

1994: The Confrontation Continues

Consultative Group Meeting January 1994

On 25–26 January 1994 the Consultative Group of Egypt’s donors pledged some \$6 billion in non-military aid for 1993–94 and 1994–95, of which 60 per cent would be grants¹³². Foreign support remained substantial, and at the end of 1992–93, \$7.07 billion of previous aid allotments had not been disbursed. On 30 June 1994 the undisbursed pipeline still contained \$6.9 billion. If one adds the foreign exchange reserves and the new aid, Egypt had an exceptional buffer of \$29 billion¹³³, providing the government ample room for manoeuvre to ward off donor pressure for further reforms. Vice-Prime Minister Kamal al-Ghazouli underlined Egypt’s regional leadership in the Middle East peace process in the fields both of politics and economics¹³⁴. The Consultative Group was “very satisfied” with the reduction of the budget deficit and inflation, and “satisfied” with the reform of the regulatory framework and the liberalisation of the trade regime. It “encouraged” the Egyptian government to proceed vigorously with the privatisation of the public sector¹³⁵.

World Bank Evaluation March 1994

In March 1994 the Egyptian government and the World Bank signed a note on the evaluation of the reform programme. Minister of State for International Co-operation Youssef Boutros-Ghali held that the World Bank would begin to appreciate Egypt’s privatisation approach and expected that Egypt would get the third tranche of its foreign debt reduction in July 1994, as envisaged in 1991, in spite of the accumulated delays¹³⁶.

Foreign Trade

On 13 February 1994 President Mubarak ratified the new Egyptian customs tariff. According to the IMF agreement it should have been effective since 1 January. The delay was due to adjustments which were made as a result of pressure by Egyptian

businessmen who feared international competition. The maximum tariff was reduced from 80 and 70 per cent (except for high-powered cars, cigarettes and alcohol). Tariffs previously between 30 and 70 per cent were decreased by 10 per cent.

On the other hand, customs tariffs were raised for eggs (from 5 to 10 per cent), milk and tyres (from 20 to 30 per cent). Additional taxes were introduced to cover the cost of inspection and classification of goods. In March the World Bank demanded that these taxes be removed in the shortest possible time as they contravened the objective of the tariff reduction. On 29 April 1994 the government decided to maintain a uniform tax of 2 per cent as of 1 July and to eliminate all other administrative charges for importers one year later. This was accepted by the World Bank¹³⁷.

The Ministry of Economy and Foreign Trade also introduced the international customs standard and abolished price fixing for export products and the requirement of prior authorisation for exports. Regulations referring to guarantees and insurance of imports for re-export purposes and related sales taxes and import duties were also eliminated¹³⁸.

The foreign trade deficit in 1994 increased by 21 per cent and reached \$6 billion. Imports increased by 18 per cent and attained \$9.5 billion (with a rise in wheat imports of 120 per cent). Exports only rose by 12 per cent to \$3.5 billion¹³⁹. Rent incomes declined: tourism because of terrorism, workers' remittances because of labour restrictions in Iraq and Saudi Arabia, and Suez Canal receipts as a result of the competing facilities of the Suez-Mediterranean pipeline¹⁴⁰.

Exchange Rate Regime

After a year of debate, the People's Assembly abolished foreign exchange controls and the obligation of exporters, travel agents and public enterprises to repatriate foreign exchange receipts¹⁴¹. This new step towards convertibility of the Egyptian pound was backed by a foreign reserve position of \$16 billion¹⁴².

Partnership for Peace with the United States

On 6 September 1994, President Mubarak and Vice President Al Gore signed a new co-operation agreement to continue "the partnership for peace initiated 15 years ago". A joint committee for economic growth was established for high-level official dialogue on trade, private investment, scientific and technological co-operation and economic policy. A consultative committee of businessmen on both sides was also established.

The Egyptian side appreciated that the co-operation agreement on science and technology was of the same type as the one between the United States and Israel. The United States maintained its aid at \$2.1 billion, \$817 million being for economic aid and \$1.2 billion for military assistance (as compared with \$3 billion for Israel, of which

\$1.2 billion was for economic aid and \$1.8 billion for military assistance)¹⁴³. The Egyptian attempt to establish a special partnership with the United States helped it to take a more independent stance towards IMF and World Bank pressure on politically sensitive issues. Close ties with the United States were also supposed to demonstrate Egypt's importance to the Arab world¹⁴⁴.

Gulf Aid

In September 1994 Kuwait decided to reduce Egyptian debts by \$2.8 billion. Generally, Gulf donors do not publicise their foreign aid activities in order to maintain room for political manoeuvre, e.g. providing aid in return for political decisions by the recipient. During the last 20 years, Arab aid to Egypt amounted to \$16.4 billion. Saudi Arabia had been particularly discreet about its aid, which has always been linked with a political rent and its security concerns *vis-à-vis* Israel, Iran and Iraq. Therefore, military aid had been an essential component following the US pattern¹⁴⁵.

IMF Postpones Third Instalment of Debt Relief

In June 1994 the IMF refused to approve the third instalment of 20 per cent debt relief by the Paris Club scheduled for July 1994, with the present value of the debt amounting to some \$4 billion. Apparently the Egyptian side had misjudged the leverage of the recent accord with the United States. Prime Minister Atif Sidqi said in September that there was no disagreement with the IMF, and Minister of International Co-operation Youssef Boutros-Ghali claimed that the debt reduction would occur before the end of 1994. Meanwhile, Egypt's foreign reserves had risen to \$17 billion, which made it less urgent to reduce foreign debt. Inflation had dropped from 20 per cent in 1991 to 9 per cent in 1994. The budget deficit was cut to 2.6 per cent of GDP in 1993–94 and was supposed to be reduced to 1.5 per cent in 1994–95. The Egyptian pound had remained stable at a rate of 3.3 to 3.4 against the dollar since 1992. The trade deficit, however, rose to \$9.7 billion. Non-petroleum exports fell to 11.4 per cent of GDP.

Devaluation

It was clear that without substantial increases in non-traditional exports and an adjustment of the overvalued pound, Egypt would not be able to support its growing population. Nevertheless, there was a struggle over the devaluation. The Central Bank kept backing the exchange rate via high interest rates for LE deposits. The Egyptian press debated the issue, and the opposition newspapers accused the government of giving in to undue foreign influence. Devaluation had been partly addressed in the Letter of Intent of September 1993, when the IMF agreement was renewed. However, no rates or time schedules had been specified, and the government refused to honour its general commitment on devaluation.

The IMF recommended a substantial reduction of the interest rate on Treasury bills following the decline of inflation. This would reduce the real interest rate and lead to a devaluation of at least 20 per cent against the dollar, since it was the interest rate policy of the Central Bank which attracted LE deposits, but Public Sector Minister Atif Ebeid vowed Egypt would “never devalue”¹⁴⁶.

Firm opposition to devaluation was also voiced by the Egyptian Businessmen’s Association which shortly before an Egyptian delegation went to Washington sent a letter to the IMF to support the official position on keeping the pound stable. The majority of the business community was mainly interested in maintaining inexpensive imports of capital goods and intermediate inputs rather than increasing exports. On the other hand, Sherif Delavar of the more outward-oriented Alexandria Businessmen’s Association objected that the devaluation debate “was guided by emotions and patriotism rather than by an analytic mind”. He held that a correction of the exchange rate was justified by the inflation differential between Egypt and the United States¹⁴⁷.

As a result of these debates the pound fell to LE 3.42 per dollar. On 27–28 July the Central Bank intervened with \$200 million to bring the rate back to LE 3.39¹⁴⁸. President Mubarak affirmed that there would be no devaluation. On 23 September, shortly after the IMF had declared that the accumulated inflation of three years and the weakness of Egyptian exports would justify a devaluation, he again said that a devaluation was not under consideration. The Egyptian outlook was expressed by Public Sector Minister Atif Ebeid who stated on 20 September that the privatisation programme had not been delayed but that “no pressure could force us to accelerate the programme”¹⁴⁹.

Further Disputes with the IMF

After critical comments of Michel Camdessus on the Egyptian reform performance in Cairo in September 1994, IMF Assistant Director General Stanley Fisher went to Cairo for another round of negotiations from 1 to 19 December. Fisher declared on his arrival in Cairo: “There are many important disagreements on the whole reform package”, whereas Prime Minister Atif Sidqi referred to the floods in Upper Egypt of November 1994 and insisted that “the economic reform programme will continue in spite of a series of natural catastrophes which have hit the country”¹⁵⁰. Similarly, the earthquake of 1992 in Cairo had been used to obtain a delay for the renewal of the IMF agreement. By the end of 1994 the criteria had not been met for the third instalment of Egypt’s debt relief, now delayed by more than eight months¹⁵¹.

The prime minister had said in October that for the time being the government refused to privatise banks and insurance companies as agreed upon in Egypt’s Letter of Intent of September 1993. In December he added that the subsidies on basic foodstuffs would not be eliminated but rationalised. “We will have recourse to privatisation as the last means to improve living conditions”¹⁵².

The IMF was demanding a devaluation of the pound within the next 12 to 18 months and opposed the support measures by the Central Bank and the four large state banks, limiting their sales of foreign currency. The prime minister made it clear on 17 December, when the IMF staffers were still in town, that the “dossier of the devaluation of the pound was definitely closed”. This was in line with statements of President Mubarak in September and on 17 November in an interview with the Associated Press, when he affirmed that Egypt would fight against the pressure of the IMF and World Bank. The prime minister added that “the government would not allow the adoption of measures moving in the direction of devaluation such as a decrease of interest on pound deposits. The delay of the annulment of the debt is no problem for us and will have no consequences on the Egyptian economy”. Meanwhile foreign reserves of the Central Bank had reached a record of \$18 billion¹⁵³.

The IMF also wanted a lower interest rate in order to encourage investment in and production of non-oil export goods. Egyptian exports were hardly larger than those of Syria (with a quarter of Egypt’s GDP). Exports in relation to GDP had declined from 6 per cent in 1987 to 4 per cent in 1994. They fell from \$1.98 billion in 1991–92 to \$1.6 billion in 1993–94, whereas the IMF had projected an increase to \$2.4 billion. The increase of the real interest rate amounting to 4 per cent for three-month Treasury bills in 1994 as compared to 2.8 per cent in 1993 created attractive investment opportunities in the financial market which discouraged investment in export production.

The Egyptian government argued that a devaluation would cause a sharp increase in prices and a loss of confidence in the pound. The vested interests of importers were stronger than those of the potential exporters.

Electricity Rates

Minister of Electricity Maher Abaza announced in October 1994 that electricity prices would be progressively raised to their production costs in 1995 as part of Egypt’s commitment to the international donors. Annual subsidies amounted to LE 750 million. The rate was 12.5 piasters per kwh, compared to a cost of 17 piasters. After a request by the Federation of Industries, however, President Mubarak blocked the increase of electricity rates for industrial use. In 1994 the public sector still paid a preferential price of 6 piasters per kwh, and the public administration paid 4 piasters¹⁵⁴. Private power production by diesel stations, e.g. for hotels and other tourism facilities was on the rise¹⁵⁵.

1995: International Challenges and Domestic Social Crises

New Moves

US Vice President Al Gore visited Cairo on 25 March 1995 to sign a number of co-operation agreements prepared during his first visit the year before. A new quality of the Egyptian–US partnership was called for under the patronage of a joint Egyptian–American Committee for Economic Growth chaired by Prime Minister Atif Sidqi and Vice President Gore. The Egyptian Businessmen’s Association supported close US–Egyptian industrial co-operation.

In April representatives of the European Union came to Cairo to negotiate for three days on Egypt’s participation in the Euro–Mediterranean Free Trade Zone to be established by 2010. Since the late 1970s Egypt had had an average annual trade deficit of 1 to 2 billion ECUs (\$1.3 to \$2.6 billion) with the EU¹⁵⁶. Both sides were to open their markets. Egyptian manufactured goods already had free access to the EU market except for cotton yarn and fabrics. Egypt also demanded access for its agricultural products and processed foodstuffs. Egyptian exports to the EU amounting to 2.2 billion ECUs still are less than Turkey’s (6.5 billion ECUs), Morocco’s (3.2 billion ECUs) and Tunisia’s (2.5 billion ECUs). Egyptian non-oil exports amounted to only 800 million ECUs, comparable to those of Cyprus or Malta¹⁵⁷. EU assistance to Mediterranean countries will be 5.5 billion ECUs during five years to prepare for the Euro–Mediterranean Free Trade Zone. Egypt’s co-operation agreement with the EU ended in 1996; total EU grants to Egypt during this period amounted to 258 million ECUs in addition to 310 million ECUs of concessional loans of the European Investment Bank (EIB). Egypt also received 300 million ECUs between 1991 and 1996 in grants and 1 billion ECUs in concessional loans from various EU regional programmes¹⁵⁸.

Under the new Mediterranean policy of the EU Egypt may expect \$2 billion in development grants and another \$2 billion of EIB loans to modernise its industrial base, education and training, and R&D facilities¹⁵⁹. Mohammed Farid Khamis, president of the Federation of Industries, expressed concern about the future chances of Egyptian industry facing non-tariff barriers of the EU.

Continuing Face-off with the IMF

During the first years a number of reform measures had been implemented wherever domestic political resistance was relatively low. Meanwhile sensitive core problems were to be addressed. Prime minister Atif Sidqi acknowledged differences between Egypt and the IMF, which was pressing for an acceleration of the reform programme. The prime minister told the press on 20 January 1995 that “the negotiations with the IMF are going on in spite of different views on technical matters”, and that

Egypt had the right to obtain the third instalment of debt cancellation. “The reform programme is 100 per cent Egyptian and no foreign authority can force us to do things which we do not want”¹⁶⁰. The debt service amounted to about \$350 million annually¹⁶¹.

New Privatisations Announced

In May 1995, Public Sector Minister Atif Ebeid stated that a third of the 314 state enterprises would be sold within the next twelve months via the stock exchange. According to Ebeid, the government prepared a programme of restructuring starting in June 1995. About 150 state enterprises could not be sold because they made losses¹⁶², but they were not liquidated either for employment reasons. “Until December we will have achieved the restructuring of some 40 enterprises, and the rest in 1996”¹⁶³, but Hisham Hasabu, advisor to the prime minister, made it clear that the limited size of the financial market in Egypt would make it difficult to absorb the announced volume of sales¹⁶⁴. The leftist and Islamist opposition argued that undervalued assets of state enterprises would fall into foreign hands¹⁶⁵.

Additional Scope for Private Foreign Investment

Ms. Faika al-Rifai, Vice-Governor of the Central Bank of Egypt, stated that foreign banks were invited to expand their activities and “the door was open for joint ventures”, even for foreign participation of more than 51 per cent. The deposits of foreign banks and joint ventures made up almost one third (LE 42 billion) of the total deposits of the banking sector in Egypt (LE 143 billion)¹⁶⁶. Minister of Industry Ibrahim Fawzi stressed Egypt’s interest in foreign automobile investors. No reduction of customs duties on imported cars was being envisaged¹⁶⁷. In 1994, 66 000 cars were imported (as compared to 34 000 in 1993), and 31 000 cars were locally produced with a work force of 72 000¹⁶⁸.

Interest Rates and Exchange Rate

The interest rate on three-month dollar deposits between January and April 1995 declined from 6.25 to 6.08 per cent, whereas the interest on pound deposits increased from 9.75 to 10 per cent. Egyptian bankers increasingly considered a devaluation of the pound or the linking of the pound to a basket of foreign currencies, possibly the dollar, the deutsche mark, the yen, the French franc and the pound sterling¹⁶⁹.

By mid-1995 the interest rate on LE loans by the banking system to the business sector was 13 to 14 per cent compared to 20 per cent in the past. Mohammed Farid Khamis, owner of Oriental Weavers Co. and president of the Federation of Industries called for a reduction of interest rates to 9 per cent for the industrial sector¹⁷⁰, still arguing in terms of government intervention. The interest rate on Treasury bills was 12 per cent¹⁷¹.

Reliance on Regular Foreign Support

The political advisor to President Mubarak, Usama al-Baz, stated in April 1995 that Egypt (being the second largest beneficiary of US foreign assistance after Israel with some \$2.1 billion annually) would need the same level of aid over a period of 10 to 15 years, “the time necessary to achieve the goals of Egypt’s economic reform programme”¹⁷².

Dependence on Wheat Imports

Egypt is the third largest importer of wheat after China and Russia. Its main suppliers are the United States with some 950 000 tons annually and France with 325 000 tons. This precarious situation caused a debate on Egypt’s food security and its dependence on the United States in relation to expectations on future wheat prices and Egyptian–US political differences on the nuclear non-proliferation treaty and the embargo against Libya. Some 50 per cent of Egypt’s wheat consumption must be imported¹⁷³. In 1995, 5.3 million tons were locally produced. Some 5.7 million tons were imported, costing \$140 million as compared to \$100 million in 1994. Egyptian per capita annual consumption is 200 kg., one of the highest in the world. The majority of experts believe that Egypt will face a serious crisis in the near future if it does not reduce its dependence on foreign supplies¹⁷⁴.

The USAID started another agricultural support programme of \$27 million for the establishment of liberalised agricultural markets and the privatisation of various agro-industries¹⁷⁵.

Employment

The Egyptian government rejected the dismissal of surplus labour under the reform process. Eleven per cent of total employment was in the public sector (1.3 million), 21 per cent in the public administration and 68 per cent in the private sector. The director of employment creation in the Social Fund, Omar al-Faruq Amin Ugumar held that massive dismissals of workers was unacceptable. “If we dismiss 500 000 people, the rate of unemployment will reach 20 per cent and the social situation will become explosive. This means revolution. Besides, the state would have to pay \$1.8 billion in compensation which it cannot finance”. According to a study by British consultants, 30 per cent of the labour force in state enterprises was superfluous, 40 per cent had a second job, and 40 to 45 per cent lacked qualifications. A transition period of seven to ten years would be necessary¹⁷⁶.

Small-scale industry employed some 6 million people, about one third of the active labour force. This sector had been neglected since Nasser’s times. The ideology of Arab Socialism had called for large-scale and capital-intensive public sector companies. The informal sector became a buffer for all those whom the government

could not supply with jobs or could not support with pensions¹⁷⁷. The USAID supported small enterprises with a credit programme of LE 45 million. Some 20 200 loans were distributed under simplified conditions, without the usual banking security¹⁷⁸.

Precarious Household Budgets

The Egyptian government had reason to be concerned about social tensions. Wages and salaries for those still holding jobs have been stagnant, and prices for basic foodstuffs went up during the seven years to 1997: rice by 413 per cent, wheat by 360 per cent, meat and poultry by 250 per cent, beans by 210 per cent, edible oil by 608 per cent. Such data are only released after long delay by the statistical authorities because of their political sensitivity¹⁷⁹. The average monthly wage was estimated at LE 150 (\$45) in 1995, whereas one kilogram of meat cost LE 15. The average family spent 52 per cent of its budget on food, a figure which is 66 per cent for poor families with less than \$300 annually as compared to 32 per cent for households with an annual income of more than \$4 000. Clothing accounted for 9 per cent of family spending in the towns and 7 per cent in the villages, while housing was between 7 and 10 per cent. The government supplied large quantities of food to the domestic markets during the month of Ramadan to avoid price increases and political unrest. In addition to two kilograms of subsidised sugar¹⁸⁰ which 47 out of 60 million Egyptians were entitled to receive each month, the government supplied another half kilogram through the Ministry of Supplies.

The annual food subsidies amounted to \$738 million, mainly for sugar, edible oil, bread and flour. Subsidised bread was sold for 5 piasters (one third of its actual cost for the state)¹⁸¹. An enriched 10 piaster bread was introduced to offset the declining availability of the 5 piaster bread, to avoid open revolt of the poor as in the 1977 “bread riots” when the price had been raised from 1 to 2 piasters¹⁸². The Ministry of Supplies intervenes with large quantities of flour to reduce domestic prices. The flour market had been partly liberalised since 1992 and bakeries may buy directly from abroad without authorisation from the Ministry.

Social Fund

Husain al-Gamal, secretary general of the Social Fund, said that by December 1994 LE 1.2 billion had been disbursed for small-scale projects and various labour-intensive development programmes which reached 3 million people, creating 230 000 jobs, some temporary. In 1995–96 another 106 projects with financing of LE 762 million were envisaged¹⁸³. A special programme to promote the creation of small businesses by university graduates fell short of expectations due to the strict loan conditions and because implementation was assigned to local administrations and the labour unions, providing considerable scope for corruption and inefficiencies¹⁸⁴.

In addition, nine agreements were concluded with the National Bank of Egypt and other Egyptian banks for a total of LE 250 million to finance 7 500 small projects supposed to create 37 500 new jobs for university graduates¹⁸⁵.

Tariff Reductions

After debates among the foreign trade-oriented ministries and the business community, the Ministry of Finance proposed a reduction of the maximum tariff from 70 to 60 per cent, and a range of 80 to 100 per cent for imported automobiles. For 22 capital goods a tariff of 10 per cent was suggested (as compared to actual rates of 50-70 per cent)¹⁸⁶.

Partial Recovery of Tourism

Tourist receipts had reached more than \$3 billion before the terrorist assaults since 1992. In 1993 and 1994 they went down to \$1.3 and \$1.5 billion respectively. Some 930 people (including 12 western tourists) had been killed during clashes of the security forces with the Islamist groups (375 in 1995 alone)¹⁸⁷. In 1995 the number of visitors reached the level of 1992 again, although price reductions and shorter lengths of stay led to foreign exchange receipts of only two-thirds of the 1992 level¹⁸⁸.

Parliamentary Elections

On 27 November and 4 December 1995, the President's NDP (National Democratic Party) won a landslide 95 per cent victory in Egypt's first parliamentary elections in eight years. Most of the opposition parties had boycotted the previous election in 1990 because of unfair procedures. This time opposition newspapers accused the authorities of widespread electoral abuses, vote rigging, intimidation and harassment of opposition candidates. Before the election hundreds of members of the officially banned Muslim Brotherhood, who had hoped to stand as independents, were arrested and 54 prominent members were given three to five year jail sentences by a military court for unspecified illegal political activities¹⁸⁹. A number of administrative courts suspended results from nearly half of the constituencies because of pending law suits alleging fraud¹⁹⁰. Having survived an Islamist assassination attempt in Ethiopia in June 1995 and successfully expelled most of the Islamist militants from the main Egyptian cities and tourist sites, the president had become "ever more concerned with his government's position rather than risking instability and further violence by pursuing further reforms"¹⁹¹. Western donors and their parliaments concerned with human rights and good governance considered the country fairly democratic. On the eve of the poll President Mubarak asserted in a TV interview: "Any change after the parliamentary elections is not on the agenda... Too much change does not lend itself to stability"¹⁹².

A Meagre 1995 Record

The privatisation record continued to be poor. Minority stakes of state enterprises were sold on the stock exchange and to their employees. Progressive lowering of tariffs stopped at 70 per cent. A number of deregulatory laws concerning labour relations, company law, antitrust and foreign ownership of property were delayed. A third of the population was said to live under the poverty line, and there was no indication of any reduction of unemployment. The *de facto* fixed parity of the Egyptian pound against the dollar and an inflation differential with its main trading partners had caused the effective real exchange rate to appreciate by about 35 per cent over the past four years. The IMF kept insisting on a devaluation of at least 25 per cent, but President Mubarak kept ruling out any devaluation, and Minister for International Co-operation Youssef Boutros-Ghali echoed him, saying that reform had to be “an indigenous process, driven by local considerations and not processed by the outside world”¹⁹³. Many other bureaucratic and regulatory obstacles to private investment remained, estimated at only 10 per cent of GDP, with foreign direct investment amounting to less than 1 per cent of GDP¹⁹⁴.

1996: Renewed Reform Efforts

New Cabinet

Atif Sidqi and his cabinet resigned on 2 January 1996, partly to divert some of the public dissatisfaction after the irregularities of the elections. President Mubarak announced the change in government and declared that the new administration under Sidqi’s successor and former Vice Prime Minister Kamal al-Ghazouli “would prepare Egypt for the 21st century by raising standards of living and renewing the impetus of economic reform”¹⁹⁵. Appointed planning minister in 1984 and deputy prime minister in 1987, al-Ghazouli had been considered as a long-standing supporter of central planning and the public sector who only recently emerged as a supporter of the private sector. The new prime minister encouraged the entry of foreign investors, including multinationals with emphasis on exports in order to avoid competition with local manufacturers, and promised greater speed with regard to privatisation, starting with public-private joint ventures.

Reform of Rent Controls

In January 1996, the People’s Assembly abolished rent controls for all new tenancy agreements. The amendment to the old housing law did not apply to an estimated 95 per cent of the housing stock where rental agreements already exist, and at price levels of the 1950s. Agreements are often passed on to the tenants’ children. New tenants had to pay huge sums of key-money in the distorted market. Once settled,

they have a guaranteed lifetime's accommodation at nominal rents, for example, 20 or 30 pounds for luxury flats¹⁹⁶. Deregulation of the old housing stock would provoke a social upheaval. On the other hand, landlords were deterred from renting or let their occupied housing fall apart through lack of maintenance¹⁹⁷.

Euro-Mediterranean Free Trade Zone

During the fifth round of negotiations on Egypt's participation in the Euro-Mediterranean Free Trade Zone the EU maintained its position that agricultural products, including processed products, were to be excluded from an agreement. It should be limited to manufactured goods. The Egyptian side insisted that a balanced agreement would have to allow for annual exports of some 1.2 billion ECUs for products in which Egypt had a comparative advantage (e.g. fruits and vegetables). After all, its agricultural export strategy for the 1990s had been devised with the support of the World Bank. Egypt's imports from the EU amounted to \$4.1 billion in 1994 (i.e. 42 per cent of Egypt's total imports)¹⁹⁸. The EU is Egypt's major export market. Pressure on Egypt increased as a result of the customs union of the EU with Turkey, Egypt's main competitor for foreign investment and trade in the Mediterranean basin¹⁹⁹.

During the negotiations in Brussels in December 1996 the EU proposals on a free trade agreement were unacceptable to the Egyptian side. Faced with the protectionism of the European Common Agricultural Policy, Foreign Affairs State Secretary Gamal Bayoumi complained that the Commission even tried to exclude processed foodstuffs such as dairy products, cereals, sugar and meat from free trade. In 1996 Egyptian imports from the EU were 5 billion ECUs, while its exports to the EU were 2.3 billion ECUs. Egyptian potato exports in 1995 had reached 430 000 tons and had provoked an immediate reaction from European producers²⁰⁰.

Box 4.2. Obstacles to Egypt's Orange Exports

“In 1993, Egypt's total citrus production amounted to 1 626 100 tons. Only nine per cent of that was exported — 146 349 tons. While other countries invest vast amounts of capital growing produce specifically for export, Egypt contents itself with exporting whatever happens to be left over after the domestic market is done. The growers and exporters face myriad problems largely due to the lack of a coherent policy on the growth and export of the fruit. Yet despite all this, Egypt is the fourth-largest exporter of oranges in the world, following Spain, Israel and Morocco...According to Mostafa Ads, director of the export department at El-Wadi Company for Agricultural Exports, Egypt lags behind its competitors in regard to orange exports because of two main factors. One is the fact that Spain and Morocco are physically closer to the European markets. One source of Daltex, a private sector citrus-exporting company, believes that Egyptian oranges are of a lower quality. ‘European importers can get better-quality oranges at lower prices from Spain,’ he says.

The Egyptian orange export industry's problems really started with the collapse of the Soviet Union. ‘El-Wadi Company for Agricultural Exports was the sole orange exporter in Egypt between 1964 and 1986’, Ads says. ‘Most of our exports during that period went to the Soviet Union in return for weapons and other products.’ Scant attention was given to quality since, according to the deal between the two countries, the Soviet Union was obliged to accept the products sent no matter what their quality was. Annual exports of 200 000 tons went to the Soviet Union, while a total of 10 000 tons went to other Eastern European countries like Hungary and the former Czechoslovakia. Following the collapse of the Eastern European bloc, the period between 1991 and 1993 witnessed orange exports plummet from 200 000 tons to almost 150 000 tons... Dr. Gharib El-Banna, director of the General Union for Fruit Exporters, admits that although the government has opened the door for export, it has not coupled this with regulations for solving the existing problems. A national campaign against the fruit fly needs to be drawn up and put into effect. Emphasis on planting quality oranges should be stressed, while shipping must be subsidized. Tax incentives must be offered to exporters ... ‘What we need is to be more aware of what's going on in the world’ ”.

Source: Business Today, February 1997.

Trade Liberalisation

Customs duties were reduced by 10 per cent on a number of imported items in January 1996. Formerly, various products such as diesel pumps, ventilators and TV cameras were subject to the maximum duty of 70 per cent. Nevertheless, trade liberalisation was far behind schedule as indicated in the Letter of Intent²⁰¹. At a seminar on EU–Egyptian trade relations, EU Representative René Milas blamed the Egyptian side for non–tariff barriers on chemicals, particularly detergents via admission procedures and norms incompatible with the envisaged Euro–Mediterranean Free Trade Zone²⁰². They were impeding local production in factories of multinationals.

Agriculture, Water and Food Security

Rising international wheat prices in 1994 and 1995 raised Egyptian concerns about the need for greater self–sufficiency. Some 6 million tons of wheat and flour were being imported annually. The prime minister set a self–sufficiency target of 70 per cent for wheat, partly to be achieved through irrigation of 1.6 million feddans²⁰³ of new desert lands. Egypt’s water needs are almost exclusively supplied by the Nile. Agriculture can use water cost free. Rates for drinking water in towns do not cover their costs, and a lot of water is being wasted. However, the crucial issue of water prices was not addressed²⁰⁴.

Danger of Social Destabilisation

In his opening speech to the newly elected parliament President Mubarak stated that Egypt’s GDP would grow by 8 per cent per annum until the year 2000, 700 000 new jobs would be created each year, bureaucratic hurdles for private foreign investment would be reduced, and economic reforms would not burden the vulnerable poor. Former minister of industry and director of the National Investment Authority, Ibrahim Fawzi, warned that a reduction of surplus employment in the public sector would lead to political destabilisation. “A further turning away from our public sector heritage is absolutely necessary, but it must be socially acceptable and intelligible for the people”²⁰⁵.

Internal security remained precarious. Since the beginning of 1996, 23 people had been killed in clashes with fundamentalists in the town of Assiut in Upper Egypt, a centre of Islamist resistance²⁰⁶. Seventeen Greek tourists and an Egyptian were shot dead by Muslim militants, and another 15, mostly Greek, were wounded near the pyramids on 16 April 1996, dealing a blow to the tourist industry²⁰⁷. A few days earlier, the security forces had arrested 245 suspected Islamist terrorists²⁰⁸.

Delays of cuts in subsidies impeded the ongoing negotiations with the IMF on the approval of the third instalment of debt relief by the Paris Club covering \$4 billion in debt²⁰⁹.

President Mubarak Promotes Privatisation

In 1996, for the first time the president clearly spoke out in favour of privatisation “to save the economy from the debt problem in the state enterprises, the only alternative being increasing public debts and taxation which would mean bankruptcy and economic decay”²¹⁰. Until then President Mubarak had supported the reforms, but had avoided addressing the privatisation issue. The IMF continued to press for more rapid privatisation (linked with the third instalment of debt relief by the Paris Club), and asked for amendments to the private foreign investment laws²¹¹.

Chirac in Egypt

French President Chirac met with President Mubarak during a state visit to Egypt in April 1996. He called for an increased European Union role in the Middle East peace process, which was not welcomed by the United States and immediately rejected by Israel²¹², and a larger European commitment to building a Euro–Mediterranean partnership²¹³. At the end of a second Middle East tour by President Chirac to Syria, Israel, the Palestinian Territories, Jordan and Egypt in October 1996, at a joint press conference with the French leader, President Mubarak observed that the United States played the main role in the peace process, Europe being secondary²¹⁴.

New Reform Package

In July 1996 Egypt and the IMF agreed in principle on an economic policy reform package after four rounds of talks under way since March. The IMF’s first review of the 1993 Extended Fund Facility had reached an impasse in July 1994 as the government refused again to devalue the pound. Talks resumed in March 1996 with the understanding that devaluation was off the agenda. Instead of attempting to review the old Extended Fund Facility, the two sides focused on a new programme. The government was keen to secure an agreement to pave the way for the Paris Club to write off the third and final instalment of debt. Before an agreement with the IMF was finalised President Mubarak made a four–day visit to Washington and discussed the Middle East peace process and US–Egyptian relations²¹⁵. Meanwhile, in July 1996 the prime minister announced that an additional 39 state enterprises with a total value of \$1 billion would be privatised before the end of the year. The new cabinet had accelerated privatisation, and for the first time majority stakes in state companies were sold²¹⁶.

IMF Stand-by Credit Agreement

Egypt and the IMF signed an agreement on 11 October 1996 for a 24-month stand-by credit, which would enable the Paris Club to approve the third instalment of Egypt's debt relief. The agreement involved further trade liberalisation, deregulation, development of financial markets, and modernisation of the budgetary structure. A final barrier to the ratification of the agreement had been removed by implementing across-the-board tariff cuts of up to 25 per cent. The maximum tariff on goods (other than luxuries) was reduced from 70 to 55 per cent. It was unlikely that Egypt would draw on the stand-by credit of 270 million SDRs (\$400 million) in view of its accumulated foreign reserves of \$18 billion.

The programme envisaged raising domestic savings and increasing the competitiveness of the economy through a more investment-friendly environment, particularly for foreign direct investment and technology, to be supported by a new investment law and additional incentives. Ninety-one state enterprises with a total value of LE 18 billion were to be privatised. Tariffs were to be reduced further, with another 15 per cent cut in the maximum rate. Income taxes were to be reduced and the tax system was to be broadened and made more transparent. No additional price increases were called for, but the civil service was to be reduced by 2 per cent. The Social Fund was to provide \$200 million for severance and compensation measures, retraining and redeployment. The programme was to be reviewed quarterly. IMF representative Arvind Subramanian in Cairo commented: "It is a home-grown program to address fundamental issues in Egypt"²¹⁷.

Food Security and Dependence on the United States

In order to avoid mass riots as in 1977, the government replaced 20 per cent of the staple wheat flour bread with cheaper corn flour to freeze wheat imports at the current level of 6.5 million tons a year at a cost of more than \$1 billion, mainly from the United States (5.2 million tons), thus creating a critical dependence on US supplies. The savings for the government were estimated at an annual \$220 million. Without subsidies, consumers would pay 14 piasters (5 US cents) for a loaf instead of 5 piasters. Current wheat production was 5.5 million tons. Egypt still had to import more than half of its total food requirements at a cost of some \$4 billion a year²¹⁸. Prime Minister al-Ghazouli had set an objective of producing 18 million tons of cereals in 1996 and increasing this figure by 3.5 per cent per annum²¹⁹.

Continuing Data Problems

International Business & Technical Consultants Inc. in charge of monitoring and evaluation of Egyptian privatisation activities (as part of the USAID Privatization Project) stated "that a large amount of current important data and information is not

available. This data covers a wide scope from the private sector's share in investment and trade, to the unemployment rate and average wage rates in the different main sectors of the Egyptian economy. Despite the importance of this data, very few attempts were actually carried out to obtain for policy makers and other parties these important sets of data. Thus, our analyses are based on partial and incomplete data in an attempt to discuss trends and identify important policy issues²²⁰.

Savings

In its 1996 annual report the Central Bank of Egypt published domestic savings rates: 17 per cent for 1991–92, 16.7 per cent for 1992–93, 15.1 per cent for 1993–94, and 16.9 per cent for 1994–95. The domestic investment rates amounted to 19.8, 19.6, 20.3 and 19.2 per cent for the four fiscal years respectively. Domestic savings financed some 85 per cent of domestic investments. Both the savings and investment rates were “considered low in comparison to other developing countries”²²¹.

Of total national savings, 43 per cent came from private households, 23 per cent from government savings, 16 per cent from private business, 10 per cent from the public enterprise sector, and 8 per cent from the financial sector²²². Between 1991 and 1996, the ratio of private business savings to GNP was only 3.1 per cent on average²²³.

Foreign Direct Investment

If Egypt wants to realise its targeted investment of LE 100 billion per year, then half of this volume must come from foreign capital inflows. Foreign direct investment increased from an annual average of \$650 million during 1981–92, to \$800 million in 1996. The government announced the abolition of approval requirements for all foreign direct investment projects. In most cases, foreign investors were opting for a joint venture with an Egyptian partner²²⁴.

Real Exchange Rate

International reserves allowed Egypt to defend the nominal exchange rate of LE 3.40 per dollar. However, due to the higher Egyptian inflation rate, compared to the inflation rates of its major trading partners, the real exchange rate had appreciated by 35 per cent since 1991. “This overvaluation in the Egyptian pound has an adverse effect on Egypt's competitiveness in the international market”²²⁵.

Trade Balance

Egypt's international trade performance continued to be a worrying issue. The trade deficit was mainly due to the simultaneous decrease of exports and increase of imports and resulted in a trade deficit of \$9.4 billion in the 12-month period from August 1995 to July 1996. Government measures to stimulate exports were not effective in raising their level and regaining some of the markets that had been lost mainly in Central and Eastern Europe²²⁶. "It is safe to expect that the trade deficit will continue to worsen or at best not to improve. This is due to the continuous rise in imports following trade openness and reform coupled by the poor performance of exports especially in non-oil exports"²²⁷.

Domestic Debt

The main tool of tight monetary policy since 1991 has been issuing treasury bills to finance the budget deficit. This monetary policy succeeded in diminishing monetary growth to 11 per cent in 1995-96, down from 30 per cent in early 1991. However, it increased domestic debt which had reached LE 150.4 billion in June and LE 152 billion in September 1996, with an increase of 9.2 per cent during the previous year²²⁸. It included the government's debt to the National Investment Bank financing public sector companies, soft loans to low income housing, and interest payments on treasury bills of LE 26 billion²²⁹.

External Debt

By the end of 1996 Egypt's external debt had reached a level of \$31 billion, \$1.9 billion less than in 1995. The ratio of debt to GDP decreased from 74 per cent in 1992 to 47 per cent in 1996. Debt to the Paris Club amounted to \$25.2 billion by June 1996, representing 81 per cent of the total. Of this amount, about 65 per cent was due to four countries, the United States, France, Germany, and Japan. Debt service amounted to \$412.1 million, compared to \$572 million in 1992²³⁰.

Financial Sector Reforms

The Egyptian financial sector had been a key target of reform initiatives. Various instruments such as treasury bills had enlarged the financial market and increased its liquidity. In October 1996, treasury bonds were issued worth LE 4 billion and a coupon rate of 11 per cent. Since financial institutions, firms, and individuals had subscribed for LE 10 billion, the Central Bank dealt with this oversubscription by allocating to each bidder only 39.5 per cent of his requested total. As to the basic monetary indicators, the USAID Privatization Project reiterated that "it should be noted that a large amount of current important data and information is not available"²³¹.

Macroeconomic Indicators

GDP at factor cost increased by 4.8 per cent in FY 1995–96, compared to 4.6 per cent in FY 1994–95. The private sector grew at 5.9 per cent and increased its share in GDP to 63 per cent²³². The exchange rate remained stable at LE 3.40 to 3.41 per US dollar²³³. Inflation declined to 5.4 per cent in December 1996²³⁴. The IMF no longer insisted on the devaluation of the pound. Central Bank reserves amounted to \$18 billion. The lending interest rate rose from 11.25 per cent in April 1996 to 12.25 per cent in December, whereas the rate on treasury bills declined from 10.27 to 10.1 per cent in line with the lower inflation rate and the government's aim to promote private investment²³⁵. The discount rate was reduced by the Central Bank from 13.5 per cent in October 1996 to 13.25 per cent in November, 13 per cent in December, and 12.75 per cent in March 1997. Interest rates on loans and deposits reached their lowest level since the beginning of the reform programme. In the past, the government had wanted interest rates to be higher than 10 per cent in order to attract capital flows, but with substantial capital inflows and the upward pressure on the pound the government felt that the interest rate could be allowed to drop to around 9 per cent without endangering the differential between rates for the Egyptian pound and the US dollar. The interest rates on dollar deposits amounted to 5 per cent. Lower interest rates were to increase investments and GDP growth, but were not expected to fall below 9 per cent due to low inflation and the high demand for capital driven by foreign participation in the portfolio market.

The government announced that it would also issue long-term treasury bonds during fiscal year 1996–97 as a part of its sterilisation policy²³⁶.

1997: Problems of Implementation

Macroeconomic Indicators

Foreign exchange reserves increased to \$19.4 billion by the end of February 1997, representing over 26 per cent of Egypt's \$75 billion GDP. The trade deficit decreased from \$2.79 billion in the first quarter of fiscal year 1996–97, to \$2.69 billion in the second quarter, as export proceeds increased from \$1.16 to \$1.22 billion, and imports declined from \$3.9 to \$3.8 billion. Despite the trade deficit, the balance of payments showed a surplus, rising to \$705 million for the second quarter of fiscal year 1996–97. Net foreign assets within the banking system increased to LE 143 billion²³⁷. Consumer price inflation declined to 5.5 per cent in March 1997 as compared to 7.6 per cent in August 1996²³⁸.

Egypt's Sovereign Rating

After having received a sovereign rating of Ba2 for long-term foreign currency bonds and notes of issuers domiciled in Egypt, and a Ba3 for long-term foreign currency-denominated bank deposits in October 1996, Egypt was assigned a BBB rating for long-term debts denominated in foreign currencies by Standard & Poor's in January 1997. It was also assigned an A2 rating for Egyptian treasury bills and bonds and A3 for short-term debts denominated in foreign currency²³⁹.

The ratings were positively affected by the macroeconomic reforms concerning trade liberalisation and fiscal policy, and central bank reserves of \$19 billion. They were negatively affected by Egypt's low per capita income, persistent unemployment, the high domestic debt burden (53 per cent of GDP in 1996-97), the weak financial sector, the poor social infrastructure, and the relatively low level of domestic savings (17 per cent of GDP)²⁴⁰ which failed to reach the 7 per cent GNP growth target set by the government.

The low levels of savings and investment "can primarily be attributed to the small number of profitable areas in the economy in which to invest, the small number of financial products in which to invest, and the inefficiency with which Egypt's financial institutions intermediate funds"²⁴¹. Thomson's drew attention to the "overvaluation of currency, the overstuffed public sector, persistent bureaucratic problems which explain the slow private and foreign investments in Egypt compared to other emerging markets, high unemployment rates, and fears from the violence of some Islamic elements which adversely affect tourism as well as the confidence of investors..."²⁴². According to Standard & Poor's, "fundamentalist trends are expected to continue"²⁴³.

Precarious Social Flank

Whereas the dialogue between organised labour and the government led to a limited consensus on an Early Retirement Scheme and other compensations, although still considered to be insufficient, "a more important source of anxiety for the government is the unorganised or 'random' labour force and unemployed educated youth. Because of their relatively low skill level and the recessionary conditions which have prevailed throughout the period of economic stabilisation, workers in the first group are barely at the subsistence level and have little expectation for the future. In addition, while they and their older relatives were always aware that they were poor, they are increasingly becoming aware of just how poor they are"²⁴⁴. The visible disparity in income and wealth has contributed to the alienation.

As Samir Radwan of the International Labour Organisation stated in June 1997, the Egyptian economy had been generating only an average of 370 000 jobs a year over the 1990s when it needed 500 000. "95.5 per cent of the unemployed are first-

time job seekers, who wait an average of three and a half years for a position... Real wages stood in 1995 at just two-thirds of their level in 1982... Income disparity is increasing”²⁴⁵.

Unemployed educated youth still “hold middle class expectations of marriage, their own apartment and a guaranteed job after graduation. These dreams are not seen as postponed, but rather as shattered”²⁴⁶. In 1993, the Cabinet Information and Decision Centre estimated the unemployment rate at 20 per cent, with three quarters of the unemployed 16–25 years old, and with 84 per cent of these youths holding a secondary school certificate or higher degrees²⁴⁷.

Liberalisation of Land Rents

On 1 October 1997 the controversial Land Law 96/1992 came into effect, revolutionising the relationship between landowners and tenant farmers. From 1952 to 1992, land rents were locked at seven times the land tax, which averaged LE 30 to LE 35 annually per feddan. Land rents did not increase between 1952 and 1975, despite the fact that taxes were increased because tenant farmers paid seven times the 1952 taxed amount. A 1975 decision, however, stated that rents would increase in proportion with taxes.

In 1992, the parliament decreed that by October 1997 the rent control system would be terminated. Law 96/1992 ordained that between 1992 and 1 October 1997, rents be increased to 22 times the amount of tax paid by the landowner, leaving it up to the owner and tenant to agree on new rents after that. The new rents will be enforced by civil laws and the police.

On 1 July, a 1996 decree from the Ministry of Agriculture came into effect which required tenant farmers to turn in their old contracts. The decree also stipulated that the local offices issue new titles to landowners that prove their ownership and specify their rights by 6 October. Without these papers, it will be difficult for landowners to convince a civil court to evict a reluctant farmer. “Opposition groups estimate that over 1 million farmers and their families will be directly affected by the new law”²⁴⁸.

New Labour Law

The new labour law has been under discussion for three years, initiated with the assistance of the International Labour Organisation in order to introduce a modern labour law supportive of Egypt’s transition to a market economy and consistent with international standards of workers’ rights. The law is to legalise the dismissal of workers, and to provide the right to strike — against resistance of the business community. The draft received judicial approval by the State Council and still has to pass the Cabinet and the People’s Assembly.

Box 4.3. Rural Unrest

“In anticipation of unrest Egyptian security services have developed reinforcements in Upper Egypt. Hundreds of army conscripts have beefed up police units in the southern provinces of Minya, Beni Suef and Assiut, where security forces are on alert throughout the villages... Since June, tension in rural Egypt has been mounting, and there have been violent clashes and sporadic arrests of both tenant farmers and peasant advocates in 10 governorates... According to the Land Center, 822 people have been detained by the police, 15 have been killed in clashes and 218 injured between 1 January and mid–August. Most incidents of violence and clashes with the police took place in early July, when tenant farmers tried to burn down the local offices of the Ministry of Agriculture.”

Source: Middle East Times, 3–9 October 1997. See also Al Ahram Weekly, 10–16 July 1997.

1997–98 Budget

The 1997–98 budget was approved by the People’s Assembly in April 1997, with a total figure of LE 83.3 billion, up 7 per cent from the 1996–97 figure of LE 77.5 billion. Expenditure was forecast at LE 77.5 billion, including LE 29.8 billion directed to social services, and LE 25.1 billion to salaries and pensions. Government expenditure was to be reduced by 6 per cent to reach an annual increase of 8 per cent. Minister of Finance Mohie al–Din al–Gharib commented that the budget reflected insistence on rationalisation and fiscal stability. He added that the government wanted price stability and continuity of subsidies to the vital services. The ministry decided to review the finances of public sector authorities on a daily basis, and to take appropriate decisions if expenditures increased above defined limits. LE 4 billion was to be directed to loss–making companies, and LE 6 billion to support the governmental General Authorities²⁴⁹. Prime Minister al–Ghazouli stated that there would be no new taxes imposed in 1997–98.

Five Year Plan

According to al–Ghazouli in his Five Year Plan statement to the People’s Assembly on 26 April 1997, real GDP growth was projected at 5.7 per cent for fiscal year 1997–98. The government target for the next Five Year Plan 1997/98–2002/03 was an average annual GDP growth of 7 per cent and the creation of 2.5 million jobs, starting with 500 000 jobs in 1997–98. The Prime Minister stated that the investment target totalled LE 58 billion, 60 per cent of which was expected from the private sector. Total investment between 1997 and 2002 was supposed to be LE 375 billion. Over the

next five years, fiscal deficits were expected to average 1 per cent of GDP, excluding privatisation revenues. The government's principal policy objectives were to reduce the budget deficit, to raise domestic savings, reduce the public debt burden and maintain monetary and exchange rate stability to support investor confidence and the inflow of foreign capital²⁵⁰.

New Investment Guarantees and Incentive Law

In May 1997 a new Investment Law (Law 8/1997) was passed by the People's Assembly and signed by the President after a long period of discussion and protests from the business community. The new law provides greater incentives for priority investment sectors such as infrastructure, automobile parts, software, oil field services, tourism and manufacturing, and longer tax holidays for projects in selected regions. Small and medium scale enterprises are being encouraged, and incentives will be given to exporters. Production and foreign direct investment are to be increased by streamlining administrative procedures.

New investment guarantees include that enterprises must not be nationalised, placed under custody, or confiscated. No administrative agency may interfere in the pricing of company products, or determine their profit. Companies may own the construction and land necessary for their activities, regardless of the nationality of the owners, the place of their residence, or their share of ownership. In addition, projects under the Social Fund for Development will enjoy a ten year tax exemption. Projects outside the old Nile valley will have a 20 year tax holiday²⁵¹.

New Privatisation Guidance

The government issued new guidance for the privatisation programme. Profitable companies are to be sold first, especially the joint-venture companies. The second priority goes to companies which only need financial restructuring. Technical aspects of restructuring and any new investment in companies nominated for sale will be left to the new buyers. However, current management is in charge of maintenance of the plants. It is recognised that substantial assets will remain within the public sector for some time to come, including industries considered to be strategic (where the government will retain 60 per cent ownership), and companies for which the government is still seeking alternatives to liquidation. "The success of the privatisation programme rests largely on the government's ability to secure strategic investors for public sector industries slated for sale, senior government officials say"²⁵².

Any use of proceeds of past divestitures and asset sales for restructuring activities as well as withdrawals from the holding companies' accounts require the signature of the Minister of Finance and the approval of the Cabinet Committee on Privatisation. The guidance clearly reaffirms the responsibility of the holding companies to sell their affiliated companies, eventually to be supported by experienced consultants²⁵³.

Prudential Regulation

The Capital Markets Authority had advised the adoption of several initiatives in 1996 which had not been implemented, especially to use international best practices of auditing and accounting. It also raised the capital adequacy requirements for new firms.

After considerable irregularities and insider trading, brokerage firms were advised to adopt a code of ethics, to upgrade training of existing brokers, and to develop the professional credentials and capabilities to warrant public trust. Initial public offerings, for example, had been approved utilising only an advertisement as a prospectus²⁵⁴. Trading of shares was impeded by delays of ownership transfer up to 35 days²⁵⁵.

Anti-trust Law

The Ministry of Supply and Trade drafted an Anti-trust Law to close the legislative gap as to the promotion of a competitive free market system. The new law defines monopoly as the practice enabling one company, or a group of companies, to corner at least 30 per cent of the trading of a certain commodity in the local market. An Anti-trust and Competition Protection Council (ACPC) is to be established to oversee the licensing of mergers. A number of mergers took place in the first half of 1997.

The British company Cadbury bought the Food Industries Development Company, and as a result, cornered 25 per cent of the sweets market. Switzerland's Nestlé purchased an ice-cream factory in the city of Qualioub from the Groppi company and acquired 75 per cent of the Egyptian ice-cream market. On the securities market, similar buyouts and mergers had taken place. The Egyptian Financial Group (EFG) and the Hermes group merged to form a major brokerage house that controls almost 32 per cent of the secondary trading market on the Cairo exchange²⁵⁶.

Egyptian Eurobonds

The Minister of Finance Mohie al-Din al-Gharib announced that the government will issue five-year Eurobonds for the amount of \$300 million at the London stock exchange in order to motivate Egyptian companies to raise debt-equity funds in the Euromarket at moderate rates given the benchmark established by the government. Holding Central Bank reserves of over \$19 billion, the government has sufficient credibility to borrow from the international markets as Egypt's ratio of debt service to exports fell to 13 per cent, compared to 23 per cent in 1991. The main target was to boost the Egyptian financial market through developing the relationship between the Egyptian private sector and the international equity market.

The issuance of Eurobonds was supposed to help to close the gap between domestic savings and investment. To increase GDP at a rate of 7 per cent, annual investment of \$7 billion is required to cover the savings gap. With its foreign investment level at \$2 billion, Egypt still needs \$5 billion, hopefully to be financed through the private sector in the international market²⁵⁷.

Interest Rate

The Central Bank reduced its discount rate from 13.5 per cent in October 1996 to 13.25 per cent in November, to 13 per cent in December, 12.75 per cent in March 1997 and 12.25 per cent in May the same year. The government continued to cut interest rates gradually in order to reduce the cost of borrowing, and thus to encourage direct investment and to protect the pound against appreciation. The decline of the discount rate was followed by a reduction of interest rates on loans and deposits, reaching their lowest level since the beginning of the reform programme. In the past, the government wanted interest rates to be higher than 9 per cent in order to attract capital flows. Meanwhile, capital inflows had reached a satisfactory level, and in order to avoid the eventual upward pressure on the pound, interest rates were allowed to drop. Between November 1996 and June 1997, lending rates fell from 12.25 to 10.75 per cent, deposit rates from 10.25 to 8.75 per cent, and rates on treasury bills from 10.17 to 8.9 per cent. The current level of interest rates was still not so low that it would restrict capital inflows. The interest rate on dollar deposits amounted to 5.3 per cent. The Central Bank announced that it would issue long-term treasury bonds in fiscal year 1997–98, to curb inflation.

Exchange Rate

While the IMF was no longer demanding depreciation of the pound, the government pledged to fight any appreciation of the currency, under pressure due to the high level of capital inflows. The nominal exchange rate was kept stable at 3.40 LE per US dollar from October 1996 to June 1997. The government considered stability of the exchange rate as a significant factor in attracting foreign capital. Central Bank reserves amounted to \$19.2 billion²⁵⁸.

New Minister of Economy

In July 1997 Youssef Boutros-Ghali was appointed Minister of Economy. For the past decade he had been carrying out support roles, first as advisor to the prime minister and then as minister of state. As a former IMF staff member, he had built up a reputation in the international donor community as a highly competent and eloquent advocate of the reform programme²⁵⁹. Boutros-Ghali represents a new generation of Egyptian administrators. Shortly before his appointment, he said in London: “What

we are trying to achieve is a change in governance. We must change the concept of the state from that of a predator to that of a mediator or a facilitator. People should react to market forces, not to administrative fear... The regulatory system must work in a predictable way”²⁶⁰.

Islamist Terrorism

On 18 April 1996, 18 Greek tourists were killed at the entrance of a Cairo hotel after being mistaken for Israelis²⁶¹. In September 1997 nine German holidaymakers and their Egyptian driver were killed by an Islamist attack on a tourist bus in downtown Cairo. On 13 October 1997 near the town of Mallawi, in a co-ordinated operation, gunmen stopped several taxis and killed all passengers they found carrying police documents. Eleven men died.

On 17 November 1997 58 foreign tourists were killed in an Islamist assault in Luxor’s Valley of the Queens. President Mubarak visited the area the following day, and fired his Interior Minister Hassan al-Alfi and a number of high ranking administrators. The massacre had a severe impact on Egypt’s tourism. So far, almost 4 million tourists had visited Egypt in 1997, generating some \$3.2 billion in revenues²⁶².

Box 4 4. Police Action against Islamist Militants

“Around 1 000 police, including anti-terrorist squads and special forces, launched a massive man-hunt in Egypt on 14 October for Islamic militants suspected of carrying out the bloodiest attacks against the police in five years. More than 100 armoured vehicles, trucks and police vans formed a five-kilometre convoy from Minya to the towns of Abu Qurqas and Mallawi. They were heading toward cornfields and other plantations in the area where the nine hunted gunmen were believed to be hiding. Nine policemen and two civilians were killed in cold blood on 13 October in simultaneous attacks near Abu Qurqas and Mallawi in the governorate of Minya, some 250 kilometers south of Cairo. Witnesses said the gunmen, some wearing police uniforms, set up roadblocks on rural roads, stopped cars, checked the identities of passengers and picked out nine policemen, whom they shot dead after binding their hands and feet.”

Source: Middle East Times, 17–23 October 1997.

Notes

1. “From 1988 to 1990 there was a continuous stream of IMF missions to Cairo with agreements repeatedly ‘about to be signed’, yet never actually finalized.” Cf. Richards, 1991. See also Lafay and Lecaillon, 1993.
2. *Égypte/Monde Arabe*, 1, 1990.
3. *Ibid.*
4. *Ibid.*
5. *Ibid.*
6. A portion of the aid financed the delivery of helicopters and missiles. Furthermore, in March 1990 Egypt signed an agreement with the Pentagon for the purchase of the parts for 555 M1 tanks to be assembled in Egypt, and for two submarines. Cf. *Égypte/Monde Arabe*, 1, 1990.
7. Boutros–Ghali, 1991.
8. Cf. Richards, 1991: “The government created ministerial committees with overlapping jurisdictions to confuse outsiders — no one knew who was really in charge (if, indeed, anyone was). This tactic had the further advantage of permitting the government to continue to be all things to all people, by having different actors making diametrically opposing statements. Thus, for example, in the spring of 1990 there were (at least) two different interministerial committees in charge of privatisation, one headed by an advocate and one by an opponent of such a policy! Finally, World Bank and IMF teams often met with a GOE (Government of Egypt) negotiating team composed of four to five ministers, all of whom disagreed with each other; the composition of the team often changed from day to day as ‘important business’ took one member away, leading to his temporary replacement with someone else. Such tactics helped to postpone a break with the IMF, buying time for Mr. Mubarak.”
9. *Égypte/Monde Arabe*, 2, 1990.
10. 1 feddan = 0.42 ha.
11. *Égypte/Monde Arabe*, 3, 1990.

12. The latter had been founded to create local and regional employment and to supply basic necessities to the people. The sale of economically viable public enterprises under the Governorates proceeded relatively quickly. Difficulties arose when enterprises were operating at a loss.
13. *Égypte/Monde Arabe*, 2, 1990.
14. Posusney, 1996.
15. *Égypte/Monde Arabe*, 2, 1990.
16. *Financial Times*, 4 April, 1990.
17. *Égypte/Monde Arabe*, 2, 1990. 100 piasters = 1 Egyptian pound.
18. *Égypte/Monde Arabe*, 3, 1990.
19. *Égypte/Monde Arabe*, 2, 1990.
20. *Ibid.*
21. *Financial Times*, 4 April, 1990.
22. Farag, 1990.
23. *Égypte/Monde Arabe*, 4, 1990. *Al Ahram Weekly*, 4 July 1991.
24. *Financial Times*, 24 June 1991.
25. *Égypte/Monde Arabe*, 5, 1991.
26. Posusney, 1996.
27. *Égypte/Monde Arabe*, 5, 1991.
28. The unions demanded that public companies should be given a chance to become competitive. The General Union of Engineering and Electrical Industries with 200 000 members argued in favour of a transformation of loans from public banks into bank participation (debt–equity swaps). The Textile Union called for higher minimum wages and the inclusion of seasonal and social bonuses in basic wages, and also for three–year instead of two–year mandates for the boards of directors in public companies, for management freedom from state intervention, participation of the labour union in setting company objectives, and respect of decisions taken in joint management–labour union commissions. The president of the General Labour Union of Egypt, also heading the Union of Chemical Industries and vice–president of the Senate, held that a report of the latter on the liberalisation issue “was dictated by foreign powers” and contrary to the interests of Egyptian society. He condemned the elimination of the previous obligation of firms to distribute 10 per cent of the profits to their employees, the abolition of the government’s right to set prices, and dismissals in public companies and administration. Wages and bonuses should be subject to negotiations between management and labour union for each company in line with its profitability. Strikes should be avoided in favour of negotiations and mediation. Cf. *Égypte/Monde Arabe*, 5, 1991; Posusney, 1996.
29. Posusney, 1996.

30. *Égypte/Monde Arabe*, 5, 1991.
31. Egypt has some 3 million civil servants, and 1 million employees in the public sector; cf. *Égypte/Monde Arabe*, 5, 1991.
32. *Al Ahram Weekly*, 30 January 1992; *Al Ahram Weekly*, 23–29 April 1992.
33. *Égypte/Monde Arabe*, 5, 1991.
34. *Égypte/Monde Arabe*, 4, 1990. Private savings of Egyptians abroad were estimated at \$83 billion in 1991, amounting to 271 per cent of GDP, relatively much higher than in other developing countries and in neighbouring Arab countries. Cf. *Égypte/Monde Arabe*, 17, 1994.
35. Until February 1991, there had still been a primary foreign currency market supplied by government exports of crude oil, rice, raw cotton, receipts from the Suez Canal and the SUMED (Suez–Red Sea–Mediterranean) oil pipeline, and the loans and grants of foreign governments. These foreign exchange assets were used to pay for public expenditure abroad, including Egypt’s debt service. A secondary foreign currency market included all other transactions including tourism, and was operated according to supply and demand. Foreign residents were allowed to hold foreign exchange deposits and to make payments abroad. Cf. *Égypte/Monde Arabe*, 5, 1991.
36. Even the entrepreneurs of the new city of Tenth of Ramadan, usually considered to be the most dynamic ones in the country, expressed worries about the effects of import liberalisation on Egyptian industry. Minister of Industry Mohammed Abd al–Wahab reassured them early in 1991 that protection would be maintained through tariff barriers and quality control. Cf. *Égypte/Monde Arabe*, 5, 1991.
37. *Égypte/Monde Arabe*, 5, 1991.
38. *Ibid.*
39. *Ibid.*
40. *Ibid.*
41. Its factories had the monopoly on production of and exports of yarn, when imports were prohibited. The General Organisation of Textiles was blamed for having caused the disaster by price increases, whereas its president Said Damuch justified the price increases by the rising prices of local cotton, the directive of the government to export certain quantities of yarn to earn foreign exchange, and by the adjustment of local prices to world levels as required by the international donor organisations. In addition, taxes, electricity costs, interest rates, and the cost of social insurance and of a number of services of the Ministry of Labour had increased. As a result, the traditional small and medium–sized textile sector largely disappeared. A representative of the surviving enterprises complained that the official discourse on the promotion of the private sector was in complete contradiction with real economic policy. Cf. *Égypte/Monde Arabe*, 5, 1991.
42. *Égypte/Monde Arabe*, 5, 1991.
43. *Financial Times*, 11 April 1991.
44. *Nachrichten für den Außenhandel*, 22 July 1991.

45. *Égypte/Monde Arabe*, 6, 1991.
46. *Al Ahram Weekly*, 29 August 1991.
47. *Égypte/Monde Arabe*, 26, 1996.
48. *Nachrichten für den Außenhandel*, 2 July 1991.
49. Ten products were exempted, another 35 products taxed at rates between 5.2 and 30 per cent.
50. *Nachrichten für den Außenhandel*, 15 May 1991.
51. The previous consumption tax had only been imposed on 124 goods and 40 services.
52. *Égypte/Monde Arabe*, 6, 1991.
53. *Égypte/Monde Arabe*, 7, 1991.
54. *Égypte/Monde Arabe*, 6, 1991.
55. Members are: the United States, Canada, United Kingdom, France, Germany, the Netherlands, Belgium, Switzerland, Italy, Spain, Denmark, Norway, Sweden, Finland, Australia, Japan, South Korea, Oman, Bahrein, Kuwait, Qatar, Saudi Arabia, the Arab Fund for Economic and Social Development, the Saudi Fund for Development, the Abu Dhabi Fund, the Kuwait Fund for Development, the Gulf Co-operation Council, the Arab Monetary Fund, the World Bank, UNICEF, the OPEC Fund, the International Fund of Agricultural Development, and the European Investment Bank.
56. *Al Ahram Weekly*, 11 July 1991.
57. *Financial Times*, 11 July 1991.
58. *Égypte/Monde Arabe*, 7, 1991.
59. *Ibid.*
60. *Ibid.*
61. Glosauer, 1991.
62. The Egyptian General Petroleum Corporation was only entitled to keep its foreign exchange earnings as far as it needed them for its own imports, whereas exporters of cotton and rice had to deliver their foreign currency receipts to the Central Bank in exchange for Egyptian pounds.
63. *Al Ahram Weekly*, 15 August 1991.
64. *Égypte/Monde Arabe*, 8, 1991.
65. Delaunay, 1992.
66. *Ibid.*

67. On the other hand, the Egyptian market offers unusual profits. It is not saturated, and high returns on investment can be realised. Labour costs one-third those of Tunisia, and one-fourth those of Morocco. Labour costs in Egypt make up 10 per cent of total costs, as compared to 45 to 50 per cent in France. One can sell with a gross profit margin of 20 to 30 per cent and often up to 150 per cent. *Ibid.*
68. Delaunay, 1992.
69. *Égypte/Monde Arabe*, 10, 1992.
70. The structural adjustment loan had been approved by the World Bank in June 1991, but had only been signed on 22 October 1991, the delay of three months being due to a debate on various benchmarks. *Nachrichten für den Außenhandel*, 4 November 1991.
71. Caio Koch-Weser, the World Bank's vice president, made it clear that state enterprise reforms and privatisation measures were "progressing slower than expected and that the delays in the implementation of the Social Fund for Development, established to help alleviate the burden of the reforms on the low-income and displaced labour, were threatening to have adverse effects on the ability to implement the reform measures". Cf. *Al Ahram Weekly*, 30 January 1992.
72. *Égypte/Monde Arabe*, 10, 1992.
73. *Ibid.*
74. *Ibid.*
75. *Al Ahram Weekly*, 14–20 May 1992; *Al Ahram Weekly*, 21–27 May 1992.
76. *Égypte/Monde Arabe*, 11, 1992.
77. *Ibid.*
78. *Ibid.*
79. *Al Ahram Weekly*, 28 May–3 June 1992.
80. *Égypte/Monde Arabe*, 11, 1992.
81. *Ibid.*
82. *Égypte/Monde Arabe*, 11, 1992.
83. 1 feddan = 0.42 ha.
84. *Al Ahram Weekly*, 4–10 June 1992; *Al Ahram Weekly*, 25 June–1 July 1992.
85. The list included various electrical household appliances, electrical machinery, bulldozers, excavators and agricultural machinery.
86. *Égypte/Monde Arabe*, 11, 1992.
87. Al-Laithy and Kheir al-Din, 1992–93.
88. At current prices LE 1 084 and LE 729 respectively; cf. al-Laithy and Kheir al-Din, 1992–93.
89. *Ibid.*

90. Defined as the population segment which is able to spend only one-third of the total household expenditure in a governorate; *ibid.*
91. E.g. between 1970 and 1989 the prices for subsidised foodstuffs went up as follows (in percentages): sugar (200), tea (191), rice (700), wheat flour (600), beans (499), white bread (200), lentils (1330); cf. Nassar, 1992–93. Additional price rises have been occurring since the early 1990s along with the cuts in subsidies. This had a large impact on nutrition: 38 per cent of pre-school age children, 45 per cent of school children and 21 per cent of pregnant women suffered from anaemia. Between 1986–87 and 1990 prices had gone up as follows: clothing (175 per cent), housing and water (121 per cent), energy (164 per cent), furniture (254 per cent), health services (161 per cent), transport (188 per cent), education (195 per cent), cost of living index (185.8 per cent); *ibid.*
92. *Ibid.*
93. Fergany, 1992–93.
94. The illiterate population in Egypt increased from 15.1 million in 1976 to 17.6 million in 1986 (with an illiteracy rate of 37.8 per cent for males and 61.8 per cent for females); cf. Al-Baradi, 1992–93.
95. *Al Ahram Weekly*, 15–21 October 1992.
96. *Égypte/Monde Arabe*, 12–13, 1992–93.
97. *Ibid.*
98. Egyptian sales of potatoes, green beans, oranges and medical herbs amounted to 95 million ECUs in 1991 (i.e. 4 per cent of its total exports to the EU), in addition to crude oil (67 per cent), cotton and textiles (9 per cent) and aluminium (8 per cent); cf. *Égypte/Monde Arabe*, 12–13, 1992–93.
99. *Égypte/Monde Arabe*, 12–13, 1992/93; *Al Ahram Weekly*, 17–12 September, 1992; *Al Ahram Weekly*, 1–7 October, 1992; *Al Ahram Weekly*, 3–9 December, 1992; *Al Ahram Weekly*, 4–20 March 1993.
100. *Al Ahram Weekly*, 25–31 March 1993.
101. *Al Ahram Weekly*, 18–24 February 1993.
102. *Égypte/Monde Arabe*, 12–13, 1992–93.
103. *Ibid.*
104. *Ibid.*
105. *Égypte/Monde Arabe*, 14, 1993.
106. *Nachrichten für den Außenhandel*, 25 November 1993.
107. *Égypte/Monde Arabe*, 12–13, 1992–93.
108. *Al Ahram Weekly*, 8–14 April 1993.
109. *Égypte/Monde Arabe*, 12–13, 1992–93.
110. *Al Ahram Weekly*, 18–24 February 1993; *Al Ahram Weekly*, 25 February–3 March 1993.

111. *Égypte/Monde Arabe*, 14, 1993.
112. *Al Ahram Weekly*, 22–28 April 1993.
113. *Égypte/Monde Arabe*, 15–16, 1993.
114. Usually reducing interest rates to 10 per cent, i.e. 4 per cent below market rates for five years with a two year grace period. *Égypte/Monde Arabe*, 15–16, 1993.
115. *Égypte/Monde Arabe*, 14, 1993.
116. *Ibid.*
117. *Ibid.*
118. *Al Ahram Weekly*, 23–29 September 1993.
119. Blin, 1993.
120. *Financial Times*, 22 April 1993.
121. *Ibid.*
122. *Ibid.*
123. Blin, 1993.
124. *Ibid.*, *Al Ahram Weekly*, 17–23 June 1993. *Al Ahram Weekly*, 15–21 July 1993. *Al Ahram Weekly*, 22–28 July 1993.
125. *Ibid.*
126. *Égypte/Monde Arabe*, 15–16, 1993.
127. Blin, 1993.
128. *Égypte/Monde Arabe*, 15–16, 1993.
129. *Al Ahram Weekly*, 9–15 December 1993.
130. *Égypte/Monde Arabe*, 17, 1994.
131. *Middle East Economic Digest*, 30 August 1996.
132. Australia, Belgium, Norway (observer status), Korea, Oman, Kuwait, Saudi Arabia, the GCC, the OPEC Fund and UNICEF, which had been at the previous meeting, did not participate. New participants were the EU Commission, the IMF, the Islamic Development Bank, UNDP, and as observers, the OECD and Greece.
133. *Égypte/Monde Arabe*, 18–19, 1994.
134. Aftandilian, 1993.
135. *Égypte/Monde Arabe*, 18–19, 1994.
136. *Ibid.*
137. *Ibid.*
138. *Ibid.*

139. The Federation of Egyptian Industries complained that 45 steps were necessary to get an export permit, involving more than 15 forms with 18 different stampings and 8 sorts of fees. A major reform was urgent. Cf. *Nachrichten für den Außenhandel*, 5 May, 1995.
140. *Égypte/Monde Arabe*, 23, 1995; *Égypte/Monde Arabe*, 25, 1995.
141. *Nachrichten für den Außenhandel*, 14 June, 1994.
142. *Égypte/Monde Arabe*, 18–19, 1994.
143. *Égypte/Monde Arabe*, 20, 1994.
144. Aftandilian, 1993, 81.
145. *Égypte/Monde Arabe*, 17, 1994.
146. *Financial Times*, 17 June, 1994.
147. *Al Ahram Weekly*, 4 August, 1994.
148. Glosauer, 1995.
149. *Ibid.*
150. *Égypte/Monde Arabe*, 21, 1995.
151. *Nachrichten für den Außenhandel*, 8 November 1994.
152. *Égypte/Monde Arabe*, 21, 1995.
153. *Ibid.*
154. *Ibid.*
155. *Nachrichten für den Außenhandel*, 4 February 1994.
156. *Égypte/Monde Arabe*, 25, 1995.
157. *Égypte/Monde Arabe*, 22, 1995.
158. *Ibid.*
159. E.g. Egyptian banks are reluctant to finance computer industries and services due to their lack of experience. Cf. *Égypte/Monde Arabe*, 25, 1995.
160. *Égypte/Monde Arabe*, 23, 1995.
161. *Ibid.*
162. According to Ebeid, 230 state enterprises had made profits of LE 3.6 billion (as compared to LE 2.9 billion the year before). Public sector losses in 1994–95 were LE 1.9 billion (as compared to LE 2.3 billion in 1993–94). 1 200 000 employees were entitled to receive bonuses of up to 5 per cent of their basic salaries depending on the performance of their enterprise. Cf. *Égypte/Monde Arabe*, 24, 1995.
163. *Égypte/Monde Arabe*, 23, 1995.
164. *Égypte/Monde Arabe*, 24, 1995.

165. *Ibid.*
166. *Égypte/Monde Arabe*, 22, 1995.
167. General Motors produced 13 000 automobiles in 1994 with a local content of some 30 per cent (LE 145 million) to be raised to 40 per cent within one year. Other foreign firms include Fiat, Peugeot, Mercedes, Suzuki, and Hyundai, the latter with a production capacity of 10 000 units annually. Cf. *Égypte/Monde Arabe*, 22, 1995.
168. *Égypte/Monde Arabe*, 23, 1995.
169. *Ibid.*
170. *Égypte/Monde Arabe*, 24, 1995.
171. *Ibid.*
172. *Égypte/Monde Arabe*, 23, 1995.
173. *Ibid.*
174. *Ibid.*
175. *Égypte/Monde Arabe*, 22, 1995.
176. *Ibid.*
177. *Ibid.*
178. *Égypte/Monde Arabe*, 23, 1995.
179. *Égypte/Monde Arabe*, 22, 1995.
180. The price of LE 0.5 per kg amounts to one third of the free market price. The sugar subsidies amount to an annual LE 1 billion (\$300 million). *Égypte/Monde Arabe*, 22, 1995. In 1995, international wheat prices rose by 40 per cent making domestic subsidies costlier. Cf. *Égypte/Monde Arabe*, 25, 1995.
181. *Égypte/Monde Arabe*, 23, 1995.
182. *Égypte/Monde Arabe*, 25, 1995.
183. *Égypte/Monde Arabe*, 24, 1995.
184. *Égypte/Monde Arabe*, 25, 1995.
185. *Ibid.*
186. *Égypte/Monde Arabe*, 24, 1995.
187. *Égypte/Monde Arabe*, 25, 1996.
188. *Égypte/Monde Arabe*, 23, 1995. *Égypte/Monde Arabe*, 24 1995. \$1.7 billion for the first nine months of 1995, 22 per cent more than in the same period of 1994. *Égypte/Monde Arabe*, 25, 1995.
189. *Financial Times*, 30 November 1995; *Frankfurter Allgemeine Zeitung*, 30 November, 1995; *Financial Times*, 2–3 December 1995.
190. *Financial Times*, 7 December 1995.

191. *Financial Times*, 30 November 1995.
192. *Ibid.*
193. *Financial Times*, 3 November 1995.
194. *Ibid.*
195. *Financial Times*, 4 January 1996.
196. *Financial Times*, 31 January 1996.
197. In Cairo the number of unoccupied flats is estimated at 1 million, cf. *Nachrichten für den Außenhandel*, 9 February 1996.
198. *Nachrichten für den Außenhandel*, 6 February 1996.
199. *Nachrichten für den Außenhandel*, 18 December 1996.
200. *Nachrichten für den Außenhandel*, 13 December 1996.
201. *Nachrichten für den Außenhandel*, 15 February 1996.
202. *Nachrichten für den Außenhandel*, 28 March 1996.
203. One feddan = 0.42 hectares.
204. *Nachrichten für den Außenhandel*, 1 February 1996.
205. *Nachrichten für den Außenhandel*, 22 January 1996.
206. *Frankfurter Allgemeine Zeitung*, 26 February 1996.
207. *Financial Times*, 17 April 1996.
208. *Frankfurter Allgemeine Zeitung*, 12 April 1996.
209. *Ibid.*
210. *Nachrichten für den Außenhandel*, 7 March 1996.
211. *Égypte/Monde Arabe*, 26, 1996.
212. *Le Monde*, 22 October 1996.
213. *Le Monde*, 4 April 1996; *Le Figaro*, 8 April 1996.
214. *Frankfurter Allgemeine Zeitung*, 28 October 1996.
215. *Frankfurter Allgemeine Zeitung*, 5 August 1996. *Middle East Economic Digest*, 6 September 1996.
216. *Frankfurter Allgemeine Zeitung*, 3 August 1996.
217. *Financial Times*, 11 October 1996.
218. *Financial Times*, 5 December 1996.
219. *Égypte/Monde Arabe*, 26, 1996.
220. International Business & Technical Consultants, Inc. (in the following IBTCI), USAID Privatization Project, Quarterly Review July–September 1996.

221. *IBTCI*, Quarterly Review July–September 1996.
222. *Ibid.*
223. *Ibid.*
224. *IBTCI*, Quarterly Review January–March 1997. Cf. *Middle East Economic Digest*, 16 February 1996. *Middle East Economic Digest*, 29 November 1996.
225. *IBTCI*, Monthly Report, July 1996. Cf. *Business Today*, December 1996.
226. *IBTCI*, Quarterly Review October–December 1996.
227. *IBTCI*, Quarterly Review July–September 1996.
228. *IBTCI*, Quarterly Review January–March 1997.
229. *IBTCI*, Semi Annual Evaluation, January–June 1997.
230. *Ibid.*
231. *IBTCI*, Monthly Report, October 1996.
232. *IBTCI*, Quarterly Review October–December 1996.
233. *Ibid.*
234. *IBTCI*, Quarterly Review January–March 1997.
235. *IBTCI*, Quarterly Review July–September 1996. The rate on treasury bills had continuously fallen since 1991 when it had amounted to 19 per cent.
236. *IBTCI*, Quarterly Review January–March 1997.
237. *Ibid.*
238. *Middle East Economic Digest*, 25 July 1997.
239. National Bank of Egypt, *Economic Bulletin*, Vol. 50, No. 1, Cairo 1997. *Financial Times*, 16 January 1997.
240. *IBTCI*, Quarterly Review, January–March 1997.
241. *Ibid.*
242. National Bank of Egypt, 1997.
243. *Ibid.*
244. *Ibid.*
245. *Business Today*, June 1997. Again, reliable data do not exist. “USAID offered four years ago to put together a comprehensive report on labour here, but the government declined”; cf. *Business Monthly*, June 1997. See also Asef Bayat, *Cairo’s Poor*. “Dilemmas of Survival and Solidarity”, *Middle East Report*, Winter 1997. Eric Denis, “Urban Planning and Growth in Cairo”, *Middle East Report*, Winter 1997.
246. *Ibid.*

247. Nassar, Heba, *The Employment Status of Women in Egypt*, American University in Cairo, December 1996. According to the World Bank, the overall unemployment rate is estimated at 17.5 per cent, or 2.8 million people; cf. *Business Today*, April 1997. See also *Al Ahrām Weekly*, 5–11 December 1996.
248. *Middle East Times*, 3–9 October 1997. *Al Ahrām Weekly*, 10–16 July 1997.
249. *Ibid.*
250. *IBTCI*, Semi–Annual Evaluation January–June 1997.
251. *Ibid. Middle East Times*, 29 August–4 September 1997. *Al Ahrām Weekly*, 4–10 September 1997.
252. *Al Ahrām Weekly*, 31 July–6 August 1997. See also *Middle East Economic Digest*, 3 October 1997.
253. *IBTCI*, Semi Annual Evaluation, Quarterly Review January–June 1997.
254. *Ibid. Middle East Times*, 15–21 August 1997.
255. *IBTCI*, Monthly Report, July 1996. cf. *Business Today*, March 1997. *Al Ahrām Weekly*, 28 August–3 September 1997.
256. *IBTCI*, Semi Annual Evaluation, January–June 1997.
257. *Ibid. Middle East Times*, 19–25 September 1997.
258. *IBTCI*, Semi Annual Evaluation, January–June 1997.
259. *Middle East Economic Digest*, 25 July 1997.
260. *Ibid.*
261. *Middle East Economic Digest*, 26 April 1996.
262. *Middle East Economic Digest*, 28 November 1997. *Al Ahrām Weekly*, 25 September–1 October 1997. *Al Ahrām Weekly*, 17–23 July 1997.

Politics and Microeconomics of Reform

Public Enterprise Performance

The Heritage of the 1980s

Egyptian public enterprises and the economic authorities employed 1.55 million people in 1984–85, or 10 per cent of the entire labour force and 20 per cent of non-agricultural employment. The wage bill of the administration, the state enterprises and other public sector activities in 1986–87 amounted to LE 8.7 billion (21 per cent of GDP)¹. The development plan for 1982–83 to 1986–87 stressed the necessity of improving the management and performance of the public sector companies as one of its six major objectives². Since the mid-1980s the government had tried to increase the profitability of state enterprises with limited success. The 1986–87 and 1987–88 fiscal years saw some positive trends concerning profits and somewhat smaller overall deficits³, but the situation deteriorated again by the end of the 1980s.

There was continuing government intervention in all company activities for the purpose of trying to maintain political control and avoid social unrest by means of high levels of employment, job security and low prices for basic consumer goods. Wages were high in relation to labour productivity⁴, and a large part of the work force was not adequately qualified, especially in more sophisticated industries⁵.

Companies also suffered from credit rationing unrelated to economic criteria. This aggravated their liquidity problems and affected their access to inputs and spare parts. The scarcity of foreign exchange often led to a “veto” on proper maintenance or replacement of old machinery by the government administration. Furthermore, the scarcity of foreign exchange prevented companies from using foreign technical experts⁶. Most companies were unable to make flexible and efficient use of their resources by concentrating on their particular strength, or to meet international business standards by adopting profit-oriented marketing strategies.

Box 5.1. The Egyptian Ship Building and Repair Company

The main obstacle to a takeoff in a market economy is excess labour. In 1994 senior management was overstaffed by 25 per cent, the positions of production supervisors by 62 per cent, and the departments of financial and commercial supervision employed 69 per cent more people than needed. Excess labour in the administrative development units was 47 per cent, office jobs were overstaffed by 68 per cent and the engineering section employed 285 people instead of the 115 needed. There were 1 054 people working in the production section which only needed 590 employees for its operations.

According to a report to the Social Fund for Development, 908 employees out of 1 807 were redundant. “The work force is capable of being militant if it suspects that any decisions are being taken to reduce its benefits. In fact, it is difficult for management to make any kind of positive changes, and the work force currently has effective control of the business to the detriment of both the business and the very work force whose interests the militants are trying to protect.”

Source: Serco Education Ltd., 1994.

The lack of managerial skills in the companies and in their public surveillance bodies (23 so-called Economic Organisations under different ministries) were a major reason for the deficiencies. The managers had been recruited from the state bureaucracy or the higher ranks of the army and were chosen for loyalty and seniority rather than professional qualifications and experience. Patronage networks allowed people unfit for their job to rise to demanding positions. The inward orientation of the Egyptian economy did not encourage learning about new technologies and markets. What mattered was the amount produced rather than the return on investment. A comprehensive system of subsidies and protection from domestic and international competition added to the low level of professional standards, and also resulted in a massive transfer of national resources to the state enterprises.

On the other hand, state intervention forced enterprises to share the social burden by fixed input and output prices, and by furnishing social services such as medical care, kindergartens and holiday resorts for their employees⁷. Thus there were significant restraints on the possibility of profit-maximising strategies.

Managers and other employees of the public sector were highly privileged. They will be the main losers from structural adjustment and privatisation. The overstaffed middle management in particular will be affected by public sector reforms. Besides poor profit-and-loss accounts, the state enterprises have affected incentive structures, work ethics, discipline and quality awareness.

Box 5.2. Conversion of Public Resources into Private Wealth: The Case of Subsidised Commodities

Subsidised commodities have been subject to many types of parasitic activities. In 1986 the Supply Investigator claimed that 800 000 kilograms of flour per day had been diverted to the black market, mainly to large macaroni producers. Profiteering from access to subsidised commodities was by no means always an illicit, undercover activity. It formerly was institutionalised in all sectors. Industrial managers in many sectors tried to increase the amount of their subsidised inputs and reduce government restrictions on the marketing of their finished goods, for example, feed mill operators using subsidised yellow corn, manufacturers who obtained electricity at a fraction of its real cost, furniture makers who used subsidised cotton. Goods or services produced with subsidised inputs were not supposed to be exported, but this regulation was circumvented by those with influence.

The ZAS Airline is Egypt's only private air freight carrier. Funded by several prominent individuals, it was granted the right to purchase subsidised jet fuel. This was a guarantee of success and by 1987 ZAS had expanded from its original fleet of one Boeing 707 to six. "Decisions such as the privilege to purchase unlimited quantities of subsidized aviation fuel are made at the very highest levels and require influence, exchange of favors, and/or bribes. Businessmen who have gained access to the resources of the state in this way and those in the state apparatus and/or political elite who have made such access possible have no interest in changing this system. For them, the milking of the state's resources, combined with monopolistic and oligopolistic control of markets, guarantees substantial rewards."

Source: Springborg, 1989.

Box 5.3. Distorted Employment Structure: Egyptian Bottling Company

In 1993 the Egyptian Bottling Company was one of the first two public sector companies privatised under Law 203. The restructuring began in 1994 when the new owners started to address the problem of the distorted structure of the work force. Middle managers had made up 33 per cent of the entire work force of 4 067, or 1 324 employees. After restructuring their work was done by 44 managers. The number of top managers was reduced from 22 to seven.

Source: IBTCI, unpublished material.

At the outset of the reform programme many state enterprises suffered from huge accumulated debts and an unsustainable financial structure. Some of the companies would be promising candidates for privatisation if they could reduce their debt burden to a manageable level.

Box 5.4. Crippling Debts: Misr Helwan Spinning & Weaving Co.

“The company carries an excessive burden of debt, and fights a constant battle to restructure its debt. Privatisation, selling off parts of the business, or attracting outside investment is not possible without some hard decisions being taken by the long-term creditors. Losses by the end of the 1992–93 financial year amounted to over LE 500 million. Interest charges totalled LE 75 million for the year although the company did not pay it. This enormous charge on sales of LE 102 million means that the Company would need to sell 10 times its present turnover to limit the interest component in the costs to only 15 per cent. The situation is compounded by weak sales so that selling prices do not even match production costs, let alone absorption costs, and the debt can only grow larger under these conditions. Some method must be found of providing an interest-free period of around three years which is the minimum time it will take to pull this company round to a quality-conscious and profitable operation. Without this, the business will fail to attract outside purchasers.”

Source: Serco Education Limited, 1994.

Most companies do not have an active marketing department, systematic and effective quality control, or up-to-date maintenance activities. Others are immobilised by unpaid suppliers because of a lack of liquidity. All companies need training and retraining. Workers, office staff, technicians and engineers lack necessary skills as a result of an educational system which is biased towards theoretical rather than practical studies. Most companies require outside consultants to carry out necessary changes⁸.

From the perspective of enterprises the macroeconomic framework was unreliable. Companies were faced with fluctuating inflation and interest rates, with risks involving bank lending and foreign trade regulations. Financial markets are still underdeveloped. The inconsistent, inefficient and inequitable tax system is another source of trouble. Lack of transparent tax assessment and a great deal of arbitrariness lead to bribing of tax administrators.

The Case of El-Nasr Clothing and Textile Company: A Promising Candidate for Privatisation

The El-Nasr Clothing and Textile Company is a 78 per cent affiliate of the Holding Company for Spinning, Weaving & Ready-Made Clothes and has been privatised under Law 203 of 1991 (Public Enterprise Law). The company belongs to the group of promising privatisation candidates although a lot of restructuring will be necessary.

Box 5.5. El-Nasr Clothing and Textile Company (KABO)

The company exports almost 30 per cent of its production. Its financial condition is relatively stable. Sales and profits show a positive trend in spite of rising input costs. In FY 1993-94 the return on investment was 17.7 per cent. Even in the past a highly motivated and experienced management tried to maintain standards of quality and efficiency. KABO uses strict quality controls which have become a competitive advantage in comparison with other Egyptian public sector textile companies. The workers are relatively well qualified. Most of the engineers have studied in Europe. However, KABO suffers from a number of typical public sector problems. An estimated 20 per cent of the work force of some 5 500 employees is redundant. The productivity of the employees must be improved. Stocks are inflated (especially for finished goods). Compared to international standards, machinery is not replaced fast enough.

The production capacities are underutilised. The preparation section of the knitting department uses only 30 per cent of its capacity. The knitting section also utilises only 30 per cent of its capacity. It would be possible to work at full capacity if high quality yarn and a better production planning were introduced. Other sections are equipped with obsolete machinery that does not allow for any increase in output.

Knitting costs are much higher than in Turkey or Pakistan and slightly higher than in Greece or Portugal, mainly as a result of labour costs. The productivity in the dyeing and finishing departments is low compared to European or US plants. In all departments labour costs and floor space could be drastically reduced by new technology, which would also increase quality and flexibility crucial to cope with changes in fashion.

The Holding Company for Spinning, Weaving & Ready-Made Clothes is to privatise all its remaining KABO shares after having transferred 10 per cent to the employee shareholder association. The remaining 68 per cent were to be sold in several batches, aiming at a complete privatisation of the enterprise, but only 8 per cent of the shares had been sold by February 1995. No further privatisation steps have been reported.

The Misr Helwan Spinning & Weaving Company: A Negative Example

In any open market economy the Misr Helwan Spinning & Weaving Company would have been liquidated long ago. The four major problems are undercapitalisation, quality of output, marketing, and size. British consultants estimated that at least 3 700 people out of a total work force of 12 000 would have to be dismissed. It is obvious that all attempts to attract prospective private investors will fail if the company is not profoundly restructured.

Box 5.6. Misr Helwan Spinning & Weaving Co.

Undercapitalisation: The cash flow is so constrained that the erratic purchase of basic materials is causing improper use of machinery with faulty production.

Production Technology: Equipment is so substandard that the finished products are of low quality. Production costs render them too expensive to generate a profit.

Marketing: Sales are impeded by a lack of advertising for three years, with the result that the company is being driven further into debt. Some of the most promising product lines have been neglected.

Size: The enormous size of the operation and its product diversity make it difficult to manage effectively. There are far too many layers of management and overhead staff, which makes communication difficult and limits the responsibilities of the employees concerned. This reduces their interest in doing their work properly.

Source: Serco Education Ltd., 1994.

Public Sector Monopolies

Public sector monopolies are still part of Egypt's economic heritage. Entire subsectors are often dominated by a limited number of large state enterprises as in the field of insurance. If these companies are not subdivided before their privatisation, a public monopoly will be transformed into a private one.

Box 5.7. Monopolies: The Egyptian Insurance Companies

The Egyptian insurance market has been dominated by three public sector companies: Misr for Insurance, Al-Shark for Insurance and Al-Ahlia for Insurance controlled 75 per cent of the market and were linked with almost all public sector companies. When public-private sector joint ventures became fashionable in Egypt during the early 1980s, three other semipublic companies were established with major shares for the public sector partners. The Al-Mohandes Insurance Co., Suez Canal Insurance Co. and Delta Insurance Co. control another 20 per cent of the market, leaving just 5 per cent to two joint ventures with foreign investors and two private enterprises.

Micro Reforms since 1990: Privatisation, The Crucial Test of Structural Adjustment

Negotiations between the Egyptian Government and the International Financial Institutions

After painstaking negotiations with the World Bank and the IMF, in February 1990 the Egyptian government agreed to implement a privatisation programme beginning with the sale of enterprises under the control of the governorates⁹. The Egyptian side promised to proceed with sales of public sector companies without further specification. President Mubarak repeatedly warned of social unrest and political disorder if reforms were implemented too abruptly. As a result of this concern the Social Fund was established. As far as the privatisation agenda was concerned, the government resisted donor pressure during 1990 and 1991 and did not publish any list of privatisation candidates. While criticising the slow pace of reforms, the World Bank agreed to a structural adjustment loan, and the IMF approved a new stand-by agreement¹⁰.

In 1992 the donors continued to criticise the slow evaluation of state enterprise assets by auditing firms, the hesitant sales, and the continuing large investments in public sector companies. By 1993 the government made some steps towards privatisation, while the IMF and World Bank continued to criticise the slow pace of reforms. As privatisation results did not meet the agreed benchmarks, the IMF postponed the final review of the results of the stand-by loan originally scheduled for December 1992, a precondition for the debt relief by the Paris Club. The World Bank agreed to the disbursement of the second tranche of the structural adjustment loan that had been scheduled for June 1992 only after a positive evaluation had been completed in March 1993.

The tug of war continued in 1993. The government objected to the low assessment of public sector company assets by foreign consultants, thinking in terms of the initial investments in state enterprises back in the 1960s in plants that had since become obsolete and with poor returns on investment. The government also argued that sales under donor pressure would bring down the prices. This was a first indication that the government preferred high privatisation proceeds rather than rapid privatisation. In the summer of 1993 Minister of Public Affairs Atif Ebeid publicly criticised the World Bank's pressure to speed up the reforms: "The advisor will not be driving the car, but might be willing to visit us in the hospital if we crash it"¹¹.

Nevertheless, the government accepted a new World Bank reform package including the privatisation of state banks and insurance companies (which in earlier drafts had been excluded from privatisation) to receive an IMF Extended Fund Facility in September 1993. The Letter of Intent of August 1993 contained a time schedule for the privatisation of 314 public sector companies under Law 203. The sales were to proceed in three stages during fiscal years 1993–94, 1994–95 and 1995–96. A quarter of the assets were to be privatised by mid-1995. As the Letter of Intent referred to book values — the subject of heated debate involving the international financial institutions, other donors, the government and the Egyptian public — the agreement remained vague and did not assign numbers, names of companies, or dates¹².

Until 1995 the IMF and World Bank continued to voice dissatisfaction with the pace of reform and threatened to withhold authorisation of the Paris Club's third instalment of debt relief until they made a positive evaluation of reform. The Egyptian government was able to resist the pressure due to its comfortable foreign exchange position¹³.

The general outlook changed after the elections of November 1995 and the appointment of Kamal al-Ghazouli as Prime Minister. A new round of privatisation announcements were made by Prime Minister Ghazouli and his cabinet members. The programme's cornerstone would be the new labour law. Indications of renewed government momentum on reform paved the way for another agreement with the IMF in October 1996.

The Politics of Legal Transformation

Attempts at creating a new legal framework conducive to economic reform began in the 1970s and have been the focus of media debate and clashes of interest groups in parliament. The various stakeholders feared negative consequences and reacted with massive lobbying. By the late 1980s a number of bills had passed parliament, starting with Law 43/1974 on Arab and Foreign Investment¹⁴. The first legislation arising from the new reform initiative under President Mubarak was Law 230/1989 which granted a number of investment incentives. The provisions included tax exemptions for projects in the new satellite cities around Cairo or in land reclamation areas, and for investments that were for promoting exports, employment or technology transfer, with equal

treatment of Egyptian and foreign investors. Law 230 projects were exempt from minimum ceilings on Egyptian equity participation, price controls, and limits on disposal of capital or shares¹⁵.

Law 203 of 1991, the so-called Public Sector Business Law, was the most radical effort to reform the state enterprises since a first attempt in 1971. It established holding companies as successors of the former General Organisations (which had been under the direct control of the ministries). The so-called affiliated companies were placed under holding companies, i.e. the individual public enterprises were grouped. The holding companies were supposed to act as profit- and market-oriented owners of their affiliated companies, to restructure them and prepare them for privatisation. Holding companies report to the public sector minister. Egyptian labour law provides for extensive rights, guarantees and entitlements of employees which put limits on the management of holding companies and their affiliated companies.

The Capital Market Law 95/1992 was another prerequisite of reform, especially for the privatisation of state enterprises through sales of shares. The law was instrumental for the re-establishment of a rudimentary Egyptian capital market, authorising brokers and investment funds and permitting free registration and trading of shares on the revived stock exchange. The new Banking Law of 1992 opened the way to international banking norms in Egypt and removed many former restrictions.

Law 96/1992, which was presented as an amendment to the Agricultural Reform Law of 1952, radically changed the legal environment of Egypt's agriculture. All restrictions on tenancy contracts were to be removed after a transition period from 1992 to 1997, with foreseeable highly negative social consequences in rural areas¹⁶.

The new Housing Law of 1996 did not lead to the same profound change as in agriculture but will be an essential step towards reforming the housing sector. Rent control no longer applies to newly constructed buildings and flats, but other housing units are not affected.

By 1997, the new labour bill was still being discussed in the People's Assembly and by the Egyptian public. It was a major source of concern for the government which was caught between the need to deregulate capital-labour relations and the risk of social upheaval.

Major Actors and Their Stakes in the Struggle for Privatisation

The Top Political Leadership

President Mubarak makes the key decisions dealing with the politics of privatisation in a small circle after having left the technical matters of the reform for a long time to the cabinet ministers. Egyptian businessmen close to the president told him early in 1996 why influential members of the business community were concerned about the slow pace of economic reforms. Highly qualified young people kept leaving

the country, and more dynamic businessmen transferred their investments to foreign countries in order to evade the stifling environment at home. If the Presidency wanted to maintain the support of the leading business circles, it would have to take the initiative to increase the momentum of reform. This incident contributed to the renewed commitment to reform. The president, not really concerned about economic policies as long as political stability was not at stake, ordered the cabinet to go ahead with a number of new reforms, not only to appease foreign donors but also to satisfy influential supporters of the government in the Egyptian business community.

A commitment to privatisation was reaffirmed after President Mubarak's visit to the United States in July 1995, where he met with President Clinton and Vice President Al Gore (responsible for US–Egyptian co-operation). European consultants who had tried for months to get the Public Sector Ministry interested in their expertise were suddenly asked to draw up privatisation plans for some 40 companies. The United States had made it clear that it would scale down economic aid if Egypt did not speed up its reforms.

In the parliamentary elections of November 1995 the National Democratic Party (NDP) remained the dominant political force¹⁷. On 2 January 1996, Kamal al-Ghazouli, former deputy prime minister and minister of planning, became President Mubarak's fifth prime minister. Known for his tough and efficient style, he was charged with the task of "preparing Egypt for the 21st century", speeding up economic reform, including privatisation, and raising living standards for the low-income strata.

The prime minister kept the planning portfolio for himself and retained Atif Ebeid in the key Public Sector Ministry, "even though international donors regard him as a major obstacle to privatisation and public-sector reform"¹⁸. In the mid- and late 1980s, Atif Ebeid had been viewed as one of the officials who promoted economic reforms. Ebeid was described as a member of a group that did not go as far as Minister of Tourism Fuad Sultan, who had pushed the large-scale privatisation of hotel facilities and was punished by losing his portfolio. A number of younger civil servants in economy-related ministries who had spoken out in favour of rapid reforms in the late 1980s had also been forced to resign, and some of them had blamed Ebeid for having been one of the conservatives at that time. Others described him as a reform-oriented government official aware of the political constraints, who would not take too many risks. A politician who wanted to stay in power had good reasons not to privatise faster than necessary in the prevailing balance of power. This balance seemed to have changed since President Mubarak's last visit to the United States.

Prime Minister Ghazouli, the new champion of privatisation, had previously been an opponent of all steps to dismantle the public sector. He belonged to a group of high administrators who adhered to a cautious and gradualist approach in which reforms would take two generations to implement. By the end of 1996, the former public sector hardliner who had held the position of minister of planning for 12 years commented: "Three years ago, I thought you could keep the public sector and still the private sector would be free to come and invest... But right now it's hard to invite the

private sector to work while we have this big pyramid of public enterprises”¹⁹. Ghanzouri’s modified approach in favour of faster and more radical reforms was related to the president’s new stand. The new official line was even followed by former opponents of reform in the cabinet, who hastened to come up with proposals to privatise assets of authorities and companies under their jurisdiction.

The Public Enterprise Office

In 1992 the Public Enterprise Office was established as part of the administrative structure of the Public Sector Ministry as a sort of think tank and support unit for the privatisation programme. The Public Enterprise Office has some 25 staff members and is in charge of evaluating privatisation proposals but has no decision making authority of its own. This leads to problems if donors are negotiating with the Public Enterprise Office. Every once in a while its staff needs ministerial approval, which makes negotiating time-consuming and inefficient and frustrates donors, potential investors and staff members of the Public Enterprise Office alike²⁰.

The Public Enterprise Office views the social dimension as the key issue (“no harm will be done to *our* workers”). In the long run the Public Enterprise Office expects privatisation to create new employment opportunities. It adheres to a step-by-step approach with periodic reviews and eventual adjustments. It is aware of its marginal role and is looking for political support in favour of privatisation, but it remains under strict control by the public sector minister.

The Holding Companies

Law 203/1991, the so-called Public Enterprise Law, had paved the way to partial or complete privatisations of state enterprises and removed the ministries from management of the companies in order to induce a more market-oriented approach. The 314 public companies (affiliated companies) were grouped under 22 newly established holding companies, whose number was later increased to 27 and then reduced to 17 in 1993. The regrouping of the affiliated companies into 17 holding companies was intended to link profitable and unprofitable enterprises, to create a sectoral mix instead of concentrating firms of the same subsector, and to end monopolistic tendencies. Some 30 per cent of the affiliated companies were transferred to other holding companies. The boards of the holding companies were recruited in 1992. Former high-ranking public sector managers and prestigious private businessmen were appointed. The holding companies are responsible for market-oriented management and the preparation of companies for privatisation. They report to the public sector minister.

The holding companies were supposed to maximise profits and were cut off from the state budget. They lost their previous relatively easy access to subsidised loans and grants. In practice, however, the holding companies and their affiliates still manage to obtain public sector bank loans and government support through the four dominant state banks.

As soon as a holding company sells at least 51 per cent of an affiliated company, the latter is considered to be part of the private sector subject to the regulations of the Private Company Law, and is no longer part of the holding company. The holding companies are allowed to sell or liquidate affiliated companies if the public sector minister agrees. Power is vested in the holding company's chairman of the board and his deputy who usually are supported by a small staff. Experience has shown that they are able to manage a portfolio of affiliates, but the institutional arrangement is unsuitable for effective privatisation, starting with limited incentives for bringing affiliated companies to the point of sale and losing their eventual profits for the holding company (e.g. making up for losses of other affiliates, financing new investments, etc.). In addition, a rapid sale of the affiliates, if approved by the Public Sector Ministry, would weaken the holding company's management and would eventually lead to its own liquidation, in line with the basic long-term policy objective.

Nevertheless, some holding company managers (e.g. in the Holding Company for Public Works) indeed took the initiative to transfer affiliated companies to the private sector. The majority of holding company managers, however, tried to postpone the sale of their affiliated companies as long as possible. They acted in this way with the apparent support of the public sector minister who had repeatedly withheld his approval of sales which had already been negotiated between a private investor and the holding company board. Sometimes he objected to the low valuation of obsolete assets of affiliated companies. In a number of cases the ministry chose not to react to a privatisation proposal.

As part of the new reform initiative in 1996 a High Ministerial Privatisation Committee was established, including the Prime Minister's Office, the Public Sector Ministry and the Ministry of Finance. It is intended to depersonalise privatisation decisions and to relieve responsible decision makers from political pressure *ad personam*. The committee may accept, reject or modify privatisation proposals.

When holding company managers try to slow down the reforms they have the advantage of having detailed technical and economic data on the affiliated companies that enable them to manipulate the decision making process. They can withhold essential information and make use of "old boy" networks in the public sector to influence general policies or proceedings on the company level. Their most effective instrument is the threat of large-scale dismissals.

The holding companies continue to invest, often only to modernise and restructure affiliated companies and to prepare them for sale. From the perspective of holding company managers, further investments strengthen their position for evading privatisation.

Box 5.8. Valuation of Assets: The Holding Company for Mining and Refractories

After an intensive search for prospective buyers the Holding Company for Mining and Refractories succeeded in attracting a potential investor who wanted to buy its affiliate, the Bani Suweif Cement Plant, scheduled for privatisation by the Public Sector Ministry. The holding company, faced with a lack of financial resources and the need to restructure its other 14 loss-making affiliated companies, was unable to restructure the heavily indebted cement company. The offer of the prospective buyer was a chance to get rid of one of the most complicated privatisation cases in the holding company's portfolio, still demanding huge amounts of cash for interest charges. The investors' offer included a reasonable price and immediate cash which would have helped the Holding Company to meet its financial obligations. Foreign consultants in Cairo said the contract was fair.

After a detailed contract had been drafted and the contracting parties were ready to finalise the privatisation the public sector minister withheld his signature on the grounds that the difference between the company's book value and the sale price was unacceptable.

The Affiliated Companies

According to the agreement with the IMF of August 1993²¹, 125 enterprises out of a total of 314 affiliated companies were selected under Law 203 for privatisation without prior large-scale restructuring, while 75 were to be restructured before privatisation, and 51 were to be liquidated. No detailed statement was made concerning the remaining affiliated companies under Law 203. This law specifies that privatisation proceeds are supposed to be used for restructuring other public sector companies to prepare them for sale.

As of August 1996, three years after the agreement, the government reported that 22 majority holdings with a total value of LE 1.9 billion had been privatised and that another 18 affiliated companies under Law 203 had started to privatise with the sale of minority shares worth slightly more than LE 1.3 billion. This meant that 292 out of 314 companies under Law 203 (93 per cent) still belonged to the holding companies, and that 274 companies (87 per cent) had not undertaken any privatisation.

Holding companies claim that their affiliated companies' access to scarce resources (such as finance, managerial capacities for debt negotiations or technical expertise, etc.) within the holding company is based on "objective economic necessities"

without specifying how restructuring policies for certain affiliates are related to the overall corporate strategies of the holding company. Obviously, holding company decision makers are caught between two conflicting tasks of sound portfolio management on the one hand and privatisation on the other, which imply different approaches to the running of the affiliated companies. The affiliated companies' managers too have a strong self-interest in preventing their companies privatisation, since they may be the first employees dismissed by the new private owners.

It is doubtful that affiliated company boards and general assemblies can make independent decisions and act as specified by the law. Holding companies' top management tends to interfere in their affiliates' affairs, sometimes aiming at personal benefits. Some affiliated companies have to muddle through on their own as far as difficult issues are concerned such as the dismissal and re-employment of excess labour. If negotiations between potential investors or donors and an affiliated company promise benefits such as access to external resources, additional returns or personal income, the holding company's top management may step in and intervene.

**Box 5.9. Bribing a Holding Company Chairman:
The Case of Abdel Wahab Al-Habak**

Abdel Wahab Al-Habak had headed the board of the joint venture Electrical and Electronic Apparatus Co. (with Philips) for ten years. In 1985 he became head of the Holding Company for Industrial Engineering.

The *Al-Wafd* newspaper reported that he took \$35 million in illegal commissions. A government source said Habak accepted bribes for helping to undervalue companies of his holding company scheduled for privatisation, in particular the El-Nasr Boiler Company, the third company which was sold under Law 203. He also imported overly expensive machine tools in exchange for kickbacks. After opposition newspapers wondered why Habak was still free and rumours presumed that he had been supported by former ministers, on 20 June 1996 the judicial authorities banned him from leaving the country. He was arrested on 24 September 1996.

Source: Middle East Times, 29 September, 1996.

Employee Stockholder Associations

The concept of employee stockholder associations aims at winning over labour for participation in privatisation through plant ownership and participation in the eventual privatisation benefits. The government plans to sell 10 per cent of the shares in at least 100 public enterprises to its own employees within ten years. Thus the employee stockholder associations would become an important partner in the

privatisation process²². However, it was clear from the very beginning that members of employee stockholder associations would not have the same stockholder rights as private entrepreneurs. They are not allowed to sell their shares during the first two years.

The Private Business Sector

The Egyptian private business sector adopted a critical position towards the privatisation programme. Even if some entrepreneurs bought shares through the stock exchange, the majority of the business community did not actively participate in the public sector reform. Entrepreneurs criticised the attempts to maximise privatisation proceeds. In a number of cases, private offers to buy state enterprises had been turned down by the government because the proposed prices were considered to be too low. Sometimes bids were just ignored or negotiations took so long that private entrepreneurs lost interest. Thus the government frustrated some leading industrialists and failed to mobilise broad support. Many plants needed substantial technological overhaul with large additional investments.

Potential Egyptian investors also regarded the economic policy framework as unstable and had doubts about the government's political will to proceed with privatisation after years of announcements not followed up by serious implementation. Some private businessmen had been transferring abroad up to 80 per cent of their profits from their domestic activities because they feared a continuation of industrial stagnation and Islamist pressure.

The large majority of the private business community is absorbed by day-to-day problems in a difficult environment and has no interest in taking over public sector firms or shares. Many are aware of the advantages of operating in a protected domestic market with limited competition from rather inefficient state enterprises. Private firms can be suppliers of state enterprises in well-protected niches. A large majority of the private companies could hardly survive in an open competitive environment. Others who might be interested in buying a public sector company may be deterred because the purchase would reveal their amassed wealth. This could raise questions about its sources, its legality and whether proper taxes had been paid²³. The prevailing interest is for strengthening the role of the private business community and its voice in the political realm.

Painstaking Moves towards Implementation

The Late 1980s: Hesitant Steps

In view of the danger of social and political destabilisation, the first tentative steps towards privatisation in the late 1980s were taken in tourist facilities and small enterprises owned by the governorates. Here the government felt that the social impact could be kept under control. Powerful economic stakeholders were not affected and the sales had little bearing on the economy. Privatisation was described as a sale of assets that were no longer needed²⁴. As the private sector was already active in the subsectors in question, the supply of goods and services remained stable while the governorate budgetary burdens were eased.

The privatisation of tourist facilities was technically more demanding and provoked an intense public debate. In the early 1980s Tourism Minister Fuad Sultan had already tried to increase the proceeds on the underutilised potential through management contracts with internationally renowned companies and some first steps towards privatisation, an approach which was profitable. In 1989 the first complete privatisations of hotels and hotel managements were carried out, while unprofitable hotels were also sold.

In July 1989 President Mubarak declared that he would only accept the sale of some loss-making enterprises, and that “strategic” and heavy industries would stay under state control. The first published privatisation plans of the government were very limited as the debate concentrated on the issue of losing control over “strategic” industries.

1990–92: Still No Large-scale Sales

In June 1990 the Egyptian General Company for Tourism and Hotels sold 80 per cent of the Cairo Meridien Hotel in the first public auction of state-owned assets. Its relative success and the moderate public reaction indicated that the political environment for privatisation had improved. This was crucial for a government anxious not to provoke millions of public sector employees.

In the following year Law 203/1991 provided for privatisation of 314 public sector companies. The bill was submitted to the People’s Assembly in the spring of 1991 but was barely discussed in parliament due to the Gulf War. However, it met resistance from trade unions whose members in parliament opposed the bill. The demand of the General Trade Union Federation for the addition of provisions in favour of employees was met, including issues of profit sharing. Public sector labour regulations from Nasserist times would remain valid until parliament passed a new labour law. This arrangement was intended to show that privatisation would not affect workers’ rights.

In January 1992 the Public Enterprise Office was established under Prime Minister Atif Sidqi to assist the privatisation programme. The Public Enterprise Office soon announced that shares of 23 public–private joint ventures would be sold and it started to prepare tenders for the evaluation of companies' assets. The government also stated that profitable enterprises would be sold.

In 1992 the Capital Market Law was approved by parliament. In July 1992 the government officially ceased financing of public enterprises through the National Investment Bank on preferential terms. Since then they have faced market conditions²⁵. During 1991 and 1992 no sales of Law 203 companies occurred, although six liquidations were reported.

1993: Mounting Donor Pressure

In 1992 and 1993 political debate on privatisation intensified. Opposition parties held that managers of public enterprises were not responsible for their huge losses as they had to act within government guidelines. They should be given a chance to restructure the public companies. The opposition, including the pro–capitalist New Wafd Party, argued that only small firms should be sold. Otherwise national interests would be at stake. The Public Enterprise Office hastened to state that sales would be carried out in line with national interests. Foreign interests would not be allowed to obtain complete control of any enterprise. The “strategic” sectors (oil companies, Suez Canal and telecommunications) would remain under state control.

The IMF and World Bank kept criticising Egypt's foot–dragging on reforms as the agreed targets were not met. The IMF postponed the final review for the stand–by loan originally planned for December 1992, a condition for debt relief by the Paris Club. Only after a positive IMF evaluation in March 1993 did the World Bank agree to disburse the second tranche of the structural adjustment loan originally scheduled for June 1992.

In February 1993 the “General Procedures and Guidelines for the Restructuring and Privatisation Programme” were issued²⁶. The holding companies were authorised to choose privatisation candidates from their affiliated companies, previously a decision reserved to the Public Enterprise Office and the minister. A third of the affiliated companies were redistributed among the holding companies to avoid excessive sectoral concentrations and monopoly situations. Early in 1993 the Public Enterprise Office had named 75 companies which needed restructuring, 51 that were to be liquidated due to their huge losses, and 125 that were to be privatised without major restructuring.

Egypt continued to differ with the IMF and World Bank in 1993 on the valuation of company assets and the speed of the reforms. The government had to accept the privatisation of state banks and insurance companies which in earlier drafts had been exempted from privatisation plans. The Letter of Intent of August 1993 contained a time schedule for the privatisation of 314 public sector companies under Law 203. The sales were to proceed in three stages (fiscal years 1993–94, 1994–95 and

1995–96). A quarter of the assets were to be privatised by mid–1995. The Letter of Intent referred to book values, which were the subject of debate between the international financial institutions, the other donors and the Egyptian government. It did not specify numbers (except for 1993), privatisation candidates, and a time schedule for privatisation²⁷. In September 1993 the IMF approved an Extended Fund Facility for Egypt.

In October 1993, proposed privatisations were delayed because of the presidential elections and the uncertainty over new cabinet members²⁸. At the end of October 1993 Atif Ebeid was appointed public sector minister. Some holding companies started to select privatisation candidates. The Public Enterprise Office began to study the offers of potential investors. The government specified conditions under which 100 per cent of public enterprises could be sold, including to whom the shares preferably should go (e.g. to other public organisations; so-called “strategic” or “anchor” investors supposed to supply funds, modern technology and promising concepts as to product mix and marketing; or employee shareholder associations). Company managers had been reacting to mounting pressure to make factories more profitable by dismissing surplus labour (with temporary contracts)²⁹.

The government announced that 22 public companies would float shares on the stock exchange in November 1993, that is just before an IMF mission to Cairo at the beginning of December was to review the Extended Fund Facility. The IMF was concerned about the slow progress of privatisation. The planned stock exchange flotation was meant to show the international financial institutions that the government was serious about the reform programme. In December Atif Ebeid announced the sale of at least 10 per cent of the Law 203 companies’ shares to the employees.

According to the agreement with the IMF, sales of 22 of the 314 companies under Law 203, with assets of LE 910 million, were to be completed by the end of 1993. But the government only managed to sell two bottling plants (El-Nasr Bottling, Egyptian Bottling) on condition that no worker would be dismissed, to assure the Egyptian public of its commitment to labour rights. A third company was prepared for privatisation. In 1993 the privatisation process had been postponed three times.

No progress was made in negotiations between trade unions, public and private sector representatives and the government to draft a new Labour Law. The trade unions demanded the right to strike (strictly forbidden since Nasser’s times). This was rejected both by the government, afraid of social unrest, or even open revolt, and by company representatives. Some officials of the trade unions (under strict government control since the 1950s) argued against the right to strike. The union establishment had been an instrument of the government rather than a representation of labour’s interests, and it had been rewarded by the state for decades by well-paid positions, status and privileges. The private sector feared the competition of eventual foreign investors in privatisation tenders, and some members of the influential Egyptian Businessmen’s Association rediscovered the anticolonial slogan of “Egypt for the Egyptians”.

1994: Further Delays

After mounting domestic criticism of the Egyptian privatisation agencies, in January 1994 Public Sector Minister Ebeid had to assure the People's Assembly and the Egyptian public that no relatives of state officials were on the staff of the Public Enterprise Office. Company chairmen and managing directors would only earn a maximum of LE 400 per month. In this way he tried to appease the public sector workers who were afraid of losing income as a result of the financial impasse of their companies and who accused the top managers of earning too much.

The IMF and the World Bank kept expressing dissatisfaction with the progress of privatisation. The government reacted to the criticism by announcing an ambitious privatisation plan in January 1994, including 50 companies which were to be sold by the end of July 1994. It remained unclear whether the new programme was an amendment or a substitute for the previous announcement, as it included a number of new privatisation candidates besides names of companies already part of the first privatisation plan, while some state enterprises previously scheduled for privatisation were no longer on the list. A series of advertisements by holding companies indicating their willingness to sell parts or all of certain affiliated companies appeared in the media, although with little effect, during the following months.

After a number of meetings with top managers of loss-making state enterprises Atif Ebeid announced in May that he was ready to replace complete boards if the companies did not improve their performance. Pressure increased by the dismissal of general managers in four big state enterprises. Again the public sector management resorted to cuts in incentives and benefits not part of fixed wages, dismissals and attempts to reduce wages and salaries. The government kept promising job security and promoted employee stockholder schemes to appease the public sector work force.

The donors were not satisfied with the pace of reform. The third instalment of debt relief scheduled for July 1994 was postponed. The US Embassy in Cairo expressed disappointment: "A demonstration of renewed government commitment to the reform program is necessary to stimulate private sector interest in the Egyptian economy and to create a climate which encourages economic growth"³⁰.

Apart from lack of political will, there was a striking lack of professional experience in managing privatisation. Very few people in Egypt were acquainted with the experience gained in other developing countries and Eastern Europe. Top officials and administrators were unable to estimate the possible positive and negative outcomes of different reform strategies³¹.

Between March and May 1994 further privatisation announcements were made and a small number of minority participations in state enterprises were sold. By mid-1994 the government had only approved the sale of El-Nasr Boilers, in stark contrast to the ambitious January 1994 programme to sell 50 state enterprises by July 1994.

According to the agreement with the IMF, assets with a total value of LE 5 billion were to be sold by the end of the year, including at least 65 companies in the first stage³².

Again the promises were not fulfilled. The government claimed to have completely privatised 12 companies. A number of state enterprises sold shares totalling some LE 744 million³³. At the end of the year only three companies had been sold completely to anchor investors [El-Nasr Bottling, Egyptian Bottling (already sold in 1993), and El-Nasr Boilers and Pressure Vessels]. Ten affiliated companies were sold to the employees through employee shareholder associations. A number of employee shareholder associations received 5 to 10 per cent of their companies' shares. Some other enterprises looked for anchor investors without formal notice of sale. The Commercial International Bank pioneered with a successful public offering of a large number of shares, thus starting privatisation in the banking sector.

1995: Poor Implementation

At the end of 1994 another privatisation schedule had been published in reaction to the World Bank and IMF position blocking the third instalment of the Paris Club's debt relief. During the first half of 1995 a number of companies under Law 203 organised initial public offerings and sold between 8 and 40 per cent of their shares to the public, employee shareholder associations, private and public commercial banks, and new investment funds created by private and public banks. The Ministry of Local Administration claimed to have sold 1 749 small public enterprises out of 1 867 under the governorates³⁴.

Meanwhile, it had become clear that the holding companies were an unsuitable vehicle for privatisation. The main reason was that their responsibility for portfolio management led to an interest in building a strong and mutually supportive conglomerate of affiliated firms rather than dismantling it by privatisation. In August a Consultative Committee for the capital market and privatisation operations was established to speed up procedures for the divestiture of state assets, to "support" the holding companies and to prevent them from setting "inaccurate prices"³⁵. New statements by the Public Enterprise Office promised that 40 per cent shares would be offered for public subscription in 50 companies before December 1996³⁶.

The Public Enterprise Office was reported as urging full privatisations instead of partial sales³⁷. After a new round of discussions with IMF officials in July, it was reported that 90 companies would float shares³⁸, another commitment not followed up by real action³⁹. Further major privatisation decisions in late 1995 were postponed due to the parliamentary elections in November 1995. New announcements were made in December.

According to the 1993 agreement with the IMF, at least 25 per cent of the assets belonging to 125 companies under Law 203 selected for privatisation by the Public Enterprise Office, having a book value of LE 10.03 billion, were to have been sold by

mid-1995⁴⁰. However, proceeds from the asset sales of all companies under Law 203 only reached LE 2.44 billion by 31 December 1995⁴¹. From the beginning of the privatisation programme until the end of 1995, only 24 out of the 314 companies under Law 203 had been privatised, including ten liquidations. After negotiations with the IMF at the end of the year, Ebeid promised “to expand privatisation from 60 to 90 companies during the coming years”⁴².

1996: Renewed Reform Efforts

After the appointment of a new cabinet in February 1996 the new Prime Minister Kamal al-Ghazouli was introduced to the public as the promoter of the reform agenda. A privatisation campaign was launched with considerable support from the state media which was clearly intended to impress the donors⁴³. The new privatisation list and its schedule were not released even after the international donors had repeatedly asked the government to provide the information. When the donors expressed dissatisfaction, the government announced a large number of state enterprise sales. Public Sector Minister Atif Ebeid stated “that 71 companies would sell shares worth LE 14 billion to employees and individuals in the coming year”⁴⁴. As had been the case previously, the announcements were unspecific and included differing numbers, but no complete list of company names and schedules for the sales⁴⁵. In May 1996 Ebeid dismissed eight of the 17 chairmen of holding companies because of the poor financial status of their affiliated companies and the slow progress on privatisation.

The reform forces gained strength in mid-July 1996 when President Mubarak visited the United States. After his return new privatisation announcements were issued and interpreted as strong signals in favour of sales of state enterprises. Public offerings were prepared and some were executed (e.g. Kafr El Zayat Pesticides and Chemicals). Meanwhile, the government tried to come to terms with the IMF officials who demanded more serious privatisation efforts, and came up with administrative changes in the privatisation agencies, legal improvements, additional sell-off plans, a number of minority share flotations, restructuring plans, and worker compensation schemes. The government also accelerated sales of its holdings in joint-venture banks and allowed joint ventures to issue new shares, thereby diminishing the relative weight of public ownership, e.g. in the Egyptian Saudi Finance Bank and the Commercial International Bank. New groups of companies were presented to international aid agencies for assessment of their assets and a request for technical assistance on privatisation procedures⁴⁶.

By August 1996, of the 314 companies under Law 203 only seven had sold majority shares, while another five had been sold almost completely to anchor investors. Ten companies of the Holding Company for Public Works had been privatised through employee shareholder associations which took over 95 per cent of the shares. Only 40 companies had taken any steps towards privatisation, 30 of which had sold shares by August 1996, but most of the offerings did not lead to majority sales. Holding companies often sold shares of their affiliates in order to get new financial resources

without giving up their majority shares in the affiliated companies. The book value of state enterprise sales by mid-1996 was LE 10.53 billion, that is less than 15 per cent of the total book value of all Law 203 companies⁴⁷ and less than 2 per cent of the book value of the whole public sector (estimated at some LE 600 billion). At least 25 per cent of the Law 203 companies should have been sold, according to the agreement with the IMF.

As the privatisation announcements of early 1996 had not produced major changes of procedures or tangible results by mid-1996, the government exerted more pressure on the institutions concerned. The privatisation plans were also supported by some prominent businessmen. The establishment of the Higher Privatisation Committee was supposed to depersonalise privatisation decisions and alleviate the fears of decision makers of being held individually responsible for the privatisation of a factory. This had been a major obstacle. The committee also serves as a bargaining place for the allocation of the sales proceeds, another source of conflict over privatisation policies within the administration.

At the end of July the public sector minister announced that 39 companies with a value of LE 3.1 billion would be sold before the end of the year. Some days later, the minister and the prime minister added that within two months 20 initial public offerings would be carried out through the stock exchange and 20 other companies would follow before December⁴⁸. In September the prime minister stated that 30 per cent of the state enterprises were to be sold by the end of the year⁴⁹. Thus the government tried to prepare a positive environment for the IMF talks in October, and leading Egyptian participants, including the Higher Privatisation Committee, competed in making far-reaching privatisation announcements. The public sector minister took the lead with a “one-company-per-week plan” for 1997⁵⁰.

The second half of 1996 saw a large number of sell-off announcements for individual companies, but the results were not convincing. Fifteen Law 203 companies were privatised by initial public offerings through the stock exchange, one company was liquidated and three firms were sold to anchor investors (Table 11). Again the targets were not met. In late 1996 it was announced that 15 companies would be sold in the first quarter of 1997 and that the Public Enterprise Office planned to sell 52 companies annually during the next two years⁵¹.

1997: Problems of Implementation

In 1997 the privatisation programme entered a critical stage. A massive commitment of anchor investors was needed for major modernisation to make the enterprises competitive. The companies which were privatised before 1996 represented the most promising ones in terms of financial status, technology and profitability from the perspective of investors, but more than 270 of the former 314 Law 203 companies were still waiting for private buyers, in addition to numerous other state enterprises

and joint ventures, many of them heavily indebted and technologically outdated losers, and hardly attractive for private investors. In 1996 the average financial performance of Law 203 companies had deteriorated significantly as compared to 1995⁵².

Past sales had used a range of privatisation methods. The recourse to anchor investors, who were expected to upgrade companies, produced unsatisfactory results right from the beginning. By the end of 1996 only six majority privatisations had been carried out with anchor investors. Therefore other methods were adopted. Whereas the government at the outset hesitated to use public offerings, since 1995 they have turned out to be a successful approach. Almost all public offerings at the Cairo Stock Exchange were oversubscribed, however, more recently demand declined. Financial analysts expected major losses as stock prices had increased mainly as a result of speculation unrelated to the economic potential of the companies. Apart from a dozen affiliates, employee buy-outs through the employee shareholder associations also failed. The 10 per cent participation which employee shareholder associations usually get when companies sell shares only plays a minor role, and so do the employees.

The government's new initiative to invite foreign, in particular multinational investors did not obtain a large response either. In 1996 Egypt's share of worldwide private foreign investment was less than 1.4 per cent.

In late 1996 President Mubarak announced that the government's shares in joint ventures would be for sale by the end of 1997. Law 203 companies held participations in 134 joint ventures. In early 1997 it became clear that the sale of government shares in joint ventures, especially in joint venture banks, would be more successful than disposing of the remaining less attractive Law 203 companies, since the best ones had already been purchased by private investors. There were other tentative suggestions to privatise telecom services, the media, electricity distribution, ports, airports, and even the National Bank, Bank Misr, Bank of Alexandria and Banque du Caire. When such trial balloons provoked public outcry, government officials and even President Mubarak immediately denied them. If no major political resistance was encountered, the government gave the impression that it was continuing its privatisation plans. Actually, the privatisation of water and sewage systems was approved by the ministry in charge⁵³. In other cases subject to controversy from different quarters, committees were established to deal with the proposals. During such manoeuvres additional ambitious privatisation announcements were made.

In the first quarter of 1997 four Law 203 companies were offered to potential anchor investors, and four other affiliated companies were privatised through initial public offerings of more than 60 per cent, with a sales value of LE 398 million. Holding companies also offered some of their own fixed assets for sale. As of 31 March 1997, Egypt had privatised 46 Law 203 companies with a sales value of approximately LE 10.4 billion.

Some Case Studies of Privatisation

The Privatisation of the Commercial International Bank

The Commercial International Bank (CIB) is a former joint venture of the National Bank of Egypt and the Chase Manhattan Bank. It was founded in 1975 as Egypt's first joint venture bank under the Infitah Policy (opening policy). Later Chase sold its participation to the National Bank of Egypt. The latter delegated the executive management to the CIB senior staff and hardly interfered in current business operations. First plans to restructure the CIB had been already drafted in 1990, before the new economic reform programme of 1991 was announced by the government. In April 1993 the CIB launched a three-year capital restructuring plan with the aim of becoming Egypt's first diversified financial services group⁵⁴.

Box 5.10. Commercial International Bank: The First Egyptian Bank on the London Stock Exchange

The first step in the capital restructuring and privatisation of the CIB was the divestiture of a large number of CIB shares held by the National Bank of Egypt to the latter's and CIB employees. The first transaction was approved in September 1991 and carried out in 1992, resulting in a 30 per cent ownership transfer to the banks' staff. In a second step the capital stock was increased by retaining profits, also in 1992.

The third step met the bank's need for LE 300-400 million in additional capital by issuing stocks available to the public in September 1993, widely announced in Cairo newspapers. This was Egypt's first large-scale share offering under the new economic reform programme. In spite of a highly critical report about the bank's financial condition in a leading newspaper, more than 2.25 million shares were sold to some 6 000 subscribers, with total proceeds of LE 585 million.

In 1996 CIB's largest shareholder, the National Bank of Egypt reduced its 42.6 per cent stake to 20 per cent by an issue of global depository receipts listed on the London Stock Exchange, marking the return of Egyptian companies to international financial markets.

Source: El-Labban, 1994.

The successful privatisation of the CIB and its placement of global depository receipts show that even complex privatisations are possible if they are supported by the government and a strong public company's top management is committed to reform. The CIB privatisation was Egypt's largest divestiture to employees, the largest public share offering in the Egyptian financial market and the first instance in which an Egyptian company used global depository receipts.

The Privatisation of the Egyptian Bottling Company (Pepsi Cola) in 1993

The Egyptian Bottling Company, holding the Pepsi Cola franchise for Egypt, was one of the first two companies under Law 203 sold in 1993 to a group of investors who guaranteed that no employee would be dismissed during a period of three years. The government was wary of reports about negative privatisation results, especially concerning workers' rights. However, the case belongs to the few success stories of Egypt's privatisation programme.

Box 5.11. The Pepsi Cola Turnaround

From 1994 to 1995 the work force of the Egyptian Bottling Company (Pepsi Cola) increased from 2 721 to 5 361 employees, i.e. by 97 per cent. The overstaffed middle management of 1 324 posts was reduced during the same period to 44, and top management positions were trimmed down from 22 to 7. The average monthly salary increased from LE 345 to LE 435. Production increased by 42 per cent, with steep rises of labour productivity.

Source: IBTCI, Cairo, unpublished material.

Media Campaigns

A continuous stream of announced privatisations attempted to conceal the small number of privatisations and the lack of commitment to the programme among government officials and public sector administrators. Over the years, this pattern became a tool to provide the momentum for bargaining when a new round of donor negotiations loomed and foreign perceptions of Egypt's structural reforms mattered.

Throughout 1990 and 1991 the government successfully resisted donor pressure to publish detailed lists of privatisation candidates and to begin meaningful preparations for large-scale sales. The conflicts over the slow pace of privatisation continued through 1992. In 1993 the government objected to the low valuation of company assets and argued that sales under donor pressure would further decrease the possible proceeds from sales. In the summer of 1993 Minister of Public Affairs Atif Ebeid publicly

criticised World Bank pressure to speed up the reforms. The government still accepted the new World Bank reform package which now included state banks and insurance companies that had been previously been exempted from privatisation plans. In late 1993, shortly before an IMF mission to Cairo was to review the Extended Fund Facility signed in September, the government announced that the 22 state enterprises which were supposed to be sold by the end of the year, were to float shares on the stock exchange very soon.

Donor dissatisfaction with the public sector reforms continued during 1994. In March the government launched another campaign of announcements with a view towards forthcoming negotiations with the IMF in June. Meanwhile, Public Sector Minister Atif Ebeid, declared the start of a new reform phase. The government turned to public share offerings of Law 203 companies at the newly revived stock exchange. But the third instalment of debt relief scheduled for July 1994 was postponed because Egypt's record on reform failed to obtain the IMF's approval.

A new round of negotiations was scheduled for September, and another wave of government announcements was unleashed in August. The prime minister, supported by other cabinet members, launched the next campaign in October, culminating in an announcement that shares of 17 companies would be floated by mid-January 1995⁵⁵ and that 65 companies would be sold by the end of the year, thus preparing for the December meeting with an IMF delegation in Cairo.

Throughout 1995 the IMF and World Bank repeatedly voiced dissatisfaction with the pace of reform, and threatened to block the third instalment of debt relief. The government always intensified its privatisation campaigns in the media a few weeks before the start of new negotiations. To reopen talks with the IMF in November 1995, the public sector minister announced in September that there would be 22 new share offerings in October⁵⁶. After the elections of November 1995 and the appointment of Kamal al-Ghazouli as new prime minister in January 1996, another take-off in the privatisation programme was announced. New negotiations began in January 1996, and the government initiated its biggest image-building campaign of the whole reform period. The campaign lasted until March 1996, just before the next round of negotiations was scheduled, since the January talks had left the donors unsatisfied. For the first time, Egyptian officials publicly discussed the possibility of privatising public utilities, infrastructure and government assets in land reclamation companies⁵⁷.

As the intervals between the meetings with the donors became shorter, there were now continuous media campaigns, mainly meant to impress the donor community, with news about planned sales, negotiations with bidders and prospective investors, and initial public offerings, in addition to special announcements a few days before the start of new talks. Before the April negotiations in Washington, a wave of new announcements was topped by the first real sale of a Law 203 company since February.

Shortly before the May negotiations with IMF officials in Cairo, the government announced plans to privatise power stations and insurance companies for the first time. After the failure of the talks, a number of public companies under the Suez

Canal Authority were taken off the sales list⁵⁸, since the political risk of selling symbols of national independence was high⁵⁹, and the offer to sell them had not brought Egypt closer to the third instalment of debt relief.

New Egyptian sales proposals of June 1996 left the IMF unsatisfied. Another round of public announcements was launched. The IMF objected to a “quasi-privatisation”⁶⁰ and insisted on majority sales to the private sector, whereas the government only floated a minority of shares at the stock exchange.

The August round of IMF negotiations was prepared in July: a privatisation committee was established, new announcements of planned privatisations were made, and the model for a concession for privately built and operated highways was presented. More announcements were made after President Mubarak returned from his visit to Washington in July. The next round of massive announcements occurred in September, in preparation for the October negotiations which were to decide on the third debt write-off.

Overall Results of the Privatisation Programme

The record of privatisations is poor in comparison to the announced programmes. The privatisation policy applies mainly to the initial 314 (still 298 in early 1996) companies under Law 203, with an estimated book value of LE 72.4 billion⁶¹. This represents less than 15 per cent of the total public sector whose estimated value is LE 600 billion⁶². Officials remain silent about the remaining bulk of the public sector, including the so-called economic authorities and the vast number of economic activities remaining under the control of the central government and its organisations, the governorates, the municipalities and the military-industrial complex. No data are available for the latter, but observers presume that its assets are not included in the LE 600 billion. In recent years the military factories, supposed to be more efficient than the rest of the public sector, have moved into large-scale production of civilian consumer and investment goods.

There are also no consistent and comprehensive data on the composition of the public sector in terms of subsectoral work force, asset values, production figures, significance of certain companies for a subsector, etc. Therefore, one cannot compare the relative share of the companies scheduled for privatisation to the rest. No detailed information is available on employment, again with the military-industrial complex covered by strict secrecy⁶³.

Another unknown is the number of companies that are doomed to be liquidated due to their accumulated losses and inefficiencies, or the number of employees who might be affected. No serious plans have been developed by the government to deal with this problem. The Egyptian side tends to shift the responsibility for the social impact of the privatisation process to the donor community and the Social Fund.

The government's commitment to privatisation until 1996 was fairly weak. Usually privatisation activity or announcements gained momentum when a new round of negotiations with the donors was in sight. Much verbal commitment to reform was not followed by effective implementation. For a number of years the government kept insisting that large subsectors of the economy or certain important enterprises such as the four dominant public banks would not be privatised, although this position has been subject to discussion and reconsideration since 1997⁶⁴. Restructuring of so-called strategic enterprises which were to remain under state control was proceeding very slowly. On the other hand, in one subsector which had witnessed strong private sector participation during recent years, efforts to reassert public dominance began in 1996. Thus the Cairo Transport Authority stopped giving new licenses to private entrepreneurs, and it procured 800 new buses for local public transport services, thereby crowding out the new private competitors.

Public companies are still investing, to increase efficiency, as their spokesmen say. Also a number of joint ventures between public and private sector units were established during the last three years. The public sector still grows in absolute terms, but since 1996 the government has pressured holding companies to speed up the privatisation of their affiliated companies. The Higher Privatisation Committee was established to protect individual decision makers from anti-reform political pressure.

From 1991 to 1996, only 42 out of 314 Law 203 companies were privatised. These included six sales to anchor investors, ten employee buy-outs through employee shareholder associations, 15 initial public offerings at the stock exchange and 11 liquidations. Thirteen joint venture banks were privatised. By the end of 1996 only 64 out of 314 companies had been affected by the privatisation programme. Total sales amounted to LE 10 billion. The shares of Law 203 companies sold on the stock exchange were worth LE 3.56 billion, anchor investor privatisation proceeds were LE 1.3 billion, asset liquidations reached LE 480 million. The companies sold unutilised assets worth LE 3.3 billion. The local governments privatised assets with a sales value of LE 300 million and privatised stakes in joint ventures amounting to LE 130 million⁶⁵.

After seven years of debate, discussions finally began to focus on technical issues of implementation since late 1996. The former anti-privatisation consensus among large parts of the elite gave way to the insight that privatisation was unavoidable, although this did not mean that privatisation would be actively supported by the public sector constituencies.

In recent years, the government had been able to keep Islamist terrorism under control and keep the internal political situation relatively stable. This allowed it to redirect resources and decision making to reform issues. At the same time, the influence of labour unions, a major opponent of privatisation, appeared to decline⁶⁶.

Thus the main opponent of reform remains the public sector establishment itself. It is unknown to what extent the privatisation plans announced in the autumn of 1996 will be carried out, especially after the IMF approved a new stand-by loan in October 1996, which was the precondition for the last instalment of the Paris Club's debt relief.

This means donors have relinquished their main leverage on the Egyptian reform programme. The internal balance of vested interests may still be too strong within Egyptian society to sustain reform. The entrenched rent-seeking outlook may continue to affect action towards building an internationally competitive business sector in the face of declining foreign assistance and mounting exposure to more successful newly developing countries both within the emerging Euro–Mediterranean Free Trade Zone and beyond.

Notes

1. Dessouki, 1991.
2. Rathmann, Voigt *et al.*, 1988.
3. Abdel-Rahman and Abu Ali, 1989.
4. *Ibid.*
5. Handoussa, 1991a: "Illiteracy and ability to read only were still accounting for 75 per cent of the direct production workers in public sector, 86 per cent in the formal private sector."
6. Soliman, 1992.
7. Abdel-Rahman and Abu Ali, 1989.
8. Serco Education Limited, 1994.
9. Out of the approximately 2 000 enterprises, a first group of 30 companies from Manufiya, Fayyoun and Dumiat were chosen to pioneer the privatisation of enterprises under the jurisdiction of the governorates. The majority of these companies was made up of small units located far away from metropolitan areas and without strong union representation eventually opposing privatisation steps.
10. Cf. Chapter 4.
11. *Middle East Economic Digest*, 18 June 1993.
12. Köndgen, 1995; Arab Republic of Egypt, 1993.
13. Cf. Chapter 4.
14. Arab investment (mainly from the Gulf states) is not referred to as "foreign" in the narrow sense in Egyptian terminology.
15. Hill, 1996; Handoussa, 1990.
16. Cf. *Middle East Times*, 23-29 May 1997: "Recent skirmishes between police, landowners and tenants have whipped Delta farmers into a panic. The farmers are afraid that a land rent law passed in 1992, which comes into effect this October and removes caps on rents and gives landowners the unprecedented authority to evict tenant farmers, will be used to force them off land that some have been renting for over 40 years. The farmers, however, vow to stay on their land and challenge police to remove them."

17. Observers and opposition parties denounced the elections “as the most fraudulent in Egypt’s modern history and the authorities were accused of widespread vote-rigging, ballot-box stuffing and intimidation. Opposition parties claimed that the police acted on behalf of the NDP, that there were mass arrests of opposition election agents, and that polling stations were closed for long periods of time. The independent Egyptian Organisation for Human Rights (EOHR) alleged that the vast majority of irregularities were undertaken on behalf of the NDP ... The US State Department expressed its reservations on December 1, stating: ‘There were some difficulties we noted with harassment, arrests, detention ..., trials of political activists and campaign workers, and reported government interference in the election.’ Nevertheless, on December 9, the Council of State overruled the administrative courts, which had declared that the results of around 80 constituencies were provisional, pending suits alleging electoral abuses. Yet in previous years the People’s Assembly has not hesitated to nullify the results of all suits against it”. Cf. Economist Intelligence Unit, 1996.
18. *Ibid.*
19. *Financial Times*, 8 May 1996.
20. A number of recognised professionals left the Public Enterprise Office because of their dissatisfaction with its ineffectiveness and limited authority.
21. Arab Republic of Egypt, 1993*a*.
22. Köndgen, 1995.
23. O’Farell, 1995.
24. *Ibid.*
25. The new regulations concerning public sector borrowing also limited the ability of holding companies to guarantee loans for their affiliated companies or to subsidise them. The Central Bank also introduced a new classification for commercial bank loans and tighter control mechanisms for commercial bank lending. These measures were aimed at ending direct and indirect subsidies to state enterprises in line with IMF demands. Nevertheless, both the public sector and the government administration still found ways to evade the hard budget constraint.
26. Arab Republic of Egypt, 1993*a*.
27. Köndgen, 1995. Arab Republic of Egypt, 1993*a*.
28. When a Saudi investor offered to purchase part or all of the Suez Cement Company no decision was made. The sales of El-Nasr Bottling and Egyptian Bottling were not finalised for the same reasons.
29. According to the Labour Law, permanent employees could not be fired, but managers decided that the large number of surplus workers would no longer receive the usual wage supplements. Additional benefits were also cut.
30. *Middle East Times*, 20 June 1994.

31. Egyptian decision makers are even unfamiliar with the large-scale unemployment resulting from the eastern European reforms. The Egyptian government in late 1995 organised a conference to clarify the relevant issues with international economists, administrators and consultants. Until then, leading officials had no real understanding of the social impact of privatisation, especially with regard to unemployment.
32. *Al-Wafd*, 3 December 1994.
33. IBTCI, 1995a; IBTCI Quarterly Review, August–December, Annex 6.
34. *Egyptian Gazette*, 17 May 1995.
35. *Al-Ahram*, 8 August 1995.
36. *Al-Wafd*, 28 May 1995. Until then, 12 state enterprises had offered 10 per cent of their shares. From June another 38 companies were supposed to make initial public offerings.
37. *Al Ahram Weekly*, 8 June 1995.
38. *Al-Akhbar*, 26 July 1995.
39. When a newspaper in August reported that the government was planning to sell the “big four” state-owned banks, the Minister for Economy and Foreign Trade and the Prime Minister denied such plans (*Al-Arabi*, 31 July 1995; *Al-Ahram*, 8 August 1995; *Al-Musawwar*, 11 August 1995).
40. Köndgen, 1995.
41. IBTCI, 1995a, Annex 6.
42. *Al-Ahram*, 18 November 1995; *Al-Gumhuriya*, 18 November 1995.
43. Egypt’s primary interest still was in the third instalment of debt reduction by the Paris Club. Despite an ambiguous record on economic reform, as understood by the donors, the government-controlled media presented the announcements as a planned transition to a second stage of reform and stressed the expected positive results.
44. *Al-Akhbar*, 6 January 1996.
45. *Al-Ahram*, 21 January 1996
46. The EU Project Monitoring Unit that had only been dealing with nine small and medium sized hotels received a list of 33 companies and was requested to organise and monitor all necessary steps to prepare future sales. On the list were firms like the Egyptian Iron and Steel Company in Helwan with its 22 800 workers. Other companies were the loss-making Alexandria Shipyard, Telemisr (producing TV sets and related products), two road transport companies and a whole range of metallurgic and engineering companies and of tourist facilities.
47. The total book value of companies under Law 203 was estimated in 1996 at LE 72.43 billion while other statements of the Public Sector Minister proceeded from an estimated book value of LE 88 billion. Cf. IBTCI, 1996a: IBTCI Monthly Report August 1996, Annex 4; *Al Ahram Weekly*, 21 March 1996.
48. *Al-Akhbar*, 29 July 1996; *Al-Ahram*, 6 August 1996.
49. *Al-Akhbar*, 4 September 1996.

50. *Al-Akhbar*, 15 November 1996.
51. *Al-Alam Al-Youm*, 18 December 1996; *Al Ahrām Weekly*, 26 December 1996.
52. IBTCI, 1996*b*; IBTCI Quarterly Review, October–December 1996.
53. *Al-Ahrām*, 21 January 1997; *Al-Ahālī*, 19 February 1997.
54. El-Labban, 1994.
55. *Al-Ahrām*, 10 November 1994.
56. *Middle East Economic Digest*, 29 September 1995;
57. Plots ranging from 50 to 200 feddans for individuals and up to 150 000 feddans for joint stock companies were offered for sale, cf. *Middle East Observer*, 21 February 1996.
58. *Al-Arabi*, 27 May, 1996.
59. Nasser’s nationalisation of the Suez Canal on 26 July 1956 provoked the military intervention of Britain, France and Israel in October–November 1956.
60. In May 1996 the El Nasr Transformers and Electrical Industries Company (ELMACO) was offered for privatisation. A majority share went to a public–private joint venture which was dominated by the public sector partner; cf. *Al-Wafd*, 22 June 1996.
61. Other statements of the Public Sector Minister estimate a book value of LE 88 billion. Cf. IBTCI, 1996, Annex 4; *Al Ahrām Weekly*, 21 March, 1996.
62. *Al Ahrām Weekly*, 21 March 1996.
63. Cf. Richards and Waterbury, 1990.
64. Cf. earlier discussion of developments in 1997.
65. IBTCI, 1996*b*.
66. *Al Ahrām Weekly*, 24 October 1996: “In the transition the role of trade unions has been restricted to discussing retirement benefits and other day to day matters, whereas formerly much larger issues would be debated.”

The Weakness of Civil Society

Weak Institutions and Political Constraints

The General Setting of a “Hydraulic Society”

Egypt’s political system does not offer sufficient outlets for creative or critical views. As a result, the small political elite supporting the political leadership is insulated from constructive criticism and the new approaches which will be necessary to meet the challenges of the 21st century.

The political system of Egypt has always been highly centralised. Its prime concern was to control the essential resources, i.e. arable land and the annual Nile flood for irrigation before the Aswan dams had been built. Water management called for central control, and Egypt traditionally was a “hydraulic society” (Wittfogel) *par excellence*.

The military coup of 1952 carried out by the Committee of Free Officers shook off King Farouk’s corrupt feudal rule, but it did not take long before a strict new centralised system had been established under which Egypt became an authoritarian state with a single party, the Arab Socialist Union (ASU). After President Nasser’s death in 1970, his successor President Anwar al-Sadat felt that it was necessary to broaden parliamentary representation¹.

In 1976 Sadat took a step towards democratisation by creating a left, right and centre within the ASU, before dissolving it 1977 and declaring each of the three groups independent political parties. The majority of the former ASU members joined the centre party which served as the president’s base of support². The party supported Sadat’s turn towards the west and the peace treaty with Israel, eager to side with the government and to share the benefits of an economy still dominated by the public sector and career opportunities for loyal adherents.

The right wing called for free enterprise and limiting the public sector. The left opposed the western orientation and supported the social achievements of the 1952 revolution. In 1978 the New Wafd emerged as a centre–right party and inheritor of the old Wafd, which had led the struggle for Egyptian independence against the British. Now, it zeroed in on the mushrooming corruption associated with the government's Open Door Policy, and supported a revival of the private sector and stronger economic and political ties with western countries³. Sadat founded the National Democratic Party (NDP), which replaced the old centre as the president's political base. A number of other new parties emerged around the same period, partly supported by High Court decisions against attempts at suppressing the opposition. The impact of these parties on the Egyptian political process remained quite limited, but they were allowed to publish newspapers with a degree of freedom of expression unique in the Arab world. The People's Assembly, however, remained dominated by the NDP's overwhelming majority which provided support for decisions made by the executive.

The Political Framework of the Reform Programme

By 1990, six parties dominated the political scene: the ruling NDP, the New Wafd, the National Progressive Unionist Party on the left, the Liberal Party, the Umma Party, siding with Islamist trends, and the Socialist Labour Party. In addition, the Muslim Brotherhood was a movement of considerable weight although it was not authorised to function as a political party⁴. With increasing Islamist activities, the Muslim Brotherhood came under fire⁵.

The struggle against the violent Islamist movement also led to a deterioration of human rights and a general marginalisation of potential political critics in the process of policy formulation. The quasi–democratic system limits expression of economic and political tensions so they can be channelled into the political mainstream. Under this political system, divergent views that do not threaten the ruling regime can be expressed, which would exclude Islamists and Communists. In practice, the system has given rise to a rigidity which does not allow for open avenues to political change and adaptation. Thus it has not adopted the sort of economic and political transformation occurring in competing newly industrialising countries, which have in varying degrees democratised their political leadership. Technocratic elites have led a successful process of industrialisation, for example, in Taiwan and South Korea, where it was understood that centralised command structures had become inadequate to keep up with the challenges of rapid economic and technological change. The Egyptian political system reflects the economy's lack of development in relation to the more successful newly industrialising countries. This became painfully apparent during the reform process. Alternative concepts are being ignored because they might threaten the power of allegedly unerring decision makers. Thus a large amount of human resources — intellectual potential, managerial ability and sources of technical expertise — is being marginalised.

The government's control over universities, research institutes, NGOs, and other forums of critical thought has been tightened in recent years, mainly as a reaction to the Islamist assault. Nonetheless, the Egyptian state is no monolithic entity. Different groupings with conflicting objectives struggle for a reallocation of scarce resources in the economic reform process⁶.

The relationship between the executive and the legislature is determined by the weak institutional structures as well as by a traditional submissiveness towards authority and a glorification of the ruler in the political culture. "The Egyptian President rules virtually by command, having little need to persuade cabinet ministers, top bureaucrats engaged in governing or even parliament, in which he invariably has a crushing majority. There are few checks on such far-reaching presidential power"⁷. The almost unlimited power of the presidency and its inner circle does not imply that the executive is absolutely unaffected by activities of other groups in the society. Their influence must be seen as a factor that has to be taken into consideration by the government.

The extraordinary power of the president also stems from the parliament's members' conception of their role. The NDP's overwhelming majority ensures that government decisions pass without real debate or essential modifications. The legislature is reduced to the function of legitimising the government without providing a corrective. Although the Egyptian constitution grants extraordinary power to the president, the complete marginalisation of the parliament was not intended⁸.

Box 6.1. Lack of Competence of Some Members of Parliament

In the governorate of Sohag, candidates for the election of the People's Assembly in 1990 were interviewed about their conception of the parliamentary system: 47 per cent were unable to explain how their own party platform differed from the others, 44 per cent identified differences which were unimportant or which did not really exist, 10 per cent felt that political participation was unnecessary, 20 per cent held that it should be restricted to persons of high social status and wealth, 25 per cent were unable to explain the advantages of citizen participation in politics, 40 per cent had no idea of the importance of political parties, and 30 per cent were unaware of the role of political parties in a democracy. Only 5 per cent could name five of the existing 13 parties, 25 per cent could only name two. Most candidates were unable to tell the difference between executive, legislature and judiciary, and 55 per cent did not know that parliament should be the only legislative body. The majority agreed that Egypt suffered from political problems but very few could name some of them.

Source: Zaki, 1995.

“The ineffectiveness of the legislature as the result of its low level of competence has led the executive to marginalise it further by treating it in the most cavalier fashion. Striking examples for this are abundant: *i*) taxes are raised by executive decree; *ii*) the budget of the armed forces cannot be discussed (on grounds of national security); *iii*) major economic policies, such as those involving the IMF restructuring programme, which deeply affect almost every citizen, are settled by the government in private negotiations with the IMF and the results are not even made officially public, except in vague general terms, if at all”⁹. Since the revolution of 1952 there has not been a single case in which the parliament did not pass a budget or a government bill and there have been no motions against the government.

The Judiciary’s Relative Independence

The Egyptian judiciary plays an important role as the defender of basic rights. During the 1990s remarkable judicial rulings often rejected arbitrary attacks on civil rights, political parties, interest groups and individuals by government decisions or administrative interference. The courts have contributed to a gradual but important change of the political system. The registration of some new political parties was only possible because of independent court decisions. There have also been a number of judgements stating that national or communal elections were faked or manipulated and therefore invalid, although the court decisions were often ignored by ministries and parliamentary committees.

This independence is being threatened by the government’s attempt to co-opt prominent members of the judicial system by offering them remunerative positions in the administration. “The government recruits from the top echelons of the judiciary consultants to the government and even appoints others to the board of directors of public sector companies... It tends to undermine the presumed neutrality and autonomy of the judiciary, thereby threatening the integrity of the most central institution of constitutional government”¹⁰. On the other hand, in the field of commercial law the judicial system cannot meet international standards and lacks professional competence and international exposure.

Political Parties and Economic Reform

The System of Political Parties and Its Weaknesses

In 1977 President Sadat introduced a multiparty system without really replacing the authoritarian system¹¹. “Besides lending greater legitimacy to his regime and enhancing stability, a multiparty system also served to improve his image in front of his new Western friends”¹². The changes were initiated from above and were not the result of political mass mobilisation demanding democracy.

With the rise of the Islamist movement the security apparatus was mobilised to eliminate any resistance against the regime. The opposition parties and their publications were tolerated, in part, to allay concerns in parliaments of donor countries, rather than as a serious commitment to democracy.

Right from the start in 1977 the Law on Political Parties made it clear that parties adhering to unwanted ideologies such as Communists and Islamists would not be permitted to operate in Egypt. Since 1977 the so-called Committee on Political Parties which is dominated by the NDP denied a number of political groups the right to establish new parties¹³. Liberal courts overruled many Committee decisions and permitted the establishment of new parties.

However, the party system and party politics never achieved credibility because of the NDP's almost unlimited access to resources and institutions of the state, and the public awareness that elections were never fair but subject to government intervention and to the financial means of the candidates¹⁴. Political parties in Egypt do not have any broad base in the society. This partly explains the important role of other organisations, especially professional syndicates. None of the Egyptian parties can claim to express the collective will of a particular social group. The parties' ability to mobilise people is weak, and the opposition parties are largely ignored by the government. They also suffer from the restrictions imposed by the laws on political parties and the state of emergency that has been in effect since the beginning of the 80's. "Government oppression remained a basic obstacle to the parties' abilities to reach the general public. The government does not allow any party to hold seminars or conferences outside its headquarters, and even in the very few cases where the government has allowed this, e.g. the Wafd conference in Suez, for example, it has been under strict security surveillance"¹⁵.

The parties are subject to factionalism. Some parties have a patriarchal leadership and undemocratic internal structures. The staffing of their top positions has been based on family links and patronage networks. Party chairs in several cases have only changed after the leader's death. Internal democracy is usually very weak.

The lack of ideological identity of the parties (except for Nasserists and Tagammu¹⁶) allows inconsistencies about their declared objectives. In up to two thirds of a sample, the political statements made by the newspapers of various opposition parties were not in line with their general proclaimed platform¹⁷. E.g. the right wing, pro-Islamic Ahrar Party, traditionally supporting capitalist concepts and economic reforms, opposed privatisation and deregulation as in the field of rent controls. The traditionally liberal Wafd demanded stricter censorship to protect Islamic values¹⁸. "The five leading parties, while managing to maintain distinctive auras about themselves, have generally failed to provide concrete well-formulated plans offering realistic alternative solutions to Egypt's developmental problems"¹⁹.

The majority of the people has no adequate party representation. "The country's workers... have not come yet to appreciate the value of political parties or democracy as the way to improve their conditions of living. In the recent past, they pinned their

hopes to attain these conditions on a benevolent populist leader — Abdel-Nasir — and in the most recent past on migration to Gulf countries. They realise that opposition political parties at present are too weak to get these conditions from the government or private employers. The government would seem to them to be the only actor who could fulfil their legitimate aspirations, if it so wishes²⁰. The ineffectiveness of the secularist parties in challenging the government's policies has given rise to the success of various Islamist opposition groups, especially because the political parties neglected the rural areas and the poor suburban districts of the large cities²¹. Some observers assume that apart from the Wafd and the Islamists none of the opposition parties has enough followers to challenge the NDP; no other parties could even nominate candidates for more than 20 per cent of the parliamentary seats²². Seven Egyptian opposition parties (UP, GP, PDP, EASP, MFP, SJP, UDP²³) are totally insignificant and are considered parties in name only.

The National Democratic Party

The NDP was founded as the president's party in 1977 when President Sadat introduced the multiparty system, but even the dominant NDP is not a party in the conventional sense as it has no public roots of its own based on ideology, supporters and party organisation. Candidates succeed in elections mainly because they are supported by the state and its administration. Both voters and members hope to obtain patronage and rent incomes resulting from close ties to the public official establishment and its clientele networks. The NDP could be considered as an extension of the governing system. It provides members with extraordinary possibilities for personal benefits (e.g. careers, business opportunities, overcoming administrative or even legal obstacles, etc.).

The NDP also maintains a high profile in the countryside due to its links with the state apparatus, provincial governors and local leaders. It has support in rural areas (despite the new tenants law), from trade unions (despite privatisation and restrictions on workers' rights) and is sympathetic to the demands of the businessmen's associations representing the new Egyptian entrepreneurs. The party has had no coherent platform since its foundation and tries to rally a maximum of divergent interests.

The New Wafd Party

After an unsuccessful attempt to get registered as a party, the New Wafd was recognised after a court ruling in 1978. The New Wafd is the successor of the old Wafd which had led the nationalist movement against the British in the 1920s and had been a mass party prior to 1952 with a very broad constituency²⁴. The New Wafd is much smaller. It has local offices only in the main cities and represents the bourgeois

upper class. The party failed to re–create the liberal middle class constituency of its predecessor. Its present voters tend to be more conservative and business–oriented and closer to the authoritarian state²⁵.

The New Wafd still suffers from its reluctance to accept the new elite that emerged from the 1952 revolution. This led to a short–lived alliance with the Islamists in 1984. The Waft was unable to renew its ideology and organisational structure or re–establish its former influence and popularity. Power is vested in the chairman who rules the party as a personal domain. The main newspaper is *Al–Wafd* (daily). The party also has the second largest variety of local newspapers.

The Left: NPUP, ADNP and Communists

The left could become a force in a freely elected parliament if the leftist parties were able to establish a coalition. Due to the Islamists' violence in recent years, the left has gradually moved towards the centre. Thus the distance from the government has declined. The collapse of the Eastern Bloc has contributed to an ideological haziness.

The Nationalist Progressive Unionist Party (NPUP-Tagammu)

The Tagammu was founded in 1977 as one of the three parties which emerged from the ASU. It rallies Nasserists, nationalists, Marxists, socialists, left social democrats and independent leftists. It has no homogeneous political organisation. Its influence has been declining during the last ten years. Its main newspaper is *Al–Ahali* (weekly). Tagammu also publishes a large number of regional and local newspapers.

The Arab Democratic Nasserist Party (ADNP)

The Nasserist Party, founded in 1992 after a court ruling, can be described as leftist–statist with a strong pan–Arab orientation. Some factions favour closer ties with the Islamic movement. Internal ideological conflicts and power struggles weaken the party's ability to become a more important player in the political arena. In early 1996 a generational conflict erupted when younger members tried to reform the organisational structure and the party's activities but met strong resistance from the old guard. The younger Nasserists want to transform the party into an efficient opposition²⁶. The Nasserist Party publishes the largest number of local newspapers. Its main publication is *Al–Arabi* (weekly).

The Communists

Several groups call themselves communists. The most important one is the Egyptian Communist Party, with historical links to the communist movement in Egypt since the 1920s. Some other communist groups have fewer than a hundred members. The communists are among the outlawed political forces and this creates organisational problems and limits activities²⁷. Their relationship with the government became less hostile after they saw the Islamist terrorists as a common enemy in the early 1990s.

The Islamic “Alliance”²⁸: Muslim Brotherhood, the Socialist Labour Party and Umma Party

The Islamist camp includes members and sympathisers from all social strata and is able to mobilise large numbers of people, even demonstrate in the streets of larger cities. Some observers estimate that the Islamist candidates would win about 15 per cent in free elections, which is much less than what their propaganda wants observers to believe. Others are convinced that the Islamists would assume power if free national elections were held. The Islamists run their electoral campaigns under the slogan “Islam is the solution”, but fail to provide a specific political and economic programme. They claim to rely on the Sharia²⁹. “The Islamists base their claim to legitimacy on a combination of Islamic credentials, the promise of socio–economic reforms, including the elimination of corruption, and an assertion of Egypt’s independence from what they currently perceive as its subservience to Western interests”³⁰.

The Socialist Labour Party (SLP)

The SLP was established by presidential decree in 1987. It started with a left wing orientation and was later transformed into an Islamic party resulting from an alliance with the Muslim Brotherhood. This ideological shift was imposed by the top leadership without regard to other views among activists and members and even the executive committee³¹. The SLP has a dictatorial leader who is unwilling to accept dissenting opinions. Its newspaper is *Al-Sha’ab* (twice weekly).

The Muslim Brotherhood (MB)

Although the Muslim Brotherhood, with an estimated 1 million members, is not a formal political party, to a certain extent it plays a similar role. The Muslim Brotherhood has a distinct ideology and political orientation, a strong organisational structure and hundreds of thousands of supporters who vote in national elections for its candidates running on the ticket of formally registered political parties or as independents. The Muslim Brotherhood is considered to be the most important group in the political arena in terms of numbers of members and sympathisers, and the depth

and intensity of its opposition towards the regime³². Its members are mainly recruited from the state bureaucracy, young professionals, the petty bourgeoisie and the lower middle class. Their influence at the universities is increasing, especially in the science and technology departments³³.

The Umma Party (UP)

The Islamic fundamentalist Umma Party was founded in 1984 after a court ruling. It does not play a major role in Egypt's system of political parties but is an integral part of the "Islamic Alliance". Family connections are a main feature of the Umma Party. The vice-chairman of the Umma Party is Samir Ahmad al-Sabahi, son of Ahmed al-Sabahi, the party chairman. The major party posts are held by a number of relatives³⁴. Their newspaper is *Al-Umma*.

Other Parties

The Liberal Party (Al-Ahrar Party)

The Liberal Party was founded in 1976 and has a rightist position with some Islamic currents which are opposed, however, by a strong Nasserist-nationalist tendency. The party suffers from a lack of basic ideological consensus. Its 21 newspapers represent different factions within the party (Nasserists, socialists, Islamic fundamentalists). The most important publications are *Al-Ahrar* (weekly) and *Al-Nour*.

The *Green Party (GP)* was founded in 1991 and has a strong environmentalist and civil society orientation.

The *Populist Democratic Party (PDP)* was founded in 1992. It has no newspaper.

The *Egypt Arab Socialist Party (EASP)* was registered in 1992 and is left of centre.

The *Misr Al Fatah Party (MFP)* was founded in 1992 and is right of centre. It has no newspaper.

The *Social Justice Party (SJP)* was founded in 1993 and calls itself libertarian.

The *Union Democratic Party (UDP)* was founded in 1993 and has no clearly defined political orientation.

The Political Parties' Reaction to the Economic Reform Programme

In earlier years different factions of the NDP clashed over alternative reform strategies. Nevertheless, since 1989 the NDP has proposed far-reaching sales of assets of state enterprises. In 1994 the NDP Economic Committee called for legislation concerning privatisation of state enterprises (Unified Labour Law, Housing Law, Unified Investment Law, Traffic Law). Some NDP members of Parliament took the initiative in starting the debates on corruption and inefficiencies in government and administrative bodies³⁵.

NDP members belonging to the influential businessmen's associations support reform policies and a stronger commitment to reform by the government, but their stand is ambivalent as private enterprises still seek protection from the state³⁶. Other NDP members oppose the sale of public sector companies for nationalist or social reasons. Some members of Parliament stated that capitalism and free markets would "take Egypt back to the days before the July Revolution". Investors, instead of buying public sector companies, should set up new companies to expand the country's productive potential. A member of Parliament stated that "offering the public sector companies on the stock market is like taking the defendant to the execution room". He asked, "Who would have the right to buy these companies, and would the Israelis be included?"³⁷ Criticism also dealt with technical questions of implementation, e.g. the number of public companies to be sold within a certain period of time or the privatisation methods³⁸.

The traditionally pro-capitalist Wafd has a contradictory position. For ideological reasons the party welcomes reforms because it assumes that economic liberalisation and democracy are mutually reinforcing. Reforms leading to a market economy are seen as a necessary precondition for solving Egypt's economic and social problems, but the Wafd stresses that national interests require certain limitations on the economic opening. A major concern is the possible "infiltration" by Israeli capital. Massive investment by foreign capital in general would impair Egypt's business community. It believes that the capital should be sought from Egyptian expatriates abroad³⁹.

The Wafd criticises the slowness of privatisation, but at the same time warns against foreign participation in privatisation and dismissals of public sector workers. The Wafd newspaper regularly reports on conflicts over privatisation within the government and among administrative bodies, e.g. the Public Sector Ministry and the Public Enterprise Office or the Higher Privatisation Committee and various ministries⁴⁰. Soon after the new privatisation initiative was announced by the government in early 1996, the Wafd started saying that its implementation lacked transparency and that there was a lack of Egyptian capital to buy the public sector companies.

The left is fiercely opposed to the reform programme and the privatisation of public sector enterprises. A contraction of the economic role of the state is considered as detrimental to national economic development, having high social costs and carrying political risks, especially in view of Islamism. The left believes that the state should

maintain its leading role in development, promote equitable distribution of income and opportunities, and guarantee social justice. Nasserists and Tagammu warn of rising unemployment and contend that since the start of the economic reform programme, large parts of the middle and lower classes have been pushed below the poverty line⁴¹. Economic liberalisation and privatisation are expected to result in growing concentration of income, wealth and economic and political power, and in a further decline of the living standards of the masses.

The Tagammu Party, which opposes the privatisation programme and many of the reforms, is especially worried about public sector sales to foreigners. Its ideology stresses issues such as independence from foreign capital, economic self-determination and resistance to neo-colonial moves by the west and Israel. Privatisation would “waste away the wealth accumulated by sacrifice, blood and sweat of the Egyptian people for over a century in favour of a group of foreigners and exploiters”⁴². Tagammu foresees mass lay offs of labour and is particularly opposed to the sale of profitable enterprises. The party is less concerned about workers’ rights as long as restructuring of enterprises is implemented within the public sector.

The party newspaper *Al-Ahali* has reported on orders given to the security forces to prevent opposition activities against privatisation, and to isolate political leaders who have tried to organise resistance.

The Nasserist Party pledges unwavering support for the public sector as the backbone of the economy. Publications and speeches of leading party members warn against layoffs resulting from privatisation and accuse the government of not having a programme for securing jobs. They call for enforcement of social obligations by entrepreneurs.

The party newspaper *Al-Arabi* has repeatedly published reports about the firing of workers in former public sector companies that have been privatised or in companies scheduled for privatisation. It has warned against the practice of dismissing large numbers of surplus employees after the expiration of the three-year employment guarantee by the new owners (which are usually part of privatisation contracts). Nasserists claim that the public sector was profitable until corruption damaged it, beginning with President Sadat’s Infitah, and that the reform programme aims at turning Egypt into a “satellite economy” without productive potential and dependent on the West⁴³. In March 1996 the Nasserists called for a national front of workers against privatisation⁴⁴, and in early April held a conference on the importance of the public sector. In late April 1996 the Nasserist Party invited labour leaders to participate in a sit-in to protest against government decisions to sell the state enterprises⁴⁵.

The Trade Union Committee of the underground Communist Party called on “Egyptian workers, nationalists and democratic forces” to co-operate with the communists “to protect Egypt’s wealth by opposing the sale of the public sector whether to Egyptian or foreign capital”⁴⁶. According to a party statement the financial problems of the public sector could be solved by private subscription to publicly owned joint-

stock companies, thus generating new funding without changing the ownership structure. The party called for “the use of all peaceful and democratic means” to protect workers’ rights by “creating grassroots committees to defend the public sector”⁴⁷.

Leftist parties concentrated on legal steps against the privatisation programme. For example, in March 1996 the Tagammu and the Nasserists filed an unsuccessful lawsuit based on the Constitution’s reference to the public sector as the foundation of Egypt’s economy. In May, together with the SLP and some lawyers and members of the public sector unions, they asked Cairo’s Administrative Court to overrule a cabinet privatisation decree authorising the sale of approximately 240 state enterprises⁴⁸. In late June 1996 the Administrative Court requested the government to present a programme for privatisation and a memorandum on the reasons for, and the aims of, selling profitable companies. The plaintiffs were requested to present a memorandum on the reasons for their opposition to the privatisation plans. A hearing was postponed⁴⁹. Thus far the left has been unable to mobilise public sector employees for large-scale political action against the privatisation programme.

The Islamists also oppose the reforms. Their arguments are based on an “Islamic economy” which accepts private business ownership but demands social responsibility by the wealthy. Islamists do not oppose privatisation, as such. Their main criticisms are the danger of giving away large parts of Egypt’s industrial assets to foreigners, especially to the “neo-colonial west” and Israel, and the unemployment problems resulting from restructuring and privatisation. Islamists in the Socialist Labour Party, Umma Party and the Moslem Brotherhood attack the reforms as capitulation to World Bank and IMF intervention. They criticised the pressure of the international financial institutions for devaluation of the Egyptian pound. They also objected to the sale of government shares in joint-venture banks⁵⁰.

Non-governmental Organisations

The relations between Egypt’s civil organisations with their long traditions (trade unions, professional syndicates, private volunteer groups) and the state are characterised by continuous tensions. The organisations try to revitalise themselves⁵¹ and wring concessions from the state while maintaining workable relationships so that some demands may be accepted. The government tries to co-opt the organisations in a corporatist pattern or tries to integrate them into semi-official bodies⁵².

Trade Unions

Egypt’s trade union movement has a long tradition. After the revolution of 1952 it was incorporated into the government’s comprehensive system of control of the society. President Nasser particularly wanted to eliminate communist influence among

workers and to weaken potential sources of opposition⁵³. Under his successors the state's control of the trade unions increased by co-opting trade union leaders into a system of privileges and benefits⁵⁴.

In the mid-1980s declining living standards of workers led to a number of strikes in Egypt's major industrial areas, which were only brought under control by massive intervention by riot police and the army. Union members in the factories felt betrayed by their representatives, who often were the first to call for the army to storm plants occupied by striking workers. The latter turned against the union leadership and began to organise outside the framework of the established state-controlled unions⁵⁵.

In the late 1980s and early 1990s there were a number of strong and often violent strikes. In spite of promises, made to calm down the situation, the demands were usually not fulfilled after order had been restored. In particular, political objectives such as the reform of the General Trade Union Federation were not achieved. The union leadership blocked any change of the institutions, arguing that the "unity of the trade union movement" was at stake. Even middle- and low-level trade union representatives lost support of the workers. "Today, Egyptian unions neither lead workers in struggle as their proper role would seem to require, nor manage to contain workers as the state would like"⁵⁶.

In mid-1994 the lay offs and wage cuts in public sector companies that had been privatised or were scheduled for privatisation were disputed in court⁵⁷. Among other scheduled lay offs, a plan to dismiss more than 5 000 workers in a single company was discussed. During September and October 1994 there was a violent strike at Kafr al-Dawwar. It "ended on 2 November in street battles between townspeople and riot police which left four people dead... The police fired in the air and then into the crowds. Estimates of wounded civilians ranged from 29 to 602"⁵⁸, five of whom remained in critical condition.

The mounting tide of privatisation announcements added to the unions' disarray. They became aware that they might lose the battle to preserve the public sector, and began to realise that the new issues were negotiations on labour laws and agreements for the time after privatisation. Even public sector managers started to cut wage benefits and to step up efficiency; this indicated that the trade unions would have to find a new strategy.

Independent Egyptian political analysts are aware that a cautious overhaul of the Nasserist labour legislation will be essential to prevent massive social tension. "The next few years may witness the outbreak of significant labour unrest, as the regime moves toward more thorough implementation of its plans. The strikes in Kafr al-Dawwar in September-October 1994 may indeed prove to be the beginning of a new wave of protest"⁵⁹. The sacrifices required from the workers "make genuine liberalisation a real danger for the regime"⁶⁰.

In March 1996 the government succeeded in getting the General Union of Labour Syndicates to express their support of the privatisation policy⁶¹. However, the more independent union branches and the newly founded Halwan Committee for the Support of the Public Sector strongly opposed privatisation and organised sit-ins and hunger strikes⁶². In reaction to workers' protests, Minister Ebeid promised at the parliamentary Labour Affairs Committee meeting in April, "that the government will pay the salaries and bonuses of dismissed workers until the age of retirement"⁶³. President Mubarak stressed security for public sector employees in his 1996 Labour Day speech. "President Mubarak is personally reviewing the privatisation programme"⁶⁴. In May 1996 the Nasserist paper *Al-Arabi* published a survey of workers' views on privatisation and concluded that they opposed privatisation, contrary to union officials⁶⁵. In June the Engineering and Metallurgical Industries Union established a strike fund to protect its 300 000 members from dismissal⁶⁶. Local councils of the militant Heavy Industries Syndicate, representing some 200 000 workers, demanded that not more than 49 per cent of public sector companies should be sold⁶⁷.

Security measures were tightened⁶⁸. While negotiations between the government and the unions on the labour law and the privatisation operations continued, opposition papers reported dismissals of public sector workers⁶⁹. Labour and union circles spoke out against the early retirement system proposed by the public sector minister. Compulsory early retirement during previous years had caused many law suits. Union bodies formed labour committees to instruct workers to reject the Public Sector Ministry's retirement conditions⁷⁰, but workers did not rely only on union officials. In January 1997, 2 700 public transport workers went on strike in Tanta, a Nile Delta city of half a million people. The walk-out also prevented tens of thousands of workers from commuting to the nearby textile mills in Al-Mahalla al-Kubra and brought their production to a halt⁷¹. In February 1997, the employees of an Alexandria shoe factory went on strike⁷².

The new private companies thus far have largely been able to prevent trade union activity. By the end of 1996, the employees of only seven of 107 new private enterprises in the new satellite city of Tenth of Ramadan had trade union representation. The new labour law will make dismissals easier, but will grant workers the right to strike in both the private and public sectors⁷³. For the time being, there are many complaints about the arbitrariness and insecurity of employment conditions in the private sector. On the other hand, public sector workers will come under growing pressure with restructuring and rationalisation measures in factories⁷⁴.

Professional Syndicates

The professional syndicates are organisations of professional groups (lawyers, engineers, medical doctors, etc.) representing the interests of their members in domains such as legal status, rules and regulations, remuneration. They have played a major political role in Egyptian society. Since the 1980s they came under pressure after Islamists managed to get elected into leading positions, and professional syndicates

became more engaged in the civil rights debate⁷⁵. The 21 professional syndicates in 1992 had a total of about 2 million members, with an annual increase of 150 000 to 200 000.

Generally the syndicates have enjoyed greater freedom since President Sadat's political opening in the 1970s and President Mubarak's abolition of various restrictions in the 1980s. However, "the corporatist formula that was used by President Nasser to maintain state regulation and control of the behaviour of occupational syndicates and trade unions remained essentially unchanged. A striking feature of this corporatist formula was that more often than not the president of an occupational syndicate or a trade union was no other than the cabinet minister in charge of the sector to which the syndicate belonged"⁷⁶.

The syndicates' ability to defend their interests against state intervention depends on the unity of members from differing social and economic backgrounds, the number of government employees in the organisations and the extent of the syndicates' financial dependence on the state. Under President Mubarak, the syndicates have had greater freedom to assume a quasi-political role in discussing and opposing various domestic and foreign policies, internal security measures or human rights issues⁷⁷. The syndicates became a forum for competing political ideas and political struggle, thus providing guidelines for Egyptian society at large.

As a result of the increasing influence of Islamist activists in the professional syndicates, however, the government has repeatedly tried to restrict the political activities of various syndicates. This led to a remarkable politicisation and heated public debates over issues such as demonstrations and sit-ins by journalists, occupation of syndicate headquarters by members, disputes in Parliament, media campaigns, etc., strengthening the solidarity of members and between different syndicates. Even the larger and more influential syndicates, however, are still too weak to shape government policies⁷⁸. In the process of a continuing differentiation among the political parties in Egypt, the syndicates will probably not retain their role as quasi-parties.

Private Voluntary Organisations (PVOs)

As of 1990 there were some 28 000 private voluntary organisations, of which more than 12 800 worked in welfare and development. Others were committed to business, artistic, recreational, environmental, professional and religious activities⁷⁹. The number of PVOs has increased by 40 per cent since the early 1980s.

Usually PVOs are considered to be a major component of civil society which strengthens democracy. In Egypt, however, they are neither effective enough to motivate the state to work with them in areas of their expertise nor do they act as agents of democratisation. Their internal structure is usually paternalistic, with a striking social distance between PVO leaders and their rank and file street workers. Upper-class

ladies create PVOs in order to establish a social platform, while males use PVOs as a political base and a tool for obtaining funds. Usually there is no internal democratic supervision of their expenditure.

PVO board members rarely meet and usually are not rotated. They often come from an influential family and tend to regard the PVO as their personal domain. The staff usually has no say in running the organisation. Often the relationship between the social workers and the board members does not differ from that of state agencies. The leaders rule and the workers obey. Efficient vertical communication is rare⁸⁰. Power, money, information, and access to networking are monopolised by the leadership.

In most PVOs professional competence is poor since no adequate training is given to the employees. Poor management and low salaries make PVO social workers soon lose any enthusiasm and altruism they may have had.

A similar paternalistic pattern without participatory elements prevails in the relationship of the PVOs to their beneficiaries. PVOs often conceive their work as charity. Class barriers between leadership and target groups prevent a co-operative approach. Most PVOs have not been created by people within poor communities to serve their own needs, and they are not autonomous grassroots institutions. Often projects are poorly prepared and implemented. PVOs tend to get involved in almost every activity that promises an influx of donor funds. In 1991 the Egyptian state contributed only an estimated LE 3 million while the main funding came from abroad.

PVOs are part of a patronage–clientele network. They provide goods and services in exchange for loyalty and support. The whole system is largely fuelled by external resources. The charity approach perpetuates a culture of dependency among the beneficiaries and weakens self-help efforts and grassroots participation.

There are exceptions to the prevailing pattern, however, in which initiatives come from people interested in development issues who organise joint activities in a more democratic way. Here professional skills, responsible recruitment and training, and voluntary work play a role, and class barriers are not emphasised between board members, social workers and beneficiaries.

PVOs have not built a strong lobby since they are not closely linked in networks despite the existence of a Federation of PVOs. They are kept under strict surveillance by the Ministry of Social Affairs, which restricts their activities, especially greater co-operation among PVOs and grassroots mobilisation of beneficiary groups.

Overall Assessment

The Egyptian reform process suffers from the lack of a broad political debate on basic strategies and objectives, techniques of implementation, and acceptable social outcomes. There is a general lack of opportunity for fresh or creative thinking, or for constructive participation. This leads to discontent or cynicism among Egyptian

intellectuals. The majority of the population apparently does not care, as implied by the low electoral participation. Thus the presidential government risks becoming increasingly out of touch with a rapidly changing environment. Islamist terrorism, security problems and an erosion of civil rights could be considered a reflection of that situation.

The ruling establishment favours centralised control rather than decentralisation and local initiative and responsibility, but a commitment to modernisation and high standards of science and technology cannot flourish in a stifling intellectual climate. The situation is not getting easier, because a considerable part of the population has become attracted to the idea that “Islam is the solution” for protecting Egypt’s cultural identity in the face of mounting economic insecurity.

Box 6.2. Pollution, Health Hazards, and Bribery

“Ezbet Mekkawi, located in Hadayek El-Qubba, is a very densely populated, low income area of Cairo... It is dotted with small and medium industries, most of which use very rudimentary technology: textile mills which seem to belong in faded photographs of 19th century industrial England, soap factories, dye factories, etc. Many of these industries belong to categories classified by the Ministry of Health as hazardous to the public. Two leading smelting factories, located just off the main street of Ezbet Mekkawi, have been so classified, yet they have not been closed down, nor indeed has any effort been made to make them safer. The people living in this area have been trying to solve the problem the ‘right’ way, through recourse to the appropriate administrative authorities, for the past 15 or so years. Meanwhile, they have watched relatives die of kidney failure and children develop lung problems... The families living in the area, aware of the hazards posed by these smelters, have filed innumerable petitions and sent countless letters to almost every authority imaginable, yet nothing has been done either to fit the smokestacks of the factories with filters, or to move them to a less populated industrial zone”...

When a group of children four to 11 years old from Ezbet Mekkawi were tested for lead poisoning, results warranted immediate hospitalisation, yet nothing was done, either about the children or about the factories...

“A number of the area’s residents allege that the owner of one of the two factories, when approached by them, boasted that he was making so much money that he could afford to bribe as many people as it took to keep him in business.”

Source: Al Ahram Weekly, 17–23 September 1992.

It is unclear how the complex blending of religious and secular tensions will be resolved. Political institutions have not kept pace with the challenges of change. The attempt to maintain social order by authoritarian rule reflects a situation where the existing institutions are unable to channel conflicting political demands into constructive change. Political reform as a vehicle of economic transformation is difficult in a “general climate where compromise has no traditional place and where the regime does not feel ready for real negotiations with the opposition... A willingness to negotiate is considered as a sign of weakness. But as negotiations are an essential condition to proceed to real democracy, this factor, per se, constitutes an obstacle to ending a long transition period where the multiparty system is limited”⁸¹.

Open political debate does not occur. Basic decisions are made by the government without consulting the parliament or public. The NDP represents vested interests linked to the establishment. The opposition is weak and divided. The political process is mainly concerned with the balance of interests within a power cartel, e.g. between the government, the bureaucracy, the military, the public sector, the Federation of Industries, the Egyptian Businessmen’s Association, etc. Political debate is kept within clear limits and is led by authorised voices. Radio and TV do not reflect the concerns of the majority of the people. The debate in the newspapers is somewhat freer but limited to urban intellectuals.

In this atmosphere, the expression of differences, the elaboration of viable strategies and the building of a social consensus are stifled⁸². For some parties the publication of a journal is the only essential activity and substitutes for a political debate. In Egyptian society neither a change in power nor participation in power is yet on the agenda⁸³. A prominent author of the Centre of Strategic Studies of Al-Ahram deplors that there is no real political discourse. Immobility still prevails two decades after Sadat’s turn to the west. “Our restricted pluralism which was supposed to constitute a transitional step towards a real democracy risks becoming a permanent state of inertia... On the other hand, a rapid transition might neglect objective social conditions and lead to an Algerian situation. But the transitional period should not be prolonged to a point of hopelessness and even violence”⁸⁴.

In a country where half of the population is illiterate, a presidential regime can, at least for a certain period, rely on the support of the people as long as basic needs are met, but transformation towards a modern industrial economy requires new avenues for expression since the technological and economic spheres cannot be tightly separated from the rest of the social fabric⁸⁵.

Repressive security measures have increased in reaction to Islamist terrorism and the rise of social tension since the beginning of the economic reform and the structural adjustment programme. A dense network of surveillance has been established in the countryside and in the densely populated, low-income districts of Egyptian cities. Penal laws and criminal jurisdiction have been tightened. The riots of 1977 and 1986 (both following cuts in subsidies) have not been forgotten by the government. NGOs are subject to strict ministerial control. Professional associations were

streamlined in 1993. In 1994 the Trade Union Law was amended to change electoral procedures so that the leaders of the state-controlled labour unions would remain in office. A new labour law is still under discussion. An increasing number of offences is being turned over to military courts. The military and the police forces have undergone a number of purges. Thus steps towards economic liberalisation have been accompanied by tighter authoritarian rule.

Notes

1. Hinnebusch, 1985.
2. Waterbury, 1983.
3. *Ibid.*
4. Vatikiotis, 1975.
5. For the Socialist Labour Party, see Singer, 1993.
6. Zaki, 1995: "Managers of state enterprises rather than state policies have often been the major determinant of worker discontent, through the granting or withholding workers' incentives and compensations and the control of their working conditions."
7. *Ibid.*
8. *Ibid.*
9. *Ibid.*
10. *Op. cit.*, Krämer, 1986.
11. Al-Sayyid, 1996.
12. Cf. Zaki, 1995.
13. This applied to all new parties asking for approval by the Committee after the three political parties emerging from the dissolved ASU had been established under Sadat in 1976.
14. "All results of parliamentary elections have been disputed in the courts, one of which was declared already invalid by both the Supreme Court of Cassation and the Supreme Constitutional Court in 1990. Other elections of the People's Council (1990) and of the Shura Council (1989) were annulled because of the unconstitutionality of their electoral laws" (Al-Sayyid, 1996).
15. Qamhah, 1996.
16. See below.
17. Zaki, 1995.
18. *Ibid.*

19. *Ibid.*
20. Cf. Al–Sayyid, 1996.
21. Mustafa, 1995.
22. Zaki, 1995.
23. See below.
24. Krämer, 1986.
25. Springborg, 1993.
26. *Al Ahram Weekly*, 21 March 1996; *Al Ahram Weekly*, 22 February 1996.
27. Muslimani, 1995.
28. The term has been coined by Zaki, 1995.
29. Traditional Islamic law.
30. Zaki, 1995.
31. Singer, 1993.
32. Zaki, 1995; Baker 1990.
33. Kogelmann, 1994.
34. Qamhah, 1995.
35. Abdel, Al–Sayed and Dahroug, 1995.
36. “Though keen to have taxes lowered, regulations concerning business activities diminished and bureaucratic power generally curtailed, they strongly resist the transformation to a truly free market economy. In particular, many resist the liberalisation of trade because of their insecurity about the prospects of competition with foreign producers, fearing injury from dumped or state–subsidized imports” (Zaki, 1995).
37. *Al–Ahali*, 17 April 1996.
38. *Al Ahram Weekly*, 24 October 1996.
39. *Al Ahram Weekly*, 22 February 1996.
40. See e.g. *Al–Wafd*, 14 July 1996; *Al–Wafd*, 11 April and 13 April 1996.
41. Zaki, 1995.
42. Cf. *Al Ahram Weekly*, 22 February 1996.
43. *Al Ahram Weekly*, 22 February 1996.
44. *Al–Ahali*, 3 April 1996.
45. *Al–Ahali*, 15 April 1996.
46. *Al–Ahali*, 8 May 1996.
47. *Ibid.*

48. *Financial Times*, 15 May 1996.
49. *Al-Wafd*, 3 July 1996.
50. *Al-Ahram Weekly*, 22 February 1996.
51. Ibrahim, 1995.
52. Cf. Awad, 1991.
53. El-Shafei, 1995.
54. Cf. Al-Sayyid, 1996; Al-Sayyid and Al-Mahdy, 1995; Auga, 1995.
55. El Shafei, 1995.
56. *Ibid.*
57. *Al-Ahali*, 6 July 1994.
58. *Middle East Times*, 9 October 1994.
59. *Ibid.*
60. *Ibid.*
61. *Al-Wafd*, 15 March 1996.
62. *Al-Ahali*, 3 March 1996; *Al-Arabi*, 1 April 1996; *Al-Arabi*, 15 April 1996; *Al-Arabi*, 22 April 1996.
63. *Al-Ahali*, 17 April 1996.
64. *Al-Arabi*, 6 May, 1996.
65. Of the 600 workers interviewed, 91.2 per cent opposed privatisation. "Of the 8.8 per cent favouring privatisation, 80.6 per cent opposed foreign control of the public sector, 77.4 per cent insisted that companies should be sold to Egyptians in the stock exchange, 38.7 per cent preferred worker buy-outs, and 80.6 per cent wanted the state to retain strategic industries. Sixty per cent of the pro-privatisation respondents said that workers should have the unconditional right to strike. Asked whether pro-privatisation respondents would agree to the sale of the company where they are working, only 35.5 per cent agreed"; cf. *Al-Arabi*, 27 May 1996.
66. *Al-Akhbar*, 19 June 1996.
67. *Middle East Times*, 30 June 1996.
68. A "top secret document was distributed to security chiefs in those locations where there exists what the document refers to as 'a movement by labour leaders to exploit the coming labour elections to cast doubt on the privatisation programme and its influence on the rights and gains of workers, and to urge them to bring court cases against privatisation by calling into question its unconstitutionality' "; cf. *Al-Ahali*, 24 July 1996.
69. *Al-Ahali*, 21 August 1996; *Al-Shaab*, 8 November 1996; *Al-Alam Al-Youm*, 17 November 1996.
70. *Al-Ahali*, 12 February 1997; *Business Monthly*, April 1997.

71. *Middle East Times*, 12 January 1997.
72. *Al-Wafd*, 26 February 1997.
73. In the private sector workers with regular employment contracts could only be dismissed after court hearing, but these legal proceedings were still easier than a dismissal of public sector workers since private sector firms were also allowed to lay off employees for economic reasons, although with dismissal compensation. As long as legal proceedings were pending, employers had to continue to pay wages. This regulation is to be abolished by the new labour bill which is still subject to debate among various stakeholders.
74. The abolition of many labour privileges in the public sector envisaged by the new labour bill is meant to reduce the attractiveness of public sector employment and to reduce political resistance to privatisation.
75. Krämer, 1992.
76. Zaki, 1995.
77. The professional syndicate of lawyers founded in 1912 is particularly engaged in political and socio-economic issues. The syndicate of journalists has spoken out against increasing suppression of the political opposition, human rights groups, Islamists, etc. Meanwhile, the syndicate is regarded as “infiltrated” by the Islamist opposition.
78. “A relatively new development in 1997 is that many occupational associations have become viable economic enterprises providing a whole spectrum of services to their members, from co-operative housing to vacation schemes and co-operative cemeteries. Thus professional syndicates with a significant stake in the system are willing, despite occasional frictions with the regime, to operate within the margin of freedoms tolerated by the state.” Cf. Zaki, 1995.
79. This paragraph draws heavily on an unpublished paper by A. Bayat, American University in Cairo.
80. Al-Sawaf, 1994.
81. Abd al-Magid, 1994.
82. Weiss, 1993.
83. Roussillon, 1994.
84. *Ibid.*
85. Weiss, 1992c.

International Actors Supporting Reform

The World Bank and IMF

The international financial institutions serve as spearheads of the international donor community. Its individual members rally behind the World Bank and the IMF to avoid bilateral diplomatic costs. All bilateral donors are aware of the fact that Egypt cannot be subsidised indefinitely, with ever increasing aid as a result of its continuing high population growth, which, if current trends continue, will lead to a population of 120 million in three decades. This would imply the loss of fertile land to urban settlements, further undermining the country's already inadequate agricultural production. Hence, the donor community has a vital interest in the transformation of the Egyptian economy into a viable competitive system able to support the population.

On the other hand, the World Bank and the IMF are subject to institutional patterns of their own. As they deal with a large number of recipient countries, one cannot expect policies precisely geared to the specific options, constraints, forms of policy implementation, and values of a particular country. In other words, if a government calls for IMF and World Bank assistance, the price is recommendations following somewhat standardised patterns. They partly reflect the institutional donor's requirements rather than the particular needs of a recipient, especially if the political process of the latter does not permit the expression of a broad-based consensus of these needs. Frictions invariably occur, especially with regard to the social implications of reform.

The US Agency for International Development (USAID)

A major part of US foreign assistance is allocated to Israel and Egypt, with the lion's share allocated to military assistance. Egypt receives \$2.1 billion in military assistance per year as compared to some \$850 million of development aid. Strategic

calculations of Egypt's crucial role in the Middle East prevail. The Middle East peace process has long been a leading diplomatic concern of Washington. Furthermore, issues of regional security are linked with oil supplies, the protection of the state of Israel and dealing with its Arab neighbours constructively. Without trying to summarise the many issues of concern to the United States, it should be noted that Islamist political movements in the region are taken into consideration.

In the domain of economic development, the United States gives strict priority to privatisation or liquidation of public enterprises rather than attempting to restructure them. For example, the USAID Agricultural Policy Reform Program is a comprehensive attempt to enforce a strict market approach to Egypt's agricultural sector. Significant changes have been achieved. However, USAID ran into the usual difficulties when it had to deal with the vested interests of the public sector. In 1995 the cotton and fertiliser sectors had been fully liberalised. Nevertheless, they were abruptly put under public control again, causing huge losses to private cotton traders who were caught up in changes of government regulations, which abruptly revoked the previous freedom to export and import cotton.

From the perspective of other bilateral donors, the comprehensive US commitment is impressive, including its willingness to enforce strategic policies and accept the political costs of its intervention. However, the weight of US aid is not always conducive to close donor co-ordination.

The European Union and Its Member States

In recent years it has become apparent that the European Union has been unable to formulate a common foreign policy or foreign economic policy, even with regard to regions where major EU interests are at stake¹. For the EU, Mediterranean security is of vital importance, involving questions such as oil and gas supplies, trade lanes, Islamist movements, and rising migrant flows. Traditional "zones of influence" such as French interests in the Maghreb are respected by EU countries but contribute to the lack of policy co-ordination.

The European Commission has administrative responsibilities for European foreign trade policies and development assistance. Foreign policy still is the domain of individual governments. As a result, the Commission's comprehensive long-term programme to establish a Euro-Mediterranean Free Trade Zone by 2010 is not backed by consistent foreign policies of the EU countries, despite a relatively large amount of aid being devoted to it (some 5 billion ECUs under the current financial protocol). The overall outcome is a low EU profile in Egypt. European donor conditionality is weak. A considerable part of EU assistance consists of grants. A major objective is maintaining friendly diplomatic relations rather than making a tangible impact on the structural adjustment process.

The “Cold Peace” with Israel

Notwithstanding official public rhetoric, all participants in the Middle East peace process are aware that geopolitical rents depend on the continuation of a certain level of conflict in the area, while preventing the outbreak of actual war. The stakes of the participants are high, and the strategic rents add up to extraordinary amounts. Logically, a termination of conflict would lead to a loss of rent income.

The Egyptian military complex has an interest in supplies of modern weaponry and other fringe benefits. The “badr” war game in September 1996 simulated the crossing of the Suez Canal by the Egyptian army, while being exposed to atomic and chemical weapons from a “neighbouring country”. The war game was referred to by the Israeli Foreign Minister as an immediate threat to Israel’s security. The real purpose, however, was to signal to the international donor community that it would be premature to phase out any of the approximately \$2 billion in annual military assistance to Egypt.

Bilateral Egyptian–Israeli relations are “correct”, although the Egyptian public remains reticent. There are mounting fears that Egyptian economic assets will become dominated by Israeli business interests and technological superiority. Egypt claims a leading role in the Arab League in dealing with the peace process, but is painfully aware of its limitations deriving from its economic weakness. Egypt’s major leverage stems from its geopolitical position which contributes to its economic survival.

Note

1. Weiss, 1995, 1996.

The Role of Ideology

Egypt suffers from an inward orientation. Very few Egyptian professionals are familiar with the experience of transformation in Eastern Europe and Central Asia. Few Egyptians have been to newly industrialising East Asian countries or are closely acquainted with their export-led development policies and efforts in research and development. The erosion of civil rights further restricts debate on Egypt's comparative disadvantages in comparison to its more successful developing countries competitors.

Having been exposed to Arab Nationalism, Pan-Arabism, "Arab Socialism" and Sadat's turn to the West, many Egyptians seek a sense of identity in Islamic concepts, amidst rapid change and declining living standards.

President Sadat abandoned previous ideological concerns for pragmatism. This pragmatism characterised the transformation of the bulk of the Arab Socialist Union, the former ruling party, into the National Democratic Party, despite their different political orientations. However, the ASU and NDP both have served the interests of the ruling elite in preserving power.

The blunt pragmatism has been marked by widespread corruption and conspicuous consumption by the *nouveaux riches* in contrast to increasing mass poverty, provoking questions about cultural identity. Various interpretations of Islam propose to deal with a widely shared sense of frustration and search for individual and communal orientation ("Islam is the answer"). With the continuing deterioration of the living conditions of the majority of the people, violent mass outbursts may occur again, as they did during the 1977 bread revolts and numerous (illegal) strikes, riots and sit-ins in many factories during the 1980s and 1990s¹.

Egyptians in their late 50s and 60s, now in leading establishment positions, often had been fervent adherents of Nasser's nationalism, Arabism and socialism in their youth. These early convictions have not necessarily been completely abandoned, especially when it comes to defending the public sector. People tend to rationalise their position by admitting that Nasserism did not present the best economic model but represented national independence, ownership of the resources by the people, although at a low level of productivity. Some adherents of a moderate liberalisation

think that China is a model for Egypt, in which liberalisation would not necessarily mean a “defenceless exposure to multinational firms”, etc. Such arguments are also used to justify present policies to old friends from the days of the Nasserist movement.

In contrast, there are firm supporters of an uncompromising liberalisation, including some private sector industrialists. This does not mean that they are ideological supporters of western concepts of the market and democracy in opposition to traditional Egyptian concepts of centralised control.

Both tendencies co-exist in the ruling establishment. The majority, however, pragmatically tries to benefit from the opportunities offered by a transitional system, without being overly concerned with viable long-term visions and ideological debates.

Islamism has not really provided convincing, workable alternatives. The regime clings to a pragmatic middle way, trying to preserve power by conciliating pressures from various sides: the international donors, Egyptian business community, public sector clientele and administration, the Egyptian middle classes and the urban and rural poor.

Note

1. El-Shafei, 1995. Clashes of striking workers and the Egyptian security forces occurred repeatedly, e.g. at the Misr Fine Spinning and Weaving Company in Kafr al-Dawwar in September–October 1994, at the ESCO Textile Company in Shubra al-Khayma in January–February and April 1986, at the Misr Spinning and Weaving Company in Mahallah al-Kubra in February 1986, at the Egyptian Railways in July 1986, and at the Iron and Steel Company in Helwan in July–August 1989. Law 3 of 1977 provided for prison terms of hard labour for strikers. With the fall in oil prices by the mid-1980s, early economic reform measures began to hit the living standards of the masses. Real wages began to fall sharply after 1984. A major increase in strike activities followed, and the press reported 50 strikes in 1986 alone. There were 153 workers’ protest actions, including strikes, sit-ins, demonstrations, and refusals of paycheques in 1988 and 1989 (El-Shafei, 1995). A number of people were killed and hundreds of strikers were arrested during the various clashes with the security forces. Shortly before the Helwan Iron and Steel Company was stormed by the security forces in an extremely harsh manner, to end the sit-in involving some 16 000 workers out of a total of 25 000, the Minister of the Interior Zaki Badr stated that if 1 per cent of the workers died during the ending of the sit-in, he would consider the operation successful. Actually, one worker died during the storming of the factory and hundreds were severely injured (El-Shafei, 1995).

Institutions and Rules of Conflict Resolution

The General Pattern

Weak, counterproductive or missing institutions are a major obstacle to structural adjustment, particularly on the meso level¹ of chambers of commerce, business federations, trade unions, social policy institutions, tax administration, trade law and related legal matters, arbitration courts, etc. The development of institutions for coping with change has been constrained by official policies for four decades. NGOs are controlled, manipulated and eventually co-opted.

The political and administrative culture is dominated by a pattern of neo-pharaonic control. The formal bureaucracy is permeated by patronage and clientele systems which share opportunities for rent seeking. New forms of corruption have emerged as a result of partial or inconsistent reforms. Political parties, even the president's majority NDP, are weak. Parliament plays no essential role. Elections are plebiscitary.

The major concern of the ruling elite is the preservation of power. It gives in to donor pressure for reforms in order to obtain rent income and debt relief. There is no broad political coalition in favour of reform and international competitiveness. The external rents are partly redistributed to pacify various clienteles and to stabilise the regime. This explains the inconsistencies of reform policies and their restrictive character. Large amounts of foreign assistance aiming at smoothing the negative social effects of structural adjustment (the Social Fund, bilateral programmes in the social sectors) are being treated by the government as a foreign substitute for domestic social programmes.

By and large, a precarious status quo is still considered satisfactory by the ruling elite. They do not yet fully understand the challenge of globalisation for Egypt's future. Basic changes in the economy would require greater political liberalisation.

The business community struggles to cope with the inconsistencies of transition but is not fully committed to thorough reform. It is exploiting opportunities for trade and speculation in protected niches to obtain short-term, windfall profits, rather than focusing on technical innovation and high quality manufacturing. It has no particular interest in competition, transparency and rationality since its rise, in large measure, occurred in the absence of a market economy and democratic society. Widespread corruption has attained unprecedented dimensions.

The legal framework is still not fully adapted to the reform agenda. A number of laws must be changed and are under discussion. Here again, as in the field of labour legislation, the government moves hesitantly.

The Egyptian capital market is still narrow. The Capital Market Law 95-1992 was a step towards reform of the Cairo and Alexandria stock exchanges. Some broker firms were admitted and the volume of trade increased sharply, but a number of weaknesses remain.

In general, reliable regulations, institutions and habits have been slow to emerge. Policies are announced but are often not put into effect. As a result, expectations are marked by uncertainty. The official preoccupation with control blocks evolutionary change. Thus, western capitalism, Islamic economics, Arab nationalism and traditional corporatism co-exist, but they cannot be discussed in a manner that would lead to a basic consensus on patterns of socio-economic development. Meanwhile, conflict in society is on the rise. The confrontation with radical Islamists is only one facet of this situation.

Creative alternative options are unwanted. The ruling elite tends to isolate itself from innovative trends inside and outside the country by insisting that "Egypt is different". Control of the universities has increased in recent years. As has occurred in other countries, the intellectual isolation of the regime makes it difficult to accept more imaginative, constructive policies. There is incomplete recognition of Egypt's mounting economic and technological backwardness by comparison with other newly industrialising countries, although a number of leading Egyptian businessmen are fully aware of current globalisation trends.

The impact of new developments such as the Euro-Mediterranean Free Trade Zone, planned to come into effect by 2010, are not fully understood. Egypt is less prepared to face these challenges than Morocco, Tunisia or Turkey. The poverty of the policy debates favours a tendency to stick to outdated concepts of public control.

Major assets are the relative independence of the judiciary and considerable freedom of the press. They comprise the rudiments of a countervailing power, but are too weak to become the basis for new institutions and rules of conflict resolution in a social system of more than 60 million people, in which ever larger groups of the rural and urban population are being pushed below the poverty line. There has been a substantial increase in malnutrition and environmental health hazards since the state diminished support for social policies. As a result, the fabric of society is disintegrating.

In the prevailing decay, Islamic charity offers support and guidance, spiritual orientation and a sense of cultural identity, particularly for the poor. The move towards a western market economy has not been accompanied by the rise of appropriate social institutions.

Deficiencies of the Legal Framework

Many laws regarding trade, tariffs, financial markets and investment are incomplete, sometimes dysfunctional and often poorly enforced. At the end of 1996 there were still 12 904 different tariff categories. Customs procedures are not transparent or reliable. Corruption is part of the daily routine. Many outdated laws and regulations are still enforced without full awareness of their effects, or are retained to protect vested interests of powerful supporters of the regime. Tax collection is subject to arbitrariness which is usually countered by bribery.

Box 9.1. Arbitrary Tax Collection: *The Middle East Times*

For years the Cyprus-based *Middle East Times* has been one of the most appreciated newspapers in Egypt, often reporting critically about sensitive issues. From time to time censorship results in half empty pages with a notice: “Apologies to our readers, we were unable to print in this space.” But the paper did not only get in trouble with censorship. A former employee filed a complaint with the tax authorities, saying that the *Middle East Times* had evaded taxes in the late 1980s. “The fact that during the period in question the *Middle East Times* sadly only saw a few thousand pounds in income from Egypt, while having to send several hundred thousand dollars to support the office here was a small point that did not deter the tax hounds.” After the Finance Minister offered to check into the case, and passed the investigation to the chief tax collector, the editors found themselves “slithering down the echelons of bureaucracy” until they “landed an hour later in the office of the tax people who had nailed them. Showing them copies of our newspaper of that period, innocent of Egyptian ads, was not of interest. That only our ad company, and not the paper, is taxable in Egypt did not register either. For evidence of our ‘profits’ they produced a copy of one 1988 invoice for LE 1 600. From this mass of evidence, the imaginative tax people figured out we must have made millions of pounds profit and should pay LE 801 000 in tax (tripled for the fine). Our regular readers will have noticed those interesting white spaces in our paper... If one week we are invisible altogether, you will know another foreign venture has fallen to the bite of Egyptian bureaucracy.”

Source: *Middle East Times*, 21 July 1996. On 22 August 1997 Egyptian police detained the publisher and editor for three hours upon his arrival at Cairo International Airport before he was informed that he could not re-enter the country; cf. *Middle East Times*, 19–25 September.

On the other hand, laws and regulations may not be enforced when friends and family members of high-ranking government officials are concerned. Exceptions can be made. No action is being taken against monopolies. Intellectual property rights are not enforced. Insider trading is normal practice in the capital market.

Box 9.2. Comfortable Niches in the TV Market

For nearly 40 years the only companies that were allowed to produce TV sets were the state-owned Telemisr (in co-operation with Goldstar of Korea) and El-Nasr Company belonging to the military-industrial complex (the Banha production line is located in a military factory). For a few years Ahmed Bahgat, one of Egypt's leading new industrialists, has been in the market and assembles some 450 000 units a year. The regulations do not allow private companies to produce TV sets, but an exception had been made for Bahgat. He received permission. Insiders note the participation of a son of an eminent political figure in the venture. Asked about how he copes with Egypt's business environment and his influential dormant partner, Ahmed Bahgat just smiles: "If you are well connected you can solve a lot of problems by phone."

The Financial Markets

The stock exchange privatisations are hampered by the narrowness of Egypt's financial markets. They were underdeveloped until the mid-1990s. The public sector banks were unfamiliar with modern investment banking techniques (evaluation of investment projects, portfolio risk management, debt-equity swaps, mergers and acquisitions, stock trading and flotations)². In spite of improvements since 1992, the banking system still has shortcomings with respect to capitalisation, information and transparency. The public sector banks still enjoy preferential treatment from the government. "Insolvent banks were left to operate through support from the banking system while adequate measures like restructuring, merging or liquidation were not applied. This policy encourages inefficient banks to continue their violation of credit standards by indulging in high risk lending, and prevents bank customers from distinguishing between an efficient bank and an inefficient one"³.

Inflows of capital from abroad were encouraged by the Central Bank's interest and exchange rate policies. If the rates are corrected, this could lead to a rapid retreat of foreign portfolio investment, with a negative impact on the demand for shares of state enterprises.

The stock exchange suffers from a lack of appropriate information, a lack of transparency, and regulations which discriminate against small investors. Supervision of the stock exchange is insufficient. "Brokerage firms themselves confirm that they believe many different forms of market improprieties are occurring regularly... Of

particular concern is the continued practice of issuing initial public offerings without an approved prospectus which meets international standards and the floatation of shares to the public before that prospectus is available to them for inspection”⁴.

Valuation methodologies for newly floated companies are still not standardised and remain a source of conflict. Hesitant privatisation policies in 1995 caused a decline in trading activities and stock prices. The massive bull market of recent years mainly resulted from speculation rather than being related to the companies’ future earning prospects. The low volume of trading on the stock market allowed some influential major players to manipulate stock prices greatly. Insider trading is widespread by people close to high-ranking decision makers enjoying access to privileged information.

The companies which have been privatised until now belong to those with the best chances of survival due to their financial status, their production technology and their position in the market. The sale of the heavily indebted losers will be far more difficult.

Spectacular profits from overpriced stocks encouraged a “casino” mentality among Egyptian investors who ignored the risk of major losses. In fact, there was a major downward correction of stock prices during February and March 1997, with a drop of up to 30 per cent and, after a brief recovery, the Egyptian standard indices (EFG/Hermes and CMA) fell further in the succeeding months. The discontent among inexperienced investors could lead to a redirection of financial resources to real estate investment or other non-productive assets.

A noteworthy phenomenon consists of financial transactions among holding companies, affiliated companies, Economic Authorities, or public sector banks buying shares of state enterprises being privatised. In other words, a considerable part of this “privatisation” consists of the sale of public equity to other public entities or public-private joint ventures.

Privatisation Institutions

The Prevailing Concept of Control

A major problem is the absence of an autonomous agency having the willingness, knowledge and instruments for carrying out effective privatisation. The government fears it would lose control of the pace and direction of public sector reforms if an independent privatisation body were established. Until the appointment of Prime Minister Ghanzouri, no official could expect career benefits from a strong commitment to reform under the system of privatisation. Instead, he would be exposed to attacks by the media, accusations in case of failure, the possibility of falling victim to political manoeuvres, etc. High-ranking government officials shied away from rapid change in view of their own vested interests in the *status quo*.

**Box 9.3. Conversion of Public Resources into Private Wealth:
The Case of Joint Ventures**

Capital can be converted from public to private control by perfectly legal stratagems. The best known are joint ventures linking the state and private sectors, Egyptian or foreign. Of the joint ventures created under the provisions of Law 43 of 1974, 65 per cent of the capital investment was provided by Egyptian private sources and the rest by the state.

The manner in which public capital has been progressively privatised is illustrated by the Suez Canal Bank, “63 per cent of the equity of which was contributed by four public–sector banks and a public–sector insurance company. The balance of the capital was subscribed by the employees’ fund of Arab Contractors, the Suez Canal Authority, and by individuals. Once established, this joint venture, like all others, is considered under law a private entity. Its chairman Zakariya Tawfiq Abd al–Fatah was one of President Sadat’s ministers of Trade and Supply. By 1982 the Suez Canal Bank had invested capital in 41 other banks and companies in the private sector. One such investment was in al–Muhandis Bank, of which the Suez Canal Bank subscribed 60 per cent of the capital and the Engineers’ Syndicate the remainder. Al–Muhandis Bank, the chairman of the board of which is Ahmad Ali Kamal, a former minister of irrigation who in 1975 issued the ministerial decree governing the Engineers’ Syndicate, in turn formed several joint ventures with Arab Contractors. In 1986 the Suez Canal Bank became one of the principal shareholders in the joint venture involving General Motors (GM) and the Egyptian public–sector firm Nasr Automotive Company for the purpose of assembling GM cars in Egypt. Even the most dedicated of the state’s accountants would, as a result of this complex pattern of ownership, have extreme difficulty in tracing the ultimate destination of the government’s original investment. That a very significant share of such funds have ultimately been siphoned off by private interests at the other end of the labyrinth of companies is suggested not only by innumerable specific allegations, but by the fact that the state has, according to reliable accounts, lost millions in its joint ventures.”

Source: Springborg, 1989.

The Holding Companies

Organisation and Management

Law 203/1991 changed the business environment of the state enterprises. The Public Enterprise Office privatisation guidelines of 1993 provided a framework for sales. The privatisation announcements of 1996 aimed at creating a new reform climate, but the economic status of most of the Law 203 public sector affiliated companies under the control of holding companies has not changed. The holding companies are subject to an organisational structure inherited from the period of central planning and direct state intervention.

The holding companies are not responsible for their affiliated companies' current operations. According to a directive of 1993 the holding companies shall concentrate on portfolio management and on the preparation of their affiliated companies for privatisation. The second task is in conflict with the first one, since profit-oriented portfolio management requires a different business strategy than preparing a company (or parts of it) for sale.

The initial holding company structures were unsuited to the objective of portfolio management. This led to attempts to reorganise the holding companies.

Another problem of the holding companies is related to the recruitment of their top managers. Most managers owe their careers to the public sector and never had any experience of a modern market economy. Now they are supposed to reform a system which they have been part of for decades and to abandon corporate concepts and values which they have supported for more than 30 years. Some of the chairmen are members of Parliament. All are tied to personal networks and clientele systems. Hence, staffing occurs on the basis of the "old boy system". Most of the holding company managers are in their 60s and 70s. As a result of these staffing practices, many holding company top managers are not adequately prepared for their new tasks.

Incentives

The responsibility for preparing Law 203 companies for sale mainly lies with the boards and the managing directors of the holding companies and affiliated companies. After evaluation of the company assets by accounting consultants, internal privatisation schedules are proposed for privatisation candidates to the Public Sector Minister and to potential investors. The final decision is taken by the minister, but holding company managers can manipulate the whole process by presenting or withholding relevant facts and figures.

The General Procedures and Guidance for the Government's Programmes of Privatisation, Restructuring and Reward System (Privatisation Guidelines) and Law 203 of 1991 do not refer to the number of privatised companies as an indicator of a holding company's privatisation performance⁵. Hence, there is no incentive for a speedy sale

of Law 203 companies, and there are no sanctions related to non-privatisation. The status of senior managers of holding companies is defined in terms of the standing of their holding company. Their fees are directly related to the number of affiliated companies under the holding company. In other words, managers of holding companies are more interested in portfolio management than in privatisation, since the latter would reduce their status and income and would make their positions redundant.

**Box 9.4. Restructuring Holding Companies:
The Metallurgical Industries Holding Company (MIHC)**

In early 1996 the MIHC was chosen to pioneer with its reorganisation to prepare it for the tasks of portfolio management and privatisation. It was supposed to provide an example for other holding companies. It was supported by international donors and foreign consultants.

In the 1980s the Egyptian public sector had been under the so-called Economic Authorities. There was an Economic Authority for the metallurgical industry which had been transformed and renamed the MIHC without a major organisational change. Under its former label as an Economic Authority, it had also dealt with the day-to-day running of the companies' affairs.

A number of divisions of the former Economic Authority (Administrative Development, Economic, Financial, and Technical Affairs) were maintained by the MIHC, while other functions were supposed to be transferred to the affiliated companies, with the explicit objective of giving them operational responsibility. Furthermore, the MIHC was to establish a number of new divisions to carry out its role in the privatisation programme: The Portfolio Management Division was supposed to be responsible for the valuation of company assets, for activities in the capital and stock markets, and for privatisation placements. The Restructuring Division was to deal with financial, organisational, and operational restructuring, and with personnel restructuring and training, whereas a new Planning, Monitoring and Evaluation Division was supposed to review and approve performance targets and their implementation. A new Administrative Division and a Department for Legal Affairs were assigned responsibility for handling all administrative and legal issues resulting from the new role as a holding company. Public Relations-Information and Investor Relations were to be reorganised for privatisation.

In late 1996 the consultants' organisation proposal of March 1996 was still under discussion. In March 1997 a spokesman of the consultants said that MIHC was willing to implement the new organisational proposal but had to present it as its own idea and adjust it to the demands of important stakeholders. The MIHC's top management felt that it had to move slowly and implement incremental changes only. A radical restructuring approach was unthinkable to the power structure of the holding company and its affiliated companies. No substantial change had occurred one year after the presentation of the consultants' proposal.

Box 9.5. Old Friends

Gamal Ed–Din Hilmi is an engineer and the vice chairman of the Nasr Phosphate Company. Born in 1933, he studied mining engineering and obtained his degree in 1953. After graduation he joined the armed forces and was appointed an officer in 1954. After retirement in 1975, he worked until 1977 with Osman Ahmad Osman, where he was promoted to general manager. After retirement from that firm he lived as a pensioner until he was suddenly recruited as vice chairman by the Nasr Phosphate Company. Since his graduation in 1953 he had no experience in the mining industry, but the chairman of Nasr Phosphate, Adel Abdel Karim, was a member of the same graduating class of 1953 in engineering.

Box 9.6. Scientists without Management Practice

According to a Helwan University source, the top management positions in the Holding Company for Mining and Refractories (HCMR) are held by professionals with various specialisations, but none of the engineers had experience in the mining industry. Dr. Adel Abdel Azim is a university professor of metallurgy and member of the Egyptian Metallurgical Research Council. Dr. Ahmad Salim Al–Sabah holds an engineering degree and worked as a university professor at Cairo’s Ain–Shams University. Like his colleague he has no experience in mining.

Dr. Eng. Ahmad Mahmud Aid, 65, had been working for decades in the defence industry before he was appointed chairman of the Metallurgical Industries Holding Company (MIHC). After his retirement he became a board member of the HCMR, and later its vice chairman.

Dr. Sa’ad Megahid Al–Raghi works as university professor of metallurgy at Cairo University and at the same time is a board member both in the HCMR and in the MIHC. Besides this, he is member of the board of the Nag Hammadi Aluminium Company under the MIHC and of the Sinai Manganese Company, an affiliated company under the HCMR.

Box 9.7. Incentives for Non-privatisation

The average annual income for acting as managing director and attending board meetings, committees and general assemblies amounts to some LE 130 000. The managing director of a holding company has a fixed salary of LE 43 200. The additional LE 87 000 are accounted for by activities related to the number of affiliated companies and by bonuses. A visit to a general assembly is rewarded with LE 225, a holding company board meeting with LE 200, a committee meeting with LE 175. The share in affiliated company profits ranges from LE 30 000 to some LE 60 000, and sometimes even more. With a portfolio of 18 affiliated companies he makes an additional average of LE 4 800 per year from each affiliated company belonging to his holding company. A chairman of the board gets on average an annual fixed salary of LE 36 000 plus bonuses, adding up to an annual income of at least LE 80 000. A public sector worker receives an average income of LE 250 to LE 300 per month or LE 3 000 to LE 4 600 per year.

Box 9.8. Profits and Bonuses

The example of the Thora Portland Cement Company which offered 32.5 per cent of its shares for sale from November 1994 shows the importance of profit-related bonuses for the board members, excluding labour union representatives.

| FY | Production | Profits | Bonuses (5% of Profits) |
|---------|---------------|-----------------|----------------------------|
| 1991–92 | 2.8 million t | LE 0.4 million | LE 20 000 |
| 1992–93 | 2.8 million t | LE 24.4 million | LE 1 220 000 |
| 1993–94 | 2.9 million t | LE 84.4 million | LE 4 220 000 |

Between FY 1991–92 and FY 1993–94 cement prices were raised from LE 80/ton to LE 195/ton by the eight Egyptian oligopolistic cement companies.

Under privatisation, the new owners will probably replace the managers of former affiliated companies. The loss of social status is a personal catastrophe for a 60-year-old manager of a state enterprise. Many such managers do not come from the old well-to-do families but acquired their position as a result of free education in Nasserist times and after many years of work in the public sector, sometimes after an army career⁶.

Top managers of holding companies are hardly restricted by formal regulations and thus can create their own policies within the framework of the incentive structure. Progress in privatisation largely depends on the holding company's management's willingness to implement reforms⁷. On the other hand, the new autonomy of public sector managers (according to Law 203/1991), freed from direct intervention into current business affairs by the ministries, gives the managers a chance to prove their ability, particularly when it comes to restructuring the affiliated companies and coping with the problems of transition. This could improve their individual chances for future careers in the private sector but requires time which is unavailable in the case of a rapid private takeover by new owners, or in the case of liquidation. Therefore, public sector managers are interested in restructuring *before* the companies are privatised. Their immediate interest is in slowing the pace of privatisation.

As long as the individual interests of the top management in the privatisation process are not addressed, they will obstruct the reforms. They are ready to resist change in the structure of holding companies and affiliated companies. Facing an uncertain future, they cling to their positions and make use of their clientele networks in their remaining time.

Manager Stratagems

Since the early 1990s many managers of state enterprises have found alternatives for retaining their income and status. Some of them were co-opted into prestigious administrative bodies. Others started a private business apart from their official state enterprise job, often draining resources, such as material and qualified workers, from state enterprises into their private company. These managers oppose the sale of their own affiliated company or holding company but not privatisation in general.

When holding companies sell a minority of their affiliated companies' shares they often are only generating fresh money while keeping control of the companies⁸. Sometimes "private" investors who present themselves as so-called anchor investors are in fact joint ventures founded by a state enterprise or having a large participation of a state enterprise.

State enterprises are still investing, to increase efficiency, as their spokesmen say. The public sector is still growing in absolute terms. There are also "insider privatisations" by managers of state enterprises or high-ranking public sector administrators involving manipulated valuations of assets or the running down of healthy companies, which are then taken over at minimum costs. There are many cases where privatisation decisions have been deferred, the delay being used to enrich insiders by a wide range of illegal practices.

Box 9.9. Running Down a Profitable Company

For more than a decade the Nasr Phosphate Company and another producer monopolised the Egyptian phosphate market. Plans were developed to build an additional plant at Abu Tartur, which was criticised by specialists for many reasons right from the beginning.

Nasr Phosphate was a profitable enterprise. It produced 500 000 tons of phosphate and generated some LE 2.4 million profits in fiscal years 1990–91 and 1991–92. It had been able to accumulate substantial reserves. In 1992 the company became an affiliated company under one of the newly founded holding companies. A new board was appointed. Its members were public sector managers aged 65 to 74 who had spent their lifetimes in state enterprises. The new chairman of the board was Fiqri Mursi, an engineer, who also held a seat in the National Phosphate Committee, an organisation that was lobbying for the highly controversial Abu Tartur project, potential future competitor of Nasr Phosphate. Soon after Mursi took over the management of Nasr Phosphate the output of the plant dropped from some 500 000 tons in FYs 1990–91 and 1991–92 to 216 000 tons in FY 1992–93 and 50 000 tons in FY 1993–94, with annual deficits of some LE 40 million in both years. Finally the company developed severe losses.

The media said that the board had deliberately run down the company. Mursi was fired, production increased to 114 000 tons in FY 1994–95, but losses still amounted to some LE 80 million. The accumulated deficit was LE 158.8 million, twice the estimated assets.

Box 9.10. When the Public Sector Buys the Public Sector

In May 1996 the Holding Company for Electricity Distribution offered its shares in El Nasr Transformers and Electrical Industries (ELMACO) to competitive bidding through Bank Misr in co-operation with Hermes Investment Co. During May only some 10 per cent was offered to anchor investors, but in June a deal was signed on the sale of 89 per cent to a specialised strategic investor. The buyer was a joint venture of a private sector company (founded by some Egyptian entrepreneurs and the privatised Commercial International Bank) and EGYMAC, a state enterprise not subject to Law 203/1991. Ten per cent went to the employee shareholder association. One per cent is held by other private investors. Nevertheless, the semi-official privatisation report to USAID claimed that ELMACO left the public sector because of a 100 per cent sale to private ownership.

Employee Shareholder Associations

In order to increase political support for privatisation, employee shareholder associations have been established in the companies. Some 10 per cent of the shares of a state enterprise being privatised are usually sold to the employee shareholder association at a reduced rate and at favourable financing, generally through the respective holding company, which also supplies management for the employee shareholder association, thus maintaining *de facto* control over the employee shares. The individual employees are members of the employee shareholder associations but do not personally receive the shares. Therefore they have limited powers of disposition. Senior managers of state enterprises whose career prospects are threatened by the reform process adopt strategies to maintain a core of public sector business entities while presenting a misleading picture of privatisation to the public. State enterprises (not only Law 203 companies) buy each other's shares in a more or less camouflaged manner. Employee shareholder associations, originally designed to support the privatisation process and to create incentives for public sector workers, are being used by managers of state enterprises to maintain control of the companies.

Box 9.11. Privatisation Camouflage: The Development & Popular Housing Company

In August 1996, 51 per cent of the Development & Popular Housing Company, an affiliated company with a paid-up capital of LE 35 million under the Holding Company for Housing, Tourism & Cinema, was offered for sale. Twenty-six per cent was sold to financial institutions, investment funds and other companies, another 15 per cent to individuals, and the remaining 10 per cent went to the employee shareholder association. Since management controls the employee shareholder association's 10 per cent share, only 41 per cent actually went to independent private and quasi-private investors including mutual funds run by public sector banks. Nevertheless the company is presented as an example of a successful majority privatisation.

A large number of the minority flotations by Law 203 companies occurred during the first half of 1995. Only seven of the 30 Law 203 companies that carried out privatisation measures by August 1996 are reported to have sold majority shares, ten companies sold shares to employee shareholder associations and some others started to look for anchor investors. In addition, various financial institutions bought part of the shares in at least ten of the 30 companies. Some of them were public sector banks or investment funds founded by these banks.

Box 9.12. The Employee Shareholder Association Game

The Egyptian Starch & Glucose Company sold a first portion of 39.7 per cent through the stock exchange, 5.58 per cent was sold to investment funds, 3.4 per cent to other financial institutions, 1.13 per cent directly to employees, and 10 per cent to the employee shareholder association. Thus 59.81 per cent had been ostensibly sold to the public. However, since the shares belonging to the employee shareholder association remained under the control of the managers, the latter still control *de facto* the unsold part of 40.19 per cent (100 minus 59.81) plus the 10 per cent sold to the employee shareholder association, a total of 50.19 per cent. Yet the company is presented as having privatised a majority share.

Misr Oil & Soap of the Food Industries Holding Company sold 54.31 per cent (25.3 per cent to the public, 6.91 per cent to investment funds, 12.10 per cent to financial institutions, 10 per cent to the employee shareholder association). As the shares of the employee shareholder association are still under the control of the management, only 44.31 per cent more or less went to private investors.

Notes

1. Esser, Hillebrand, Messner and Meyer–Stamer, 1996.
2. O’Farell, 1995.
3. IBTCI, 1997a.
4. *Ibid.*
5. In practice, management performance is measured by three criteria: 1) Does the holding company have more profitable affiliated companies than in the past fiscal year? 2) How many affiliated companies of the holding company have earned higher profits than in the past fiscal year? 3) How many unprofitable affiliated companies of the holding company were able to reduce their losses as compared to the last fiscal year?
6. O’Farell, 1995: “The combination of free education and the disconnection of the rapidly growing public sector from the wealthy elite provided them with an opportunity for social mobility which was not historically available in Egypt to people of their backgrounds. These managers fear that even if they are performing well, a wealthy buyer of the public enterprise may replace them with relatives from the wealthy elite.”
7. Managers of holding companies who are relieved can be compensated by political careers. The Minister of Industry had previously been chairman of the Nag Hammad Aluminium Company with a labour force of 25 000. “Victims” of privatisation can thereby preserve their economic privileges and their social status, the latter often being more essential for people above age 60.
8. With the establishment of the Higher Privatisation Committee in 1996 restrictions were introduced against these manoeuvres.

Random Influences on the Reform Process

Coping with Uncertainty

Relatively small economies are increasingly dependent on influences from the international economic system. One of Egypt's problems is a widespread lack of awareness of these long-term global trends, or of how more successful economies have been able to adjust to them. The claim by Egyptian officials that "Egypt is different" obscures the real issues.

Some future changes in the world economy are foreseeable. Others are not, and thus they place a premium on flexibility for being able to adjust to new requirements. Egypt has not been particularly successful in coping with the new challenges of the world economy in recent decades and has not been able to keep pace with the newly industrialising economies of East Asia and Latin America. Apart from changes due to globalisation, there have been random influences on the pace of reform.

The Assassination of Sadat

The first random event was the assassination of President Sadat in 1981, following a mounting government confrontation with Islamic fundamentalists. His successor President Mubarak adheres to a cautious approach, trying to balance Nasser's and Sadat's legacies. This may explain the image of a somewhat more cautious leader often "muddling through" towards an inconsistent compromise. On the other hand, a substantially different approach would require a comprehensive political and economic overhaul of the country that would not spare a ruling elite, whose highest ranks have been virtually the same since the 1952 revolution.

The Collapse of the Soviet Bloc

A second random influence was the collapse of the Soviet Union and the state economies of eastern Europe. This came as a shock to the public sector establishment which in its early Nasser years had been conditioned by its “own way to socialism”. Sadat had changed sides in 1974 after years of despair after the defeat in the 1967 war with Israel. Rebuilding Egyptian self-esteem was the main motivation for the successful Egyptian attack on Israeli positions on the East Bank of the Suez Canal in 1973, which was a surprise for the United States (according to Henry Kissinger) and for Israel. This was not easily understood by the western democracies with different conceptions of “honour”. From the Egyptian perspective, however, the restoration of national pride was instrumental in building a viable bargaining position supported by the Egyptian people at large.

Henry Kissinger’s policies helped to encourage Egyptian trust in its new partner. Soviet support for Egypt had been a disappointment for years. Yet Sadat still had made a tremendous step by proclaiming Egypt’s Open Door Policy in 1974, a 180-degree turn against official rhetoric on “capitalism, colonialism and imperialism” since the Free Officers’ Revolution of 1952. Under Sadat’s grand design, Egypt became a major recipient of annual US financial support by making peace with Israel at the price of being ostracised and expelled from the Arab League.

As long as Soviet Union existed, because of the close personal relationships between Egyptian and Soviet officers and because military equipment and spare parts were largely of Russian origin, all players knew that Egypt still had a second option, albeit a far less remunerative one. The collapse of the Soviet Union ended that.

Egypt’s diplomatic recognition of Israel and the Camp David peace accord played a major role in reducing tensions in the region, although with an ambiguous impact on strategic rents. On the one hand, the danger of a major military confrontation had been eliminated. On the other hand, regional strategic considerations now had to include Egypt’s social and political stability as a major element of the Middle East peace process. Thus, Egypt was able to shift part of its social problems to the major western donors.

After the collapse of the Soviet bloc, concerns of some EU countries, especially those of northern Europe, shifted away from the Middle East towards political problems, foreign aid and private foreign investment in eastern Europe.

The 1990–91 Gulf War

A third random event was the 1990–91 Gulf War, following the Iraqi invasion of Kuwait. Consistent with its strategic policy, Egypt joined the anti-Saddam coalition, providing some 30 000 troops. This commitment, of great importance for the image of the US-led UN military intervention, was rewarded by a 50 per cent cut of Egypt’s

\$50 billion foreign debt by the Paris Club in addition to substantial foreign assistance. Egypt's request for an additional \$9 billion was by and large accepted by the donors who pledged \$8 billion for the first two years. Egypt's strategic calculation had paid off. On the other hand, the exceptional flows of strategic rents allowed the government to postpone essential reforms necessary for a viable, internationally competitive economy to support its growing population and become independent of the rent income.

The Middle East Peace Process since the Oslo Agreement

The fourth random influence was the Middle East peace process after the Oslo conference and the Washington agreements between Israel and the Palestinian Authority, as well as with Jordan. A reduction of political tension will lead to a decline of the geostrategic rent. It could be replaced by more effective development and private foreign investment. From the perspective of the ruling Egyptian elite, however, this might involve increasing demands for greater civil rights and requests by the younger generation for political participation and more rational and transparent decision making. Moreover, the private sector would question the present system in which relatives of high-ranking political figures are "partners" in most lucrative business ventures.

All major regional players in the Middle East peace process are aware that a certain degree of tension keeps rents flowing.

The Change of Government in Israel since 1996

A fifth random influence was the outcome of the 1996 Israeli elections, which led to the Netanyahu government and a new interpretation of the Oslo Agreements signed by its predecessor. After weighing the implications, the Egyptian government decided to maintain its basic support for the US Middle East policies while maintaining a prudent independence by not participating in the Clinton–Netanyahu–Arafat–Hussein talks in Washington in October 1996 during the US presidential campaign.

The Barcelona Initiative

The last major random element was the Brussels initiative to establish a "Euro–Mediterranean Free Trade Zone of peace and stability" by the year 2010. It was the outcome of different foreign policy priorities of EU members. Those neighbouring North Africa had a direct interest in co-operation with Arab countries, while most of the northern European states were less concerned with the area and more involved with eastern European issues.

A compromise between the proponents of the eastern and the southern orientations resulted in promises of 5.5 billion ECUs to eastern Europe and 4.9 billion ECUs to the non-European Mediterranean countries. The economic potential of the Euro-Mediterranean initiative and an EU eventually enlarged towards the east means vast new economic opportunities which will require considerable structural adjustment by the Middle Eastern, North African and eastern European countries concerned. The EU will support this adjustment by financial and technical assistance.

This means that Egypt will have to face greater competition with Morocco, Tunisia, Turkey, Malta, Cyprus, Israel, Jordan and possibly some other Mashrek countries. Neither the public nor the private sector of the Egyptian economy is prepared to face this new subregional competition.

Dealing with Turbulence

The acceleration of global change and international turbulence require an ability to react to new challenges from a position of relative strength¹. Under conditions of socio-economic tension and pressure of time, decisions are often made by small circles where there is much uncertainty. Egypt's foreign policy since Sadat has demonstrated strategic and tactical prudence, but its economic policies have been far less efficacious.

Developing countries have taken different approaches for dealing with new economic challenges in recent decades. Concepts which Egyptian officials traditionally cherished — stability, order and “pyramidal”, “neo-pharaonic” control — have proved inadequate for coping with turbulence. Experimentation, studying new approaches and adapting them to Egyptian conditions would have been more productive. The Egyptian approach to economic policy makes a striking contrast with efforts of East Asian countries to adapt to new challenges and opportunities in the global economy.

Note

1. Weiss, 1990, 1992*a*.

Egypt's Reform Impasse

Major Bottlenecks

Economic development requires commitment, determination, effort, individual incentives and social discipline. There is ample evidence that the basis of successful development derives from the society itself. It requires a degree of social consensus expressed in political will. Strategic visions must be translated into shared goals, operational objectives and well-defined policies effectively implemented. Many of these essentials have been weak in Egypt.

As mentioned in previous chapters, Egypt has been a “pyramidal” society conditioned to centralised control, with no widely shared domestic consensus on future basic issues and options in a changing global economy. Contemporary economic policy debate does not always deal with the essential issues. The government does not have access to channels of communication providing a relatively free flow of ideas and a variety of policy options. Without democratic expression in the society, the government becomes isolated from new ideas. The 1995 elections, with a 94 per cent vote for the ruling NDP, were marked by official manipulation, denial of free expression, intimidation, threats and even some assassination at the local level. An initial announcement after the elections that the cabinet would not be reshuffled provoked public discontent. After the US government indicated it would not co-operate with the old cabinet, a new prime minister and government were appointed.

The new Prime Minister Ghanzouri began to streamline the government, introducing regular weekly meetings of the whole cabinet, which had been unknown under his predecessor Atif Sidqi. Official statements supporting privatisation and transformation became clearer, but vested interests did not retreat, and kept impeding reform. On the other hand, major multilateral and bilateral donors maintained their pressure, and the government wavered between conflicting demands as its room for manoeuvre decreased.

The main obstacle is the lack of a broad coalition supporting reform. Many stakeholders are potential losers: the political elite, the bureaucracy, public sector managers, labour, and even the many private entrepreneurs who have comfortable niches in the existing system.

Many stakeholders are also unfamiliar with the imperatives of the newly emerging international economy. The ruling elite is aware that the foreign donors must support Egypt because of strategic concerns such as Middle East oil, Israel's security and the Israeli–Palestinian conflict. The government would like the major donors to share responsibility for Egypt's mounting social problems. Meanwhile, little is being done to resolve problems like population growth, the need for international competitiveness, and renewed current account deficits. This immobility is all the more dangerous as some major bilateral donors are facing problems of structural adjustment, ailing industries, unemployment and cuts in their own social welfare nets. Recipient countries can no longer rely on unlimited help from the donor countries.

Rent seeking has become an unintended result of international aid. Essential developmental tasks have not been tackled, starting with efforts to build a national consensus on the urgent need for change, the options, constraints, policies and their expected economic and social effects. Instead of clearly stating the issues, the government has concealed the tremendous challenges and avoided an open debate. All social groups have been told that changes would not affect them, that the public sector would remain the backbone of the economy, that there would be no labour dismissals, etc. The majority of the population believes the promises and has not yet grasped the hardships they will experience as a result of reform. A national consensus on the tasks ahead has not yet emerged. The slow pace of privatisation helps the government to preserve its access to economic resources as an instrument of political control.

The institutional framework for carrying out reform has been neglected. The legal system is still inadequate and the institutional framework lags behind that of other newly industrialising countries. The ability to formulate economic policies and programmes is comparatively limited. There is no economically viable plan for dealing with the future social costs of adjustment. The benefits of reform are not clearly defined, and policies are geared to satisfying donors and securing rent income. There is a lack of basic educational reform and of research and development.

Changes in the Power Equation

The Bureaucracy

The three major forces in Egypt are the state bureaucracy, the public sector and the military. Their outlook and political weight have been altered during the process of reform. The Egyptian bureaucracy permeates the society. From 1952 to 1992 it increased from 350 000 to 4 million employees. From 1980 to 1992, during 12 years

of hesitant reform, it grew by 240 per cent. In other words, although some liberalisation occurred, the bureaucracy continued to grow and “provided a climate that encouraged clientelism, corruption, nepotism and general waste of state resources”¹. On the other hand, informal patterns of working with the state sector on the town and village level made it possible for the people and the bureaucracy to circumvent cumbersome rules and regulations.

Opposing Groups

On the whole, the governmental administration has become weaker. In practice, it is usually absorbed by one major policy issue. In recent years this has been the struggle against the Islamist opposition. In the 1990s, political surveillance of NGOs came to the forefront. In spite of attempts at harsh repression, a rising number of NGOs attracted young people to deal with problems of daily life in their immediate neighbourhoods².

There have been major strikes of public sector workers, e.g. the textile strike in the Nile Delta in 1994, involving some 20 000 workers, and the strike in the Nasr Automobile Factories in 1995, involving some 10 000 workers. The government efforts to manipulate the elections of labour union representatives encountered mounting resistance.

The professional syndicates are very influential, in particular those of lawyers, engineers, dentists, medical doctors and pharmacists. Elections of their representatives have been blocked by the government to impede a further advancement of Islamist candidates. In September 1996 the Administrative Court dealt with a suit brought by the lawyer’s professional organisation against the president of the Court of South Cairo, accused of delaying the election of their board³. The representatives of the professional elite are increasingly speaking out, including the traditionally influential engineers whose officers are also under judicial tutelage⁴.

Mounting dissatisfaction is being voiced by skilled younger people. The impoverishment of the lower income strata, the uneven distribution of income and wealth and the excessive conspicuous consumption of the *nouveaux riches* adds to the general discontent.

The Military–industrial Complex

The military–industrial complex emerged during the late 1950s and has been relatively well supplied with funds and technical personnel⁵. Many army engineers were later appointed to the boards of public sector companies. In the 1960s a fairly efficient military industry, including automotive and machine tool factories, had been established to deliver standard equipment and weapons systems. No official data on the military sector have been made public apart from rare hints at production units

named by numbers (“military factory 123”). The prestige of the military apparatus plummeted after the catastrophic 1967 war with Israel but recovered with the crossing of the Suez Canal in 1973. No information is available on decision making in the military and its views on the reform policies, but it is clear that former President Sadat could not have carried out Egypt’s turn to the west without the support of the armed forces, who were disappointed with the poor support of the Soviet Union and attracted by the US option, views which became stronger during the 1970s and especially the 1980s.

Increasing military co-operation between Egypt and the west provided substantial benefits for Egyptian officers. Up to 200 officers per year were trained in the United States. “Military facilities, vehicles, and even uniforms have been significantly upgraded. The constant flow of state-of-the-art weaponry, even if in quantities considerably less than those being obtained by Israeli or even Saudi forces, provided a basis upon which military self-esteem could comfortably rest”⁶. A wide range of benefits is provided such as flats “for purchase at highly subsidised prices by officers, for many of whom serving as a second, third or fourth source of rental income”⁷. A chain of military consumer co-operatives sells inexpensive domestic and imported goods, unavailable elsewhere. An exclusive educational system was established, topped by the Military Academy, the Military Technical College, an Academy of Military Medicine and a Military Academy for Administrative Sciences, preparing officers for lucrative jobs in the military-industrial complex. There are health and recreational facilities⁸, catering for family events like marriages, either free or at nominal cost in officers’ clubs, and lucrative management jobs for retired colonels and generals.

Military manufacturing began in the Nasser era in the field of weapons, but rapidly moved into agriculture and land reclamation projects, construction and service industries, all heavily subsidised. In particular since President Sadat’s Infitah it branched out into other areas of industry, such as automobiles (in co-operation with General Motors), electronics, and a wide range of other production lines.

Since the 1980s, leading members of the Egyptian military establishment have understood the risks of Egypt’s precarious budgetary and foreign exchange situation for the armed forces and the opportunities created by the reform policies for their own industrial activities. They have understood that in spite of ample military deliveries by the United States, the budgetary impasse made it necessary for the military sector itself to generate earnings, as in other former socialist countries⁹. The most privileged class in Egyptian society has provided essential support to the three presidents since the 1952 revolution, all three former military officers.

Nonetheless, the officer corps has been purged repeatedly to eliminate Islamist tendencies, especially among the lower grades where there was extensive indignation at the extent of social disorder, moral decay and corruption in Egyptian society. The military is believed to contribute to stabilising a precarious status quo, sharing its benefits and exposed to its risks. Hence, the army and its military-industrial complex have high stakes in preserving their privileged positions, linked to the status quo and

to the impact of reforms, especially on the military factories. They are also exposed to the risks of insufficient reform and hesitant moves towards modernisation. Hence, the military has stakes on both sides. It must push for technological innovation, which is impeded by irresolute reforms, while still enjoying the benefits of a comfortable and well-protected niche exempted from public accountability and pressure to reform. The government kept insisting that there would be no privatisation of the military-industrial complex. As a result, the military establishment is caught in the same dilemma as the Egyptian leadership, between a need for change (e.g. US congressional objections to the high costs of assembling US M-1 Abrams tanks in Egyptian military factories), and the negative consequences of reform for their current military and business affairs, at least in the short run.

The military is the crucial pillar of the ruling establishment. Thus far, its power structure has hardly been affected by the reform measures. Large inflows of foreign aid, especially US military aid, have allowed the Egyptian military to meet the demands of its rank and file. The political role of the military could decline if a profitable private industrial sector gains economic strength, political influence and attraction for talented young people, who might have chosen an army engineering career with its promising avenues for top management jobs in state enterprises.

Public Sector Managers

Although the public sector tries to defend its vested interests, this does not mean that versatile managers of state enterprises will not take advantage of the new market opportunities. Private sidelines parallel to one's official state enterprise job offer ample possibilities for self-enrichment by making use of insider information, clientele networks, illegal transfers of resources from public companies to private own ventures, etc. By and large, the public sector establishment has been able to maintain its power. Like other beneficiaries of the status quo, managers of state enterprises are aware of the necessity for change but also oppose it to protect their economic and social prerogatives.

The Donor Dilemma

All major political groups are aware that change is unavoidable. The present stalling on implementation is being challenged by foreign donors. Their dilemma, however, is that development assistance has had a counter-productive effect on Egyptian commitment to reform. In addition, since 1996 a number of events have influenced strategic calculations, foremost being the outcome of the election in Israel and greater political tension in the Middle East.

This again increased the political weight of the Egyptian government as a moderate pro-western partner, leading to a feeling of urgency among western donors for getting the Egyptian reform process on track, and to greater willingness to exert pressure, as during the Clinton–Mubarak talks in early 1996. That meeting led President Mubarak to order his prime minister to proceed with the reform agenda.

Both the donors and the Egyptian government will eventually have to face the social costs of the massive disguised unemployment in the state enterprises. They could reconsider their strategies if the political costs appear to be prohibitive. Apart from the Social Fund with its limited impact, no programme has been devised by the Egyptian government, or by the major donors, for dealing with social protests which could threaten the survival of the Mubarak presidency. Understandably, the Egyptian government has no interest in a change of the power equation. An ever stricter political surveillance provokes criticism from professional elites, organised labour, non-violent Islamic reform movements and other groups in a slowly emerging civil society, linked to an international network that insists on respect of human rights, irrespective of the cultural tradition. Effective commitment to development must come from within a society, but this would require political reforms which are unacceptable to the existing power structure.

Major Failures

Commitment. The long history of hesitant moves towards building a competitive Egyptian economy since President Sadat's October Working Paper of 1974 demonstrates the weakness of the commitment to reform. The slow pace of change made it possible for anti-reform forces to persist for more than two decades.

Credibility. The government's hesitation in confronting old and new vested interests has undermined the credibility of reform.

Coalition. The government failed to establish a coalition of reform supporters or incentives for reform geared to major groups of stakeholders. The scandalous self-enrichment of a new class of speculators and traders — only a small number of technology-oriented manufacturers — close to the political elite and high ranking public sector officials, has discredited the reforms in the public's eyes.

Corruption. The ruling establishment is identified with extensive corruption. A son of a leading politician is eager to share in any larger successful private business. The new business community is one of the regime's main constituencies and therefore shares the flows of rent income. The public is informed about such phenomena by a relatively free press, and reacts with growing political discontent and frustration.

Lack of technical policy expertise. Since the early years of President Sadat's reform initiative, the government has lacked technical expertise for developing clearly defined objectives, for operational planning with schedules, or for adequate

implementation, monitoring, and evaluation. There is a role for foreign experts, but they cannot substitute for lack of domestic know how in general, let alone provide the political will to move ahead with a reform agenda. Foreign prescriptions did not meet broad support from the Egyptian recipients. After decades of state planning, there was a general lack of experience in dealing with the intricate problems posed by reform. There have been no systematic attempts to draw on the eastern European experience, or on successful reforms in developing countries.

Neglect of the social issues. The lack of professionalism in administrative bodies became apparent in the spheres of economic and social policies. Thus far the government has no idea for dealing with the substantial surplus labour in the overstuffed state enterprises which may be restructured, privatised, or liquidated. Another example is the ending of land tenure and the liberalisation of agricultural rents under a 1992 law which is becoming fully effective in 1997, after a five-year transition period. Hundreds of thousands of tenants will become landless labourers, displaced by large commercial farms. It seems to have been forgotten that the high inequality of land distribution had triggered Nasser's land reform immediately after the revolution of 1952. Apparently the devastating social consequences of the new law for political stability, possibly even for the survival of the regime, have not been considered.

Transparency. The government has been operating on amazingly short time horizons. Short-term political survival supersedes long-term development. The government never had the courage to present the realities of the reform programme to the public: the requirements, hardships and social costs for attaining long-term benefits. The agreements with the World Bank and the IMF are not published in the Egyptian media. The dimensions of the envisaged reform measures remain confidential. The public and even the People's Assembly have been deliberately misled in some instances to avoid opposition. As a result, a broad social consensus on the reform project could not emerge.

Disinformation. Many stakeholders were led astray. Government employees were told that there would be no dismissals, state enterprises were assured that they would continue to be the backbone of the economy, labour was promised that no employee would lose his job, and the private sector was reassured that trade barriers would continue to protect its markets from international competition.

Appeasement rather than appealing to joint effort. The ruling elite does not conceive of the people as partners but rather as of petitioners, following an ancient tradition in the Nile valley. Government receipts are relatively independent of the productive capacity of human capital, since they are based on various forms of rent (geostrategic rents, Suez Canal fees, oil income, SUMED pipeline fees, tourism exploiting historical monuments) to meet its immediate financial needs. Thus far social pressure has been partially relieved by raising the wages of government and public sector employees by 10 to 15 per cent annually. Current consumption to appease the masses has precedence over badly needed long-term investment.

Neglect of productivity. There is no determined commitment to raise economic productivity, e.g. by modern management tools, investment in education and in research and development, or in creating synergies between privatisation of state enterprises and private sector development.

Lack of self-renewal. One of the most conspicuous failures is lack of renewal of the ruling elite itself. By and large in its top ranks it still consists of the group which participated in the 1952 revolution, enlarged by co-optation of technical professionals, in particular engineers. The lack of democratic participation has made it difficult to bring new people from different backgrounds and with fresh ideas into influential administrative positions.

Macroeconomic Stabilisation, Structural Adjustment and Institutional Reform

The first stabilisation measures hardly met organised resistance. The IMF's advice to abstain from deficit financing by central bank credit and to shift to issuing treasury bills to reduce macroeconomic liquidity did not provoke immediate resistance from pressure groups.

The reduction of public spending followed the standard recommendations of the IMF to reduce macroeconomic demand for heavily subsidised basic consumer goods (especially bread, energy, and social services). Here the impact was substantial and hit the majority of the population, and especially the urban poor, but this segment of the population was poorly organised and unable to mount any effective resistance.

Thus, the general budget was stabilised in a relatively short period, with sharply falling deficits in relation to the GDP. Politically more sensitive steps for increasing budgetary receipts by raising taxes and stepping up tax collection, especially among the higher income strata and the private business sector (still with low marginal income tax rates, compared to western countries), needed more time for preparation and were tackled more hesitantly after opposition from the business associations. Following the logic of minimising political resistance, tax reforms focused on the introduction of a general valued added tax which replaced the previous sales tax. It strengthened the share of indirect taxation without arousing resistance from powerful groups. The burden was again greatest for the majority of low income consumers.

Devaluation encountered fierce resistance. It would have harmed the interests of the influential upper class and importers. Foreign luxury items such as automobiles would have become more expensive. In this domain the resistance of powerful domestic stakeholders could not be overcome in spite of substantial IMF pressure.

The removal of export barriers was also politically complicated. This was welcomed by the outward-looking segments of the business community, although its impact has been limited because of the lack of internationally competitive Egyptian export goods and an unfamiliarity with international marketing practices. Liberalisation

of imports, on the other hand, was subject to lengthy debates with the private and public manufacturers having stakes in the protection of domestic markets, trade monopolies, etc. Nevertheless, it could be enforced under continuous donor pressure. The middle classes benefited from less expensive and higher quality foreign products.

The core political issue has been privatisation. Here a phalanx of vested interests has been able to block serious reform. In the final analysis, the international donors gave in to Egyptian resistance in spite of strict World Bank and IMF conditionality. Quasi-privatisation measures such as selling 10 per cent of the shares to a company's labour force, without transferring common shareholder rights, or selling a minority of the shares to other state enterprises or public-private joint ventures, were finally accepted as "privatisation". To a considerable extent, these measures simply redistributed state resources among influential players in the public sector.

When the IMF decided in October 1996 that Egypt had met the necessary conditions and agreed that the third instalment of debt reduction by the Paris Club could proceed, the donors lost leverage on Egyptian decision makers. New leverage may come from the commitment of the Consultative Group for Egypt in May 1997 in Paris to pledge another \$2.5 billion for 1997-98 on the assumption that a "rapid reduction and the eventual elimination of poverty must be one of the top priorities" of the government¹⁰.

In retrospect, macroeconomic stabilisation by presidential decrees (without a parliamentary vote) proved to be easier than structural adjustment because it met less organised political resistance. It greatly affected the lower income strata, but in an anonymous way, whereas structural adjustment measures forced the regime to confront vested interests of public sector managers, labour unionists, administrators, public and private entrepreneurs, and business associations. Macro stabilisation was also supported by foreign aid, whereas apart from small allocations of technical assistance for accounting and privatisation consultants, there were no comparable aid incentives for restructuring, privatisation of the public sector and the institutional and administrative reform, which did not get off the ground.

Furthermore, institutional reform could benefit from knowledge of modern administrative management techniques and experience of reform in other countries, knowledge which would have been hard to find in the Egyptian bureaucracy.

The IMF decision to prolong the reform programme and let the third instalment of debt relief proceed was influenced by the impasse of the Middle East peace process. President Clinton met with PLO leader Arafat, Prime Minister Netanyahu and King Hussein in Washington on 1-2 October 1996. Egypt considerately abstained from that summit and insisted "that it could not be bought". While anger was uniting the Arab world again on the Israeli position, the Egyptian government remained one of the west's reliable allies. As in the past, Egypt managed to make its stand instrumental in obtaining US support against the IMF.

External and Domestic Actors

The dominant bilateral donor, the United States, has an ambiguous position. On the one hand it has an interest in helping Egypt to build a viable economy. The US Agricultural Reform Policy Program is an example of effective aid linked to a strict conditionality. In the field of privatisation, the USAID has rejected Egyptian attempts to restructure state enterprises before their sale. US experts and consultants have spoken out on various sensitive issues. This strategy aims at preventing Egypt from becoming a permanent, increasing burden on the US budget, especially since the Egyptian population could double again during the next three decades, even though it is hard to imagine how Egypt's economic and ecological resource base could sustain some 120 million people. Moreover, it cannot be expected that the US Congress will indefinitely approve increasing annual aid in line with Egypt's growing need for international subsidies.

On the other hand, the United States has vital strategic interests in the region. This is expressed in the predominance of US military over developmental assistance for Egypt, about an annual \$2 billion and \$800 million respectively. Furthermore, it cannot be ruled out that the US government and Congress might have different regional priorities in the future.

The majority of the other donors try to maintain a relatively low profile, leaving highly sensitive issues of the Middle East peace process to the parties immediately concerned. The European Union has difficulties achieving a clear stand because of the different interests of its member states. The aid from the EU as a whole and the majority of its member countries supports technical projects, rather than getting involved in the sensitive issues of reform. Therefore, they support the IMF and the World Bank but try to avoid the diplomatic costs of a bilateral conditionality.

On the Egyptian side, a long habit of relying on foreign aid, and its corollary, an unwillingness to take full responsibility for reform, have blunted the ruling elite's awareness of the long-term risks of rent-seeking instead of creating the foundations for future development. Changes in the international environment are only perceived dimly. There is a lack of dynamic response to these changes, which could have negative effects on Egypt's international political role and its competitive position with respect to other developing countries.

Despite the country's extensive poverty, the Egyptian people have not yet experienced the real costs of change. The public is largely unaware of the fundamental problems, much less what could be done to resolve them.

As a result, there is little public discussion of approaches to the country's problems and future challenges. One of the most pressing issues is Egypt's inability to meet its own basic food needs, while having hardly any competitive manufactured goods or services to earn the foreign exchange necessary to buy foodstuffs on the international

market. It is necessary to create a solid technological base supported by research and development and an adequate educational system in a climate that encourages innovation, initiative and critical thought.

Foreign Assistance Has Unintentionally Weakened Egypt's Commitment to Development

Could the Reform Process Have Been Smoother or More Successful?

The public's pride after the military triumph of 1973 on the East Bank of the Suez Canal could have been channelled into popular support for economic reform. President Sadat's October Working Paper of 1974 announced a basic reorientation of economic and foreign policies. The Camp David accord became the key to continuing foreign financial support by the western donor community. The *quid pro quo* is Egypt's pro-western stand in Middle East politics.

The economic results of development, however, have been less impressive. In part, this has been due to the system of centralised presidential rule and the fact that President Sadat's military background had not been conducive to understanding the details of economic policy. Under the prevailing political culture, the president would not delegate power to responsible technocrats, not even prime ministers, who were replaced often, especially if they gained prestige and could be considered as potential political rivals. Cabinet ministers were replaced even more often, also to counterbalance potential rivals¹¹. Any Egyptian success used to be ascribed to the president, while failures were always due to the prime minister or the cabinet members. One of the consequences was that from the very beginning of Sadat's Open Door Policy, there has been hardly any serious attempt to establish an efficient, high-level body for the design and implementation of consistent development policies. This shortcoming contrasts with the experience of the high-performing Asian economies¹².

Particularly with regard to structural adjustment the reform process could have been more successful, although not necessarily smoother. Again referring to the East Asian experience, democratic forms of government are of relatively recent origin and the transition to democracy has still not been completed, but in Asia there has been increasing understanding that elements of civil society and more flexible management tools are more adequate to cope with complex socio-technical systems than centralised bureaucratic leadership, in an epoch of unprecedented technological development and global economic change. Both in South Korea and in Taiwan a technocratic elite was allowed to play a major role, and recent years have seen political restructuring up to the top level, making a striking contrast with Egypt¹³.

Egypt failed to move towards privatisation when the costs would have been much lower than today. In earlier decades in a friendlier world economy, Egypt still enjoyed certain comparative advantages in the Mediterranean and international environments.

Meanwhile, the social costs of inaction have accumulated. Poor implementation of structural reforms has created a credibility gap. The government has been fencing with the donor community, repeatedly announcing reforms which were never going to be implemented. A coalition of vested interests benefits from and defends the status quo, while a falling standard of living burdens the majority of the people. This situation is accompanied by an erosion of the social consensus, with increasing risks for political cohesion and stability.

Notes

1. Zaki, 1995; cf. Hansen and Radwan, 1982; Desouki, 1991; Fergany, 1991.
2. Regulations that NGO meetings have to be observed by a civil servant can easily be circumvented by arranging the meetings on Friday afternoons (the Islamic holidays).
3. Another 11 professional syndicates have been subjected to the same government intervention. Law 100/1993 gave the courts the right to decide, among other things, the date and the place of election, giving the state total control of the professional associations, with the objective of blocking Islamist tendencies. Since the adoption of this law, 12 syndicates have not held elections and some have been put under judicial tutelage.
4. Salah Abd-el Karim, an engineer, expressed his dissatisfaction in the press: "The professional syndicates have stepped over certain red lines which has worried the government. Therefore they cannot let them be free anymore." Amr Hachem, a researcher at the Center of Political and Strategic Studies of Al-Ahram, held that "the relationship between the government and the civil society will go from bad to worse" (Cf. *Al-Ahram Hebdo*, 25 September–1 October 1996).
5. Waterbury, 1993.
6. Springborg, 1989.
7. *Ibid.*
8. *Ibid.*
9. Cf. Karmel, 1997, on the case of China: "As the central government decreased the amount of money earmarked for the military, the government promoted limited experiments to find unconventional means to support military budgets and programs. In 1984, Beijing gave the order to devote idle or underutilized resources to the production of civilian industrial machinery and consumer goods... Defense conversion and turning out products for civilian use became prominent priorities... Since 1987 the value of the military's civilian production has been greater than the value of its military production, and new marketization efforts begun in 1990 and 1991 have accelerated defense conversion. This trend creates an obvious shift in priorities for China's military-industrial complex. In the 1990s, more and more military organizations are struggling to turn themselves into for-profit corporations, with an emphasis on producing civilian goods. Altogether, there are perhaps 15 000 to 20 000 businesses run by the PLA (People's Liberation Army), the Ministry of Defense, and related defense organizations, and the larger businesses among them contain many production sites with independent accounting. Indeed, the military is

struggling to create corporate structures and earn profits in virtually every type of industry. In addition to military bases, the 'holdings' of this military-industrial conglomerate include electronics factories, mines, energy plants, roads, research centers and schools, automobile plants, broadcasting stations, publishing houses, hotels, department stores, retail outlets, farms, and grazing lands. The military is also involved in producing many value-added products with civilian rather than military applications, including textile machinery, special-use vehicles, drilling and exploration equipment, medical products, electronic devices, laser and infrared products, and sea-exploration and transportation equipment. All are being converted into for-profit enterprises, joint ventures, and limited-stock companies."

10. *Middle East Times*, 30 May–5 June 1997.
11. Shimizu, Amany and Iman, 1988. For example, during the 11 years of President Sadat's rule, the average tenure in office was 18 months for ministers of finance, 22 months for ministers of planning, 18 months for ministers of economy and only four months for the ministers of supply. "Each new minister became greatly concerned with the redistribution of specializations and functions, and also became preoccupied with cancelling or freezing former ministerial decrees and laws. All of these repercussions had a very negative impact upon the economic policies which soon lost their clarity, consistency and coordination"; *ibid.*
12. World Bank, 1993.
13. Springborg, 1989.

General Conclusions

Five Major Findings

The analysis of the Egyptian experience may help other developing countries to deal with the political economy of transformation and design appropriate reforms. Five key questions¹ arise:

i) How have initial political conditions and aspirations shaped the reform approach?

After two decades of Nasserism, President Sadat's western orientation since 1974 and the peace treaty with Israel established Egypt as a firm ally of the United States and European donor countries. After Sadat's assassination in 1981 by Islamist terrorists, that change of alliances was maintained by his successor President Mubarak and was rewarded by massive aid flows from western, Arab and international donors. This aid enabled the Egyptian government to avoid making unpopular decisions. It believed that restructuring, privatisation or liquidation of loss-making state enterprises were too risky for social and political stability since they would entail large-scale layoffs of excess labour.

At the end of the 1980s Egypt's balance of payments position and its \$50 billion debt had become unsustainable. The collapse of the Soviet bloc had eliminated Egypt's option of again turning to the Soviet Union. Another economic reform and structural adjustment programme supported by the international financial institutions was undertaken in 1990.

The 1990–91 Gulf War, however, relieved Egypt from immediate pressure to carry out reforms. Egypt's decision to join the Washington-led anti-Saddam coalition was rewarded by cancellation of \$25 billion in debt by the Paris Club and by new aid flows. Stabilisation measures recommended by the IMF for dealing with inflation and public finance were implemented, but structural adjustment was delayed for fear of

social turmoil. The administration, the ruling party, public sector managers, organised labour and large elements of the private sector with protected niches defended their vested interests.

ii) To what extent has the reform process itself produced new political constellations in terms of interest groups and power equations that influenced the reform strategy?

The resistance to the demands for reform was made possible by the massive flow of political rents. US military aid amounts to \$2 billion annually, in addition to some \$800 million in development assistance. Arab Gulf states and western donors contribute another \$2 billion in order to stabilise Egypt because of its geopolitical position in the Middle East and its support of the peace process. Rent elements are also a factor in workers' remittances from the Gulf states (which gave privileged access to Egyptian labour), the Suez Canal and SUMED pipeline receipts, crude oil sales, and tourism exploiting Egypt's pharaonic and Islamic heritage.

The bilateral donors did not insist on vigorous privatisation because they, too, feared the risks of political destabilisation. US presidents have personally intervened with the IMF and the World Bank to soften the conditionality of the reform programme because of the Islamist insurgency. European donors tend to avoid the bilateral diplomatic costs of insisting on more effective privatisation measures.

The rents are distributed to patronage–clientele networks and strengthen the anti–privatisation coalition. They lead to postponement of painful steps for achieving international competitiveness.

iii) Can it be concluded that institutional reform, including privatisation, is politically more difficult to carry out than macroeconomic stabilisation or trade liberalisation?

Privatisation was by far more difficult to carry out than stabilisation. The central question is how organised and powerful stakeholders are affected. Cuts in subsidies of foodstuffs, kerosene and public services severely hit the most vulnerable groups but did not provoke revolt because the poor are not organised and not (yet) ready to fight (as during the 1977 bread revolts) as long as adjustments are cautiously implemented step by step and in just tolerable doses. Macroeconomic stabilisation measures tend to affect large anonymous groups through technical instruments not clearly understood by the majority of the people, and usually do not expose a clearly identifiable antagonist.

On the other hand, a devaluation of the Egyptian pound, unsuccessfully requested by the IMF in the 1990s, would hit the influential importers, investors dependent on foreign machinery, and luxury consumption (e.g. automobiles) by the *nouveaux riches* who have sprouted since the Sadat era. Moreover, privatisation measures challenge the public sector establishment and thus provoke resistance from a powerful and well–organised front of potential losers. There was insufficient pressure to stimulate the emergence of a strong coalition supporting far–reaching economic transformation.

iv) Have reform processes been influenced by external economic events or political pressures?

The collapse of the Soviet Union and its eastern European bloc was a major ideological shock for the old public sector establishment and, more concretely, it led to a loss of markets. The more dynamic phases of the Middle East peace process led to concerns about the future of Egypt's international rent. Meanwhile, the flare-up of tensions has strengthened Egypt's role as a mediator under President Mubarak.

After the Gulf War, the minister of defence said that US–Egyptian military co-operation should be put on an equal footing with US–Israeli co-operation. While not necessarily accepting this view, the United States tried to strengthen ties with Egypt by agreeing to the assembly of M-1 Abrams tanks in Egyptian military factories and providing substantial military and economic aid.

v) Can policy options be identified which could have helped to prevent deadlocks or overcome political obstacles?

Commitment to development, social discipline, qualifications, motivation and innovative potential are well-known essentials for development. All these factors are relatively weak in Egypt, compared to competing developing countries, even in the Mediterranean basin. The country has a long habit of depending on foreign assistance. For two generations large sectors of the economy have not been exposed to the experience of competitive international markets. The public enthusiasm after the 1973 triumph against Israel was not channelled into a comprehensive programme of modernisation.

Stricter donor conditionality could have supported transformation by encouraging the domestic reform forces, by building coalitions with potential winners, by compensating potential losers, and by changing the incentive system with a view to creating strong groups of supporters of reform. The overall approach could have taken into account the political economy as a whole, going beyond technical orthodoxies, clearly evaluating potential political obstacles and promoting economic reforms with obvious benefits.

Nonetheless, other matters had to be considered: Egypt's central role in the peace process, its influential position in the Arab world, the strategic role of the Suez Canal and Egypt's strategic role more generally in the eastern Mediterranean and as a neighbour of Israel, its mediatory role with regard to other Arab states, and its moderating influence on various radical political movements in the Middle East.

Meanwhile, the costs of comprehensive reform have increased, not least because of rapid population growth and rising mass poverty. Hence, no extensive privatisation is politically sustainable without a reliable social safety net. As a result, the donors refrain from exercising sufficient pressure for reform in order to keep in power a regime that appears to be associated with stability, while discounting the possibility that the present order could eventually lead to a social upheaval.

Concepts of western assistance have proved to be counterproductive. The geostrategic rents have worked against Egyptian commitment to reform. An alternative policy might have left Egypt exposed to the painful learning processes of international competition, thereby creating pressures for effective adjustment while avoiding counterproductive, excess aid. Social frictions could have been dealt with by *ad hoc* relief measures by donors while avoiding permanent subsidies.

During the coming years far more serious adjustment measures will be unavoidable. They are still being delayed by counterproductive aid policies. The Egyptian reform process has entered a deadlock which is difficult to overcome under the existing “parallelogram of forces” as long as foreign assistance reinforces this paradoxical constellation.

Other Lessons Learned

- i)* The Egyptian case confirms the old insight of Irma Adelman and Cynthia Taft Morris² that the essential ingredients of development are a commitment by the political leadership, together with social discipline and social consensus in favour of reform, and a social and cultural system which encourages the human factor, its motivation for achievement and its creative and innovative potential.
- ii)* The commitment must arise from within a society and its internal dynamics of political organisation. A political culture perpetuating concentration of power at the top is usually not conducive to reform.
- iii)* Science and technology are essential components of a competitive economy. They cannot be obtained through aid or bought by petrodollars. Creativity requires an intellectual environment putting a premium on critical thought and innovation in general, even though it challenges established hierarchies of power.
- iv)* The high-performing Asian economies have shown that the development of more sophisticated economies must be paralleled by a transition from authoritarian control to more participatory and democratic patterns of government. Authoritarian rule counters the emergence of a civil society. It is essential to find ways to encourage the development of new perspectives, options and policies, eventually arriving at a broad consensus on the nature and pace of social transformation which can awaken dormant creative potential.

Authoritarian rule also isolates the ruling elite, leading it to cling to outdated policies that are inadequate for coping with the challenges of a rapidly changing international environment.

- v)* A non-revolutionary pattern of transformation requires a pro-reform coalition within the existing power structure. In other words, domestic decision makers will only support reforms if they can expect not to be negatively affected by them.

In other words, contrary to conventional views of foreign observers the ruling pre- and post-reform elites will probably remain the same.

- vi) The Egyptian case illustrates what happens if essential elements of economic transformation are lacking, making poor performance all but inevitable. Moreover, avoidance of fundamental reform could become self-perpetuating. As long as international financial obligations can be met by foreign aid and debt relief, the power equation in favour of reform may not change despite grave problems such as continuing rapid population growth, impoverishment of large segments of the lower income strata, large-scale ecological damage, and decreasing international competitiveness.

Moreover, the public sector will not give birth to a reform coalition which will eliminate its own privileges. A government whose main political constituency is the state bureaucracy and a public sector establishment cannot be expected to undermine this constituency.

- vii) Private business is not necessarily a supporter of economic reform. On the contrary, it has established comfortable and remunerative niches offered by the public sector, and shares its vested interests in a variety of protectionist measures. The lack of exposure to international markets may encourage an entrepreneurial bias in favour of trade and speculation rather than manufacturing, especially if fragmentary and inconsistent reform measures have created a new incentive system that encourages short-term profiteering.

The newly emerging private business elite may be partly co-opted by the old administrative and public sector establishment. For instance, it may be invited to occupy influential and remunerative posts in the ruling establishment, on government commissions, semi-official committees, etc. In return, they may back the old regime on sensitive issues, including cuts in social welfare.

- viii) Macroeconomic stabilisation policies are impeded by lack of political will in domains where reform encounters organised resistance, contrary to measures which affect the majority of the unorganised poor. However, the impact of the latter on social coherence and long-term political stability may be disastrous. In Egypt, the Islamist opposition focuses on these social issues by appealing to generally shared concepts of Islamic brotherhood, social justice and communal order.

Moreover, selective implementation of an originally comprehensive reform package leads to inconsistencies and new remunerative niches which can be exploited by rent-seekers, thus increasing inequalities of income and wealth.

- ix) Structural adjustment has met massive resistance. East European experience has not been used. Generally there was no inclination to privatise state enterprises in the first place. Furthermore, private businessmen had little interest in buying public enterprises because of fears of continuing political and bureaucratic

intervention, overvalued assets, technological obsolescence, narrow domestic markets, internationally uncompetitive products, etc. Similar considerations prevailed among foreign private investors.

Acquisition of public enterprises by Egyptians would also mean exposure to investigation into the (partly illegal) sources of previous capital accumulation, charges of tax evasion, and the possibility of harsh exposure in the press.

- x) A subject of general interest in many reforming countries (including Russia and China) is the new capitalist role of the military. The veil of secrecy prevents in-depth analysis of this phenomenon. There is still no way to include the Egyptian military-industrial complex on the reform agenda, even though it is producing an increasing share of non-military consumption and investment goods. On the contrary, the privileges of the military as the main pillar of the regime have been extended.
- xi) One of the most striking features of the newly emerging class of private Egyptian businessmen, “new Russians”, or former officers in China’s army who have become managers in the military-industrial complex, is the lack of awareness and sensitivity regarding the political risks of rising mass poverty. This poverty is often more desperate than before the days of the “glorious revolutions”. In Egypt the lessons of the social upheavals in the 1950s seem to have been forgotten.

The new private business community has been falling back on traditional attitudes of social irresponsibility, thus running the risk of another social upheaval in the future. A telling example is the elimination of a cornerstone of Nasser’s land reform by ending the previous legal limits to land tenure and on housing rents. The inherent political risks have not yet been fully perceived by the government.

Substantial further reform measures have to deal with the demands of the industrial labour force in the public sector. Egypt experienced strikes which were dealt with by tough military repression in recent years. These are not encouraging avenues to a civil society. In fact, the human rights situation has been deteriorating. Similar trends may appear in other reforming countries.

- xii) The Egyptian case also shows the ambiguous role of foreign assistance and donor pressure for reform. They may be counterproductive if aid replaces instead of strengthening domestic efforts. Eventually, rent incomes (not earned by own productive efforts) can lead to unsustainable patterns of governance and macroeconomic mismanagement.

Paradoxically, foreign aid can help to promote an anti-reform coalition of vested public sector interests and rent-seeking by the private business community.

As a result, rather than moving towards civil society and free markets, Egypt maintains the pattern of a semi-*rentier* state trying to accommodate increasing external and domestic political pressures without implementing reform measures rapidly enough. The social engineering approach of foreign technical assistance working its way through

a transformation agenda does not take into account the rationale of Egyptian decision makers: the attempt to consolidate power by sharing the geostrategic rent with their public and private sector constituencies.

- xiii)* The donor approach is not fully consistent with the objective of stabilising the Egyptian government in the face of mounting external and domestic risks. Conflicts over the distribution of resources, income and wealth are on the rise. Support for stabilisation and structural adjustment policies is a necessary but not a sufficient condition for building a sustainable socio-economic order, all the more so in the face of rising mass poverty and a concentration of newly amassed wealth, often not from legal or productive activities.
- xiv)* Enforcement of conditionality and political intervention are related to diplomatic costs. The 1990s have been characterised by a continuous protracted struggle between the international financial institutions and the Egyptian government without a major breakthrough of the former on essential matters such as devaluation and privatisation.

It has been argued above that a stricter conditionality might have produced more tangible results, but this would have required political will by the donors to make full use of the leverage of debt reduction and aid.

Another alternative would have been to reduce the general aid commitment to Egypt, thereby exposing the country to international competition and the risk of eventual social unrest.

Under either of those alternatives, it would not have been possible to link Egyptian foreign policy to western interests to the same extent. Aid administrators often do not address this dilemma explicitly, leaving foreign policy to their colleagues in foreign ministries. The outcome may be a lack of consistency between goals and means.

- xv)* Both the Egyptian government and private business lack a viable vision of Egypt's future role in a globally competitive environment. This also refers to the problems of the Middle East-North Africa region, including their precarious ecological dimension (Nile water management, desertification and soil salination, uncontrolled settlements on scarce farm land, etc.). The power structure is far from moving towards a transparent dynamic policy framework, geared to economic, technological and social development capable of dealing with the existing challenges, much less those of the future. Egypt's rising population cannot be sustained by the existing productive base. The long-term costs of further delays will be very high, possibly also for the donors presently avoiding short-term political costs. A similar dilemma exists in a number of other reforming countries, albeit not always in such an extreme form. There is no easy way out of the dilemma. What is needed, however, is clarity about costs and benefits, policy objectives and constraints, and time horizons.

xvi) From the standpoint of the gravity of the situation, the obstacles to open political debate prevent the development of viable options. The restrictions on creative, innovative thought actually affect the government's ability to perceive problems and react early and realistically to inevitable change. Considerations of short-term stability can undermine long-term political viability.

There seems to be a lack of understanding among the ruling elite of the dynamics of changing value systems and their impact on national development under global conditions.

The crisis of the late 1980s (which led to an economic reform and structural adjustment programme in 1990) was eased by the large flows of geostrategic rents stemming from the 1990-91 Gulf War. However, the donor community cannot be expected to subsidise Egypt on such a scale on a permanent basis.

Notes

1. Hiemenz, Ulrich (1997), "The Economics and Politics of Policy Reform—Work in Progress." Paper prepared for the 1997 Meeting of the Developing Countries Committee of the German Economic Association, Zurich, 6–7 June, OECD Development Centre, Paris, 1–18.
2. Adelman, Irma and Cynthia Taft Morris (1967), *Society, Politics and Economic Development: A Quantitative Approach*. John Hopkins University Press, Baltimore.

Annex

Tables

Table 1. National Accounts
(LE billion)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|---------------------------|-------|-------|-------|-------|-------|-------|----------|
| GDP at market prices | 96.1 | 111.2 | 139.1 | 157.3 | 175.0 | 205.0 | 230.9 |
| Net indirect taxes | 4.5 | 2.4 | 8.0 | 11.1 | 10.6 | 11.8 | 12.9 |
| GDP at factor cost | 91.5 | 108.7 | 131.0 | 146.1 | 164.3 | 193.1 | 217.9 |
| Agriculture | 17.7 | 19.1 | 21.6 | 24.4 | 27.5 | 32.0 | 35.4 |
| Industry | 26.2 | 36.1 | 43.6 | 48.3 | 53.8 | 61.7 | 69.5 |
| of which manufacturing | 22.3 | 25.1 | 30.6 | 34.4 | 39.9 | 46.5 | 53.2 |
| Services | 47.5 | 53.4 | 65.6 | 73.3 | 83.5 | 99.3 | 112.9 |
| Resource balance | -10.1 | -7.6 | -6.8 | -5.7 | -9.7 | -9.4 | -8.3 |
| Exports | 27.2 | 37.3 | 40.4 | 42.7 | 41.0 | 44.5 | 51.4 |
| Imports | 37.4 | 45.0 | 47.2 | 48.5 | 50.8 | 54.0 | 59.7 |
| Total expenditures | 106.2 | 118.8 | 145.9 | 163.0 | 184.7 | 214.4 | 239.2 |
| Consumption | 77.9 | 92.2 | 118.4 | 137.5 | 147.8 | 172.0 | 192.1 |
| Government | 11.1 | 12.7 | 14.6 | 17.7 | 19.8 | 21.9 | 24.2 |
| Private | 66.7 | 79.4 | 103.8 | 119.8 | 128.0 | 150.1 | 167.9 |
| Gross domestic investment | 28.3 | 26.6 | 27.5 | 25.5 | 36.9 | 42.3 | 47.1 |
| Government | 14.2 | 10.1 | 12.3 | 10.9 | 10.6 | 11.2 | 12.5 |
| Private | 12.2 | 17.6 | 16.3 | 14.5 | 26.2 | 31.0 | 34.5 |
| Total fixed investment | 26.5 | 27.8 | 28.7 | 25.5 | 36.9 | 42.3 | 47.1 |
| Domestic saving | 18.1 | 118.9 | 20.6 | 19.7 | 27.1 | 32.9 | 38.8 |
| + Net factor income | -3.5 | -3.3 | -2.4 | -9.9 | -3.2 | -2.6 | -2.7 |
| + Net current transfers | 9.7 | 11.2 | 18.2 | 16.5 | 10.9 | 11.1 | 11.3 |
| = National saving | 24.3 | 26.9 | 36.4 | 26.3 | 34.8 | 41.3 | 47.3 |
| Gross national product | 92.5 | 107.8 | 136.6 | 147.3 | 171.7 | 202.3 | 228.1 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 2. **Shares of GDP at Current Prices**
(percentages)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|---------------------------------|-------|-------|-------|-------|-------|-------|----------|
| Gross domestic product | 100 | 100 | 100 | 100 | 100 | 100 | 100 |
| Net indirect taxes | 4.7 | 2.2 | 5.8 | 7.1 | 6.1 | 5.8 | 5.6 |
| Agriculture value added | 18.5 | 17.2 | 15.6 | 15.5 | 15.7 | 15.6 | 15.3 |
| Industry value added of which | 27.3 | 32.5 | 31.4 | 30.7 | 30.5 | 30.1 | 30.1 |
| manufacturing | 23.3 | 22.6 | 22.1 | 21.9 | 22.8 | 22.7 | 23.0 |
| Services value added | 49.5 | 48.1 | 47.2 | 46.7 | 47.7 | 48.5 | 48.9 |
| Resource balance | -10.6 | -6.9 | -4.9 | -3.7 | -5.6 | -4.6 | -3.6 |
| Exports | 28.3 | 33.6 | 29.1 | 27.2 | 23.5 | 21.7 | 22.3 |
| Imports | 38.9 | 40.5 | 34.0 | 30.8 | 29.1 | 26.3 | 25.9 |
| Total expenditures | 110.6 | 106.9 | 104.9 | 103.7 | 105.6 | 104.6 | 103.6 |
| Government consumption | 11.6 | 11.5 | 10.5 | 11.3 | 11.3 | 10.7 | 10.5 |
| Private consumption | 69.5 | 71.5 | 74.6 | 76.2 | 73.2 | 73.2 | 72.7 |
| Government investment | 14.8 | 9.2 | 8.9 | 7.0 | 6.1 | 5.5 | 5.4 |
| Private investment | 12.7 | 15.9 | 11.8 | 9.2 | 15.0 | 15.1 | 15.0 |
| Gross domestic saving | 18.9 | 17.1 | 14.8 | 12.6 | 15.5 | 16.1 | 16.8 |
| Gross national saving | 25.4 | 24.2 | 26.2 | 16.7 | 19.9 | 20.2 | 20.5 |
| GDP deflator (% change) | 18.4 | 14.5 | 19.8 | 9.8 | 7.2 | 12.0 | 7.4 |
| Consumer price index (% change) | 19.0 | 19.6 | 21.1 | 11.2 | 7.2 | 12.0 | 7.4 |
| Total GDP (billion current \$) | 36.8 | 36.9 | 41.8 | 47.2 | 51.8 | 60.4 | 67.9 |
| Exchange rate (LE/ \$) | 2.61 | 3.01 | 3.32 | 3.33 | 3.37 | 3.39 | 3.40 |
| GDP per capita (in constant \$) | 740 | 720 | 730 | 740 | 850 | 940 | 1 050 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 3. Annual Growth Rates
(1992 prices) (percentages)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|--------------------------------|------|-------|-------|------|-------|------|----------|
| GDP at market prices | 4.8 | 3.6 | 1.9 | 2.9 | 3.9 | 4.6 | 4.9 |
| Exports | 1.7 | 13.0 | -1.4 | 7.0 | -4.7 | 1.3 | 9.9 |
| Imports | 7.6 | 1.7 | -7.1 | 1.0 | 1.8 | 1.2 | 5.8 |
| Total expenditures | 7.4 | 3.9 | 4.2 | -4.2 | 10.8 | 4.4 | 3.9 |
| Consumption | 8.8 | 5.4 | 7.4 | -4.6 | 9.8 | 4.3 | 3.7 |
| Investment | 6.1 | -11.4 | -7.2 | 1.8 | 15.0 | 4.7 | 4.5 |
| Gross domestic income | 7.9 | 1.9 | 3.5 | 2.2 | 3.3 | 5.2 | 4.9 |
| Gross domestic savings | 4.7 | -11.7 | -14.5 | 41.4 | -21.9 | 10.0 | 11.4 |
| Per capita GDP | 2.6 | -1.5 | 2.6 | 0.8 | 1.6 | 2.2 | 2.7 |
| Per capita total consumption | 5.6 | 2.8 | 5.6 | -6.7 | 7.4 | 2.0 | 1.5 |
| Per capita private consumption | 7.8 | 3.3 | 7.4 | 7.3 | 6.8 | 2.8 | 1.7 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 4. GDP at Factor Cost
(1992 prices) (LE billion)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 ^(a) |
|--|-------|-------|-------|-------|-------|-------|---------------------|
| GDP at factor cost (at constant 1992 prices) | 123.6 | 127.7 | 131.0 | 134.3 | 139.9 | 146.1 | 153.3 |
| Agriculture and irrigation | 20.7 | 21.2 | 21.6 | 22.2 | 23.0 | 23.7 | 24.4 |
| Manufacturing & mining | 20.2 | 21.4 | 21.7 | 22.3 | 23.2 | 25.0 | 26.9 |
| Petroleum & petroleum products | 12.4 | 12.7 | 13.0 | 13.2 | 14.3 | 14.3 | 14.3 |
| Electricity & energy | 2.0 | 2.1 | 2.2 | 2.2 | 2.3 | 2.5 | 2.6 |
| Construction | 6.3 | 6.6 | 6.7 | 6.8 | 7.0 | 7.4 | 7.8 |
| Transportation & communication | 8.6 | 8.5 | 8.7 | 9.0 | 9.3 | 9.8 | 10.4 |
| Suez Canal | 5.8 | 6.1 | 6.1 | 5.8 | 5.7 | 5.5 | 5.6 |
| Trade | 20.4 | 21.3 | 21.7 | 22.3 | 21.3 | 24.6 | 25.9 |
| Finance | 4.2 | 4.4 | 4.5 | 4.6 | 1.5 | 5.5 | 5.9 |
| Insurance | 0.07 | 0.07 | 0.07 | 0.07 | 0.08 | 0.09 | 0.14 |
| Tourism | 2.5 | 2.2 | 2.4 | 2.5 | 2.0 | 2.3 | 2.6 |
| Housing | 1.4 | 1.5 | 2.3 | 2.4 | 2.5 | 2.7 | 2.8 |
| Public utilities | 0.3 | 0.3 | 0.4 | 0.4 | 0.4 | 0.4 | 0.5 |
| Social & personal services | 9.3 | 9.7 | 9.8 | 10.2 | 10.6 | 11.1 | 0.1 |
| Social security | 0.08 | 0.08 | 0.08 | 0.09 | 0.09 | 0.1 | 11.0 |
| Government services | 8.6 | 8.9 | 9.3 | 9.7 | 10.1 | 10.5 | 11.8 |

^(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 5. Trade at Current Prices
(\$ billion)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|--|-------|-------|------|------|------|------|----------|
| Total merchandise exports | 4.3 | 5.7 | 4.7 | 6.3 | 4.7 | 4.8 | 5.4 |
| Primary products | 2.8 | 4.0 | 3.0 | 4.8 | 3.3 | 2.6 | 2.6 |
| of which petroleum | 2.4 | 3.7 | 2.8 | 4.6 | 3.0 | 2.0 | 1.9 |
| of which cotton | 0.2 | 0.08 | 0.03 | 0.03 | 0.08 | 0.3 | 0.3 |
| of which other agricultural products | 0.1 | 0.1 | 0.2 | 0.1 | 0.1 | 0.3 | 0.3 |
| Manufactured goods | 1.5 | 1.6 | 1.7 | 1.4 | 1.2 | 2.2 | 2.7 |
| of which textiles | 0.6 | 0.5 | 0.5 | 0.4 | 0.5 | 1.0 | 1.3 |
| of which other manufactured goods | 0.8 | 1.1 | 1.1 | 0.9 | 0.6 | 1.1 | 1.4 |
| Total non-factor service receipts | 6.0 | 6.7 | 7.3 | 6.5 | 7.6 | 8.2 | 9.6 |
| of which tourism | 1.0 | 0.9 | 1.7 | 1.5 | 1.7 | 2.2 | 3.2 |
| of which Suez Canal | 1.4 | 1.6 | 1.9 | 1.9 | 1.9 | 2.0 | 2.1 |
| Total merchandise imports | 11.4 | 11.4 | 10.0 | 10.7 | 8.4 | 11.2 | 12.4 |
| Food | 2.5 | 2.0 | 2.2 | 2.3 | 1.9 | 2.7 | 3.0 |
| Other consumer goods | 0.8 | 0.8 | 0.5 | 0.5 | 0.3 | 0.4 | 0.5 |
| POL and other energy | 0.4 | 0.5 | 0.5 | 0.6 | 0.3 | 0.7 | 0.8 |
| intermediate goods | 4.7 | 4.8 | 4.0 | 4.3 | 3.3 | 4.2 | 4.6 |
| Capital goods | 2.9 | 3.0 | 2.6 | 2.8 | 2.3 | 3.1 | 3.4 |
| Total non-factor service payments | 2.9 | 3.5 | 4.1 | 3.8 | 6.5 | 4.6 | 5.1 |
| Memorandum items: | | | | | | | |
| Net international reserves (NIR) | 8.2 | 15.2 | 20.3 | 20.4 | 26.6 | 28.1 | 30.6 |
| NIR in months of imports | 6.6 | 12.8 | 16.8 | 19.1 | 20.0 | 19.2 | 19.9 |
| Exchange rates | | | | | | | |
| Annual average (LE/ \$) | 2.61 | 3.01 | 3.32 | 3.33 | 3.37 | 3.39 | 3.40 |
| At end year (LE/ \$) | 2.71 | 3.27 | 3.32 | 3.35 | 3.39 | 3.40 | 3.38 |
| Index real average exchange (1990=100) (decrease is real appreciation) | 102.4 | 106.0 | 99.9 | 92.4 | 88.9 | 83.2 | 81.0 |
| Current account balance (per cent of GDP) | -1.8 | -0.1 | 1.9 | 0.1 | -1.2 | -0.5 | -0.1 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 6. Balance of Payments
(\$ million)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| Total exports | 10 456.6 | 12 424.8 | 12 161.9 | 12 833.9 | 12 178.8 | 13 134.4 | 15 117.5 |
| Merchandise | 4 374.2 | 5 709.7 | 4 790.8 | 6 301.9 | 4 573.5 | 4 854.0 | 5 438.0 |
| Non-factor services | 6 082.4 | 6 715.1 | 7 371.1 | 6 532.0 | 7 605.3 | 8 280.4 | 9 679.5 |
| Total imports | 14 361.3 | 14 977.3 | 14 230.4 | 14 557.5 | 15 083.8 | 15 910.9 | 17 567.0 |
| Merchandise | 11 441.1 | 11 424.5 | 10 039.5 | 10 728.2 | 8 488.4 | 11 279.9 | 12 454.0 |
| Non-factor services | 2 920.2 | 3 552.8 | 4 190.9 | 3 829.3 | 6 595.4 | 4 631.0 | 5 113.0 |
| Resource balance | -3 904.7 | -2 552.5 | -2 068.5 | -1 723.6 | -2 905.1 | -2 776.5 | -2 449.5 |
| Net factor income | -1 344.0 | -1 099.7 | -724.8 | -2 991.6 | -949.5 | -790.6 | -818.6 |
| Factor receipts | 776.9 | 1 049.4 | 1 080.2 | 1 258.0 | 853.5 | 1 625.5 | 1 755.5 |
| Factor payments | 2 120.9 | 2 149.1 | 1 805.0 | 4 249.6 | 1 803.0 | 2 416.1 | 2 574.2 |
| Interest | 1 805.8 | 1 238.5 | 940.1 | 1 236.6 | 1 211.8 | 1 327.7 | 1 452.1 |
| Other factor payments | 315.1 | 910.6 | 864.9 | 3 013.0 | 591.2 | 1 088.4 | 1 122.0 |
| Net private current transfers of which workers' remittances | 3 742.6 3 742.6 | 3 750.6 3 750.6 | 5 477.9 5 477.9 | 4 960.0 4 960.0 | 3 232.4 3 232.4 | 3 279.0 3 279.0 | 3 326.2 3 326.2 |
| Net official current transfers | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Current account balance | -1 727.7 | -113.7 | 2 697.9 | 208.5 | -622.2 | -288.1 | 58.0 |
| Official capital grants | 1 093.7 | 1 486.9 | 1 039.3 | 1 357.0 | 813.6 | 918.6 | 964.5 |
| Private investment (net) | 136.4 | 140.5 | 358.7 | 453.0 | 1 287.4 | 680.6 | 535.0 |
| Direct foreign investments | 136.4 | 140.5 | 358.7 | 453.0 | 1 284.9 | 676.5 | 500.0 |
| Portfolio investments | | | | | 2.5 | 4.1 | 35.0 |
| Net foreign lending | 1 189.7 | -143.3 | 75.1 | 220.9 | 75.0 | 295.1 | 560.4 |
| Disbursements | 3 186.9 | 1 999.0 | 1 730.3 | 1 405.4 | 1 018.5 | 1 133.9 | 1 668.9 |
| Repayments | 1 997.2 | 2 142.4 | 1 655.2 | 1 184.5 | 943.5 | 838.8 | 1 108.5 |
| Other capital flows | -55.6 | 5 618.9 | 971.0 | 1 433.9 | 992.8 | -51.7 | 189.8 |
| Change, net international reserves | 636.5 | 6 989.3 | 5 142.0 | 3 673.3 | 2 544.1 | 1 550.4 | 2 530.4 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 7. Trade at Constant 1992 Prices
(\$ billion)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|--|-------|-------|-------|-------|-------|-------|----------|
| Price Indices (1992 = 100) | | | | | | | |
| Merchandise exports | 99.7 | 105.7 | 100.0 | 95.3 | 90.3 | 99.2 | 104.9 |
| Merchandise imports | 95.8 | 98.0 | 100.0 | 100.9 | 102.5 | 107.1 | 112.0 |
| Merchandise terms of trade | 104.0 | 107.9 | 100.0 | 94.5 | 88.1 | 92.6 | 93.6 |
| Non-factor Service Indices (1992 = 100) | | | | | | | |
| Exports of NFS - volume index | 88.5 | 94.1 | 100.0 | 86.9 | 99.5 | 104.1 | 117.2 |
| Exports of NFS - price index | 93.2 | 96.8 | 100.0 | 102.0 | 103.7 | 107.9 | 112.1 |
| Imports of NFS - volume index | 74.8 | 87.6 | 100.0 | 89.6 | 151.8 | 102.4 | 108.8 |
| Imports of NFS - price index | 93.2 | 96.8 | 100.0 | 102.0 | 103.7 | 107.9 | 112.1 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 8. Foreign Debt
(\$ million)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996(a) |
|--|---------|---------|---------|---------|---------|---------|---------|
| Gross Disbursements | | | | | | | |
| Public and publicly guaranteed | 3 044.9 | 1 825.7 | 1 590.4 | 1 385.4 | 958.5 | 1 133.9 | 1 068.9 |
| Official multilateral | 416.3 | 238.6 | 266.0 | 743.7 | 481.9 | 637.9 | 503.8 |
| Official bilateral | 1 333.5 | 911.7 | 745.4 | 435.3 | 321.6 | 375.7 | 378.0 |
| Private creditors (guaranteed) | 1 295.1 | 675.4 | 579.0 | 206.4 | 155.0 | 120.3 | 187.1 |
| Private creditors (non-guaranteed) | 142.0 | 90.0 | 20.0 | 20.0 | 60.0 | 0.00 | 200.0 |
| Total long-term loan disbursements | 3 186.9 | 1 915.7 | 1 610.4 | 1 405.4 | 1 018.5 | 1 133.9 | 1 268.9 |
| Total disbursements | 3 186.9 | 1 999.0 | 1 730.3 | 1 405.4 | 1 018.5 | 1 133.9 | 1 668.9 |
| Amortisation | | | | | | | |
| Public and publicly guaranteed | 1 775.0 | 1 738.5 | 1 305.4 | 1 064.5 | 758.5 | 769.4 | 1 062.5 |
| Official multilateral | 238.0 | 370.6 | 385.6 | 294.0 | 292.0 | 334.3 | 382.5 |
| Official bilateral | 692.2 | 590.4 | 257.7 | 123.0 | 95.4 | 154.2 | 348.6 |
| Private creditors (guaranteed) | 844.8 | 777.5 | 662.2 | 647.5 | 370.2 | 281.0 | 331.3 |
| Private creditors (non-guaranteed) | 192.0 | 321.0 | 270.0 | 120.0 | 185.0 | 0.0 | 0.0 |
| Total long-term loan net disbursements | 1 967.0 | 2 059.5 | 1 575.4 | 1 184.5 | 943.5 | 769.4 | 1 062.5 |
| Net credit from IMF | 30.3 | 82.8 | 79.8 | 0.0 | 0.0 | 69.3 | 46.0 |
| Total repayments | 1 997.2 | 2 142.4 | 1 655.2 | 1 184.5 | 943.5 | 838.8 | 1 108.5 |
| Net Disbursements | | | | | | | |
| Public and publicly guaranteed | 1 269.9 | 87.2 | 285.0 | 320.9 | 200.0 | 364.5 | 6.5 |
| Official multilateral | 178.3 | -132.0 | -119.6 | 449.6 | 189.0 | 303.6 | 121.3 |
| Official bilateral | 641.3 | 321.3 | 487.7 | 312.3 | 226.2 | 221.5 | 29.3 |
| Private creditors (guaranteed) | 450.3 | -102.1 | -83.2 | -441.1 | -215.2 | -160.7 | -144.2 |
| Private creditors (non-guaranteed) | -50.0 | -231.0 | -250.0 | -100.0 | -125.0 | 0.0 | 200.0 |
| Total long-term loan net disbursements | 1 219.9 | -143.8 | 35.0 | 220.9 | 75.0 | 364.5 | 206.5 |
| Total net disbursements | 1 189.7 | -143.3 | 75.1 | 220.9 | 75.0 | 295.1 | 560.4 |
| Interest and Charges | | | | | | | |
| Public and publicly guaranteed | 1 232.8 | 850.1 | 713.3 | 1 021.0 | 1 018.7 | 1 236.8 | 1 398.8 |
| Official multilateral | 190.7 | 212.9 | 189.2 | 192.0 | 214.3 | 232.6 | 258.0 |





Table 8. Foreign Debt
(\$ million)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|--|---------|---------|---------|---------|---------|---------|----------|
| Official bilateral | 781.9 | 418.4 | 363.4 | 684.6 | 696.7 | 898.4 | 1 036.7 |
| Private creditors (guaranteed) | 260.2 | 218.7 | 160.7 | 144.4 | 107.8 | 105.8 | 104.0 |
| Private creditors (non-guaranteed) | 107.4 | 123.8 | 54.9 | 41.4 | 38.5 | 17.5 | 8.5 |
| Total interest on long-term loans | 1 340.2 | 973.9 | 768.1 | 1 062.4 | 1 057.2 | 1 254.3 | 1 430.4 |
| Interest on short-term credit | 465.5 | 264.6 | 172.0 | 174.2 | 154.6 | 73.3 | 10.1 |
| Total interest | 1 805.8 | 1 238.5 | 940.1 | 1 236.6 | 1 211.8 | 1 327.7 | 1 452.1 |
| Debt & Debt Burden Indicators | | | | | | | |
| Total debt service | 3 803.0 | 3 380.9 | 2 595.3 | 2 421.1 | 2 155.3 | 2 166.5 | 2 560.6 |
| Interest | 1 805.8 | 1 238.5 | 940.1 | 1 236.6 | 1 211.8 | 1 327.7 | 1 452.1 |
| Principal | 1 997.2 | 2 142.2 | 1 655.2 | 1 184.5 | 943.5 | 838.8 | 1 108.5 |
| Debt/exports ratio (%) | 227.2 | 149.2 | 173.0 | 165.4 | 200.4 | 195.5 | 176.0 |
| Debt/GDP ratio (%) | 92.2 | 69.6 | 77.4 | 66.7 | 62.8 | 58.4 | 52.3 |
| Multilateral debt/GDP ratio (%) | 78.7 | 58.7 | 69.9 | 60.9 | 57.8 | 54.4 | 48.5 |
| Total debt service/exports ratio (%) | 25.4 | 19.6 | 13.9 | 12.7 | 13.3 | 12.0 | 12.7 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 9. Budget
(LE billion)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 (a) |
|------------------------------------|-------|-------|------|------|------|------|----------|
| Total current revenues | 17.0 | 25.6 | 37.8 | 43.5 | 49.4 | 52.9 | 57.7 |
| Direct taxes | 4.2 | 6.4 | 10.0 | 11.1 | 12.0 | 12.1 | 13.7 |
| Indirect taxes | 7.4 | 9.0 | 14.2 | 16.1 | 19.3 | 22.1 | 24.5 |
| On domestic goods and services | 4.5 | 5.8 | 9.6 | 11.1 | 13.2 | 15.1 | 16.6 |
| On international trade | 2.9 | 3.2 | 4.5 | 5.0 | 6.1 | 7.0 | 7.9 |
| Non-tax receipts | 5.3 | 10.1 | 13.5 | 16.2 | 18.0 | 18.6 | 19.4 |
| Total current expenditure | 22.4 | 29.6 | 36.1 | 40.8 | 46.0 | 47.6 | 51.9 |
| Interest on external debt | 0.6 | 2.8 | 3.1 | 3.9 | 4.6 | 3.6 | 3.7 |
| Interest on domestic debt | 2.9 | 4.1 | 6.3 | 9.2 | 11.8 | 11.1 | 12.2 |
| Transfers to private sector | 1.9 | -1.7 | -0.6 | 1.5 | 1.1 | 0.4 | -0.7 |
| Subsidies | 2.9 | 6.6 | 6.2 | 5.0 | 8.7 | 10.2 | 11.5 |
| Consumption | 11.1 | 12.7 | 14.6 | 17.7 | 19.8 | 21.9 | 24.2 |
| Wages and salaries | 6.0 | 7.1 | 8.0 | 9.7 | 11.0 | 12.5 | 14.0 |
| Budgetary savings | -5.3 | -4.0 | 1.6 | 2.6 | 3.3 | 5.2 | 5.7 |
| Capital revenues | 4.8 | 2.9 | 3.5 | 2.9 | 3.1 | 2.7 | 3.1 |
| Total capital expenditures | 13.9 | 15.8 | 11.3 | 10.9 | 10.1 | 10.6 | 11.9 |
| Overall balance | -14.5 | -16.9 | -6.1 | -5.3 | -3.6 | -2.5 | -2.9 |
| Sources of financing | | | | | | | |
| Foreign financing | 3.2 | 13.5 | 1.7 | 0.1 | 0.4 | 0.1 | -0.3 |
| Monetary system credit | 7.6 | 1.6 | -3.4 | -3.2 | -0.2 | -1.0 | 4.3 |
| Other domestic financing | 3.5 | 3.9 | 7.6 | 8.4 | 3.4 | 3.5 | 3.6 |
| Residual sources and discrepancies | 0.1 | -2.1 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 10. Selected Economic Indicators

| | 1991/92 | 1992/93 | 1993/94 | 1994/95 | 1995/96 (a) | 1996/97 (a) |
|----------------------------|---------|---------|---------|---------|-------------|-------------|
| Inflation (%) | 21.1 | 11.1 | 9.0 | 9.4 | 7.1 | 6.2 |
| Government finance | | | | | | |
| Total revenue (%) | 44.3 | 13.4 | 12.6 | 6.0 | 9.3 | 7.3 |
| Total expenditure (%) | -9.9 | 13.0 | 7.1 | 4.5 | 9.4 | 6.8 |
| Revenue (% of GDP) | 34.9 | 29.7 | 30.4 | 27.8 | 27.2 | 26.3 |
| Expenditure (% of GDP) | 39.8 | 33.2 | 32.5 | 29.1 | 28.5 | 27.4 |
| Overall deficit (% of GDP) | -5.0 | -3.5 | -2.1 | -1.3 | -1.3 | -1.1 |

(a) Estimate

Sources: Central Bank of Egypt, Central Agency for Public Mobilisation and Statistics, Economist Intelligence Unit, World Bank.

Table 11. Law 203 Privatisation by Method as of June 1997

| Method | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | Jan.-June 1997 | Total |
|-----------------------------------|------|------|------|------|------|------|----------------|-------|
| Initial public offerings | | | | | | 15 | 8 | 23 |
| Liquidations | 4 | 2 | 1 | 1 | 2 | 1 | | 11 |
| Employee shareholder associations | | | | 10 | | | | 10 |
| Anchor investors | | | | 3 | | 3 | 2 | 8 |
| Total | 4 | 2 | 1 | 14 | 2 | 19 | 10 | 52 |
| Per cent of the total | 8 | 4 | 2 | 27 | 4 | 37 | 19 | 100 |

Source: International Business & Technical Consultants, Inc.1997.

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