

# Structural Adjustment in Egypt: The Case of Agriculture

By  
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The candidate confirms that the work submitted is her own and that appropriate credit has been given where reference has been made to the work of others

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## **Abstract**

This thesis assesses the appropriateness and effectiveness of the economic reform and structural adjustment programme adopted by Egypt in 1991. It also examines the main political and economic constraints of such policies. It argues that it is unlikely to provide sustainable or equitable growth. It also argues that privatisation programmes in Egypt have a limited effect on improving levels of investment and growth. It stresses the need to encourage new investment to increase the productive capacity of the Egyptian economy in order to generate sustainable growth. The thesis examines in particular, economic reforms in the agricultural sector. It focuses on assessing price reforms so as to enquire how evenly distributed the benefits have been among farmers with different sizes of land holding. Those with big farms are likely to gain more while very small farmers and the landless are likely to lose. Within agriculture the thesis assesses the impact of structural adjustment on Egypt's agribusiness community. This sector is economically fragmented, has limited effectiveness and is politically weak regarding its participation and its influence on economic policy. The thesis argues that the success of this sector is based on the availability of a strong and effective state to provide the legal and regulatory infrastructure needed for an effective market economy, to abolish administrative obstacles and to enhance investors' credibility. In short, the thesis maintains that sustaining the economic reform is based on reviving productive investments and enhancing state capacity and democratisation.



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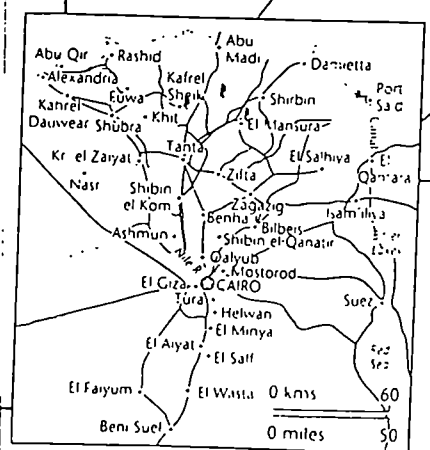
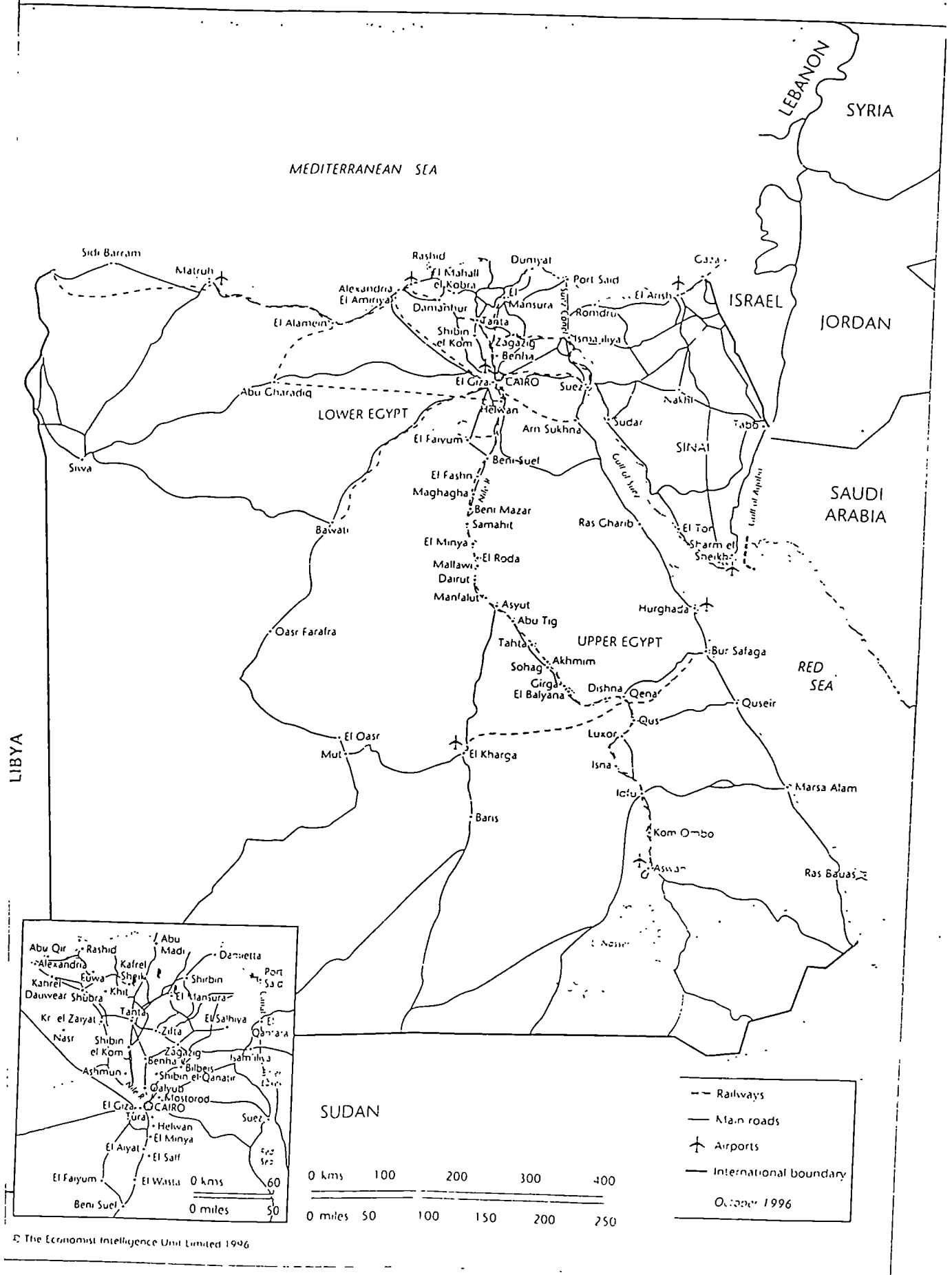
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## Abbreviations

BSE	Bovine Spongiform Encephalopathy (Popularly known as ‘Mad Cow Disease’)
CAPMAS	Central Agency for Public Mobilisation and Statistics
CCFF	Compensatory and Contingency Financing Facility
EAAPA	Egyptian Association of Agrochemical for Producers and Affiliates
ECES	Egyptian Centre for Economic Studies
ECU	European Currency
EGFLU	Egyptian General Federation of Labour Unions
EIU	The Economist Intelligence Unit
ERSAP	Economic Reform and Structural Adjustment Programme
ESA	Employees Stockholders Association
ESAF	Enhanced Structural Adjustment Facility
FEDA	Friends of Environment and Dessert Association
GOE	Government of Egypt
IDA	International Development Association
IFIs	International Financial Institutions
IMF	International Monetary Fund
INP	Institute for National Planning
LFSS	Labour-Force Sample Survey
MALR	Ministry of Agriculture and Land Reclamation
MOP	Ministry of Planning
NDP	National Democratic Party
NPUP	National Progressive Unionist Party
PBDAC	Principle Bank for Development and Agricultural Credit
PEs	Public Enterprises
RCC	Revolutionary Command Council
SAF	Structural Adjustment Facility
SAL	Structural Adjustment Loan
SAMP	Structural Adjustment Monitoring Programme
SAP	Structural Adjustment Programme
SFD	Social Fund for Development
SPR	Sector Policy Reform (Programme)
SSA	Sub-Saharan Africa
UNICEF	United Nation Children’s Fund
USAID	United States Agency for International Development
WB	The World Bank Group

# Egypt



## Chapter 1 Introduction

Structural adjustment policies were introduced to developing countries in the wake of debt crises in the early 1980s. Their main aim was to liberalise the economies, roll back the state from economic activities and encourage private initiatives. The policies also had the aim of changing the type of incentives available to economic activities from reliance upon rents to reliance on market forces. Structural adjustment was introduced with two sets of policies. They were meant to be complementary, although at times they seemed to be contradictory. The first of these were policies of economic stabilisation usually led by the International Monetary Fund (IMF) and the second was the adjustment programme sponsored by the World Bank (WB). Stabilisation programmes were aimed at restoring internal and external balances and their main instruments were interest rates, and the exchange rate. Adjustment policies dealt with supply side issues and aimed to rely on market incentives to direct resources towards better utilisation, mainly through changing relative prices. The resistance with which such policies were met in some developing countries and the complete or relative failures in some of them raised considerable debate. Other contentious issues related to the negative consequences of increasing poverty, inequality, unemployment, and declining growth rates. In recent years such drawbacks of the programme have encouraged both the IMF and the World Bank to review the content of their policies and conditionalities in developing countries. They have also produced concern about the distributional impacts of adjustment, the environment, technical assistance and governance issues. The latter includes issues which range from improving the government's administrative capacity, fighting corruption and improving the state's capacity in general to express a concern regarding initiating public participation and enhancing democratisation. Nevertheless the validity and effectiveness of their programmes remains debatable.

Egypt embarked on a structural adjustment programme in May 1991 under the name of the Economic Reform and Structural Adjustment Programme (ERSAP). It followed the conclusion of an agreement with the International Monetary Fund (IMF) followed by one with the World Bank. The signing of the agreement came after long protracted negotiations during which a previous agreement was reached in

1987 that was never fulfilled. The resistance of the government to accept the IMF recommendations or conditions for debt relief and Mubarak's later acceptance have raised a number of questions. Did the acceptance by the Government of Egypt (GOE) of the ERSAP relate to changes in Egyptian economic conditions or to changes in the content of the IMF conditionality or to both? The public's experience with a similar agreement with the IMF in 1977 led to massive increases in the prices of some of the main staple foods, and violent demonstrations across the country created an antagonistic attitude from the public towards the IMF and the WB. Furthermore the negotiations and the initiation of the programme promoted a profound debate between academics, intellectuals and political figures about the appropriateness and the effectiveness of the programme. Part of the debate was ideological as the programme entailed a shift from a state-led developmental model to a free-market model. The old model had its proponents among those who believed in the effective role of the state, the left-wing, Nasserists and the beneficiaries of such a regime -amongst others, bureaucrats and labourers, while the new World Bank model of liberalisation and rolling back the state had its proponents in investors and academia who believed in economic liberalisation and the entrepreneurial skills of businessmen. These conflicting views and interests, and the fact that the programme entailed gains and losses which were likely to be unevenly distributed along the time horizon and between different socio-economic classes, required skilful management of the reform by the government.

In this respect, the thesis is concerned with raising a number of questions and issues. In particular it is concerned with what was the response of the main political forces to the ERSAP? Was the reform a result of public discussion? Did it receive the approval of the main political parties, and political powers? Was the government able to create a wide consensus or coalition of beneficiaries to the reform? Was the government able to provide transparency and to create credibility in its willingness and its ability to carry out the reform programme?

This study emphasises the notion that even an economically well-designed programme is insufficient for success. Political factors are also crucial for a programme's success and more importantly for sustainability in the long run. This study argues the importance of three main economic and political factors which are

essential for sustaining the programme. These are reviving investment; enhancing state capacity; and promoting democratisation.

Investment is crucial as experiences of developing countries have revealed that stabilisation measures have contractionary effects leading to sharp reductions in both public and private-sector investments in the short-term. In the long-term the liberalisation package does not ensure the pace during which investment can recover. The delay of investment response exacerbates negative consequences on the economy and hence increases political risk. This study gives particular emphasis to the importance of increasing the productive capacity of the economy, in order to achieve sustainable growth. High investment rates and growth rates during the 1970s proved fragile because they were biased against the commodity-producing sectors, and the productive capacity of the economy was not increased. Growth was derived from rent particularly from oil, tourism, and the Suez Canal which rendered the economy fragile to external shocks. The importance of productive investment is also clear if we consider the main challenges facing the Egyptian economy. These include: the rapid increase in population which already score low qualities of human resources; the following increase in labour-force with an already high rate of unemployment and its implications on social and political arenas; the weak productive capability as appeared from the contribution of different sectors to the GNP and from the level and composition of foreign trade; and the expected near depletion of oil resources which were expected to be consumed within fifteen years and where the last report of the World Bank (1997) about Egypt estimated the annual increase in Egypt's productive capacity to reach *zero* if we take into consideration the depletion in natural resources. All these challenges facing Egypt suggest the urgent needs for a massive increase in productive investment. Investment should be directed to increase the productive capacity to avoid external shocks and to provide the bases for sustainable development. Investment in human resources would be another way to improve the quality of life of the population and to foster growth at the same time. From this perspective, this study lays particular importance on studying the privatisation programme in Egypt.

At the same level of importance is the argument for enhancing state capacity during the path of the reform programme. The World Bank evaluating reports of adjustment experiences in developing countries placed great stress on the way



governments were managing their programme in relation to its success and found it one of the main explanatory factors for the uneven performance of adjustment programmes in developing countries. While this is true, it is also true that state capacity is important for the success of the developmental effort using any development model. At the same time that the proponents of adjustment programmes admit the weak institutional structures and performance of developing countries, they do not provide detailed or relevant views in this respect. The original neo-classical view concerning rolling back the role of the state to its minimum does not provide a suitable solution to the problem of weak state institutions and capabilities. The increasing criticism of neo-classical thought has led to greater realisation of the importance of the state capacity issue rather than its size.

The argument for democratisation is very diverse. However, in different ways it is very supportive of the positive relationship between democratisation and adjustment. Experiences of developing countries show that there is no clear relationship between a political system and the success of structural adjustment programmes. The initiation of structural adjustment programmes has been successful in countries under authoritarian regimes as well as in countries under democratic regimes. Nevertheless, Joan Nelson (1992) differentiated between the two phases of initiating the programme and that of consolidating it and found it essential to have a democratic regime in the consolidating phase of the programme. The argument in favour of democratisation is related to achieving more public conviction and support for the programme through political participation in the decision-making process. Others see it as a compensation process for the increasing austerity under stabilisation and adjustment measures. We can add that democratisation is important to the process of balancing power between different interest groups during adjustment as it can lead to a more equal distribution of gains and losses.

This thesis gives particular attention to the effect of the ERSAP on the agricultural sector where I assess the impact of the policy on farmers and agribusiness. The study is concerned with the equitable distribution of benefits and costs among farmers from different strata and about the sustainability of the achieved growth in the agricultural sector.

The agricultural sector in Egypt used to be subject to intensive state intervention, however it was a leading sector for liberalisation. Before the SAP, the agricultural sector witnessed a deteriorating performance where agricultural production was sluggish, leading to an increasing food gap, a massive deficit in the agricultural trade balance in addition to increasing poverty and unemployment in the rural areas. State intervention was blamed by IFIs of being responsible for this deteriorating performance. Liberalisation measures were initiated from the mid-1980s and included eliminating the role of the Principal Bank for Development and Agricultural Credit (PBDAC) in the input trade and distribution and confining its task to providing finance. Subsidies on agricultural inputs were curtailed and both input trade and prices were freed. The Private sector was allowed to work in the agricultural input trade and distribution. Agricultural projects and reclaimed land came under privatisation. The reform programme in the agricultural sector also entailed changes in land tenure arrangements where rents were increased and then freed and rent contracts were no longer permanent. A proposed cost recovery programme by the World Bank is still debatable. Liberalisation, it was claimed, would achieve a better use of scarce resources and to increase agricultural production and exports. This in turn was thought to increase the living standards of farmers. The study investigates whether this policy was able to achieve its targets. Have agricultural production and exports increased? Which objectives have been achieved and which not? Why? Have the gains been equally distributed?

As liberalisation policies have meant 'rolling back' the state and relying more on the private sector, it is important to assess the response of agribusiness to the reform measures. Has the reform succeeded in encouraging more private participation? What was the impact of the reforms on private business. What are the main obstacles that the reform succeeded in overcoming? What are other obstacles that still face this sector? How have changes in economic policy affected investors' credibility in the government? How has it affected their political behaviour? Has it encouraged more political participation? Have agribusiness investors formed coalitions of beneficiaries to support state policy? Were they able to influence state policy and the decision-making process?

### *Aims and Objectives of the Study*

This study has two general objectives which need to be investigated at the national, meso, and micro levels. These are: to identify political and economic constraints to the reform programme; and to assess the programme's ability to provide sustainable and equitable growth. The study sets more specific objectives at the sectoral level of agriculture and the sub-sector of agribusiness. It assesses the impact of the applied reforms on the agricultural sector with regard to its ability to achieve sustainable and equitable growth. The impact of reforms are discussed on the sectoral, household and business levels. The assessment tries to investigate whether the reforms have been relevant to the sector and farmers needs, and whether gains and losses have been distributed equally between them, if not, who gains and who loses? and why? It also assesses the state's ability to carry out the reform programme in this sector. Which reforms have been carried out successfully and which delayed? The study also assesses the agribusiness response to the reforms. While there is little data available about this sub-sector, the study provides a descriptive and analytical profile of it as a distinctive business group. The study then continues to demonstrate more empirical evidence of the impact of the reforms on these activities and the impediments to investment. It also illustrates the state-business relationship in this sector, the ability of reforms to build credibility between investors and the state, and the agribusinessmen's political participation and their ability to influence economic policy.

This study has used a multi-disciplinary approach to assess the reform programmes, investigating both the economic and political dynamics. The reform programme has been evaluated from two different angles. Its validity and appropriateness to developing countries in general and Egypt in particular were assessed against its theoretical bases. This was done in chapter two and throughout the subsequent chapters. The effectiveness of the content of the programme was investigated with reference to the Egyptian case.

The study starts by discussing the theoretical and conceptual aspects of the SAP. Arguments are carried out and concepts tested at the macro, meso and micro levels. Macro policies at national level are examined and their impacts assessed. The effect of macro policies is not limited to the national level but is extended to the sectoral and enterprise levels. however, there are always specific sectoral policies,

which affect sectoral performance. The deflationary effect and the effect on poverty was an inescapable result of the programme at national and sectoral levels. While the literature review shows that this negative effect is not limited to one country, the macro, meso, and micro investigation proves that these impacts are penetrative and can profoundly affect sectors and productive units. The depth analysis of these impacts helps to assess their severity and their needed recovery time and measures. The severity of the impact of macro-policies can also vary from one sector to another and from one socio-economic group to another. So it is important to disaggregate these impacts.

The macro, meso, micro approach is not only useful for assessing the severity of the reform impacts it is also important for the development of some conceptual issues which are debatable according to neo-classical economic thought. These issues relate to the anticipated role of the state, changes in state capacity during the reform and the balance of power between the state and different interest groups. Since one of the main sources of Egyptian state power was clear in its penetrative role in the rural areas, it is useful to assess the effect of state withdrawal from economic life in this sector. The effect on both state power and economic activity is vital, so is the effect on the balance of power between the state and different interest groups, where our study focuses on the relationship with the agribusiness community.

To assess the first two general objectives of the study, there is a need to assess economic performance under the SAP. The impact on economic performance can be assessed in comparison with the achievement of the programme targets; improvements in the situation compared with the pre-reform conditions, and with the needs of society. The first two methods provide a limited view concerning the real impact of the programme as they take the programme targets as given, the matter which might ignore the real needs of society. At the same time they ignore the other negative impacts of the programme. The programme's ability to satisfy people's needs is important for political stability and the sustainability of the programme. For that reason there is a need to discuss the political aspects of the programme. The study investigates the ability of the SAP to create a consensus about reform measures; to build a coalition of beneficiaries and to keep a strong support base. It also considers changes in state power and the ability of the state to enhance its

capacity and to maintain the balance of power between the state and the different interest groups in society. Thus the state-civil society relationship is discussed.

This study used a variety of data from different sources, secondary data, data from official sources e.g. the MOP, CAPMAS and MALR. The study also used unpublished data from the MALR and the PBDAC. Two interviews with senior official of the MALR, with Dr. Saad Nassar, and Dr. Hassan Khedr were conducted. A field work study was also conducted in Egypt concerning the agribusiness community. The study selected a sample of 36 agribusiness companies.

### *Field Work*

There was a need to survey the approximate size and characteristics of the agribusiness community in Egypt in order to select our sample. I used three different directories to do this: The Green Business Directory published by Ahram (1994); Cairo Yellow Pages (1995) and the Kampass Misr Directory (1994). The last directory was particularly useful in providing more information about the companies' activities and size. However, its classification entails its use in conjunction with other directories for easier access to companies. Although we relied on recent publications of these directories the data obtained was sometimes incorrect. During my field work one of the respondents provided me with a more recent directory prepared for the 'Shura 96' international exhibition that has been updated. However it was less comprehensive. The EAAPA record was also useful for obtaining names of companies working in the agro-chemical sector.

A random sample was selected that covered almost all the different activities of the agribusiness community involved in the production of agricultural products or products with backward links to the agricultural sector -inputs. The sample amounted to 36 cases, which represented between 12-15 percent of the size of the total community at that time. However, the companies approached were about 70 in number, so I had a very low respondent rate.

Nine governorates were represented in the sample, these included Cairo, Giza, Alexandria, Domyat, Dakhlia, Gharbia, Sharkia, Beheira, and Monofia (Sadat City). About half of the sample were located in Greater Cairo. Upper Egypt was not represented, however, due to the normal distribution of the agribusiness community in Egypt which is concentrated in the Delta. The sample contained companies from 11 major investment groups, six of them practised various activities and five were

exclusively to the agribusiness. Large companies were more responsive and cooperative and seemed more sympathetic to the objectives of the study. One investor who managed a group of companies returned four questionnaires. Only one was used, however, as his answers and views were identical. Using the four questionnaires was thought to give his answers more weight.

The study used structured questionnaires prepared for qualitative data analysis. The intention was to apply this through interview technique, however, this technique was applied to only about half of them. Others preferred to self-administer their questionnaires. Investors were approached either directly by personal visits or by telephone first. Data collection took four and a half months, from December 1995, to mid-April 1996. Companies located outside the Greater Cairo area were approached directly or by correspondence. A pilot study was conducted at the beginning of the field work.

The field work suffered from some limitations. The first was the absence of complete and accurate data about the size and activities of this sub-sector. This problem is part of the problem of data availability in Egypt in general. It is also due to the absence of a clear definition of the agribusiness. Some activities of the agribusiness were classified under different categories in different directories. This study defines the agribusiness sector to include any economic unit whose main activity provides agricultural products and/or services which are necessary for agricultural production. This includes activities with which the agricultural sector has backward linkage, i.e. activities that provide the sector with inputs; fertilisers, seeds, pesticides and agricultural machinery, equipment and tools or any other services of consultation and know-how. In this study we deal with the formal sector where these economic units are registered as companies and working either under private sector law or investment law. Thus it excludes farmers and small merchants who are not registered as private companies. The study tried to build its own frame of reference and to incorporate activity like new irrigation systems under the definition of agribusiness, as they used to be classified under plastic (Chemical) industries. Data obtained from the available directories were also incorrect concerning the address and telephone numbers which wasted the time of the researcher.

The second main limitation was the low response-rate, which might be explained by various factors. First of all it is partly a lack of credence in research institutes in Egypt and the long time taken to conduct researches. It also reflects a lack of confidence in government organisations and officials and the absence of a positive response to these researches. Few investors thought that the results would be published within ten years, others were hesitant about the response of the MALR officials and expected them to add more obstacles. They were not able to criticise them openly. Another reason was related to the crisis of political participation in Egypt in general, where investors were reluctant to express their political views in particular. The low response was also related to the ignorance of some investors about the real meaning of the reform policy and its objectives and components. It was also related to the targeted community in particular where investors found it difficult to fit in an appropriate period of time to answer the questionnaire. Another limitation to the study was related to some aspects of the Egyptian culture. Agribusinessmen were reluctant to express their unwillingness to participate openly and directly or to discuss the reasons behind this. The way they behaved to avoid taking part in the study was time-consuming and frustrating in some cases. However, some of them were very co-operative.

### ***Focusing on the Agricultural Sector***

There are four main reasons behind my choice to study the agricultural sector in Egypt. The first is the importance of the sector in the economic structure of the country, as it used to be, and still is, the main contributor to domestic production and exports, and the main absorber of the work-force. The agricultural sector also used to contribute to the public revenues through indirect taxation -or unfavourable terms of trade between the agricultural and non-agricultural sectors. Adjustment programmes push agricultural prices to their market levels and particularly deprive the public budget from a substantial source of finance. Meanwhile the public deficit is the main concern on the path to reform. Increasing revenues is one of the most debatable issues. A number of questions arise here concerning who will pay. Should the rural sector share the burden? How viable is it to shift from indirect tax to direct and how relevant are the cost recovery programmes introduced in rural areas? The second reason is that agricultural performance has deteriorated over time as can be seen from its failure to meet the increasing needs of the growing

population. Before the adjustment it was blamed by some economists (see Kheir Eddin, 1989 & Abdel Khalek, 1994) for being responsible for Egypt's main economic problems. This view was based on evidence of the responsibility for the large food gap and for the trade and public deficits and inflation. The third reason is that this sector was the leading sector for liberalisation efforts in Egypt, beginning as early as 1986. And finally, because of the challenge which faces this sector in the near future. It was estimated that the population of Egypt would reach 123 million, almost double, after 30 years if the population growth-rate continued the same. Dr. Wali himself warned that by that time Egypt would have to direct all its income to import food and few resources would remain for development projects (Wali, 1998 as quoted by Ragab in *Al-Ahram International* 4/9/98). While the challenge is high, the dividend of growth of this sector is wide in terms of its contribution to overall growth and to job opportunities. A 2 percent increase in the agricultural sector growth-rate (to 4.5 percent) would provide an estimated additional 309,123 jobs annually (combining direct and indirect effects) with about 132,662 more jobs than these needed to absorb the annual increase in the rural labour force (JMA, 1995: 5-6).

### ***Contribution and Significance of the Study***

The main contribution of this study lies in the empirical evidence concerning the practices of agribusiness sector during economic reform. While interest has recently increased in studying the business community in Egypt, there are two main drawbacks to these studies. The first is that they deal with businessmen as homogeneous groups ignoring the differences in their economic and political interests and in their political behaviour and power. The second is that these studies focus on studying the relationship between businessmen and the political decision-making centres and their influence on policy making. They do so by analysing the relationship between the state and the big Businessmen's Associations (see for Example the work of Amani Kandil, 1991, 1994; Awad, 1992; Abel Mesih, 1996). This might be acceptable in part as these studies focus mainly on the relationship between such associations and the political decision-making centres and their influence on policy-making. However, this ignores the fact that small and informal private business constitute a great part of the Egyptian economy that is not represented in the big Business Associations or even in any other kind of association.



Yet such studies even reveal the dominance of a few prominent businessmen to such associations.

This study avoids these drawbacks by limiting its analysis to one particular group: the agribusiness, realising that it represents a relatively more homogeneous group than other sectors with regard to interests and positions in economic activity, which differs from other activities. It also assesses state-business relations not only through business associations, but also the direct relationship between businessmen and the state. The scope of the study is also very rich as it discusses the economic and political impacts of the reform. Focusing on one sector of the economy has enriched the scope of the study as it has enabled me to discuss in greater depth some of the economic aspects of the reform and their effect on these activities, assessed for the first time from the view point of the investors. At the same time, this enables an indirect assessment of some of the political outcomes of the reform, concerning its credibility and political support.

### ***Organisation of the Thesis***

This thesis is divided into eight chapters. Chapter one is this introduction. Chapter two examines the theoretical and conceptual issues of structural adjustment policies in developing countries. It assesses the appropriateness and effectiveness of such policies. The chapter argues that these policies have inner contradictions and inconsistencies and limited effectiveness. Chapter three examines the recent historical foundations of Egypt's development experience. It assesses its performance from two different experiences of economic development. The first is state capitalist and the second is a partial liberalised economy. Chapter four discusses the political economy of adjustment in Egypt. It argues that the programme is not able to generate sustainable or equitable growth. It also argues that the privatisation programme has a limited effect regarding increasing the levels of investment and growth. The chapter also argues that the state was not able to enhance its capacity during the reform and that there is a need for political reform and more democratic space in order to sustain the economic reform. Chapter five focuses on the impact of the economic reform on the agricultural sector. It argues that the reform programme focused on price reforms while institutional reforms lagged behind. It also argues that the limited gains achieved are unsustainable and unevenly distributed. Big farmers are likely to win more while very small farmers

and the landless are likely to lose. Chapters six and seven draw on empirical work carried out on the agribusiness community in Egypt. Chapter six examines the possible impacts of the SAP on the agribusiness community in Egypt. Chapter seven discusses state business relationships. It argues that Egypt's agribusiness community has limited economic effectiveness and is politically weak. Chapter eight is the conclusion.

## Chapter 2      **The Political Economy of Adjustment**

### *2.1. Introduction*

During the 1980s the world economy experienced a decade of crisis and weak performance which resulted in stagnation and low growth rates. It was named the lost development decade. The debt crisis in the early years of this decade paved the way for the shift to a new policy agenda in the developing countries and for the reviving of a new orthodoxy of liberalism. International Financial Institutions (IFIs), the International Monetary Fund (IMF) in particular, revived and enhanced their previously declining role in the developing countries. The need for urgent finance and repayment arrangements was traded for a new type of conditionality. This was based mainly on the monetarist view of managing the monetary and fiscal policy in order to restore external and internal balances. It was also based on the neo-classical idea of rolling back the state from the economic arena and allowing free market forces to allocate resources. The main premise of this new orientation was that restoring macroeconomic balances will allow market forces to allocate resources efficiently by creating the needed incentives for the private sector.

The uneven nature and the limited success of these policies created a major debate about the appropriateness and the effectiveness of such policies. The neo-liberal agenda success was noted in Asia while it proved to be a failure, in particular in the countries where the crisis was severe, namely Africa in general and sub-Saharan Africa (SSA) in particular. While growth was difficult to restore and investment continues at low levels, the costs were high in the form of recession and increasing unemployment and poverty with unequal distribution of losses and limited gains. The weak performance of African countries was explained by the nature of the states and their political structures. The experience of African countries initiated the increasing interest and realisation of the importance of increasing state capacity and the need for political reform in general as an important prerequisite for successful economic reform.

The role of the state has occupied considerable space in the debate. The earlier perspective of a minimal role for the state introduced at the earlier stages of SAP proved a failure and has been gradually changed. The central role of the state

in managing and leading the process of adjustment was understood and there has been a recognition of the need for a strong state in order for markets to perform effectively. There was also a realisation by both IFIs and academics for the need of a state role, in developing countries in particular, to overcome the gap between the short-term preferences of individuals and the long-term preferences of society to achieve sustainable development. With the increasing interrelation between national and international markets the need for selective state intervention to regulate this relation continues or even increases (see Bromley, 1995)

This chapter explores the main causes of the economic crisis in the developing countries and the role of both external and internal factors in the move to the ' neo-Liberal' policy agenda of development. It also examines the validity and efficiency of this policy for the developing countries. It argues that these policies have inner contradictions and inconsistencies and are not applicable to developing countries. Emphasis will be given to examine the two main pillars of the policy which are liberalisation and privatisation. These two principles are at the core of the current debate about the role of the state in development. It also assesses the political management of the programme in the light of the changing balance of power between the state and civil society. It argues that although the state has to reduce its direct involvement in the process of economic production and diminish the size of its inflated bureaucracy, it needs to augment its capacity in the legal, regulatory and administrative areas in order to monitor markets. This in turn raises issues of how to increase state effectiveness and how is the role of civil society to be complemented by that of the state. Is there a need to increase democratisation? and why? The study further argues that it is the state's capacity to manage economic life irrespective of the type of applied developmental model which decides the outcome of any policy. However, the current changes in the international economy cannot be ignored and have had their impact on applied strategy.

This chapter is divided into nine parts. The following part reviews changes in the world economy before the introduction of structural adjustment policies. Part three examines the changing role of the IMF due to changes in the world economy and the rise of conditionality. Part four assesses the role of internal and external factors in reform programmes. Part five examines critically the components and objectives of adjustment programmes. Part six discusses SAP effectiveness and

distributional impacts. Part seven examines the role of the state in economic activities. Part eight reviews possible political management of adjustment programmes. Part nine is the conclusion.

## *2.2. Changes in the World Economy*

The last few decades have witnessed many changes in the international economy which have led in turn to parallel changes in the international institutional setting and in the role of both the International Monetary Fund (IMF) and the World Bank (WB). Industrial countries experienced high growth rates after the end of WWII with the help of the new monetary and financial arrangements of the world economy. Many Developing countries gained their political freedom in the 1950s and early 1960s and tried to find their own strategy for growth as well. The residue of antagonism towards the west, and the emerging success of the USSR influenced third world choice of their economic strategy. They tried to apply independent economic development based mainly on ISI, nationalisation and state protection and regulation in economic life. This strategy functioned well during the 1960s with a downward trend during the 1970s which deteriorated even further during the 1980s. Table 2.1 summarises the main changes in the world economy.

**Table 2. 1 World Economic Indicators, 1965-90** (*percentage change a year*)

	1965-73	1973-80	1980-90
<i>GDP Growth</i>			
Industrial countries	4.4	2.5	3.1
Developing countries	6.2	5.1	3.2
per capita	3.7	3.0	1.2
<i>Inflation</i>			
Industrial countries			
GDP deflator	5.4	9.3	4.5
Exports (US dollars)	5.6	12.0	2.6
Developing countries			
GDP deflator	9.7	24.9	61.8
Non-oil exports	4.5	12.5	0.2
<i>Terms of Trade</i>			
Industrial countries	+0.5	-1.3	+0.6
Developing countries	+0.7	+7.7	+0.2
Non-oil developing countries	+0.6	-0.7	-0.4
<i>Interest Rates</i>			
U.S. Prime (nominal)	5.3	8.1	11.9
U.S. Prime (real)	2.6	1.0	7.0

*Source:* Little et al, 1993. *Boom, Crisis, and Adjustment: The Macroeconomic Experience of Developing countries*. Washington DC: the World Bank (For GDP and Inflation); Stallings, B, 1992. *International Influence on Economic Policy: Debt, Stabilisation, and Structural Reform*. In Haggard and Kaufman, *The Politics of Economic Adjustment*. Princeton: Princeton University Press (for terms of trade and interest rates).

Economic growth rates were high during the 1960s and early 1970s in both the industrial and developing countries. From the mid-1970s a downward trend in growth-rate in both worlds started and continued during the 1980s. The growth-rate in developing countries was higher than in industrial countries however, the faster population growth in developing countries offset this difference and the growth of per capita income did not differ much between the two worlds (Mosley *et al*, 1991: 5). The high growth-rates in the first period of 1965-73 was generally matched by relative price stability. The second period witnessed a commodity price boom and a massive increase in oil prices in 1973, which was termed the first oil shock, and in 1979 the world was struck by a second oil shock. This led to high inflation rates accompanied by economic recession in industrial countries and even higher inflation rates in developing countries together, with deteriorating terms of trade for oil-importing countries.

During the 1970s the Third World suffered from deteriorating terms of trade, a decline in the demand for their raw materials, and consequently a decline in foreign exchange. They tried to compensate for this by borrowing in the financial markets. However, for the third world it was the period of cheap credit due to the availability of oil revenues in the commercial banks with low demand from industrial countries' investors due to northern recession. With this situation, banks were eager to lend to Third World countries with low interest rates and little conditionality concerning the use of the loan. Between 1973-1982, 65 percent of gross disbursement to Third World countries came from private banks; for middle-income countries this share was as high as 80 percent (Stallings, 1992: 59).

In 1980 the industrial countries suffered a serious recession and accelerated inflation due to the second oil shock in 1979. The right-wing governments which came to office in the major industrialised countries applied tight macroeconomic policies, especially for monetary policies and adopted the monetarist view of cutting back the money supply through high nominal interest rates to control inflation. This policy succeeded in reducing inflation rates and at the same time the growth of real output fell dramatically. The increase in nominal interest rates and the subsequent decrease in inflation rates had its effect on Third World countries in the form of high real interest rates and an increase in the cost of borrowing. Those countries that had borrowed under variable interest rates faced a considerable increase in their debt

burdens. On the other hand, The Third World countries suffered a fall in the demand for and the prices of their exports and a deterioration in their terms of trade. When this combined with the high capital outflows for debt services the result was a huge deficit in the balance of payments of these countries (Mosley *et al*, 1991:7-8). These shifts in the financial markets were most dramatic in their effect on the Third World countries. The net receipt of average annual capital inflows of US\$ 23 billion, about 1.7 percent of GDP between 1970 and 1982 turned to outflows of the order of US\$ 21 billion per year during the rest of the decade (Stallings, 1992:58). This change had deep and profound effects on the economies of these countries as well as on their social and political life. Its impact extended to threatening the international financial system and the world economy with the emergence of a debt crisis. The rise in international interest rates during 1980-81 sharply increased the debt service of the highly indebted countries in Latin America. Meantime, their capacity to pay was declining due to the reduction in their foreign exchange earning from exports because of the global recession. In 1982, Mexico declared its failure to pay its debt which was mainly to commercial banks. Due to the huge indebtedness of Mexico, and the existence of similar problems in other Latin American countries, the crisis threatened commercial banks with bankruptcy and the collapse of the whole international financial system.

The crisis of the 1970s and 1980s had an uneven impact on Third World countries which depended to a large extent on the economic structure of the country concerned. The impact of changes in terms of trade varied according to the size of trade and its composition. The Asian economies were more able to recover from the shocks of the 1970s and early 1980s although they are more open compared with other countries because their economies were more diversified. Latin America and Africa were more affected because their economies were less diversified (Stallings, 1992:47-52). During the period 1965-1990, the share of manufactured goods, including semi-processed non-ferrous metals, increased from 26 percent of the total exports of developing countries to 53 percent. This increase was not only due to increases in the East Asian countries' manufactured exports but also as a result of increases in the manufactured exports of Latin America countries where manufactured exports have increased from 7 percent in 1965 to 32 percent in 1990. However, sub-Saharan African countries continued to export mainly primary

products, as did the major oil-exporting developing countries. On the other hand, many were significant importers of primary products, mainly petroleum and staple foods such as grains, in addition to cotton and other industrial materials. However, it must be noted that these increases in exports did not affect the total share of developing countries as it remained at the level of 27 percent of world exports between 1965-1988 (Little *et al*, 1993: 13). This means that the industrial countries were able to protect their share of trade, due to the increased protectionist policies adopted by industrial countries, beginning in the mid-1970s. The gains of some developing countries were achieved at the expense of other developing countries which means increased disparities between developing countries themselves, never mind the disparities between the losing developing countries and developed countries. The East and South East Asian countries were the best able to markedly raise their share of exports during the same period, while the share of African countries and the Western Hemisphere declined sharply. Little draws attention to the fact that 'by 1990 Korea alone was exporting more than Africa' (*ibid*). Changes in the financial markets also had a negative impact on countries with a low volume of export revenue and/or low domestic savings rates (Stallings 1992: 47-52).

### ***2.3. The Changing Role of the IMF and the World Bank and the Rise of Conditionality***

The changes in the world economy had a profound impact on the role of both the IMF and the World Bank. The role of the Fund was to some extent marginalised from the early 1970s due to several factors. The first of these was the collapse of the fixed exchange rate in 1973. The failure to sustain the convertibility of US dollars into gold, currency speculation, the accumulation of dollar foreign exchange reserves abroad led some countries, starting with Canada in 1970, followed by the United Kingdom in 1972, to float their currencies so as to insulate domestic monetary conditions from external influences. In March 1973 floating exchange rates among major currencies became general (Little *et al*, 1993:10-11, 16-17). The shift to a generalised flexible exchange rate was followed by the privatisation of the financial system during the 1970s after the first oil shock. The Fund responded to the rise in the price of oil by introducing the oil facility and by expanding the Compensatory Financing Facility in the mid-1970s. However, the Fund's credit was limited to the



poorest countries which could not afford borrowing from commercial banks (Bird, 1995: 3-5). Table 2.2 shows the changes in the private banks' credits to developing countries which it increased during the 1970s to reach its highest point in 1980 to cover about half the net flows to the developing countries. The Fund's role as a source for reserve creation was marginalised during the 1970s as well. Although the Special Drawing Rights were introduced at the beginning of the decade the switch to the flexible exchange rate and the private financing of payment deficits rendered the amount of official reserves unimportant. The final factor that helped to marginalise the role of the Fund was the increase in regional arrangements which was strongly illustrated by the establishment of the European monetary system in 1979 (*ibid.*:4-5).

**Table 2. 2 Net Flows of Foreign Capital to Third World Countries, 1961-1989**

Year	Bilateral	Multilateral	Banks	DFI
1961	31.0%	12.2%	14.2%	42.6%
1965	35.3	11.3	11.2	42.2
1970	30.4	9.0	21.8	38.8
1975	24.1	10.6	35.6	29.7
1980	20.0	12.7	50.8	16.5
1985	15.8	30.4	37.6	16.1
1989	18.7	36.4	8.0	36.8

Source: Stallings, B. 1992. "International Influence on Economic Policy: Debt, Stabilisation, and Structural Reform". In Haggard, S. & Kaufman, R. *The Politics of Economic Adjustment*. New Jersey: Princeton University Press.

The IMF's original responsibility was to monitor currency stability, finance balance of payment deficits and create international reserves. However, other events have helped to revive its role. The emergence of the debt crisis in the early 1980s led to profound changes in the financial markets, in the relationship of the developing countries with lending institutions and governments, and in the IMF and World Bank's role and policies. The Mexican government's failure to pay back its debt pushed the commercial banks to declare a general cessation of 'voluntary' lending which extended the crisis to other nations that relied on new borrowing to meet the increased debt services. The IMF, whose resources could not respond to the huge financial needs of the indebted countries, played a central role, with the US government, in preparing Rescue Packages. The Fund urged the commercial banks to participate in these Rescue Packages by introducing what became known as Involuntary Lending. In addition to the new money from the private banks, the measures included rescheduling of payments, and additional finance from the international institutions. In return, the government of Mexico, and other debtor

countries with problems in servicing, were committed to a reform programme to cut the budget deficit and produce trade surpluses in a Stand by Arrangement (El-Naggar, 1991; Mohammed, 1987: 79 & Stallings, 1992: 59-60).

Policy changes imposed on Mexico and other debtor countries after 1982 were not new. The use of the Fund's resources was explicitly associated with pursuing policy changes from its early stages onwards, as the US insisted. In the 1980s the notion of conditionality was formally incorporated into the amendments of the Articles of agreement of the Fund (Kahler, 1992:89-90). This is consistent with the IMF's main role, which is to manage the international monetary system so as to achieve international stability. It provides consultation and collaboration on monetary problems to help maintain exchange stability and balance of payment equilibrium through policy advice and short-term credit. This was thought to benefit the expansion of international trade and then help to raise the levels of employment and growth (Bird, 1995:1-2). However, the amendments of the Articles of Agreement gives the Fund more flexibility to develop its conditionality and to increase its leverage<sup>1</sup>. The subsequent international economic developments and the increased critique of the Fund programmes to debtor countries concerning their appropriateness and effectiveness also paved the way for an extension of its conditionality to different areas and in different ways. Killick (1995:20) recognised four areas where the fund developed its conditionality in one way or another: type of provided facilities; objectives of the programmes; content of the programmes (changing emphasis & new conditionality); and flexibility in conditionality (negotiation of conditionality & implementation). In the next section I shall try to assess if these changes tightened the conditionality or made it more concessional. And what was the impact on its appropriateness to Third-World conditions and hence on its effectiveness?

As the early experience of the Fund rendered costly and reflected recessionary impacts with low growth rates, the US Secretary of Treasury James Baker introduced what was then known as the Baker Plan in 1985. The plan stressed the need for growth as well as stabilisation, hence, initiated the first shift in conditionality as it directed the attention to two changes in conditionality. These

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<sup>1</sup> However, the Fund's Articles of Agreement put a limit on the Fund's conditionality concerning the political aspects, as I shall explain later.

concerned its content, to encompass new measures to deal with structural aspects, and its duration to provide medium-term finance. It also implicitly enforced the role of the World Bank by stressing the need for longer term policies and finance. In 1986 and 1987 the Fund introduced Structural Adjustment Facilities (SAF) and Enhanced Structural Adjustment Facilities (ESAF) respectively. Both facilities are in support of medium-term programmes and restricted to low-income countries. They have concessional financial terms, however, ESAF has a more 'vigorous' programme and continuing access to it is conditional on the observance of performance criteria. This is because ESAF is much larger in size than SAF. Still in value terms, SAF and ESAF credits accounted for only a third of the total credit of the Fund in 1993/94. But ESAF credit comprised a high ratio of lending to low-income countries especially for sub-Saharan Africa (Killick, 1995: 14). In addition to introducing medium-term facilities, the Fund allowed for repeated use of Fund credits. Officially the fund does not encourage more than three successive programmes, in reality, a recent study revealed that about 50 percent of a sample of 17 countries had a minimum of six programmes covering a minimum of six and a half years during the period 1979-89 (Killick 1995:18-22).

The Fund also developed its Compensatory Financing Facility for automatic non-conditional lending, dealing with external shocks to the balance of payments beyond the countries' control, to be confined to countries which already agreed on stand-by or high conditionality facility. This means that access to such a facility was tightened. However, its coverage was widened to include climate-induced shocks and difficulties in implementing the Fund's programmes due to unexpected international changes in circumstances. The facility is now called the Compensatory and Contingency Financing Facility (CCFF) (*ibid*,:16-17).

Shifting to medium-term finance entails spontaneous changes in the content of the conditionality and objectives of the programmes. The main objective of the Fund's programmes was to achieve a sustainable balance of payments to enable the country to increase growth. In the ESAF programmes growth was the main concern. The report of the Group of Twenty-Four helped to persuade the IMF and by 1990 the managing director of the Fund stressed that economic growth was a prime objective (*ibid*,:18-19). The empirical experience of the Fund that was growing in developing countries during the 1980s, led some elements within it to note the reversible nature

of the stabilisation package and the realisation that the problems may be structural in nature. This was reflected in an IMF's member comment that the deteriorating economic conditions of the developing countries in the 1980s with huge financial and external imbalances, declining production and increasing inflation were not temporary defects, but a result of deep structural problems. While the IMF as an organisation has not very readily pursued this characterisation, it has imposed a challenge to the design of conditionality, curtailing demand only to achieve the needed corrections will lead to considerable and unacceptable pressures on local demand. Thus the supply side policies which aim to enhance growth; e.g. Limiting the role of the state and opening the economy to external competition, became part of the conditionality. An emphasis was directed also to the possibility of the policies continuing for the medium-term (Schadler, 1996:14).

These changes expanded the Fund's conditionality from macroeconomic policy areas that mainly affect the demand side through the exchange rate, interest rate, money and credit control, to policies with a structural nature that affect supply side, such as initiating market incentives, changing relative prices, and the privatisation of public enterprises. The content of the Fund's programmes continued to be in line with monetarist views, with an increasing balance between traditional demand management issues and supply side measures. Trade liberalisation was given greater priority and there was also considerable concern with the detailed components of public expenditure rather than the spending ceiling, as in the previous phase. This was to be consistent with growth-oriented programmes and to avoid cuts in productive expenditure. However, recent experiences still show that due to political considerations cuts still fall hard on government capital formation. Because some structural measures included in the SAF/ESAF conditionality were those of the Bank concerned. The country seeking the loan must have a policy framework paper which claims to be the "country's own statement" but is prepared in close collaboration with the staff of the World Bank and the Fund. It outlines a three-year adjustment programme with greater precision for the first year of the programme (see Mohammed 1987:82-83; El-Naggar, 1991: 214-18 & Killick, 1995:23-4).

The critics of the UNICEF report, in 1987, related to the negative impact on the poor and the call for a more human face in the Fund programmes, drew attention to the distributional impact of the programmes. While the Fund used to think that

this was a matter for the government of the borrowing countries, it gradually responded by discussing such issues when negotiating with the government concerned. The Policy Framework Papers prepared in connection with SAF/ESAF were also required to consider the distributional impacts. More areas of concern to the Fund programme were developed including military spending<sup>2</sup>, although this could not be included in its formal conditionality. In general there was increased interest in discussing the detailed composition of government expenditures. The Fund also increased its technical assistance to improve the implementation of the programme especially in the area of fiscal policy and showed interest in environmental issues (Killick, 1995:20, 23-24).

#### ***2.4. External and Internal Factors in Reform Programmes***

As we have seen, subsequent changes in the international economic environment in the 1970s and 1980s led to the debt crisis. This forced the debtor countries to seek the help of the IMF. Thereafter both the IMF and the World Bank played a pivotal role in providing the needed finance. In return, they introduce their own conditionality within the same ideological orientation which was based on the monetarist doctrine in dealing with inflation and neo-classical views of the free market and the minimal role of state. The new ideology was completely opposed to the one prevailing in the developing countries which was based on state-led growth and allowed the state extensive intervention in economic life. This shift in development policy and the resistance and sometimes hostility which the IFIs programmes were met with raise an extensive debate about the main impetus behind these policy changes. Was it a result of a realisation among the governments of developing countries of the shortcomings and irrelevancy of the adopted ideology or was it a result of external influence and pressures to abandon the old orientation. The analyses of the causes of the debt and economic crises in general in developing countries and the investigation of the way in which, and the channels through which, the shift of policy have taken place, could help to throw light on this controversy. Both internal and external factors were recognised as being the causes of the crisis, however, a different emphasis was given to the role of each factor. The IFIs and neo-classical writers (see for instance, Roe *et al*, 1989; Corbo & Fischer, 1992; Kreuger,

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<sup>2</sup> As was negotiated in the Egyptian case.

1993; Bates & Krueger, 1993) thought it was a result of policy errors of the previous developmental model of state-led growth. They mainly blamed the extensive state intervention in economic life in the form of trade and price control, and direct involvement in production. They thought that these kinds of intervention promoted unsustainable patterns of resource-allocation which relied on subsidies to keep large part of the productive system in operation (Roe *et al*, 1989: 3-4). While they admit that changes in the international economy exacerbated the problems of developing countries, they think that the political and institutional weaknesses limited the capacity of these countries to respond to the external shocks (Corbo & Fischer, 1992:7). Those with the opposite view see the crisis as intimately linked to changes in the international economy (Ghai, 1991:1). Killick's (1995: 123) extensive assessment stresses the mutual responsibility of both exogenous shocks and domestic policy weaknesses where exogenous shocks uncovered these weaknesses. Even for countries exporting primary products, who are vulnerable to changes in terms of trade, the mismanagement of the benefits of the boom years failed to elevate the effects of the adverse trends. Killick also highlighted the effect of natural disasters which was generally undermined (*ibid*).

Stallings stressed the role of international factors and the asymmetries of power between donors and recipients. These international factors are not limited to what was mentioned earlier about changes in the international markets of goods and capital. Donor countries and institutions can influence developing countries through linkages. They build a network of interest and cultural ties between some third world groups and counterpart groups in industrial countries. These ties are built through business, academic, educational, training and travel relations. Thus the international actors can build coalition groups inside third world countries. These coalition groups could include businessmen, technocrats, military and middle class who share the same interests, ideological orientations and cultural habits (Stallings, 1992:52). The final channel through which international actors influence developing countries is leverage which is not limited to the IFIs' conditionality. It could be exerted through bilateral Aid and Multinational Corporations practices, thus it is not limited to the economic arena. It could be political as well. Leverage is directly linked to the policy of reward and punishment (Stallings, 1992:55-56). However, Stallings recognised the role of domestic policy which could have reduced the

vulnerability to external shocks. Stallings criticised spending priorities in developing countries where investment booms contributed to the accumulation of debt, and overvalued exchange rates suppressed exports and encouraged financial expectations and capital flight (Haggard and Kaufman, 1992:15).

Haggard and Kaufman (1992:15-16) found in the cross-country variation of the speed through with which they adopted the neo-liberal agenda and in the content of the applied policies, a case for highlighting the role of domestic economic and political structures. They gave example for this: “Hard-hit countries such as Korea, Chile, Costa Rica and Ghana responded relatively early in the decade with comprehensive programmes of stabilisation and structural adjustment; while others, such as Argentina, Peru, and Zambia either experimented with heterodoxy or were unable to sustain adjustment policies of any sort.” In contrast to Haggard and Kaufman’s conclusions from these variations, I find it an argument supporting the dominant role of external factors in selecting policy choice, where ‘hard-hit’ countries were more in need of financial support and more vulnerable to the external pressures of the International Financial Institutions to shift their policies. Literature about the determinants of the tightness of the conditionality proves that the recipient country is forced to accept tighter conditionality when it suffers severe economic problems with serious debt and with its foreign exchange position; the amount of help needed is large; and when the recipient country has a history of slippage over credit. All this weakens the position of the recipient in negotiating the facility in return for conditionality and gives the donor reasons to tighten the conditionality. However, the political weight of the country can secure it favourable treatment in concluding the agreement (Mosley, 1991: 74-75 & Kahler, 1992).

Mosely (1991), Kahler(1992) and Killick (1995) used the high slippage rate of the IMF and World Bank programmes to argue that the coercive nature in introducing such programme is overrated. Mosely *et al* found that only two countries: Turkey and Thailand met only two thirds of the conditions attached to their SAL and SCAL. Malawi, Ghana, the Philippines, and Jamaica implemented between 55 and 63 percent of the conditions, and Kenya, Guyana, and Ecuador had implemented less than 38 percent (as cited in Haggard & Kaufman, 1992:16). Mosely believed that the World Bank allows such slippage because it has to fulfil its

disbursement target and because of the unclear evaluation criteria in the early stages of introducing programme loans:

While the weak performance and institutions in the third world cannot be ignored, nor the role of external shocks, it is quite a different matter to challenge the whole ideology upon which these policies are based, as the IFIs did. Is the state irrelevant in undertaking the developmental role or is it incapable or both? It seems that neo-classical orthodoxy believes in both, which entails the need for a completely different ideological base. (See my analysis below for the role of the state). It is a completely different argument if the belief only encompasses inability which entails the possibility of improving and enhancing its capabilities, which could be through the support of private efforts. We need to explain why the shift was towards liberalisation policies. Did the state admit its failure and relate it to the irrelevant role it undertook in the past, or did it discover its inherent limited capacity and decided to role back? Was it the political will of interior political forces to shift to a new ideology in order to achieve certain gains? Or was it the result of the leverage of the international financial institutions in the wake of the debt crisis? While it cannot be that the state chooses voluntarily to give up its power and control over economic life, it was agreed among many researcher 'that changes in the external economic environment have narrowed the range of policy choice' for developing countries (see Haggard & Kaufman, 1992:9). It is important for the success of any new policy to be initiated domestically in order to gain the political support needed for its sustainability. When political powers or the public perceive it as the practice of the power of external forces for their own interests, they are more likely to resist it.

The influence of international financial institutions on the shift toward the neo-liberal agenda finds its outlet in the debt crisis where the problem countries have to commit themselves to reform programmes. The poor effectiveness of such programmes ensured a continuing need among most of these countries for more finance. In the meantime, international creditors were able to collude and arrange among themselves a consistent lending policy through which they were able to exert their leverage. On the other hand, the debtors have failed up till now to organise themselves into a similar cartel. Stallings (1992:60-1) stated that between 1982-1985 thirty four countries in Africa, Asia, Latin America, and Eastern Europe needed



to reschedule their debt with commercial banks, a stand-by arrangement with the IMF was required first. The creditor countries who organised themselves into the Paris Club also asked for IMF agreement first.

### *Conditionality as a Bargaining Process*

As we have seen, conditionality is not new, it was always a dimension of IMF and World Bank lending, however there have been changes in its scope, objectives, content and tightness. Some writers consider conditionality as a coercive action (see Springborg, Hayter, 1971) in the sense that it is always implemented and always damaging to the recipient. The other contrasting view sees conditionality as in the mutual interests of the donors and the recipients. Mosley challenged both views on the basis of his empirical study, which revealed that around half the Bank's conditions have not been complied with; and it is not of mutual interest as long as the recipient countries do not apply it spontaneously. In his view it is a game or in other words a bargaining process between the donor and the recipient where each side has conflicting views. The recipient tries to maximise the amount of credit and to minimise the political risk. The donor tries to induce as much policy reform as he can, however, he has an interest in spending his budget (Mosley, 1991:68-73). In fact, I see the process as being more coercive than of mutual interest. The recipients would not have embarked on such policies voluntarily. However, the mutual interest of both sides is in negotiating, in the hope of meeting half way, whereby each side achieves part of his interest but usually the losses lie with the recipient. So it is a coercive game which the recipient is forced to play in order to obtain the loan while he is trying to minimise other losses.

The influence of both the World Bank and IMF on structural adjustment programmes is admitted even by those who do not believe in the coercive nature of imposing the programmes. Frischtak (1996), a World Bank collaborator, when describing the situation in developing countries after the debt crisis wrote that "Policy makers were thus faced with an agenda of policy changes that was largely defined abroad and lacked significant constituencies at home" (P2). Killick (1995) wrote that "The macroeconomic policies of developing countries are strongly influenced, not to say dominated, by the terms of the (IMF) programme" (p36). He also refers to the fact that signing an agreement with the Fund is usually a prerequisite to debt rescheduling. However, he describes the Fund's conditionality

as a “toothless tiger”, where conditionality does not seem to be an effective modality in achieving policy changes. Killick also refers to the extensive slippage in programme execution and the vitality to increase government conviction and responsibility for the macroeconomic policies (*ibid*,:120-21).

### ***2.5. Adjustment Policies: Objectives, Components, and Rationale***

Adjustment programmes usually combine two sets of policies and are intended to be complementary. Although to some extent they are, they also contain some internal contradiction, as will be discussed later in the critiques. The first is stabilisation which is a short-term policy, while the second is structural adjustment which is a long-term policy. Stabilisation is a programme of demand management supported by IMF Stand-by Arrangements, aiming at reducing external and internal imbalances and controlling inflation rates. Due to the reversible nature of the programme results, the IMF -under its extended fund facilities- may ask for the structural reforms needed to sustain stabilisation (see Silva Lopes, 1989:22, Corbo & Fischer, 1992:7). Structural adjustment is usually supported by the World Bank Structural Adjustment Loans (SAL) and is aimed at improving the mobilisation and allocation of resources and the restoration of growth (Corbo & Fischer, 1989:7). From the neo-classical point of view this means mobilising and allocating resources towards tradable goods and improving the conditions of supply by creating appropriate incentives, by correcting distortions in economic policy i.e. deregulating the domestic goods markets, liberalising the trade regime and reforming the public sector. Later on they call for complete privatisation, and the removing of obstacles to investment. It also implies some institutional changes (*ibid*).

Stabilisation is designed to restore the balance between the level of demand and its composition, and the level of output and the available external financing, by using expenditure-reducing policies to cut domestic demand and expenditure-switching policies to shift domestic demand from tradable to non-tradable goods. The programme relied on limited sets of policy instruments: currency devaluation, interest rate increases, credit ceilings, and sometimes wage control and adjustment of some key prices (Silva Lopes, 1989:22).

To achieve fast and easy cuts in expenditure in the short-term, it is easier to cut public expenditure rather than private. Increasing taxes and administered prices

are usually politically and socially costly. That is why in the first stages of achieving fast stabilisation governments usually tend to cut public investment; while in the medium-term there is more chance of introducing other measures that affect consumption rather than investment. For demand-switching, the main instrument is currency devaluation, however its effectiveness is usually questionable in the developing countries.

### *Privatisation*

The two corner stones of the structural adjustment programme are privatisation and trade liberalisation. High Inflation is viewed by neo-classical writers as the most important difficulty in the economies of developing countries which leads to the perceived need for reform (Bates & Krueger, 1993:7, Krueger, 1993). They also think that high and prolonged inflation usually results in the failure of stabilisation programmes (Corbo & Fischer 1992). From their point of view, the main reason for high inflation rates in developing countries is a fiscal deficit where public enterprises are the main contributor to that deficit. High rates of inflation result in highly overvalued exchange rates and an excessive demand on foreign exchange. The overvalued exchange rate and the excessive demand increase imports and lead to trade deficit. Thus public enterprise deficits are responsible for macroeconomic imbalances ( budget deficit, balance of payment deficit and inflation).

In their views they also have repressive impacts on private investments. Massive public borrowing also promotes high interest rates. Moreover, credit bias towards public enterprises crowds out private investment, which they consider more efficient. In addition, the resulting inflation creates uncertainty about the economic benefits of investment. It encourages a shift towards short-term, fast-return activities and away from longer-term productive ones. They also increase the probability for political change, due to the discontent resulting from high costs for both consumers and producers. The measures needed to control inflation by increasing taxes and reducing public expenditure to curtail budget deficit are also politically difficult to sustain well (see Bates & Krueger, 1993:6, Krueger 1993:5).

Public enterprise reform and restructuring were vital in the structural adjustment programme when it was first introduced (see World Bank, 1987; Roe *et al*, 1989; and Corbo & Fischer, 1992). Later the World Bank called for the complete privatisation of public enterprises, asking governments to withdraw from productive

activities. The increasing emphasis on complete privatisation was also supported from outside the two main sponsors of the reform programme -the IMF & WB. Thus one of the main objectives of US development assistance during the 1980s was directed towards private-sector development with strong emphasis on privatisation. Furthermore, the US government urged the WB to embrace lending to the private sector, including financial support for privatisation activities. The Bank's enthusiasm for such loans increased in the late 1980s. By 1991, the number of World Bank Loans with privatisation components had risen to 74 (Reed, 1996:12). Privatisation was accompanied by deregulation of labour markets to allow labour prices to be determined by markets rather than collective bargaining or other government influence, and the elimination of "labour market rigidities" including reducing the number of public employees and the scale and level of benefits and other measures associated with privatisation (*ibid*).

### ***Trade liberalisation***

Trade liberalisation is a key component of the adjustment policy. The World Development Report 1987, when referring to the East Asian countries, claimed that developing countries which followed policies that promoted the integration of their industrial sector into the international economy through trade, have fared better than those which insulated themselves from it. In those countries where protection has been relatively modest, the impact on exports has been offset through other incentives (WB 1987).

The arguments against distorted trade represented by some neo-classical economists, is that they generate a dislocation of resources within import-competing sectors; they tend to express exports and contribute to socially unproductive rent-seeking activities; and they tend to slow technical progress (Corbo & Fischer, 1992:10). Trade liberalisation aims at lowering import protection and turning from non-tariff barriers to only tariff, with a tendency to reduce the average level of tariff rates. The earlier view that well-designed government intervention enhanced growth in East Asian countries, which was based on the new trade theory, has been criticised by some neo-classical and World Bank members on the bases that it is invoked by the pressures of interest groups rather than for efficiency considerations. The recommended reforms were derived from the standard theory of commercial policy (Corbo & Fischer, 1992:10).

### *Structural Adjustment , Investment and Growth*

Developing countries often face the problem of low saving rates. They try to remedy this problem through foreign inflows in the form of direct foreign investment and/ or external debt. Adequate participation of both kinds of finance is crucial to avoid the risk of resource drain through transfers outside the country, either in the form of transferred profit or in the form of debt service. Debt overhang was thought to create uncertainty in the macroeconomic environment of the debtors and to crowd out private investment. It acts as an anticipated foreign tax on current and future income. The required amount of transfer itself could be uncertain due to changes in international interest rates and in the terms of trade. It could also imply the need for changes in the exchange rate of domestic currency and the demand management policy, consistent with the level of debt service. Thus investors could face the risk of large swings in relative prices, taxation and demand management (Serven & Solimano, 1992:127).

It is one of the IFIs objectives to improve the countries' ability to serve their debt through dealing with foreign imbalances and better allocation of resources. From the neo-classical point of view private investors use resources more efficiently than in the public sector. They are also in favour of foreign direct investment, according to their arguments above, rather than foreign debt. In their view the recovery of domestic investment would spur the participation of foreign direct capital (Chhibber, Dailami & Shafik, 1992:1).

It is difficult to deny the negative impact of adjustment in the short-term, either on the analytical level or empirically. However, the response and behaviour of private investment in the medium-and long-term is the most debatable one (See Chhibber, Dailami & Shafik, 1992; Chhibber, 1992; Shafik, 1992; Serven & Solimano 1992; Solimano, 1992; Jayarajah, Branson & Sen, 1994). Based on empirical evidence, one study has identified three phases in the response of private investment to the adjustment programme: initial contraction, a long pause, and sustained recovery (Solimano, 1992). The period needed to ensure a recovery and the conditions for recovery are still questionable.

In the short-term, during stabilisation, cuts in public investment are the easiest and fastest way to reduce demand. A devaluation of the currency exchange rate often increases the cost of production, due to the increase in the price of

imported capital and intermediary goods. Hence, it has adverse effects on investment. Increases in interest rates raise the cost of capital and reduce investment as well. Empirical evidence confirms this analysis in different countries.

Medium-and long-term investments need of time to revive. Neo-classical analysis assumes that the profitability of export-oriented industries increases and so does the demand which encourages more investment in tradable goods (see Chhibber, Dailami & Shafik, 1992:6). Although cuts in the fiscal deficit are important to reduce inflation and, hence uncertainty about future profits, direct cuts in public investment can adversely affect private activity if these cuts are directed to activities complementary to private investment. But if curtailment took place in the activities that compete with private investment, private investment may receive a net stimulus (Shafik, 1992; Shalaan, 1990:27).

There are a number of other questions that are important to raise: how long does it take for private investment to revive? And what are the conditions for it? Two important factors relate to uncertainty and credibility. Credibility can be created by avoiding unpredictable and inconsistent changes in economic policies. Credibility reduces uncertainty about the economic environment. Certainty and policy predictability are also important for investment decisions due to their irreversible nature. Once capital is installed it is difficult to put it to other use without considerable cost (Shalaan, 1990:31). In an uncertain environment investors often wait for new and better information, the 'wait and see approach' which affects the desirability and the timing of investment (Solimano, 1992:13). There are different forms of uncertainty: uncertain demand; uncertain future real interest rates or exchange rates which may cause investors to refrain from investment even if current conditions have proved to be profitable (Shalaan, 1990:31). Even with the adjustment programme, uncertainty may lead investors to postpone investment decisions until stability is affirmed. The imperfect credibility in the programme could be the main source of uncertainty.

Non-conventional variables that can explain the behaviour of private investment include important political factors as well. Political and social instability is another important factor that affects investment decisions. Many empirical studies about the relationship between social and political stability- in the form of political violence, social unrest, and/or propensity of government to collapse and investment

or growth show the adverse relationship between them (Alesina *et al*, 1992; Alesina and Perottii, 1993). Other factors can be added like war and peace (see El Naggar and El Erian, 1993). Bureaucratic red tape and administrative corruption could be one more important factor in depressing the level of productive investment.

It is not only the size of private-sector participation in economic activity which matters but also its type and distribution between different economic activities. It is important to emphasise here that unregulated liberalisation, or the absence of a legal and regulatory frame work, can crowd out high-quality productive investment through the increase in commercial cheating and dumping on the market of low-quality low-price merchandise. This could happen not necessarily from foreign competitive producers, but rather from domestic ones. The absence of administrative reform to cut out routine and red tape can promote corruption on a large scale and favour fast profit and activities of a rent-seeking nature. Even with a good legal and regulatory environment, market forces will encourage high-profit activities which do not add to the productive capacity of the economy, e.g. investment in the estate and luxury housing sector, which does not lead to sustainable growth. In this case government redistribution of incentives between different activities is advisable.

### *Critiques of the SAP*

The neo-classical analysis of the justification for the adjustment programme and its mechanism can be criticised on the following grounds:

- a- It uses short-term solutions to face chronic disequilibrium resulting from structural problems (stabilisation is reversible), and ignores the structural rigidities of the developing countries' economies.
- b- It contains inner contradictions between the different components of the programme and its objectives.
- c- trade liberalisation and export-led growth do not work for several reasons.
- d- the programme is not conducive to sustainable growth, never mentioning equitable growth.
- e- Market imperfections.

While one of the main objectives of the stabilisation programme is to control inflation, some of the adopted measures work in the opposite direction and can increase inflation. This refers to cuts in subsidies and changes of price for some

food items in addition to input and energy, which increase the cost of production and the cost of living. Increasing the cost of production offsets the positive impact of currency devaluation on export industries.

Stabilisation measures are meant to restore macroeconomic balances, with the aim of gaining credibility with investors and reducing uncertainty. Meanwhile the recessionary impact of the programme due to reductions in demand and credit ceiling policy, crowds out investments and creates a state of “wait and see” between investors waiting for improvements in the demand which in turn needs a public investment injection to stimulate the demand and encourage private investments.

Trade liberalisation can also be criticised on the grounds that, if all developing countries followed the same strategy of export-oriented production, competition in the market would increase and not all countries can benefit in the international market. The effect of currency devaluation on the prices of exports is usually offset by the increase in the cost of production, due to cuts in subsidies and increases in the prices of imported inputs, as the industries of most developing countries characterised by high components of imported intermediaries. It also ignores the rigidities of the production sector as prices are not the only barrier to the international markets, there is the capacity of the production sector itself, quality issues in addition to administrative barriers. Furthermore, the international market is not a competitive market, rather it is monopolised by a few transnational companies. Historical experience tells us that most developed countries build their industries under a protectionist trade policy. Introducing trade liberalisation in the early stages of adjustment, before enabling the local environment to build a strong industrial base increases the risk of exposing them to the full force of international competition (Roe *et al*, 1989:4-5). Finally, the increase in the degree of openness of the developing countries to the international economy make their economies more vulnerable to external shocks.

The argument suggests that market failure and market imperfection in developing countries is very strong here. Market imperfections appear especially in the barriers to entry and competition, such as red tape, cronyism, corruption and risk aversion. These are thought to be reinforced under structural adjustment since governance reform usually lags behind (Fergany, 1997: 2).



## ***2.6. SAP Effectiveness and Distributional Impacts***

In this section I assess programme appropriateness and effectiveness, relying on the empirical data of previous studies. The main criteria for effectiveness is the ability of a programme to achieve its goals. Goals can be unrealistic, or be exacerbated by IMF staff so as to force governments to work hard. I consider the general goal is to improve the previous situation (i.e. to reduce macroeconomic imbalances). I also examine the efficiency of achieving these goals. By efficiency I mean that the benefits outweigh the costs. However, it is difficult to quantify both cost and benefits using the same measure. Therefore I study the distributional impacts of the programme with particular emphasis on the effect on poverty and unemployment as the main reason for political unrest. The programme's ability to increase investment and growth is a good indication that it is sustainable and can remedy the cost in the near future. The failure to complete the programme has two implications, it means that either the programme is not appropriate for the country or that its cost is so high that it outweighs the benefits.

The recent IMF review of experience under SAF/ESAF-supported programmes in 36 countries during 1986-95 (1997) is the most recent available review which assesses the experience in the 1990s from the perspective of IFIs. It is useful to assess the impact of developments in programme objectives, duration, and conditionality on the outcome of the programme. Has performance during the 1990s been improved due to these developments? What is the implication of the assessment on the IMF adopted strategy and the design and content of its programmes? The report revealed two main points in this respect. First, it reflected a conviction of the Fund's staff that the basic strategy underlying the ESAF is the right one and is not subject to any reconsideration and that any drawbacks are due to defects in the design and execution of the programme. However, they did not deny that the basic strategy might need to be refined and improved (IMF, 1997:2-3). Second, the report emphasised an earlier realisation of the structural nature of the problems of most countries under ESAF, as appeared in the 'persistently weak growth, the chronically high inflation and fragile external position' (*ibid*:4). They are willing to improve the design, provide technical assistance to improve execution, but not to contradict the basic strategy of their reform programmes.

SAF and ESAF facilities are medium-term concessional financial facilities which were introduced in 1986 and 1987 to help low-income countries to carry out strong macroeconomic policies as well as structural and institutional reforms through a vigorous adjustment programme with the objective of promoting higher economic growth and external viability (IMF, 1997b:vii,1). The IMF introduced two review reports for this experience, the first in 1993 and the following one in 1997. As these facilities were directed to low-income countries most of the countries were African. African countries, as we saw earlier, were the countries most affected during the crisis in the 1970s and 1980s and they performed badly under adjustment programmes. It was important to assess their response to more concessional and less short-term facilities to help them deal with their structural and chronic problems. The first report examined the experience of 19 countries till mid-1992, all of them except four were African. The second examined the experience of 36 countries between 1986-1995 from which 22 were African.

The conclusions of the two reports were generally positive. SAF/ESAF programmes strengthened macroeconomic policies and helped structural reforms. The result was an improvement in the indicators of economic performance. The first report referred to growth in output and export volumes in particular (as quoted in the IMF 1997 report p1). Killick, however, draws attention to the fact that the growth rate rose from 2.1 percent prior to SAF/ESAF periods, to 4.0 percent during SAF arrangements and scored 2.8 percent during ESAF. Growth may not be as significant as the report indicated and the report does not provide sufficient data to test this (Killick, 1995:78). The greatest achievement was in export volumes, although the current account deficit actually rose from an average of 12.3 percent of GDP in the pre-programme period to 16.8 percent in the most recent year (IMF, 1993 Table 9, as quoted in Killick, 1995:77). Nearly half the countries reviewed failed to achieve noticeable progress towards external viability, although almost all succeeded in halting deterioration in their debt situations (IMF, 1997:1). The programme also succeeded in controlling inflation, but was of limited fiscal impact. The first report also revealed little success in reforming banking systems and public enterprises.

A study of IMF conditionality in 36 countries revealed that most macroeconomic aspects were improved. Achievement was clear in external balance

while limited in the controlling inflation and encouraging investment and growth (Schadler, 1996:14). However, improvement in the external balance did not include countries of SSA and Central Europe. Very few countries witnessed little increase in the total investment/GDP ratio. This was justified by the low levels of savings, constrained public investment and the time lag needed for private investment to build credibility and to respond. The Fund's study confirms that the cuts in expenditure were slightly higher than the target while the increase in revenues was less than the targets and cuts in capital expenditures were higher than cuts in the current ones (*ibid*,:16). This was to reduce the political risk, yet it had a negative long-term impact on the growth rate.

Different assessments of IMF and World Bank programmes revealed the uneven nature of the performance of different countries. African countries especially those of SSA and Central Europe were the worst in most assessments (see Schedler, 1996; IMF, 1997; Killick, 1995). They received very low levels of foreign direct investment while the highest share went to East Asian countries followed by Latin America (Shan & Bergsman, 1995: 6). African countries were less responsive to the SAP measures because the crisis was more severe in nature and the imbalances were larger, which made the costs higher. This is also due to the structural characteristics and rigidities of their economies in addition to the nature of the state and political system. The less diversified economies of SSA compared with those of Asian countries was another reason for the weak responsiveness. The high cost of the reform and the distributional impact of these costs suggest less political sustainability in African countries due to the prevailing political structure (Sadoulet & Janvry, 1994:2-5).

### ***Distributional Impact of the Programme***

The following section assesses the distributional impacts of the SAP programmes in general. The main components of the programmes are more or less the same in developing countries and therefore we can reach some generalisation in our analysis.

It is usually argued that the main winners of SAP are the private economic agents who usually benefit from government withdrawal from economic activity by selling public enterprise and ending commercial monopoly of importation and input trade and price liberalisation. However, the impact of the new policy varies between different categories of the private sector. Industrial producers can suffer from

increases in costs of production in the short run due to increases in interest rates, devaluation of local currency which increases the prices of imported inputs. Trade liberalisation can have far-reaching impacts on local industries which are not ready to compete in the international markets. Private agents who work in trade are more likely to win, especially those who work in importation. However, those who used to monopolise import licenses or import for the government are likely to lose due to opening the market to more traders. Exporters, although currency devaluation makes their goods cheaper in the international market, other components of the package increase their costs (see my analysis above about the contradictions inherited in the components of the package). Their ability to increase exports is also a function of other things rather than the price, administrative facilities, elasticity of demand for their goods, competition from other developing countries pursuing the same measures.

As for the impact on government bureaucrats and employees in public enterprises, the traditional recipe of the SAP is to cut size and salary, or at least control the growth of this category. On the other hand, the cost of living increased due to direct cuts in subsidies, and in spending on public services. Governments used to be the main employer in most countries who pursued a development ideology based on the command economy. These measures are supposed to affect a wide range of people. And this is the main threat to the government through labour riots of people in fear of losing their jobs.

The impact on farmers in rural areas varied according to the size of holdings. Whether waged labour or landless, their living standards are more likely to deteriorate drastically due to many factors. Employment opportunities decline because of the increase in input costs which push small farmers to increase their family labour and reduce waged labour in order to compensate for the increase in other input costs. When economic measures are accompanied by land reform, which frees the market of the land and increases the rent level, small holders are likely to lose their holdings and turn to waged labour which increases the labour-force supply. There would be an increasing tendency towards big farms which in turn need less labour either as a result of an increase in use of mechanisation or to a shift in cropping patterns towards horticulture and plants with less labour requirements. In

addition to a decline in work opportunities and increased periods of unemployment, the cost of living increases because of cuts in food subsidies and public services.

Smallholders as mentioned in the analysis above, may lose their farming lands and suffer from increasing costs of production and cost of living. This might be compensated for by an increase in crop prices attendant on price liberalisation. The final effect depends on the relative change in the prices of final crops and the prices of inputs. Even if they could achieve some benefit in the short-term this could be endangered in the long run if private traders managed to control and manipulate the market.

Big landlords are more likely to benefit from liberalisation. They benefit from freeing the market of land and the increased rent. They also enjoy paying low wages for hired labour owing to the increase in labour supply. Although the cost of their input increases, they benefit from economies of scale and are able to introduce modern technology and improved inputs. They can also invest in other complementary activities such as input trading, cattle breeding and so on.

Empirical evidence from different experiences showed a general deterioration in income distributions and there is likely to be an increase in the number of poor. Benefiting and losing groups may vary from one country to another. In a country like Morocco the social cost of stabilisation during 1982-1986 was high and inequality was accentuated. The reduction in poverty and malnutrition was only noticed in Indonesia and in Malaysia where the adjustment carried out had no negative impact on poverty and did not compromise equity (Lafay & Lacaillon, 1993:100).

The urban working class and sections of the middle classes have suffered significantly, as has been proved by different studies for different countries, in Sub-Saharan Africa, Latin America and the Caribbean (see Ghai, 1991:6) in countries like Cote d'voire and Ecuador the urban population tended to be affected more through cuts in employment and lower wages (Lafay & Lacaillon, 1993:100).

Lafay and Lacaillon's study concluded that the reform measures are against the poor because they are generally the least powerful politically and can pose no threat, at least in any predictable way. These social costs can even be higher with an increase in the repressive forces of the country, as in the case of Chile where the per capita consumption was reduced by 15 percent between 1982 and 1986, with a fall in

wages of over 20 percent and an increase in unemployment of 30 percent (Lafay & Lacaillon, 1993:100).

Changes in the level of income due to reform measures resulted in corresponding changes in the balance of power between the different social groups. The power and influence of some of the established groups, such as unions and co-operatives, have declined while others have gained more power, such as business associations. Some new ones have emerged such as neighbourhood and self-help groups to assist the basic needs of provisioning marginal sections of the population. (Ghai, 1991:10). Such distributional changes are to be assessed, in the Egyptian case, in chapters four and five.

## ***2.7. The Role of the State***

Neo-classical thought is based on the assumption of rational behaviour of individuals in pursuing their interests which ensures at the same time the Pareto-optimal allocation at the equilibrium position. The neo-classical economist did not find any conflict between individual interests and those of society nor a conflict between the present individual preferences and the long term goals of maximising the growth of total production (Leys, 1996: 87) which entails a minimum role for the state. There is only a case for state intervention if the assigned number of assumptions which ensures that the equilibrium is a Pareto-optimal are not satisfied. This could be due to externalities, public goods, increasing returns to scale and any violation to perfect competition e.g. imperfect information, or oligopolistic relations, which can lead to market failure and to allocative inefficiencies and unemployment (Dutt *et al*, 1994:4).

In the neo-classical economics markets restore their equilibrium automatically in response to any changes in supply or demand thanks to the assumption of perfect competition where prices of goods, services and factors of production are determined by impersonal market conditions. Consequently the state is exogenous to the economic process and its role is limited to solving problems that arise (*ibid*). However, the new institutional economists, within the assumptions of neo-classical economics, realised that market players do not respond automatically to changes in prices, rather do they do so through more webbed transactions that have costs. Markets get more complex and impersonal with the benefit of specialisation

and economies of scale where information becomes imperfect and transactional costs increase. The need for non-market institutions -sets of rules- arises here to reduce the costs (Leys, 1996: 84-5). It is the role of the state to establish property rights, provide legal and monitoring frameworks and organisations and to allocate the costs of externalities (see, Leys, 1996; Handoussa, 1995:3). Investigating the purpose of institutions drives us away from the pure economic neo-classical base assumption of individual rationality to a realisation of the interests of society as a whole and the effect of formatting such institutions and the change in their role and nature in the long-term on polity and society. This implies that the assumptions of the rational-choice theory must be abandoned as they fail to explain the conflicting preferences between the short-term and the long-term goals of individuals or between their individual preferences and the collective preferences of society (Leys, 1996: 87).

In defining the role of the state and that of the market, political economists did not limit their analysis to the behaviour of individuals, but they analysed the behaviour of state bureaucrats and the implication of such behaviour on individuals and the economy. They applied microeconomic methods of analysing individual behaviour on the state itself. The neo-utilitarian political economists believed that the state bureaucratic apparatus was only interested in maximising its interests with realisation that its survival is tied to the survival of its supporters. The utility exchange relation between the incumbents and supporters was believed to be the essence of state action. The state transfers resources either directly, mostly in form of subsidies, jobs, and/or the provision of services, or indirectly by restricting the operation of market forces allowing favoured groups to create rents. Extracting rents is not limited to supporters. One motive for the competition of incumbents for public services was assumed to be the extracting of rents. The neo-utilitarian analysis assumes that exchange is a natural activity that requires only minimal institutional underpinnings. This suggests that the state's role should be reduced to a minimum, the same as the neo-classical, in order to free the market from rent-seeking behaviour (Evans, 1992: 143-46).

This analysis suggests that the target function is to maximise the interests of the bureaucratic apparatus. This cannot be valid for all countries. It is more valid for developing countries in varying degrees subject to some political and economic

constraints. These constraints are related to the degree of development of political and economic institutions, and the available resources. It may be more common to see the state trying to maximise the public welfare function (the target function) subject to certain political constraints. These constraints contain among other factors; that of widening and/or strengthening the support base to achieve political stability, in addition to the individual objectives of the bureaucratic apparatus of the state which seeks to strengthen its power and rents. Both objective functions lead, in varying degrees, to a lop-sided development function which favours some classes at the expense of others. However, neo-classical thought disregards this effect of inequality if the result is a Pareto-optimal allocation. In the reality of the developing countries there could be a pendulum swing between the two functions. New leadership brought about by a coup d'état to face a deteriorating economic and political situation. However, with time in office, the tendency of the ruling elite towards power and economic gains increases and the target function can shift from one objective to another. Variations of the ruling elite's objectives are constrained by the degree of development in monitoring political institutions and the space of democratisation. Leys found the solution in pursuing "social goals through the collective effort of the societies and the communities to which people belong" (*ibid*). Empirical studies find that markets should be supported with other kinds of social structures, formal or informal (see Evans, 1992: 144-46). This draws attention once again to the importance of political reform in fostering economic growth. Democratic practices and the revival of civil society, in particular, are important to achieve by rationalising the decision-making process.

The minimalist view of the state was reviewed at the end of the 1980s with an increased realisation of the pivotal role of the state in managing reform. This moves us to what Evans named the third wave of thinking -the first was the state-led growth model and the second was the neo-liberal/neo-utilitarian view of the minimal role of state (*ibid*,:140). The third wave was a result of the increasing interest in studying the success story of East Asian countries, though differently interpreted, and the outcome of the implementation of structural adjustment policies in developing countries. The early experience of adjustment revealed the vitality of the role of the state and its apparatuses in implementing and managing reform; differences in performance between different countries was attributed to the failure



of governments to implement the reform effectively. This vitality was revealed more with the implementation of the structural adjustment phase, which unlike the first phase of stabilisation, needs more collaboration and effectiveness (see Nelson, 1989). Market economy relations also unveiled the weak institutional infrastructure of the developing countries where the legal and regulatory framework proved essential to transactions. The central role of the state was recognised even in the reform era and the question raised was how the state which was described as the root of the problem, turned out to be the solution. This paradoxical situation was described by Kahler (1990) and Evans (1992). The answer was in the recognition that it is not the state's size but rather its capacity that is important (see Evans, 1992: 141; World Bank, 1997). How to improve state capacity and to enhance its effectiveness occupied a great deal of this third-wave thinking.

Such thinking gradually involved the World Bank. As with the increasing criticism of the neo-classical state-market dichotomy, the World Bank Report of 1991 took one step forward in providing some flexibility concerning the role of the state and that of the market. The report stated that it is 'not a question of intervention versus *laissez-faire*' rather it is 'the interaction between governments and markets'. The report was still biased towards markets, as it described competitive markets as 'the best way yet found for efficiently organising the production and distribution of goods and services'. The report introduced the concept of the market-friendly approach which recognised the role of the state in the legal and regulatory framework, infrastructure and essential services to the poor, and incentives for domestic and international competition. This approach did not ignore state-intervention as long as it was market-friendly, that is to intervene reluctantly, openly and to allow for checks and balances. The report used the experience of the successful East Asian economies, with particular emphasis on the Japanese experience, to prove its view.

However, the World Bank interpretation seems to have been misconceived. Economists and political scientists have different interpretations of the experiences of these countries built on strong evidence (See Singh, 1994; Evans, 1992). Singh investigated the experience of Japan to examine whether or not the Japanese state intervened 'reluctantly' and how 'transparent' was the intervention. And finally, how did the Japanese economy integrate with the world economy? Singh brings

evidence that the government of Japan did not intervene in the markets 'reluctantly' but rather 'aggressively' through adopting forceful and an aggressive industrial policy. Japan, starting from a deteriorating situation, but did not follow the pattern of light industrialisation prescribed for developing countries; neither did it follow the narrow concept of comparative advantage. It selected heavy, chemical and electronic industries which were thought to contribute to rapid growth in productivity and per capita income under the 'structural policy' aimed at adaptation and technological development. The same was the case in South Korea where its steel company became the most successful and efficient steel producer in the world, despite the fact that it was a state-owned company (Singh, 1994:41).

The World Bank report of 1997 while admitting the important role of the state in the East Asian Experience drew attention to the fact that their performance was a miracle and described them as 'miracle' economies. It also drew attention to the idea that competition in the coming years of globalisation will be fiercer. It warned that "even where governments have done a good job in the past, many worry that they will not be able to adapt to the demands of a globalising world economy" (p1). However, the report realised the importance of state effectiveness and considered it the 'determining factor' behind the contrasting developments in different parts of the world. To distinguish the new prospected role from that of command and welfare economies, the report stated clearly that "the state is central to economic and social development, not as a direct provider of growth but as partner, catalyst, and facilitator" (p1). The report stressed the complementary role of the state and the market.

So what is this new role for the government? What is meant by state capabilities and effectiveness? And how are they to be improved? State capability was defined by the report as 'the ability to undertake and promote collective actions efficiently', and effectiveness means to use these capabilities to achieve society's interests. The report implied that the role of the state was relative to its capabilities and varied according to each country's circumstances. When state capabilities are limited the report suggested focusing first on the fundamentals and trying to enhance its limited capability through partnership with the business community and civil society, then raising its capabilities by reinvigorating public institutions, that is, by providing the necessary rules, regulations and organisations; increasing performance

and efficiency for such institutions via the controlling of corruption and by improving pay and incentives; and finally to be more responsive to the needs of the people by promoting public participation and decentralisation (*ibid*,:3). The report assigned five fundamental objectives which every government should try to achieve: “Establishing a foundation of law; maintaining a non-distortionary policy environment, including macroeconomic stability; investing in basic social services and infrastructure; protecting the vulnerable; and protecting the environment (*ibid*,:4). The state while supplying these fundamental items does not have to do it alone or be the sole provider of infrastructure and services. It is also to be noted that the report stressed the need to protect vulnerable and marginalised people, not from the point of view of equality, but rather to achieve social and political stability, the importance of which was recognised “to make development stable and sustainable”.

The emphasis given to the idea of improving state capacity, which correctly dominated the third wave of thought about the state’s role, was discussed in a broader prospective in other World Bank studies. The early evaluation studies of the Bank on structural adjustment policies tried to explain the uneven nature of the programme outcomes. They tried to define the unidentified factors from a rather limited economic point of view. The report of the World Bank in 1990, for instance, referred to the role of the state in managing and implementing the programme and to the importance of building credibility and providing transparency in government policies. Gradually these issues gained more momentum in the comparative analysis of the performance of different countries. Such issues were then conceptualised as governance issues.

The World Development Report was not the first to emphasise the importance of enhancing state capabilities and governance issues, but the realisation of such issues started gradually from the bank experience in Africa and Latin America as appeared in some reports: *Sub-Saharan Africa- From Crisis to Sustainable Growth: A Long-term Perspective Study, 1989*; *Accelerated Development in Sub-Saharn Africa: an Agenda for Action, 1981*. The issue of governance was also dealt with directly as a separate issue in some World Bank reports: *Governance and Development*, and more recently in its report *Governance, Leadership, and communication: Building Constituencies for Economic Reform*,

1996. This report recognised that well-functioning markets need capable state involvement. The report emphasised the need for changes in culture, realising that enhancing state capabilities is not limited to reshuffling or restructuring government agencies or providing incentives, it should be accompanied by a change in the established beliefs, expectations, and perceptions for state agents and citizens alike (Iskander, 1996: vii). The raising of cultural issues and their impact on work habits and ethics are very relevant in the era of free markets, as negative beliefs and perceptions could be more dangerous in the market than in the controlled economy, they might accelerate corruption and create new utilitarian coalitions between bureaucrats and private business. At the same time, positive beliefs and ethics are important for economic transactions in market economies. While cultural aspects need a long time to change, the provision of a good legal and regulatory framework to provide property rights and to respect contracts, the provision of a strict system of rewards and punishment, in addition to a strict application of these laws and regulations can help to offset the impact of negative cultural aspects and help to change it faster.

The need to improve state capacity was raised following the weak performance of the programmes, whose main problem areas were seen to be the ability to increase growth, provide the relevant political and economic environment to encourage the private sector to replace the government and the lack of skilled labour and administrative capacity to build a competitive private sector. Problem areas were also seen to lie with a lack of administrative skills to improve state performance needed for both private and public sectors, the failure to address the distributional problems and to establish social safety nets for the poor. Finally the problem was perceived of failing to address the environmental impact of the reform. These main issues were then reflected in the literature discussing the role of the state. On the other hand, IFIs responded by integrating such issues in their conditionality.

In most developing countries state capacity was weak under the old development agenda and was further weakened by the crisis of the 1970s and 1980s where the state even failed to deliver public services and ultimately failed to provide sources of finance. The performance of such states under the reform agenda even for those states that were committed to adopting reform programmes in the 1990s was

uneven. Short-term successes could not continue because of long-term difficulties and political conflict about the distribution of costs and benefits (Frischtak, 1996:2). In the long-term, the political sustainability of the reform programmes started as a major theme in the late 1980s and in the early 1990s. State management of the reform programme was seen in the early stages as a form of coalition management to marginalise the opposition and mobilise the winner to build new coalitions. The failure to build wide constituencies for the reform was due to the weak outcome of the reforms which revealed the importance of an effective performance of the state in the programme and raised the question of how to improve its capacity to implement programmes and the governance issues were the main concern.

The recent report of the Fund Executive Board emphasised that good governance is closely linked to many issues of central concern to the Fund. They thought that the IMF contribution to good governance through “reducing the scope for generalised rent seeking, discretionary and ad hoc decision-making and preferential treatment on taxes and subsidies, and enhancing capacity to design and implement economic policies and improve public sector accountability... promoting transparency in financial transactions..” would help in “.. using public resources efficiently, creating environment conducive to private sector activity, and bolstering public support for economic reforms” (IMF, 1997:41). To argue for a close link between the above-mentioned issues of good governance and economic performance is valid. However, the disagreement is related to the legitimacy of the Fund to interfere in such aspects especially when the concept of good governance could encompass other aspects with a close relation to the sovereignty of the state, such as corruption, democracy and human-rights. Even among the Directors, some still think that it is difficult to differentiate between economic aspects of good governance and political aspects. They were concerned that the Fund might go beyond its mandate. The board realised that it was a sensitive issue and more clarification of the fund role and the governance issues that were within its mandate and expertise was needed and how to use it in an even-handed way among its members (IMF, 1997:41-42).

## ***2.8. Political Management of the Reform***

The political management of the reform is a continuing process which started before initiating the reform and continues during the different phases of the reform. The state may need to develop different types of techniques to cope with different phases of the reform. We can distinguish four different phases: negotiating the reform, initiating the reform, the move from stabilisation to structural change; and sustaining the reform. The state has to manage the reform at two levels one with the creditors institutions and the other internal. Both levels entail high levels of political skill and state capacity. The state has to negotiate the programme with creditors institutions to obtain the highest amount of finance with less conditionality bearing in mind the possible internal response of different pressure groups. It has to use all available technical and political resources to achieve a better bargain. (See Section 2.4. for more details about the bargaining process.) On the internal level, the early writings considered the process of political management of the reform as one of coalition management, as a result of the quick response of social discontent in the stabilisation phase and the expected change in the support base of the state. With the move from the stage of stabilisation to structural change more emphasis was directed towards the efficiency of the state to implement the programme and to smooth the change and more attention was directed to the issue of state capacity concerning timing, phasing and implementing the programme. The process of coalition management continues through the different phases of the reform, so should the process of enhancing state capacity. However, a capable state is needed more in managing structural adjustment than stabilisation measures. The later phase of sustaining the reform needs more democratic transformation, as will be clear in the following elaboration.

The process of coalition management of the reform is a process of balance of power between the state and the different socio-economic groups. Both the state and the various civil and political groups are subject to fundamental changes in their role and power during the period of adjustment. The leadership may have to shed some coalition partners during SAP. This could be risky in the long run and threaten isolation and loss of power for those who are pushed out of the coalition (Waterbury, 1989:41). The state tries not to affect major members of the coalition simultaneously, to eliminate the negative impacts on the most politically powerful

groups and to contain their response to such impacts in order to avoid political instability and to maintain a strong support base. As the SAP entails a distribution of gains and losses it entails a reformation of the support base. Developing countries are usually dominated by pro-urban coalitions which encompass the military, public sector managers, organised labour, and urban white-collar interests (*ibid.*:46). The state has to choose the right time for initiating the reform; the sooner the measures introduce to deal with the crisis the better the results. However, due to the contractionary impacts of the programme and the sequence effect on the level of living it usually provokes social discontent and sometimes unrest. The political leadership tries to postpone in order to avoid political risk, as the resistance is expected to be more severe if programme was implemented in the early years of crisis. The public and different interest groups are more likely to accept it when the crisis is severe and the situation is deteriorating massively. However, the more severe is the crisis the more severe are the taken measures and the less likely it is for the measures to succeed (Barkey, 1992:3). It seems that many countries prefer the second choice. Egypt is one of them.

Before launching the programme, the state tries to neutralise opposition and motivate the supporters through various techniques. Previous experience of similar programmes shape its methodology. It assesses public response in the light of its previous experience or other countries' experiences. In many countries the public show antagonism towards IFIs, considering them as imperialistic powers and their policies are usually associated with austerity measures and increases in prices. The public can pass these feelings to their governments and accuse them of being allied to or subject to the will of such institutions. While trying to use these pressures to achieve better conditionalities, the government seeks to convince the public about its autonomy in order to maintain its prestige and political popularity among its constituencies. It could share some of the hostile attitudes towards IFIs in official political addresses and seek to convince the public of the national ownership of the programme.

Since the early stages of negotiating and designing the programme and during its passage the state faces a difficult trade-off between different measures. For example, when the state chooses between different alternatives to restore balance to the public budget, it has to strike a balance between increasing revenues and cutting

public expenditure. Increasing revenues entails increasing taxes which in turn should not add a greater burden on the most economically suppressed groups and should, from technical economic point of view, be directed to big businesses which are politically powerful and whose support the state do not wish to lose in the early stages of reform. With many experiences there was more success in the area of curtailing public expenditure than in increasing revenues. This could be also attributed to the weak capacity of the governments. The same problem exists when choosing between the different alternatives, whether to cut capital or current expenditure. In the short-term cutting capital expenditure is less politically painful, but more economically painful. This increases the contractionary impact and political cost in the long run. In cutting current expenditure there is a similar trade-off, whether to cut subsidies on agricultural inputs, which is more likely due to the common political weakness of farmers, or on food and energy. Here the influence of IFIs could affect the choice and the government has to add another technique such as gradualism.

This means that it is better for the government to assess the impact of different measures and the responses of different groups and to use a sequencing technique. It tries not to affect major coalitions simultaneously and whenever possible, to introduce first, measures with less impact on the powerful groups. It could also use gradualism and phasing by cutting the subsidies or wage bills of different tranches. In many cases the burden of the reform falls on the most politically weak groups. The political strength of each group depends on its size, degree of organisation, the degree of influence on national production and political linkages and ties with decision-making centres. The second and the fourth factors seem to be the more influential ones. In the case of farmers, in spite of their numbers and their high share in domestic production, they lack political influence due to lack of defending organisations, in contrast to Trade Unions who are more organised. Business Associations usually have more influence because of good organisation and tight linkages with decision-making centres. However, Nelson (1989:5, 1992:113) draws attention to the fact that gradualism is easier to use in the launching of structural changes than macro-economic stabilisation programmes. The relatively short time-frame of stabilisation and the need for some measures to be effectively implemented to apply simultaneously, limit the possibilities of phasing.



At the same time, during stabilisation the costs are obvious and immediate while benefits lag behind. This would suggest that it is better for a stabilisation package to be implemented in the shortest time possible to shorten the austerity period. However, the state has to be sure that it has other things right to receive the right response to structural measures.

The state tries to neutralise, limit or control opposition and, in the meantime, to keep its coalition partners using various techniques which could start before launching the programme and continue through different phases. This could be through persuasion and the disclosure of the severity of the economic problems, emphasising the need for a rescue programme and promising that austerity will be short and followed by prosperity. The media could play a vital role in addressing the public, special groups might be addressed via direct meetings or seminars. In addition to persuasion, partial compensation, obfuscation, or social pacts, the same techniques are useful for retaining coalition partners. The donors may push to use compensatory or social safety nets to protect the poor. Nevertheless the poor are not strong political opponents. The Bolivian social fund was thought to serve both political and equity targets by offering benefits to laid-off miners in addition to social projects. Evaluation revealed that the fund benefited very few miners and many of the jobs went to others than the poorer (Nelson, 1992:113-14). In the case of Egypt's social fund political goals also affected the allocation of loans. The loans went mostly to help jobless university graduates who were not necessarily the poorest. Compensation also went to redundant labour in the public sector. Social 'pacts' can be negotiated with unions and other interest groups, who trade co-operation for partial compensation (*ibid*). Again, there is a similar case in Egypt where the government urged businessmen and leaders of Trade Unions to sign a Business-Labour Accord shortly before launching reform officially. However, the unions could not discipline the behaviour of their own members. Some specialised unions considered the accord a betrayal of their interests and some had to act individually when measures directly affected their interests. And finally the government could act to weaken opposition directly by encouraging rival groups and splits, or by using oppression.

It should be noted that all approaches to neutralise or suppressing opposition are either temporary, costly or both (*ibid*:112). It is also expensive to maintain large

coalitions with incompatible interests. The policy of using sequential rewards and punishments entails considerable discretionary control over resource allocation. This is difficult as donors usually oppose some sorts of expenditure especially those directed to rents and spoils (Waterbury, 1989: 40-41). It is better for the state to focus its effort on better design and implementation of the programme, to limit the period of austerity and encourage early recovery, this would pacify opposition and at the same time facilitate the implementation of the following phases of the package.

Consolidating the reforms is as important as initiating them or even more. As the techniques used during the early stages prove temporary and costly the actual government performance and capacity during implementation is crucial in building credibility for the reform and in activating potential winners. It assures them that benefits are real and near. The phase of structural reforms entails fundamental changes in both the role and power of the state and that of different interest groups. Although the initial change means a relative decline in state power, since a vital part of the economic decision-making has been transferred from the government to international financial institutions, initiating and pursuing the programme needs strong centralised authority (Nelson, 1992:111). The Adjustment phase entails cuts in the size and function of the state and of state bureaucrats. This directly affects its relative power unless fundamental improvements in state performance and capacity have been achieved. Unlike the stabilisation period, where measures of the kind that could be set by central economic agencies, structural adjustment measures are not under the control of these central agencies. They often require the co-operation of a number of state agencies and private groups some of whom do not understand and/or fundamentally oppose the changes. On the other hand, the power of civil and political groups is related directly to the process of distribution of economic benefits and losses of the programme and with the degree of political freedom available for them to organise and participate in the decision-making process.

The political management of the reform is not only a management of balance of power between the losers and the winners or opponents and proponents of the reform, but a change in the composition of government constituencies to achieve the balance of power between the state and the different interest groups. It is also a management for conflict and rivalry for power between government members and government bureaucrats. Governments could face self-initiated obstacles from

inside conflicts about the content of the reform or its pace, from the performance of its bureaucratic team which could impede rather than facilitate the performance. Three main conditions are needed to be created and strengthened during the reform path: desirability; capacity; and credibility. The bureaucratic elite could be the main source of resistance inside the government when there is a threat to dismantle their power. In a corrupt regime the political power of this group is usually associated with economic gains, so any curtailing of their power means the loss of these gains. Those losing most among the government bureaucrats are the public enterprises managers and those who are involved in the planning process and in the control of internal trade. These groups could be main stratum in the government support-base affecting the government's autonomy to undertake certain reforms. A World Bank report defines political desirability as the state when benefit to the leadership and its constituencies must outweigh the costs. This only happens if there is a change in the leadership and its constituencies or in case of severe economic shock or crisis (World Bank, 1995:178). If there is no change in leadership the government has to carefully change its constituency composition during reform, so as not to jeopardise the interests of the existing dominant social forces before creating the new ; a matter which relates to the sequencing of the reform.

The second condition relates to the government capacity. The government has to build its capability during the reform and to enhance it gradually. Even if government bureaucrats did not lack the will of reform they could lack the ability. Overstaffed bureaucrats are usually characterised by weak performance. The existence of routine and complicated legislation and administrative steps could be a fundamental impediment to reform and to private investment in particular. The suppressed wages during the stabilisation period and the deterioration in living standards together with these administrative impediments, could be one of the causes of corruption. While corruption was considered one of the results of excessive state intervention or the concentration of power, it could spread among the bureaucrats during the liberalisation period, just as in the state-led period especially with the absence of administrative reforms. The change in the role of the government from direct involvement in production to monitoring the markets and the lack of experience of its staff in this respect could result in private-sector corruption in the

form of monopolising the market and in commercial cheating, by using bribes and illegal ways to escape weak monitoring systems.

The third condition is credibility which is usually created in the light of government performance and commitment, and the outcome of the applied package. Credibility could change during the reform process, according to the development in the state performance and the outcome of this performance. The outcome depends on the content and effectiveness of the applied economic package and on the political management of the reform which, which we explained earlier. As the government has to change its coalition management tactics during the reform it has to change its performance and capacity to improve the outcome. On the other hand, credibility can enhance the supply side response and speed growth, providing more momentum for the reform process.

## ***2.9. Conclusions***

External factors have played a vital role in the process of change in the adopted development agenda, from one based on state-led growth to a more market-oriented one. The external changes in the international markets of goods and capital during the 1970s and 1980s were crucial for the performance of developing countries and helped to exacerbate the crisis. While internal factors cannot be ignored when discussing the causes of the crisis, the external factors were dominant in selecting the type of policy reform used. New private sources of finance in the international market could gradually reappear again to provide an outlet for developing countries to obtain unconditional finance. At present, the main challenge for developing countries in order to sustain the reforms is to restructure the state's tasks and improve its capacity, which has proved to be a difficult task. Political reform and democratisation are urgently needed.

## Chapter 3      Egypt's Development Experience before the Structural Adjustment

### *3.1. Introduction*

The 1952 revolution was a turning point in Egypt recent history. It produced among other things the country's second attempt at achieving independent development. The free officers under Nasser's presidency sought to promote a nationalist developmentalist state; shift the regime gradually to state capitalism with the state controlling the production process and running a fast-growing public sector. Import-substitution industrialisation was adopted, and comprehensive central planning was introduced for the first time. Nasser's experience achieved great success until the mid-1960s, when it started to face problems exacerbated by the 1967 defeat. The outcome of Nasser's experience continued to shape the Egyptian economy and polity into the 1990s. In the political arena Nasser replaced incomplete democracy with an autocratic regime that long continued in one form or another into the contemporary period. In the economic arena, the public sector continued to lead the economy during Sadat's *infitah*. Sadat tried to liberalise the economy and increase the role of the private sector, however public enterprises remained significant. While import substitution was not successful, neither was Sadat's export-oriented strategy.

This chapter examines the recent historical foundations of Egypt's development experience. It explores how each of the two experiences, that of Nasser and Sadat dealt with resource allocation and the process of capital accumulation. It examines the main impetus to Egypt shift in the adopted economic ideology. Particular emphasis is given to the role of external factors and how they influenced the process of resource allocation. I also examine the interaction between political and economic change and how economic policies were used to serve political goals. I examine the state structure in the different periods and the role of economic policy in achieving legitimacy. And finally this chapter investigates why the incomplete attempt to liberalise the economy and polity failed to overcome

Egypt's economic problems, and what lessons can be drawn for the contemporary liberalisation process.

### *3.2. Nasser's Experience*

When the free officers took over in 1952, they did not have a clear political and economic ideology, only their patriotic feelings. They had a deep interest in building national independence not only from foreign imperialistic powers but also from their alliances and the domestic elite who controlled the corrupt political life. In March 1955, Nasser's public address announced six main objectives: ending imperialism; eradicating feudalism; breaking the political and economic domination of capital; establishing social justice; founding a truly democratic polity; and creating a powerful army (Barnett, 1992:82). These basic six principles were restated in the 1962 Charter of National Action (Abdel-Fadil, 1980:1).

In order to achieve their broad goals the free officers sought to consolidate political power and to enhance the legitimacy of the regime. They sought to eliminate the old regime's political figures and to destroy its coalition. The old regimes coalition was narrow-based and encompassed mainly big landlords and industrial and commercial capitalists. Nasser and his colleague aimed to replace it with a wide-based cross-class coalition. A mix of political and economic steps were adopted. The first government action in September 1952 was the immediate suspension of the Constitution and all party activities (Barnett 1992:82), and the enacting of a land reform law, putting an upper limit to land ownership of 200 feddan. Big landlords were known to control political life through their stranglehold on political parties and their membership in parliament. The main purpose was to eliminate the political power of these most influential and representative groups of the old regime, and to remove a dangerous source of opposition to the new regimes (Mabro, 1976:5). Parliament was dissolved and organised groups such as the Federation of Industry, the Labour Unions, and the Professional Syndicates were denied their political arms. To fill the political vacuum a single national party "Liberation Rally" was established in 1953 and operated by Nasser -replaced in 1957 by the National Union (NU), which in turn was replaced in 1961 by the Arab Socialist Union (ASU) (Hansen, 1991:110-12). More authoritarian characteristics of the regime appeared in the state's strict control over the media and political opposition. Expropriations were used to punish political suspects. Travel abroad was

extremely restricted and communications were censored (Abdel-Rahman & Abou-Ali, 1991:152).

The regime soon characterised itself as an autocratic military regime with Nasser at the top surrounded by a narrow ruling elite comprised of the Revolutionary Command Council (RCC), joined gradually by some technocrats and bureaucrats. The new ruling elite belonged to the middle class and some of the RCC members were members of the main political organisations of that time, such as the Muslim Brotherhood, the *Misr El-Fatah*, and the left (Harb, 1991:89). Nasser himself used to be a member of all such organisations at different times of his life. This mixed experience and thought and the similar roots and national feelings of the members of the RCC shaped their later policy choices. However, Nasser's personality and charisma had prior influence on these policies. One analyst described the relationship between Nasser and the RCC members thus: "Nasser was raised above the rest of his colleagues turning them, in effect, into his 'staff.'" (Hinnebusch, 1989:189). The only rival member was Amer whose influence was limited to the army. The regime gradually increased its reliance on bureaucratic instruments of power in implementing its policies. The size and influence of the bureaucracy increased with the policy of the employment guarantee and with increased state intervention in economic life. The bureaucratic nature of the state continued and was strengthened during the following years.

Nasser's personality and charisma played a crucial role in gaining popular support. He was able to touch genuine national anti-British sentiment among the people and to build a strong sense of Arab nationalism. Nasser was considered not only as a leader for the Egyptians and the Arab World but also as a supporter of anti-colonialist revolutions in the Arab World and Africa as well. The events surrounding the financing of the High Dam, the nationalisation of the Suez Canal and the Suez War elevated Nasser to the status of a hero in the eyes of the masses. Even after the defeat of 1967, people poured into the streets refusing to accept his resignation, and asking him to resume power.

Neither Nasser's charisma nor the antagonistic attitudes of the masses toward the old ruling elite was sufficient to provide the required public support and political acquiescence to give the regime the legitimacy it sought. A distributive economic policy and direct political oppression were used to achieve political stability. The

new regime was keen to eliminate the power and privilege of the old elite and to defend the rights of the middle class and the poor. Nevertheless, because the free officers belonged to the middle class and were aware of its ability to organise and to provide active opposition, they were cautious of any independent organising initiatives of labourers or farmers which were quickly contained (Harb, 1991:91). Thus the regime was ready to defend its economic rights while denying political rights. Economic gains were traded for political acquiescence. The regime provided a wide range of distributive policies to guarantee the provision of basic needs and social welfare. These included subsidies for basic foods and services, the setting of a minimum wage, an employment guarantee in addition to direct distribution of assets, as in the case of land reform and later on in the nationalisation procedures. These distributive policies referred to an unwritten social compact between the government and the citizens where the public won economic gains and the regime achieved stability and legitimacy.

### **3.2.1. Development Strategies**

The revolutionary government sought to achieve economic diversification, with particular emphasis directed towards industrialisation. There was also a deep belief in the importance of increasing per-capita income and the standard of living. Some organisational and institutional changes were introduced to enhance development and to enable the state to achieve its targets. There was a tendency to copy the Eastern model of heavy industrialisation with an import-substitution industrialisation-oriented strategy. Industrialisation in general, was thought to solve the problem of increasing manpower and import substitution was thought to improve the balance of payments and increase state autonomy. The centrepiece of the agricultural development strategy of the new regime was the Aswan High Dam whose electrical power station was thought to contribute to industrial development. In agriculture both export promotion (cotton and rice) and import substitution (cereals and meat) were involved (Hansen, 1991:129). Free trade was also replaced by controlled protected trade by the state as the main importer through bilateral agreements and a quota system.

In the early stages of the new regime, the new leadership did not challenge the industrial capitalists, in contrast to its position with the big landlords. Both Nasser's public addresses and new legislation were used to attract private



entrepreneurs and to gain their confidence in order to encourage them to participate in the development efforts. On many occasions Nasser assured them that the revolution's government was not biased towards any single class "it is the government of the entire nation; the government of the labourers and the farmers; the government of the civil servants and the students; the government of the capitalist and businessman; the government of the poor and the rich; the government of the young beginners and the government of the very successful." There was another parallel attitude against exploitation and capital monopoly; however, the government thought that it could regulate and direct its activity, as it needed its cooperation. In another public address in 1954 to the workers of Suez and Alexandria, Nasser made it clear that "the government does not have enough capital for industrial development, therefore we have to encourage all who need to invest their money to benefit the country and the labourers in succession" (as quoted in Harb, 1991:93-4). During the 1953-1954 period, a number of laws were issued to encourage both foreign and domestic private investment. Law 26 of 1954, for example, eased regulations for the repatriation of earnings and revised a 1947 law so that foreign investors could hold up to 51 percent of a firm's shares, as opposed to the previous 49 percent. The 1953 Mining and Quarrying law revised that of 1948 and allowed foreign interests to undertake new petroleum concessions. Law 430 of 1953 and 25 of 1954 extended tax holidays for seven years to new industrial ventures and for five years for existing companies that undertook capital expansion (Waterbury 1983:63).

† The private sector response was not as it was hoped. All incentives offered by the government proved not to be sufficient to increase private capital participation. On the contrary private gross fixed investment fell from £E 87 million in 1952 to £E 72 million in 1956 (Hanson & Marsouk 1965:321 as quoted in Waterbury, 1983:165) and the private share of total gross fixed investment fell from 75.6 percent in 1952 to 59 percent in 1956. At the same time public investment increased to fulfil development objectives. While Tax rates on undistributed profits were reduced (Issawi, 1963:53 as quoted in Waterbury, 1983:63) private industrial companies paid ever larger proportions of their earnings out as dividends rather than reinvesting them. The dividends share of profits rose steadily from 59 percent in 1954 to 80 percent in 1958 (Mead, 1967:121 as quoted in Waterbury, 1983:62). In

general, the private sector investment in industry was very low compared with other fast profit activities. During 1954 and 1955 private investment in industry was only £E 17 million, while £E 83 million went into urban housing (Da'ad, 1973:69 as quoted in Waterbury, 1983:165).

Uncertainty about government policy and the distrust between the government and the private sector were the main causes of the reluctant response of the private sector. The early steps of land reform from 1952 provoked private-sector scepticism of government intentions towards private property. Before the revolution, most Egyptian capitalists had aristocratic agricultural roots, the families with big estates were the same that ran big factories and companies. This can be seen from the members who established the Bank Misr Group, as most of them were big landlords. Moreover, most of this capitalist class attempted to strengthen their economic power through political power, hence sought to increase their participation in public policy via their membership of the political parties, professional syndicates, and parliament (Said, 1987:43-44). After 1953, with the political parties officially dissolved, parliament disbanded, and the constitution was suspended (Waterbury, 1983:62) and this class's interests were severely shackled.

Moreover, private-sector scepticism was accelerated by the setting up of a national planning committee in 1955. This issue of national planning was also embodied in the 1956 Constitution and in the same year the Egyptian Sugar Company (and its subsidiary for distillation) was reorganised, with 51 percent public ownership. Other factors that could have affected investment in this period were the dwindling sterling reserves, which were released annually, after accumulating in London during the World War II (Abdel-Rahman & Abou-Ali 1989:145-146). Figures prove that gross and private investment started a downward trend in 1950. In 1950, gross fixed investment was £E 141 million compared with £E 121 million in 1956, while private investment fell from £E 122 million to £E 72 million in the same period (Hanson & Marsouk, 1965:321 as quoted in Waterbury, 1983:165).

Industrial planning was initiated in 1957 and comprehensive planning was introduced in 1960 in the form of a five-year plan for the years 1960/61-1964/65. Egyptianisation, nationalisation, sequestration and price policy were the main instruments for the government to control the economy, raise revenues and build state capitalism. State control of production was intended to enable it to produce its

own source of revenue, decrease its dependence on private actors and hence increase its autonomy. State capitalism was also considered as one of the sources of state power (Barnett, 1992:95). By the early 1960s the system was recognised as a controlled mixed economy, with a large modern public enterprise sector under an autocratic ruler, or what Ataturk called 'etatism' (Hansen 1991:110). In the political arena was a highly centralised, military-bureaucratic regime, parliament and the single party being nothing but cosmetic devices (Hansen, 1991:110).

During 1957-1960 there was a new political set-up in Egypt which changed the investment path during this period and thereafter. The main feature was the increasing state intervention in the economy. The main changes in Egypt's political economy started at the end of Suez war. The Egyptian government began its initial steps towards nationalisation by sequestering the British and French assets largely concentrated in banking and insurance. A special state organisation- in a form almost equal to a holding company was established to manage these and other assets in which the government already had a share. Other foreign banks and insurance companies, and commercial agencies which did not suffer the sequestration were required to be converted into domestically-owned joint stock companies within five years (Ikram 1980:19).

During 1960-65 more procedures leading to nationalisation were adopted. Nationalisation reached Egyptian firms, while it had been earlier limited to foreign firms. Early in 1960 the two leading banks, namely Bank Misr and the National Bank were taken into public ownership. The National Bank played the role of Central Bank while Bank Misr was the largest commercial bank and the largest holding company made up of about twenty nine companies controlling about 20 percent of Egypt's industrial output including half of all textile production (Ikram, 1980:20). The biggest wave of nationalisation occurred in 1961,

"starting with the Egyptianisation of all companies dealing with the cotton trade....then the remaining banks and insurance companies were taken over in addition to 44 companies in basic industries (such as cement, electricity, and copper); half the capital of 86 firms, mainly in commerce and light manufacturing, was expropriated; and the share holders of another 146 firms were dispossessed of a large part of their assets by a law that limited individual holdings to a market value of £E 10,000.- all shares in excess of that amount passed into public ownership. The nominal capital of the companies affected by the nationalisation laws of 1961 was put at £E 258 million, about two-thirds of the total share capital of companies then registered in Egypt."(Ikram, 1980:21).

After nationalisation the private sector was completely marginalised. The National Charter presented in May 1962 made it clear that economic development could not be left to individual efforts motivated by private profit, but must be based on socialism. According to the Charter, private sector activity was limited to internal trade and light industries (*ibid.*:22) in addition to agriculture within the ambit of a new land reform law for the year 1961.

While the revolution did not seem to have a clear economic philosophy at the beginning, it appeared that it was more formalised by the early sixties as socialist or state capitalist. In the early fifties foreign institutions and the big landlords were excluded from economic life and so were the national capitalists in the sixties. With this restriction of private-sector participation in economic activity no new capitalist class was allowed to appear, which affected economic life thereafter.

By 1968 the political economy of Egypt leaned in a new direction. The economic reform brought in on 30 March (1968) was considered by some analysts to be the jumping off point for economic liberalisation in 1973 (Cooper, 1982: 79). The state was faced with two choices either to "deepen" its experience by extracting savings from the middle classes, or turn away to seek a closer integration with the world capitalist system. The latter path ensures that the state can retain support from the middle classes. Nasser sought support from these middle classes through liberalisation measures and by a gradual relaxation of import and foreign exchange controls (Springborg, 1991:146). There were clear efforts to recoup the foreign currencies held abroad by Egyptians. Foreign currency deposits could be used to buy consumer goods domestically and to finance export transactions. This policy allowed for an increase in the consumption of the upper middle-classes in spite of the call for a doubling of the war effort.

During the period of defeat Egypt also experienced a bureaucratic transformation. Tensions emerged between the military and the technocratic elite. Technocrats saw themselves as having considerable professional skills, while criticism increased about the performance of the military-rooted elite. Nasser began to purge the cabinet of military men and insert in their places many civilians and academics who were thought to be "professionals" and able to implement Nasser's economic policies. These technocrats placed greater controls over the public sector and asserted greater market discipline over its operations (Barnett, 1992:104-105).

### 3.2.2. Resource Allocation

From a resource-allocation point of view, there were three main objectives during the Nasser years competing together namely, development, welfare, and defence. Or in other words investment, which was directed to present and future generations, consumption which was directed to present generations and defence. Nasser did not want to sacrifice one generation for the other and went along with building a developmentalist, populist state. However, the main challenge for resource allocation came from external factors which affected the available funds and the amount of those funds that could be directed to development and welfare. In the early period of the regime Nasser tried to solve the dilemma of resource allocation by encouraging domestic and foreign investors to increase their participation in economic activity. The other possible solution was to increase the tax burden, however given the meagre living standards of the masses, this solution was out of the question. With the increase in the defence budget which rose by 75 percent as a result of the border tension with Israel and the delivery of the first Soviet-made weapons, the choice was formalised from an early stage, as that of borrowing from domestic and international lending agencies (*ibid.*:88).

The general tendency towards economic planning started to be formalised in 1957 in the form of a three-year industrialisation programme. The total investment required by the programme reached £E 250 million, which meant £E 50 million per annum -compared with £E 9 million per annum during 1952-1956, 60 percent of it to be in foreign currency (Abdel-Rahman & Abou-Ali 1989:147). The key question was about the sources of finance. Starting from 1957, Egyptian investment relied more and more on foreign finance. This tendency, as will be clear later, continued until the contemporary period with changeable sources of finance according to the change in political alignment in the different periods of peace and war. After the Suez canal war in 1956, as Egypt started to have a closer relationship with the Eastern bloc countries and away from the western powers, the USSR offered a loan of 700 million roubles early in 1958, with an interest rate of 2.5 percent a year. This was followed by the Federal Republic of Germany and Japan offering facilities totalling DM 545 million and Y 1700 million respectively. The total sources available accounted for £E 125 million in foreign currencies and about 50 percent of the total required investment (Abdel-Rahman & Abou-Ali, 1989:146-147).

The first half of the sixties was characterised by the adoption of a comprehensive planning. The first five-year plan was designed before the nationalisation procedures and about 40 percent of the total required finance (total planned gross investment in the five years was £E 1.7 million) or 70 percent of all locally-financed investment was expected to be financed by the private sector (Waterbury, 1983:85). Whether or not the private sector failed to fulfil its role in the first three-year industrialisation programme its role was changed after nationalisation. The government was able to secure finance for the plan through the retrained profits of the nationalised corporations. By 1963 the state was responsible for 45 percent of domestic savings and 90 percent of gross domestic capital formation (Radwan, 1974:707 as quoted in Waterbury 1983:85). The second area of domestic finance was generated by allowing the terms of trade between agriculture and industry to deteriorate. The third source was foreign, to cover about one third of the total finance needed for the plan. It came mainly from Soviet loans for industrial projects and for the Aswan Dam; US food-for-peace grain shipments; and from a range of countries in both the socialist and capitalist world (Waterbury, 1983:85-86).

Actual investment during the five years of the plan reached about £E 1.5 million, accounting for 83 percent of planned investment at fixed prices. According to the official estimates the annual growth rate during the plan reached about 6.4 percent, while Mabro agrees with Hanson's estimate of 5.5 percent per annum. Whatever the estimate the growth rate in the period of the plan was unprecedented, compared with the growth rate of 3.3 percent per annum during 1950-60 (Ikram, 1980:31). It was also quite fair if we look at the ratio of total investment to GNP. This ratio rose from about 11.9 percent in 1950 to 15.6 percent in 1960 and to 16.9 percent in 1965 (Waterbury, 1983:38, calculated from table 2.4).

How far was investment able to build new productive capacity to help in achieving sustainable growth in the future? A close look at the investment composition may help to answer this question. The main characteristic of the investment pattern was the substantial increase in the share of commodity sectors from about 41.2 percent of total investment on average of 1952/53-1956-57, and 44.6 percent in 1957/58-1959//60, to 57.4 in 1960/61-1964/65. This increase was at the expense of the housing sector whose share in total investment decreased

drastically from 32.5 percent in 1952/3- 1956/7, to 10.7 percent in the five-year plan period (Mabro, 1974:187). Diversification of economic activity was one of the main targets of the Egyptian government, so as to increase the productive capacity of the economy and reduce the independence on the foreign markets. Due to the limited resources available, priority was given to both the industrial and agricultural sectors. It was realised that housing provided less employment opportunities and it probably generated less external economies and a smaller reinvestable surplus than the other sectors. The increased tendency towards industrialisation, with a strategy for import-substitution industrialisation, continued during the five-year plan. The industrial share in total investment during the plan was the highest among different sectors, accounting for 26.6 percent. However it was not the fastest growing sector, as its share increased from 23.8 percent of the total investment in 1952/3-1956/7. In fact the increase in the agricultural and transport sectors was faster than that in industry. The share of the total investment of agricultural and transport increased from 11.4 percent and 14.7 percent respectively in 1952/3-1956/7 to 23.4 percent and 19.3 percent respectively in 1960/61-1964/5 (*ibid.*:186-87).

If we look at the outcome of the sectoral investment we find that the products of industry and electricity increased by about 9 percent per annum during the five-year plan (El-Graity, 1977:19), and its share in GDP increased from 17.2 percent in 1956/7 to 23.1 percent in 1964/5 (Mabro, 1977:189). The expansion of the industrial sector was biased towards consumer goods. Investment in consumer goods accounted for 40.6 percent of the total industrial investment, while it was planned to reach only 24 percent. This expansion of consumer goods was at the expense of capital and intermediate goods whose share reached 24 percent and 35.4 percent of total investment respectively. It was planned to reach 35.9 percent and 40.1 percent of total investment respectively (*ibid.*:89).

The expansion of the industrial sector resulted in an increase in manufactured exports from £E 34.1 m in 1959-60 to 65.4m in 1964-65 with an increased share in GNP from 2.4 percent to 3 percent. It should be noted that this period experienced a major devaluation of the Egyptian currency. Apart from this modest increase in exports, the strategy of import-substitution industrialisation could not reduce the import bill as was planned. On the contrary, imports increased from £E 229 m at the

beginning of the plan (15 percent of GDP) to 413 m by the end of it (20 percent of GDP), and the current account deficit reached £E 166 m (Waterbury, 1983:89-91).

The ambitious first five-year plan resulted in high inflation rates in addition to a large deficit in the balance of payments. The crisis in cotton production in 1961, in addition to the increased military expenditure and the involvement of Egypt in the Yemen war, was considered partly responsible for these difficulties. While in fact the problem was inherent in the nature of the regime in general. As it sought to create a wide-base coalition, it constructed a regime which was a combination of semi-populist, state-capitalist, and developmental nationalism, with the aim of distributing gains to most groups. The contradiction between the investment policy which was aggressively developmentalist aiming at achieving a rapid and broad-based industrialisation, and consumption policy which was aggressively populist, granting a rapid expansion in living standards (Cooper, 19), resulted in partial failure in the investment policy.

The first five-year plan which was supposed to start in 1965/66 has faced with economic difficulties with achieving the planned investment. These difficulties were complicated by the 1967 war, and after 1966 investment plans could not be achieved. The per-capita national income did not increase because of the increased defence burden, the increased population and the increased subsidies (El-Graity, 1977:21). After the defeat of 1967, more sources were needed while fewer were available. Egypt lost three major sources of revenue: a total of \$400-500 million annually, from the Suez Canal (\$230-250), the Sinai oil fields (\$100), and tourism (\$100). The government had a limited chance to increase its domestic revenues through direct methods, as it could not promote forced savings, or cut subsidies. The government, on the contrary, allowed consumption to grow even faster in order to compensate the people for the moral pain. On the other hand the nationalisation of 1961 had effectively rid the country of any corporate sector, a potentially important source of income (Barnett, 1992:110-111).

### **3.2.3. The Redistributive Policies**

If we look at the economic policies that were directed to maintain adequate consumption levels, we are faced by a variety of policies, some of which can be defined as direct ones, such as the price control policy, and the subsidising of subsistence goods. The others are indirect, like the employment guarantee policy



which meant an income guarantee, the minimum wage policy, and the import substitution industrialisation policy. During the 1960s, the management of prices affected all major sectors of the economy including, agriculture, housing and industry. Subsidies were used extensively to check possible rises in the cost of living (Ikram 1980: 23). The price policy was not limited to food items. It was also used to provide electricity, water, and transport (Hansen, 1991:165). By subsidising basic subsistence goods, the state reached the poorer segments of society, the peasantry and more importantly the private-sector working class whose gains, judging by income levels were limited (Cooper, 1982:28).

The adoption of import-substitution industrialisation and the expansion of consumer goods manufacturing, especially for consumer durable, increased the demands of the new emerging class which was composed of the administrative and military elite, and senior civil servants, whose consumption patterns have larger components related to services and manufactured goods than the rest of the population (Abdel-Fadil, 1982:69). The price control policy and the instalment sales policy of these goods encouraged demand from the middle-income groups.

Policies for direct improvement in income both in rural and urban areas took the form of setting a minimum wage for both agricultural and industrial workers in order to improve the living standard of the lowest-paid wage-earners. A study for the period 1952-72 showed that the minimum wage rose at a much faster rate than did the cost of living index. In addition to the monetary increase there was a rapid build-up in fringe benefits for wage-earners in the organised urban sector. Pension schemes formed the core of such fringe benefits (Abdel-Fadil, 1980: 47). In the meantime, distributive policies were adopted to improve the relative income of the low and middle-income classes. An upper limit on income was set at £E 5000 per annum.

### ***3.3. Sadat's Experience***

Although there were some major changes in the state's structure, system, and orientation during Sadat's regime, some of the main features of Nasser's era continued to dominate. One of the major changes was the departure from a one-party to a multiparty system, however, the regime continued to be authoritarian with unlimited authority in the hands of the president. There was also a shift from moderate alignment with the USSR to a strong alignment with the USA. The

development strategy was directed towards economic liberalism under the banner of economic opening the '*infitah*'. Nevertheless the economy continued to be managed by strong bureaucratic controls, and the public sector continued to play a leading role in the economy. Furthermore, the public sector became more involved in economic activities under the new investment law which allowed it to participate with capital in the private sector. The government continued to exercise control over public-sector earnings, the marketing of agricultural-sector commodities, petroleum exports, and a substantial part of the banking system (Waterbury, 1985:69). The populist nature of the regime continued or even deepened and Sadat could not completely deprive the masses of the revolutionary gains of the Nasser's period. So what initiated changes in some policies and what required continuity in others? This will become clear in the following analysis.

When Sadat became president, he was confronted by two challenges: to consolidate his power and to recover the Sinai from the Israeli occupation. After the first important step towards recovery of the Sinai, the 1973 October war, development and welfare goals came to the fore, together with a further consolidation of power. When Sadat took-over the presidency he lacked the wide public support enjoyed by his predecessor. His main characteristics were hardly known by the public. Nasser never allowed his colleagues to enjoy outstanding recognition. Sadat also had rivals among the main leftist figures of the Nasser regime, but he succeeded forming a countercoalition with the right-wing. He was able to gain the support of the military by loosening the ties with the USSR and seeking assistance from Saudi Arabia and then from the United States (Sadowski, 1991: 103). The military also enjoyed preferential treatment under Sadat where, in addition to well-paid salaries, they enjoyed other facilities such as special shops for cheap food-items, imported consumer goods, and the provision of special housing units. Sadat still needed to consolidate his power among the masses and to build a wide constituency. He maintained Nasser's gains with the masses and even extended them by expanding higher education and the employment guarantees policy for high school and university graduates and widened the subsidy system. After the October war Sadat acquired some legitimacy for his regime, However, he worked to gain more legitimacy to sustain it. He sought to 'traditionalise' and to 'institutionalise' his regime (Hinnebush, 1991). In addition, while events since the

early stages of his presidency directed him to the right, the October war convinced Sadat of the vital role the United States could play in the peace process. This turn to the right entailed some economic and political liberalisation. Sadat managed to use this reorientation to enrich the financial resources of the state through foreign economic assistance, which increased to unprecedented levels during his era, to distribute wide economic gains to the masses in the form of subsidies. Sadat also with this reorientation of economic policy, and by allowing labour migration, opened new opportunities for individuals to improve their economic conditions and/or to accumulate wealth.

### **3.3.1. The Economic Opening, the '*Infitah*'**

The October paper issued in April 1974 by President Sadat introduced the new policy of economic openness. The rationale behind the policy was the need for external finance to support the limited domestic resources, which had been exhausted by military spending, and to restore the pre-1965 high growth rates. The paper also referred to the positive changes in international circumstances, which made external finance available. The attraction of Western technology was also emphasised. So the main argument about the rationale behind the opening was finance and technology which was expected to combine with Egyptian labour to stimulate the Egyptian private sector and promote exports (Abdel-Khalek, 1982:260 & Waterbury, 1982:70). Many internal and external factors led to the economic openings. At the domestic level, there were three main factors: first, Nasser's socialist regime had not managed to entrench his ideology very well and his junta did not have a profound socialist philosophy. They adopted socialism as a means to achieve social justice, but did not consider it as an end. The old capitalist class was not completely eliminated. Some of the old capitalists found in their way into the state apparatus as the state sought their expertise to manage the nationalised enterprises (Issawi, 1982:75-76). While others encouraged their children to be part of the bureaucratic apparatus of the regime, and the final section of the old capitalist class still existed in trade and construction.

Second, the expansion of the public sector and the centrally controlled economy created new elite groups of senior bureaucrats and public enterprise managers. Some of them were interested in the survival of the regime as the source

of their power, while others preferred to invest their expertise and connections they gained in the public sector in private sector activities.

Third, after the defeat of June 1967, there was a need to direct resources to rebuild the army and open the door again for private domestic companies to increase their participation in economic activity, as the government realised that it could not afford the burden of development by itself. Since then attitudes towards private activity and its role in economic development started to change. The government started to relax its control over imports and foreign exchange (*ibid*,:79).

At the international level, both the IFIs and the US tried to put an end to the Egyptian experience and to direct it towards economic liberalisation. It started in 1965, when the US stopped its food-grains aid shipment to Egypt, and was enforced by the 1967 defeat which pushed the Egyptian regime to reconsider its Arab-relations -especially with conservative governments such as Saudi-Arabia- and its relation with both of the two international powers, the USA and the USSR. The development in the relations between the US and the USSR affected Egyptian relations with both these countries. Under pressure of the economic situation in the USSR, the country sought American technology and goods. In this situation the USSR played the Egyptian card, when Breshnev announced in May 1972, that the USSR cared much more about improving its relations with the USA than its military or political obligations to Arab Countries, especially Egypt (Stephens, 1973:3-12 as quoted in Amin, 1982:102).

The process of opening the Egyptian economy relied on the following measures:

#### A-Investment Legislation and Incentives:

The first attempt to attract non-Egyptian investors during Sadat's era started in 1971 with law 65 for Arab investment and free zones. In 1974, after the fear of war had diminished, a new law of investment was issued. Law 43 of 1974 was introduced as part of a broader policy for economic liberalisation, the "*infitah*", of which law 43 was one of the main pillars. A special authority to deal with investment under this law called The General Authority for Investment and Free Zones-GAIFZ was established. While the old law 65 of 1971 was limited to Arab capital, the new law opened up more economic activity -almost all economic activity except petroleum which was regulated by a special law- to both Arab and Foreign capital.

Law 43 of 1974 offered a wide range of incentives and provided more guarantees against expropriation and nationalisation. Projects operating under this law enjoyed income tax holidays of between 5 and 15 years, depending on the type of activity. The main attraction of the law was exemption from labour laws, exchange control regulations, and from the need to obtain licences for importing and exporting (Handoussa, 1990:148).

Law 43 of 1974 was amended by law 32 of 1977. The main addition was that it offered Egyptian investors the same opportunities and incentives, with the criterion for a project's eligibility was the use of foreign currency rather than foreign nationality. Moreover it allowed investors to buy foreign currencies from the local market, removing the condition of having foreign currency accounts fed by export-earning or transfers from abroad (*ibid*).

#### B- Import and export regulations:

A new import system of 1974 enabled anybody who had access to foreign exchange resources from sources other than the banking system to use them for importation. This process opened the door for speculations about the Egyptian pound. A new import export law of 1974 was issued to support the previous facility. This law dismantled the state monopoly and control of foreign trade. It entitled individuals, both Egyptians and foreigners, to import anything except for eighteen strategic commodities. In addition foreign exchange transactions outside Egypt was liberalised by law no. 97 of 1976. It affirms the freedom of every legal entity - except for government bodies, public authorities and public enterprises- to keep the foreign exchange acquired from any source - except from merchandise exports and tourism- and to make transactions in foreign exchange through the officially authorised banks. The last supporting measure was phasing out of the existing bilateral trade agreements (Abdel-Khalek, 1992: 265:270).

#### *Investment Performance*

I examine here the impact of the *infitah* measures. How affective was the *infitah* in attracting investment? From where was it able to attract capital? What sectors were more attractive to capital and why?

1- Size of investment, by the end of 1979, the total approved inland projects from 1974 were £E 4,190, of which equity capital represented only 54.4 percent. However, the total investment in projects starting production was only £E 804.2

million. If investment in financial capital was excluded, this gave an annual rate of about £E 8.6. This represented only 7.6 percent of average annual gross fixed investment for the period from 1975 to 1979 (Abdel-Khalek, 1982 :270) which is quite modest contribution.

2- Sectoral allocation of investment. If we examine the sectoral breakdown of investment which started production, we find that by the end of 1979, investment companies, accounted for one third of the total investment. If we add banking projects which accounted for 13 percent the total share of the financial sectors, it amounts to almost one half of total investment. Industrial investment accounted for 22 percent, followed by agriculture accounting for 15 percent, tourism for 8 percent, While the remaining was directed to other services (*ibid*,:272-73).

3- The share of National and foreign Capital. By the end of 1978, about 54 percent of authorised capital was Egyptian (Handoussa, 1991:162). By the end of 1983 this share rose to 64.21 percent and about 38 percent of total authorised capital belonged to public enterprises. Arab capital accounted for 22.9 percent and foreign capital accounted for only 12.6 percent (Abdel-Moula, 1985:108). Thus we could say that the investment laws were mainly able to attract Egyptian capital and that Egyptian investors are willing to contribute to development efforts if they found an adequate environment and incentives. It also proved to be more effective and sustainable to try to attract Egyptian capital.

### **National Response, Who Invests?**

While Nasser's regime succeeded in curtailing the economic and political power of the national capitalists, it did not create a new class of entrepreneurs or a new generation of businessmen. The main beneficiaries of that policy were the middle and the lower classes in addition to the bureaucratic elite, as the ambitious Egyptian programme for national development relied heavily on bureaucracy. The large public sector which emerged, resulted partly from the nationalisation of the late fifties and the early sixties and partly from the new industrial and economic expansion. This bureaucratic system was headed and controlled by a militocracy and then increasingly, by a growing technocracy. The performance of this bureaucracy was not satisfying at any level. Complaints about routine and red-tape continued.

Public services and enterprises were increasingly over-staffed, with devastating results upon rational organisations and management, financial rewards and morale. However the bureaucratic elite gained political power from the monopolistic control of the public sector, nevertheless they were the only possible emerging business class. The movement of socio-economic events from the late sixties put the bureaucratic elite at the cross roads. Some of them were interested in the survival of the order which brought them into a position of eminence and power and for the benefits which were to be gained from it. At the same time an increasing group thought of the public sector as a stepping-stone to the private sector (Ayubi, 1991:5-10). They thought of utilising either the experience they had gained in their work as managers or experts in the private sector, or the experience and the money some of them gained through commissions or bribes, to establish their own business.

Although in the late sixties old capitalist class was reluctant to promote investment, it was tempted by the change in the political regime, the new incentives and the new liberalised direction after 1974. One of the main incentives to bring back the old traditional capitalist elements was the restoration of their expropriated estates and agriculture land which was still held by the state. This provided more sources of capital for this class (Said, 1986:57).

The open door policy provided a good opportunity for the traditional capitalist to participate with the bureaucratic elements of the sixties and become the new political coalition of the new policy. Said's study proved that the first corporate companies established in the early years of the new "*infitah*" policy were mostly financed by old traditional capitalists. Some of the old capitalist class had joined the bureaucratic and the public sector staff during the sixties, and had continued their work as businessmen after the open door policy. In addition to this group, Said's study highlighted that the old capitalist group had allied with the bureaucratic bourgeoisie and elite to formulate different forms of investment (*ibid*).

One question raised was whether the *infitah* allowed for a new class of capitalists in addition to the old one and the bureaucratic elite? What we can conclude is that the new policy as a whole gave the opportunity for some groups to accumulate wealth but it was unable to create a strong national bourgeoisie from them. We can basically discern between two classes or groups that had the opportunity to accumulate wealth. The first includes the various groups that had the

chance to work in Arab countries. According to the Ministry of Manpower and Training, as many as 1,890,000 Egyptians were working abroad in 1978 (as quoted in Ayubi, 1991:73). Although their remittances provided the country with a vital source of foreign exchange, most of the savings of this group were directed either to luxury consumption or to small commercial projects. Another substantial group preferred to invest in money companies with the option of gaining a fixed amount of money every so often rather than take the risk of investment. The behaviour of this group was characteristic of the new national attitude and work ethic developed during the *infitah* which promoted the commercialisation of the economy.

The second group was what some have termed parasitic elements. The parasitic activity, although not specifically defined, was composed of mainly unproductive operations dependent on transactions and the circulation of money. It related to capital growth not to capital accumulation. It also relied on the exploitation of others and it might use illegal ways to achieve its objectives (Said, 1986:123). Some examples of parasitic activities which grew during the "*infitah*" were those concentrated in the sub-contractor business, the illegal trade in foreign currencies, black-market activities, smuggling imported goods from free zones, housing associations, dealing with customs, and travel agencies (Abdel-Fadil, 1984:192).

### **Foreign Response**

In the first few years of the "*infitah*" the policy appeared to catch the imagination of numerous potential investors; one US businessman was quoted as saying, "It is like the California gold rush" (Gillespie, 1988:27). But initial interest did not automatically produce investment. Some foreign investors' interests were turned down through a lengthy process of project approval and bureaucratic red-tape, while others did not meet the Egyptian targets. In January 1975, Prime Minister Abdel-Aziz Higazzi reported to President Sadat that apparently foreign companies' proposals did not meet the government's criteria: 552 projects had been proposed after the liberalisation had been announced, but only 196 of these had been accepted. In 1978 Herman Elts, the US Ambassador to Egypt, noted that over 3,500 American businessmen had visited Cairo to investigate the Economic Opening; almost 1000 had spoken with the Ambassador himself; but in the end "almost nothing" had materialised from this initial interest (Gillespie & Stever, 1988:27-33). The foreign



share in the total authorised capital invested under law 43 of 1974 accounted for 26.5 per cent by the end of 1979 (Abdel-Moula, 1985:108). If we look at other countries' contribution (including foreign loans and aid) and these in favour of investment we find that Arab capital, which accounted to £E 270 m by the end of 1978, represented 16 per cent of the total value of investments. It was directed to the following areas: investment companies (28.5 per cent of Arab capital); housing (16 per cent); chemical industries (9 per cent); banking (8.5 per cent); tourism (8 per cent); engineering industries (6 per cent). Over 40 per cent of all capital investment in metallic industries and of all investments in "investment companies" were provided by Arab sources.

The American capital committed up to the end of 1978 amounted to £E168.6 m, representing about 10 per cent of total investment. It was directed to the following areas: education, training and services (72 per cent of total American investments, and 92 per cent of all capital allocated for education, training and services); banking (7 per cent); agriculture and husbandry (6 per cent); engineering industries (3 per cent); weaving and textile industries (37 per cent).

The Western European (EEC) countries had committed £E 100 million which represented 6 per cent of total investments. It was directed to: engineering industries (24 per cent); tourism (20 per cent); banks (13 per cent); investment companies (6 per cent); and chemical industries (6 per cent). In addition to 66 per cent of all funds allocated to the petroleum industries.

Other countries not included in the previous categories (Japan and Greece being of particular importance) had, until the end of 1978, committed £E223 million representing 13 per cent of all investments. The main areas were tourism (67 per cent of capital committed by these countries); weaving and textile industries (10 per cent); banking (3.5 per cent); construction materials (3.5 per cent); and health services (0.5 per cent) (Ayubi 1981:39-40).

Although the previous estimates did not distinguish between foreign loans and foreign direct investment, a different study for the period 1974-1980, estimated that total foreign investment spending on direct investment under law 43 of 1974, was about £E 533 million, accounting for only 7.9 per cent of the total foreign resources used to finance investment. In the same period the capital utilised from foreign loans was £E 5,950.3 million (88.3 per cent of total foreign finance) and the

grants utilised, with the exception of Arab support grants, accounted for £E 255.3 million (3.8 percent) (Abdel-Moula, 1985:110-111). This explained that foreign direct investment was very low compared with other sources of foreign finance. Foreign investors had been tentative in their approach to Egypt as they wanted to minimise their risk by riding the wave of Arab and Western public financing that has poured into Egypt after 1974. The IBRD had been a tacit ally in this process. It has already been noted that the IBRD had made loans to public sector companies contingent on their entering joint ventures under law 43, and the USAID supplied the foreign exchange component of at least one law 43 project, the Egyptian Cement Company. In essence foreign investors sought to limit their equity commitments by taking advantage of abundant public and private financing, or by assigning equity value to their technology and know-how (Waterbury, 1983:155-156).

On the other hand not all approved projects had actually been implemented. Only 32 percent of all projects approved had started operations by the end of 1978. Their investment spending represented only 116 percent of the total for all approved projects, they employed only 11 percent of the manpower that was supposed to be employed by the approved firms. A sizeable number of projects, however, were reported to be in process or under construction. By the end of 1978, these represented 44 percent of the capital committed, 66 percent of the employment envisaged (Ayubi, 1991:49). If, however, all approved projects were actually implemented, within five years the law 43 sector could dwarf the public sector in terms of productivity and sophisticated technology (Waterbury, 1983:155).

### *Main Determinant of Investment*

Many factors had affected the inflow of Arab and Foreign investment to Egypt. One of them was the conflict and peace with Israel. The October War of 1973 led to the inflow of Arab aid and private investments, while moving forward with the peace process and the signing of the Camp David Accord in 1979 were the main reasons for the Arab boycott of Egypt and the curtailment of both aid and Arab private capital. Another related effect was the increasing distance between the USSR and the Eastern bloc, as Sadat decided to terminate the role of USSR experts and wanted the war decisions to be fully Egyptian. The relations between the two countries soured further after the second Sinai disengagement agreement. The trade between the two countries was sharply curtailed. While the trade agreements with the USSR and the

Eastern bloc encouraged the establishment of hundreds of private sector firms, the USSR and the Eastern bloc's careless attitude about the quality of products did not help these firms to survive after the cutting of the trade agreement (Waterbury, 1983:171).

On the other hand, there was a rapprochement with the United States after the war, as Sadat saw what the massive role the United States could play to advance the peace process and the leverage that it could have on Israel. Sadat announced on many occasions that 99 percent of the game cards were in the hands of the USA. The rapprochement with the US opened the gates for US aid flows in addition to the prospect of the inflow of private investment. The US and other Western countries actively encouraged private investment in order to consolidate Egypt's return to the Western camp and to underwrite Sadat's Peace (*ibid.*:156).

The financial incentives proved ineffective in the face of the political situation of the country. The continuing possibility of war with Israel discouraged potential investors. Although law 43 was amended by law 32, and more incentives were given, foreign companies remained nervous about the country's political situation, both external and internal. A survey revealed that political uncertainties were perhaps the most important deterrent to investors entering Egypt. This concern was among others that prompted Sadat to take initiatives to hasten the peace process with Israel (Gillespie & Stoeber, 1988:30-32). The Arab boycott of Israel also discouraged some multinational companies with profitable operations in Israel from approaching Egypt. Ironically, when Sadat went forward with the peace process and signed the Camp David Accord in 1979, almost all Arab countries curtailed their political and economic relation with Egypt. Many joint ventures which were premised on access to the domestic market and the Arab markets, especially among the oil-rich. Access to these markets became uncertain, and the lure of the Egyptian market might not prove sufficient to hold investors' interests (Waterbury, 1983:155).

Political stability had also a great bearing on investment in 1977. The riots in that year because of the reduction of subsidies was one of the reasons that encouraged the government to hasten the rate of investment inflow and the benefits envisioned in the economic opening. For example in a single day- March 27, 1977- the board of directors of the Investment Authority approved 65 investment projects

valued at £E404 million (approximately \$577 million at the official free rate) (Gillespie & Stoeber, 1988:31).

The inefficient administration and the lengthy process of project approvals was one of the usual complaints of investors. Investors complained about the stifling bureaucracy, noting that applicants could be kept waiting for weeks trying to see the appropriate government official. Approval by the Investment Authority, however was often the first step in a lengthy process. Investors had to obtain authorisation from other Ministries responsible for the various activities of their project. Negotiations with these different government departments could initiate considerable duplication of effort (Gillespie & Stoeber, 1988:29). The bureaucratic routine was complicated by a lack of clear criteria for project selection, and often inconsistent changes in the regulations and requirements. The large degree of discretion given to the lower-level bureaucratic staff sometimes caused much confusion through their arbitrary judgements rather than facilitating the process. It also opened the door for corruption through bribes and commissions.

Corruption grew considerably during the "*infatih*". It took various forms. In public enterprises, there was the phenomenon of theft and embezzlement. The rate of public officials accepting bribes and securing illicit gains was on the increase (Ayubi, 1991:65-66).

Other related themes were the growing inter-relationships between the public and the private sectors, developed since the seventies, which led to the growth of the latter at the expense of the former. Public officials sought to establish private enterprises of the same nature as their public office (i.e. competing with) under the name of one of the family members. They benefited from the networks of contacts and affiliations acquired in public office, they exploited the facilities and personnel of the public sector for the promotion of their private activities (Ayubi, 1991:14-15).

We can recognise the following factors as responsible for corruption:

- "El-Tasayoub", or the relaxation of government control not only in economic life, but in all aspects of political and social life as well. There was new legislation, but little of it was effective. Even though there were plenty of control agencies, few of the corrupt actors were brought to justice. Moreover justice became very slow and special lawyers emerged to manipulate the law. It became quite common to refuse cases due to improper arresting procedures. The state changed to become a soft state

that legislated laws. However, it was unable or sometimes unwilling to implement them. All this created a situation of distrust or disrespect between the government and the clients. The war period could partly be responsible for this situation, as there was a tendency to ignore small cases of disorder or corruption, in an unwillingness to increase the consequences of defeat.

- Consumption policy, both Nasser and Sadat encouraged extrovert consumption policies. While Nasser relied mainly on price controls and subsidies, import policy was an additional factor in Sadat's era. It provided different substitutes in addition to new varieties of luxury goods. Consumption became one of the determinants of social prestige. This prompted people to seek fast and easy earning sources.

- The rapid increase in cost of living due to inflation, and both the real and relative deterioration in wages following the increasing disparities between income levels during the *infitah*, created a feeling of inequality, and promoted corruption.

- The continued bureaucratic control over economic activity give more opportunities to civil servants to find ways of seeking commission.

### **3.4. Conclusions**

The main dilemma of Nasser's era was how to manage the limited domestic resources to achieve three main competing goals:

The first was extracting resources for investment to achieve development, the second was to finance the semi-populist nature of the state to achieve political stability, and the third was building a strong army to face the regional threat. Unwilling to sacrifice any of the three goals, Nasser found the solution in foreign finance via the assistance of outside patrons. Although the tendency towards fixed finance gave little cause for alarm at that time due to its modest rates, it established a pattern that would prove difficult to correct in the future (Barnett, 1992:89). Since then, Egypt has relied heavily on foreign assistance to finance its investment expenditure.

Two main factors dominating Nasser's era continued to affect resource allocation and the capital accumulation process in Sadat's era. The first was the war and international policies, the second was the semi-populist nature of the state. War preparations were one of the factors competing for resources which forced Nasser to sacrifice, though unwillingly, his investment objectives after the 1967 defeat. The Suez war was a turning point in Egypt's political economy and it induced Nasser's decision to Egyptianise foreign assets and paved the way for nationalisation in 1961

which built the state's capitalist system. The war had also diverted Egypt's international relations and economic affairs from the Western bloc to the Eastern after the Suez war in 1956 and the other way round after the October war in 1973.

On the other hand, while Nasser promoted economic policies aiming at distributing economic gains to almost all groups of society, Sadat followed the same line but on the other hand he distributed more gains in return for political acquiescence.

If we look at the other economic features of the regime in Nasser's era: state capitalism was one of the sources of power in both the economic and political arena. It enabled the state to create its own source of revenue, hence, to increase its autonomy. It also allowed the rapid growth of a powerful bureaucratic apparatus which comprised the main part of its coalition. In Sadat's experience, the deteriorating performance of public enterprises and public bureaucracy in addition to the relaxation of government control over both public and private activity, negatively affected state power. However, we can not relate changes in state power to the type of economic system, rather is it related to state performance in controlling and managing the public or private sectors.

The incomplete democratic experience of Sadat's era was not effective in enhancing development. The weak opposition parties were not able to effectively rationalise the government performance. The relatively free press which was able frequently to criticise and refer to corruption cases, did not guarantee effective actions against them.

The main features that characterised the political and economic systems built during the Nasser era were difficult to abandon and deeply influenced the later regimes. This was the bureaucratic and populist nature of the state. Lacking Nasser's charisma especially at the beginning and trying to fulfil his promises of providing welfare to the Egyptian citizens, Sadat enhanced the populist nature of the state in the sense that he was more committed to free education and employment guarantee policies, as well as to increased food subsidies. In addition to the effect of such policies on the public budget, the policy of employment had profound effects on the policy and the economy. This policy created bureaucracy and increased the bureaucratic influence over the economy, with the application of the '*infitah*' it was more suitable for promoting corruption and rent seeking. Another important issue was that such a policy created an increased reliance on the state as a 'first' not 'last'

resort for recruiting, but not job creating, as the state failed to create real employment opportunities and simply added the new graduates to its bureaucracy. The restrictions on the private sector during Nasser's era and the continuing provision of easy recruitment during the '*infitah*' partly impeded the growth of a real entrepreneurial class, as the new generations were averse to risk and preferred stable jobs. That was clear from the nature of the new investors where most of whom came from the old entrepreneurial class, with a few opportunists who sought fast and easy profits.

While Nasser's regime failed to institutionalise its system which was mainly personal by nature, Sadat laid the foundations for a new institutional system built on pluralism in spite of the controls imposed on it.

## Chapter 4      The Political Economy of Adjustment in Egypt

### *4.1. Introduction*

Unlike the second half of the 1970s, which witnessed high rates of growth for the Egyptian economy, the 1980s experienced declining trends unveiling the fragile economy and structural imbalances and problems. The growth of the 1970s depended highly on rents while the share of the commodity sectors was declining and the productive capacities of the economy were not developed. The economic crisis promoted several critiques notably against the applied liberalisation policy launched under the name of the *Infitah* -the open door policy. This criticism was at two levels, economic and ideological which led a debate discussing the causes of the crisis and the ways out of it. Two major approaches or scenarios were crystallised. The first was the socialist, Nasserist, which believed in government regulations, the role of planning and in the public sector as a leading sector for development (Abdel-Khalek, 1982; El Essawy, 1989; Zaki, 1989; El-Emam, 1995). The second was a policy of liberalisation similar to the IMF scenario. Liberalism thought that the open door policy was only partially successful because it was seen to have been incomplete (El-Naggar, 1991). Others thought the *Infitah* was the only available alternative to the failure of the past experience of socialism. Between the two main scenarios were those who supported a mixed economy (Montasser, 1991). The mixed economy had been implemented for several years but the government was also accused of failing to achieve any progress during the period of negotiations with the international agencies and the earlier refusal of IMF proposals. The political choice was made in favour of liberalisation as the socialist scenario was invalid politically due to changes in the domestic and international environment, however the government did not consider it an ideological choice.

This study argues that there was no political consensus during the early phase of initiating the new policy. Until the late 1990s there was little change in support base of the state for economic liberalisation. Little has also been achieved in the area of enhancing state capacity.



As regards the economic content of the programme this study challenges the effectiveness of two main measures considered by neo-liberalism as the cornerstone for successful adjustment in Egypt (World Bank, 1997), that is, to accelerate both the process of privatising public enterprises and trade liberalisation. This chapter argues that what Egypt really needs is to increase its productive capacity in order to achieve sustainable growth and if that growth is to benefit the Egyptian economy, it must emanate from a new private-sector activity rather than by simply privatising the public sector. Privatising public enterprises in Egypt does not seem to achieve the declared objectives of improving efficiency, productivity and increasing investment. Bearing in mind the method applied in privatisation, as will be discussed below in detail, privatisation proved costly and time-consuming and has also crowded out new investment in the private sector by absorbing private savings. The result of privatisation is more a change in the type of ownership rather than the introduction of new investment. As for trade liberalisation, it is unhelpful to talk about increased gains for the economy from increased liberalisation, at least in the mid-1990s, as the productive capacity of tradable goods has to be increased.

While sound economic performance is important to enhance credibility and make changes more feasible, the distribution consequences of the reform and its social cost have important implications for the balance of political power and the composition of the support base. It is equally important for social and political stability and furthermore for equity issues. This study argues that the social cost of adjustment was high in terms of unemployment, increased poverty and availability of social services. There are few indications that these negative costs will be remedied in the near future. While macroeconomic performance has shown some improvements in recent years the challenges remain high.

Finally the study argues in favour of political liberalisation as an important requisite during the reform consolidation phase. An increased pace of democratisation and more consolidation in civil society organisations are important to guarantee public participation in the decision-making process, to reflect public preferences and in monitoring the process of redistribution of gains and losses.

This chapter contains three main sections after the introduction. I review the SAP measures and their macroeconomic and distributional impacts. Secondly I

review the political debate about reform and thirdly I assess the effect on state-civil society relations.

#### ***4.2. ERSAP in Egypt***

Egypt's first agreement with the IMF in 1987 was terminated due to the slowness and partial nature of the measures undertaken. Accumulated problems, however, pushed her to resume negotiations with the IMF in the early 1990s. This time, Egypt was willing to accelerate reforms and to undertake more comprehensive measures with the simultaneous use of all instruments of the monetary, fiscal and exchange adjustment. A stand-by agreement was concluded in May 1991 and the implementation of the stabilisation programme started even earlier on January 1st (Handoussa, 1993:89). While Egypt resumed negotiations with the IMF under pressure of its economic crisis, some favourable events on the external front during negotiations encouraged it to pursue the agreement and to carry on with the comprehensive reforms which it refused to undertake earlier. The Gulf crisis revived Egypt's regional role and Egypt was compensated for both its losses and vital role in the war to liberate Kuwait by direct transfers (\$ 3.5 billion as emergency aid) and by debt forgiveness (\$7.2 billion represent all of Egypt's debt to the Gulf countries and \$ 7.5 million represents the outstanding military debt to the USA) (Handoussa, 1993:5). Another incentive for Egypt to conclude the agreement was the promise of the Paris Club to write off part of the external debt when the agreement was signed. Handoussa (1993) noted that the IMF was ready to accept a somewhat more 'gradual' implementation for a number of key components of the programme due to Egypt's regional role.

The reform programme was planned to be implemented in different phases supported mainly with the IMF and the World Bank. Two phases were completed by the mid-1990s while the third was in progress. The first signing with the IMF was that of May 1991 under Stand-by Arrangement for 18 months, May 1991- Nov. 1992, but this had to be extended to March 1993 with a 278 million SDR (\$ 390 million) credit. The second was the Extended Fund Facility Arrangement, July 1993-June 1996 (see Galbis, 1995:2 & Nakamura, 1993:53). The signing of a Stand-by Agreement with the IMF was shortly followed by a Structural Adjustment Loan (SAL) with the World Bank in June of the same year, which was formally signed in November 1991. The SAL was equivalent to \$ 300 million. In addition,

an IDA credit of SDR 105 million for the Social Fund project was approved. The second phase was also supported by the Bank through a three-year Structural Adjustment Monitoring Programme (SAMP) (EAP, 1993 & World Bank, 1993). The reform programme was also supported by other foreign creditors and their conditionality was related to performance criteria agreed to as part of the Fund stand-by arrangement. The African Development Bank would provide co-financing of a sum equivalent to \$130 million and the European Economic co-financing of ECU 60-100 million. USAID also introduced the Sector Policy Reform Programme (SPR) to complement and reinforce the reform programme was agreed to with the IMF and the World Bank. The SPR focuses on macroeconomic stabilisation and medium-term structural adjustment. It establishes specific policy reform measures, supported by technical assistance where necessary in four sectors: Financial, Fiscal, Trade, and Enterprise. The cash transfer is a two-year \$400 million grant divided equally between the two years in addition to \$ 10 million technical support (EAP, 1993).

The signing of the agreement with the IMF was conditional on the pre-implementation of some liberalisation measures. Price liberalisation was completed for half the industrial production, energy prices were increased by 43 percent in the mid-1990s, food subsidies were sharply reduced, a number of taxes were raised and tariff rates on most utilities were also increased. Draft legislation for public enterprises which gave autonomy and allowed their privatisation was prepared. Measures were taken to deregulate and simplify investment licensing and abolish some public monopolies in agricultural distribution and foreign trade (Handoussa, 1993:6-7).

In the case of Egypt, the use of cross conditionality was clear and the role of the Stand-by agreement as a 'seal of approval' by other creditors was played and all other credit agreements and the debt write-off for the Paris club was a result of the agreement with the IMF. In turn the IMF put a stricter conditionality on Egypt's implementation of the agreement this time. Both the IMF and the World Bank divided the disbursement of their credit into two tranches and related the release of each with the fulfilment of certain reform measures. Before each disbursement a World Bank and/or IMF mission would visit Egypt to review with the GOE the fulfilment in the previous phase and to set performance criteria for the following

phase. This could be in a joint IMF/ Bank mission as in Nov. 1991 when the first supervision of the macroeconomic framework components was carried out. The World Bank's SAL for instance, would be disbursed in two equal tranches of \$150 million each. The first tranche was even released in two disbursements. On Feb. 1st to 14, 1992 a World Bank mission reviewed with the GOE's representatives, the areas related to the SAL effectiveness, and the second tranche release conditions and the monitoring arrangements for releasing the SAL second tranche. On February 22, 1992, the first disbursement (first tranche) released \$60 million. A team from the World Bank arrived Cairo in July 1992 to discuss the measures that were executed for releasing the second tranche. In Sept. 1992, the GOE received the second disbursement of the first tranche release amounting to \$90 million.

This extensive monitoring by the World Bank was followed by even more strict members of the IMF. The IMF stand-by credit was also divided into two tranches. Disbursement of credit depended on Egypt meeting the criteria of the programme agreed upon with the IMF. The second tranche of SDR 130.8 million (\$ 183 million) which was due in November 1992 was not released till May 1993 (Nakamura, 1993:53). The amount itself was not enormous, however, it was the credit conditionality which related other credits and debt write-off to the fulfilment of the IMF Stand-by Agreement. In addition, the implementation of the whole reform programme would collapse for the second time and Egypt would lose its creditworthiness. The delay was because the pace of reform was too slow from the IMF's point of view and some criteria could not be achieved in the scheduled time. The IMF believed that the criterion on public credit was not observed and its main demands centred on the promotion of public enterprises, wide-ranging trade liberalisation and the amendment of labour law (Nakamura, 1993:54, EAP, 1993). The dissatisfaction with the progress of the privatisation programme was shared by the World Bank as well as being a matter which the GOE tried to correct by announcing the first substantial privatisation programme in Feb. 1993 (Handoussa, 1993). The implementation of such a programme was behind schedule as well and privatisation was always the most criticised area by both institutions. The privatisation programme only gained momentum in 1996 with the new cabinet, since then the international institutions' reports have been more optimistic about Egypt's situation (see details of privatisation below).

#### 4.2.1. The ERSAP: Objectives and Rationale

The development strategy under the ERSAP in Egypt aims at moving away from a public-sector led and inward-looking development to one based on exports and the private sector by eliminating state intervention and freeing market forces. To achieve this the ERSAP had three main declared objectives related to three major policy areas:

- a- to restore the macroeconomic balances of the economy; mainly in the Balance of Payment and Government Budget, and to control inflation through the stabilisation Programme;
- b- to achieve more efficient use of resources, to enhance the capabilities of the financial and productive sectors and to improve the regulatory and administrative framework of the economy through the Structural Adjustment Programme; and
- c- to alleviate the negative impacts of the programme on limited income categories through the establishment of the Social Fund for Development (SFD) (Mustafa, 1994:15).

Stabilisation is a short term programme supported by the IMF stand-by agreement. It aims to restore internal and external balances by applying a demand management policy, which includes expenditure reduction and expenditure switching, using mainly monetary and fiscal policies. The programme assumes that imbalances were caused by excess aggregate domestic demand which is created by excess money supply (Soliman & Kheir El-din, 1992:7) also by distorted prices. Structural adjustment is a medium-term programme supported mainly by the World Bank which deals with the supply side. It contains three main policy areas: price liberalisation, trade liberalisation, and investment reform. Investment reform includes public-sector restructuring and privatisation and improving the investment environment for private activities. Stability was thought to be a prerequisite for market forces to work which also require prices to reflect the real values of goods and factors of production in order to guarantee efficient resource allocation and specialisation in goods with competitive advantage. This argument is built on the assumption that economic structures are flexible enough to allow for supply and demand to respond promptly to market forces (*ibid*) an assumption which should be taken cautiously due to the fact that markets could be incomplete and/or segmented.

The macroeconomic objectives of the programme were to reduce inflation gradually so as to reach 5 percent by 94/95 and thereafter. The investment ratio was expected to rise from 19.5 percent of GDP in 1990/91 to 24.6 percent in 1995/96 with an emphasis on efficient private sector investment. Public investment outlays were to fall from about 15 percent of GDP in 1990/91 to less than 8.5 percent in 1996/97. The saving rate was targeted to rise from an average of 9.4 percent of GDP 1990/91-1991/92 to 16.9 in 1995/9 (the large factor of this increase being higher transfers from abroad). As a result of the reform programme real output growth was expected to gradually recover, reaching 3 percent or more by 1994/95 (EAP, 1993).

#### **4.2.2. Economic Impacts of the Programme**

In this part we evaluate the outcome of the programme in relation to its objective. Different components of the programme will be reviewed before discussing the impacts. This analysis will be followed by a general assessment of its impact on and relevance to the economy.

##### ***4.2.2.I. Stabilisation***

The stabilisation programme was meant to restore equilibrium in the government budget, balance of payment and to curtail inflation.

##### ***The Governmental Budget***

To curtail budget deficits some policies were adopted to reduce expenditure on the one hand and to increase revenues on the other. On the side of expenditure, direct cuts in subsidies and public investment, in addition to the constraint on the growth of wage bills were the main measures adopted. Government investment as a percentage of GDP was decreased from 13.45 in 1990/91 to only 5.5 in 1995/96, and the explicit subsidy burden as a percentage of GDP was reduced from 5.9 to 1.9 during the same period (see Table 4.1).

On the other hand, measures to increase revenues focused mainly on the increase in taxes which succeeded to a large extent by increasing indirect taxes, imposing a new sales tax instead of the consumption tax, stamp taxes in addition to a unified income tax. By increasing revenues and decreasing expenditure the government succeeded in curtailing the deficit from 18.1 percent of GDP in 1990/91 to only 1.3 percent in 1995/96. The government managed as well to stop financing its deficit through borrowing from the central bank (printing money) which was effective in controlling inflation, instead the government relied mainly on the issuing

of treasury bills. The worrying issue concerning the budget deficit in the mid-1990s' Egypt was the increase in domestic lending which in turn led to an increase in the debt service and government expenditure. Due to increases in the interest rate and the placement of treasury bills, interest payment doubled in one year between 1989/90 and 1990/91 (Abdel-Khalek, 1994:46).

**Table 4. 1 Selected Economic Indicators, 1990/91-1995/96** (% GDP, unless otherwise noted)

	1990/9 1	1991/92	1992/9 3	1993/94	1994/95	1995/96*
Real GDP growth rate (%)	3.5	1.9	2.5	3.9	4.7	4.9**
Inflation (% change in CPI)	14.7	21.1	11.1	9.0	9.4	7.2
Consumption	85.9	83.0	83.3	84.9	83.1	86.0
Investment	23.3	18.2	16.2	16.6	16.3	16.7
Government Investment	13.4	8.5	7.0	6.1	5.5	5.5
Domestic saving	16.0	17.0	16.7	15.1	16.9	13.9
Overall Fiscal Balance (excl Grants)	-18.1	-5.4	-3.4	-2.1	-1.2	-1.3
Current Account Balance (including transfers)	5.2	4.1	5.1	0.2	0.6	0.2
Official Reserves \$ billions	6.1	10.6	14.9	17.0	17.9	18.4
External Debt/GDP	107.7	89.5	69.2	58.0	55.7	49.2
Explicit Subsidy Burden	6.3	5.2	2.5	1.9	1.9	1.9

\* Estimated

\*\* Real figure

**Sources:** Ministry of Planning, Ministry of Finance and Central Bank of Egypt as quoted in WB: Arab Republic of Egypt, Country Economic Memorandum; Egypt : Issues in Sustaining Economic Growth, Report No. 16207-EGT, except for GDP growth-rate, calculated directly from MOP figures with a growth-rate 2.5% in 1992/93 different from that mentioned in the WB report (2.9%), and for Subsidy: Ministry of Economics: Egypt Economic Profile, Cairo 1996:12.

### **Balance of Payments**

The main policies in relation to the Balance of Payment were currency exchange, trade and interest rate reform. The currency exchange reform unified the previous multiple price system and established a free foreign exchange market. The reform also involved a devaluation of the Egyptian pound. The devaluation was meant to reflect the real value of the currency, provide more competitiveness for Egyptian exports and reduce demand on imports. Trade reform involved trade liberalisation with most non-tariff barriers were eliminated and the tariff rate reduced (for more detail about reductions in the tariff rate and trade liberalisation, see Abdel-Khalek 1993:26-33, 40-42). Trade reform also included facilitation of administrative measures for exportation and importation, however it seemed that trade liberalisation was more effective on the import side rather than the export (*ibid*:32). While the current account deficit turned to surplus starting from 1990/91 onwards, this surplus witnessed a continuing deterioration and if we exclude transfers it becomes a deficit.

It was the same for the trade balance which continued in deficit, while exports increased imports increased more rapidly. The improvement in the current account balance was not mainly due to the devaluation of the currencies, as it was not the first time that the Egyptian pound experienced devaluation. The previous devaluation did not witness that much improvement in the balance. That was due to the increase in the interest rate of the Egyptian pound, the decline of foreign currency and the liberalisation of the foreign exchange market which encouraged cash inflows (see Korayem 1996:13-14).

### ***Inflation***

The programme aimed at controlling the growth of the money supply. It did so by using treasury bills to finance the public deficit instead of borrowing from the Central Bank, and by constraining credit through credit ceilings. It also aimed at reducing total demand through direct cuts in expenditure and currency devaluation. While these measures were to some extent effective, the programme contained different sets of measures which led to an increase in inflation. This included the direct rise in prices and other measures caused an increase in the cost of production. Such measures were, an increase in the indirect tax and the increase in interest rate. In addition currency devaluation led to an increase in the cost of imports of intermediate goods due to the high intermediate import content of domestic production and food imports. This had its impact on the cost of living (see Abdel-Khalek, 1993 & Korayem, 1996).

As a result of the reform programme the inflation rate was reduced according to official figures from 21.1 in 1991/92 to 7.2 in 1995/96. Many estimates were introduced to calculate the inflation rate and most of them did indicate a decreasing trend. Many economists still think that the usual way of calculating the inflation rate in Egypt needs some updating as regards the component of the basket of goods and the estimated cost to some services in particular, such as housing, health and education (See Fergany 1995, Korayem 1996). While the estimated rate for 1994/95 was 9.4 another study estimated the figure would reach not less than 15 percent (The National Council for Production and Economic Affairs 1995).

#### ***4.2.2.2. Adjustment Programme***

At the core of the structural adjustment measures were price liberalisation, privatisation and trade liberalisation. The aim of this phase was to stimulate market



forces and to improve the environment for private sector participation. It was thought that these together would achieve a better allocation of resources and stimulate growth.

### ***Price Liberalisation***

The policy of price liberalisation aimed at gradually increasing prices and removing subsidies to reflect international prices. Agricultural crops were the first goods to have their prices liberalised, shortly after the subsidies on agricultural inputs were gradually phased out. Energy prices -petroleum products and electricity- were increased gradually to reflect international prices and to eliminate what was considered an implicit subsidy. Subsidies for most food items were eliminated as well, except for one kind of bread considered as a staple food for the poor.

### ***Investment Reform and Privatisation***

Investment strategy in Egypt since 1974 aimed at increasing private sector participation in economic activities. This policy gained more momentum under the ERSAP with two fundamental changes recognising the new strategy starting from 1991. The first was that the increase in the role of the private sector would be supported by a more liberalised economy where government intervention in economic activity was drastically reduced compared with previous eras. The second was the announced policy of privatising public enterprises, in contrast with the era of *infitah* when public sector participation was even increased through its participation in joint venture companies. Two main components of the investment strategies during the 1990s can be recognised, the first was the restructuring and privatising of public sector companies, which will be discussed below under the term "privatisation". The second was the providing of an enabling environment for the private sector based mainly on market incentives, where state participation in production and trade has been reduced providing the legal and regulatory institutions.

### **Privatisation**

Public-sector restructuring was the first step to qualify the PEs for privatisation. They had lost the privilege of cheap credit and subsidies and were allowed to operate under similar conditions as those of the private sector. A new law to organise public enterprises was issued - Law 203 of 1991- which reorganised them into 17 holding companies affiliated to 314 companies. The holding companies were responsible for

managing the portfolio of equity shares of their affiliated companies and for preparing financial and productive policies. The law gave the holding companies the right to partly or entirely privatise them or even to liquidate them (Handoussa, 1993: 7-8, Samak, 1996: 98). The early stages of privatisation were led by tourism and land reclamation.

### **Privatisation- the Strategy**

The privatisation programme in Egypt covers small local government owned enterprises, government share in joint-ventures and public enterprises operating under law 203 of 1991, except companies viewed as strategic. Privatisation started in 1990/91 by selling 2000 small local government-owned enterprises and the selling of one large hotel. In the following years privatisation continued by selling the remaining local government owned enterprises, selling the public sector share in companies law 203, and increasing the private sector share in companies law 97 which had private shareholders (Mohieldin & Nasr, 1996: 68). According to the Public Enterprise Office action plan issued in 1993, companies under public sector law no. 203 who were eligible for privatisation were those of small or medium size, profit makers, commercially viable, operating in competitive markets and with a limited number of redundant workers (as quoted in Samak, 1996: 100). Late in 1995 the Minister of Public Enterprises emphasised that only profit-making companies would be privatised. Loss-making companies would be restructured to be sold when achieving profit level of 10 percent (Mohieldin & Nasr, 1996: 44). In 1996, only fifty-nine companies were considered profitable and were candidates for share offering (*ibid*). Another study revealed that the main percentage of companies in different sectors needed a comprehensive restructuring which in turn needed a long period of time (Samak, 1996: 104). These companies were not eligible for privatisation by private sale or stock flotation and needed a detailed study, according to their financial or technical problems and the type of product. This meant that these companies would absorb a high percentage of the privatisation proceeds which limited the proposed positive impact on the government budget.

In the early stages of privatisation the government adopted a strategy to sell the entire company to an anchor investor. Three companies were sold by this method: El-Nasr for Bottling- Coca Cola; the Egyptian bottling Company- Pepsi Cola; and El-Nasr Boilers and Steam Vessels, while the total sale to anchor investor

was more likely to achieve the privatisation objectives of improving efficiency and productivity through new management and technology. The process was subject to criticism concerning the value of the companies and the sale to foreign investors. The selling of Coca Cola and Pepsi Cola were the most debatable. The two companies enjoyed oligopolistic positions where the first controlled 40 percent of the market and the other 30 percent. Their chances of increasing their oligopolistic position after privatisation was high, which endangered other smaller companies in the market. This oligopolistic position was also claimed not to be calculated in the price. Selling the trade mark of the two companies was not included in the government package, the buyers had to negotiate with the mother company for it who intended not to sell it and to compete themselves to buy the companies. This situation raised the question about other companies enjoying similar positions of keeping the trade mark for themselves. It posed the threat that similar companies would be sold to foreign investors at a low price. These companies were those that had the right to trade marks, or monopoly rights over technology or input materials, as in soft drinks and medical drugs companies (Wahba, 1994: 35-37).

At the following stage the government changed its strategy in favour of minor sales in the stock market. The Egyptian Federation of Industries, which was headed by a private investor, played an active role in this shift in the privatisation strategy. The head of the federation claimed that selling in the stock market was important to revive it and to attract small and medium savings. In his opinion a total sale would destroy the economy (Khamees' comments in seminar discussion of the social and political aspects of the reform, June 1995). Private sector fears from foreign competition could be the undeclared reason. The minor sale strategy was to release a small percentage of the shares in order to test the price and market response. Nevertheless it was a slow process which did not allow major changes in management.

Table 4.2 Privatisation Status to the End of 1996

Company Name	Sector	% Sold	Method of Privatisation
Nasr for Bottling (coca Cola)	Industry	100.0	Private Sale
Egyptian Bottling	Industry	100.0	Private Sale
Nasr Boilers & Stem Vessel	Industry	100.0	Private Sale
Egyptian Electro Cables	Industry	70.0	Mixed
Wadi Kom Ombo for Land Reclamation	Agriculture	95.0	ESA
Egyptian Akkaria	Agriculture	95.0	ESA
General Mechanical Excavation	Construction	95.0	ESA
Egyptian Dredging	Construction	95.0	ESA
General Co. for Land Reclamation	Agriculture	95.0	ESA
Arab Co. for Land Reclamation	Agriculture	95.0	ESA
REGWA	Agriculture	95.0	ESA
Upper Egypt Dredging	Construction	95.0	ESA
Engineering Design & Irrigation Projects	Service	95.0	ESA
Behera	Agriculture	95.0	ESA
Alex. Pharmaceutical & Chemical Industry	Industry	21.0	Stock Flotation
Alex. Portland Cement	Industry	20.5	Stock Flotation
Alex. Spinning & Weaving	Industry	45.6	Stock Flotation
Eastern Tobacco & Cigarettes	Industry	20.0	Stock Flotation
Extract oils	Industry	20.0	Stock Flotation
Middle Egypt Flour Mills		20.0	Stock Flotation
Misr Chemical Industries	Industry	34.2	Stock Flotation
Nasr Clothing & Textiles (KABO)	Industry	37.7	Stock Flotation
Nile Pharmaceutical & Chemical Industries	Industry	20.0	Stock Flotation
North Cairo Flour Mills	Trade	20.0	Stock Flotation
Paints & Chemical Industries	Industry	12.5	Stock Flotation
South Cairo & Giza Flour Mills	Trade	40.0	Stock Flotation
Torah Portland Cement	Industry	32.5	Stock Flotation
ELMACO*	Industry	89.0	Private Sale
Madinet Nasr Housing & Development*		75.0	Stock Flotation
Egyptian Financial & Industrial (EFIC)*	Industry	75.0	Stock Flotation
Egyptian Starch & Glucose*	Industry	59.0	Stock Flotation
United Housing*		8.8	Stock Flotation
Abou Quir Fertilisers*	Industry	2.8	Stock Flotation
Kafer El-Zayat Insecticides Chemicals*	Industry	74.4	Stock Flotation
The Nile Match*	Industry	54.5	Stock Flotation
Miser Oil and Soup*		61.1	Stock Flotation
El-Nasr Dehydrating Agricultural Products*		61.0	Stock Flotation
West and Middle Delta flour Mills*		61.0	Stock Flotation
TeleMisr*		66.2	Stock Flotation
Upper Egypt Flour Mills*		60.9	Stock Flotation
East Delta Flour Mills*		60.7	Stock Flotation
Development and Popular Houses*		65.6	Stock Flotation
Arab Cotton Ginning*		62.6	Stock Flotation
El Nasr Utilities*		90.0	Stock Flotation
El Ahram Beverages*		90.0	Stock Flotation
Helwan Portland Cement*	Industry	29.6	Stock Flotation
Ameria Cement*	Industry	35.0	Stock Flotation
Misr Free Shop*	Trade	61.0	Stock Flotation
United Arab Spinning & Weaving*	Industry	61.0	Stock Flotation
El Nahda Agricultural Co.*	Agriculture	100.0	Stock Flotation
West Nobarria Agricultural Co.*	Agriculture	100.0	Stock Flotation
El Nile Cotton and Ginning*	Industry	61.0	Stock Flotation

Note : \* = companies subscribed for the first time within the privatisation programme during 1996. ESA = Employee Stockholders Association

Source: for the year 1996, INP. 1996. Egypt Human Development Report 1996, others from Ministry of Economy and International Cooperation, 1996. Egypt Economic Profile.

Selling to employees was another method of privatisation. This was applied in 10 companies affiliated to the holding company for public works and land reclamation where 95 percent of their shares were sold to employee shareholders associations. According to Capital Market Law No. 95 of 1992, employee shareholder associations were entitled to buy 10 percent of the shares of their companies. The Association could acquire this percentage, or less, with a 20 percent reduction, and its value could be divided into 8 interest-free annual instalments. During 1996, 5 percent of 10 companies' shares were sold to the Workers Associations. Another 10 companies sold 10 percent of their shares to workers. The total value of these shares was estimated at £E 290 million (INP, 1996: 62).

### **Sales proceeds**

When comparing the use of sales proceeds with regard to the privatisation objective - increasing efficiency, hence productivity and investment and to reduce the burden on public budget - the result is rather contradictory. The sales from all transfers of assets to private ownership during the period of 1994 to May 1996 were estimated at £L 5.37 billion. 34 percent of which was uncollected instalments, 23 percent directed to financial restructuring, 13 percent to re-investment, 17 percent to bank deposits and 13 percent to transaction fees and tax, none of the proceeds was directed to debt reduction ( World Bank, 1997: 30). The largest share was used to restructure public enterprises and to finance its deficits. In this sense privatisation proved to be very costly as it absorbed private savings just to finance the public enterprise deficit. This method replaced the traditional bank credit and still crowded out private investment. The Share of re-investment was rather low, and data revealed that one of the holding companies that used the proceeds of the capital increase- Metallurgical Holding Company - to increase capital in the same company that realised the sales proceeds, while another - the Mining and Refractors Holding Company, utilised the money with several of its affiliates. The use of "cross-subsidies" to prop up ailing firms dragged down the entire performance of public enterprises (Mohieldin & Nasr, 1996:48-49).

### **Privatisation Assessment**

Any assessment of the privatisation programme in Egypt should be made in the light of its objective and of its costs compared to its benefits. Would privatisation

increase efficiency i.e. productivity, investment, and employment opportunities? Would it reduce the burden on the public budget? Would benefits overvalue the losses? This depends to a certain extent on the method of privatisation, the sequence of privatisation and the use of privatisation proceeds.

There have been acceptable agreements between commentators, as appeared earlier, on the importance of increasing the macro efficiency of PEs. Some activities have no strategic importance for the Public sector to participate in it, especially after removing subsidies, and where the private sector can undertake these activities effectively. In front of these activities are those related to the trading in different kinds of food, hotels and restaurants, local enterprises, where the government replaces farmers and the private sector in producing poultry and providing local transportation. Considering efficiency on a micro level, the list could also include the loss-making companies which were used as an excuse for privatisation in the early stages of the debate about privatisation. It is the companies which the government failed for several years to reform and which have been a burden on the public budget and have cost society some lost opportunities for investing the money in other rewarding activities. However, a further investigation of the technical and financial situation is needed to decide which of these companies could cope with the new regulation for PEs according to law 203.

A study on the feasibility of the privatisation of PEs on the manufacturing sector grouped the companies into 6 categories:

- 1- Those that do not need any restructuring and are feasible financially, technically and operationally which turned out to be only three companies in food manufacturing.
- 2- Those that need complete restructuring and which could be done in the short-term.
- 3- Those that need financial restructuring but are feasible technically and operationally.
- 4- Those that need technical and operational restructuring and are feasible financially.
- 5- Those that need complete restructuring over a long period of time due to severe deterioration in financial and productivity indicators and which include a high percentage of companies inside every sector.

6- Those that face more complicated problems and could not be restructured easily. These also encompass a high percentage inside each sector.

The study concluded that companies eligible for privatisation were those in groups 1, 2 and 4 respectively (Samak, 1996: 103-04). This view is based on the same argument used by the government for the sequence of privatisation. According to this view, profit-making companies should be given priority for privatisation while others should be restructured in preparation for selling. This was to allow fair prices and to find buyers for their shares in the stocks market.

One would argue against this strategy however on several fronts, it deprived the government of the revenues achieved by the profitable companies while still burdening it financially by keeping unfeasible companies especially those in groups 5 and 6 which represented the majority. It postponed facing the problems of these companies which would probably be left to the end of the privatisation process in the hope of reducing the social cost. The main problem of privatising or liquidating these companies would be with employment because the low value of these companies had to be accepted. Postponing privatising or liquidating these companies would not improve the value if we consider the long period of time for restructuring these companies, or the more feasible ones, depending on the sequence followed, and the money used for restructuring, in addition to the losses which the government had to cope with during that period.

An important issue in this respect was the use of proceeds and the expected time horizon for the whole privatisation process. There was no declared plan for the different phases of privatisation to assess the progress in the programme. However, short-term plans were recently declared for the prospects of privatisation during the year. Meantime there was no public monitoring for privatisation as it was not represented in the Peoples Assembly and there had been no detailed information about the use of proceeds since the privatisation started. The only evidence we obtained were estimates from the World Bank for a specific period of time while it did not provide information about the restructured companies whose groups of companies were given priority for restructuring. It also did not provide figures about the amount used for employment compensations. The declared strategy now was that main targets for the use of proceeds were those for restructuring and employment compensation, but no more information was provided.

If we accept that the sales proceeds of the profitable companies would be wasted over the long term needed for restructuring other companies, in addition to the unfeasibility of a high percentage of companies to continue or to be privatised, one would suggest some reverse in the sequence of privatisation. The government for example might get rid of these unfeasible companies while keeping profit-making companies for later stages, with minor sales of their shares in the stock market. While the contemporary sequence of privatisation is meant to increase credibility in the programme and to reduce the risk of job losses, the proceeds of the minor sale of profit-making companies can be mainly used for labour compensation. The slowness of the privatisation programme has one advantage of making private savings available in the market to finance the establishing of new private activities rather than directing it to restructuring PEs. It also increases competition between public and private activity which encourages PEs to improve their efficiency or crowds them out. Meanwhile it reduces the burden on the public budget.

The announced goals and rationale beyond the public enterprise restructure according to law 203 of 1991 imply a decline in the need for privatisation of the PE as it allows them to operate according to private sector conditions, curtail their privileges (e.g. access to cheap credit, subsidies & monopoly) then any difference in performance should be due to management and level of technology. A World Bank study (1994) suggested that bureaucratic managers of the public sector are no less efficient than those of the private sector and it is the system through they work which is responsible for bad performance. Improving the system should improve performance, but changing the system in their view means bringing private businessmen not a private system of management. However, in the Egyptian case it is fair to refer to the subjectivity of selecting public sector managers which drives them away from efficient performance. Corruption, and embezzlement among public managers is there due to the lack of effective and monitoring system. However, there are some examples of successful management in the PEs, among which is the case of the Naga Hamadi Aluminium Company. The Performance of public managers in Egypt varies considerably because of some factors related to personal variations in competence and experience and others related to the system. The improvement of the system in the late 1980s proved to have a positive impact on performance, as Handoussa pointed out above. The new law 203 provides a more



favourable economic environment which should be supported with improved political conditions concerning the criteria for selecting the managers and a monitoring system concerning the way they use their power.

Meantime some of the methods used for privatisation used do not bring about substantial changes in management, such as a minor sale in the stock market. The same happens in the case of selling the companies to employees, as the management team is unlikely to change and changes in performance in this case would relate to changes in the incentive system and the abolishing of the central control rather than changes in the ownership type (Abdel-Fadil, 1996:39). However, based on the experience of other countries, it is claimed that commercialisation-increased competition, hard budget constraints, regulation of monopolies, financial market reforms, and incentives for managers to perform efficiently- is not bound to bring changes in investment behaviour and only leads to an improvement in productivity. While privatisation increases both productivity and investment, the improvements in productivity would be higher than in the case of commercialisation. The reason that commercialisation does not change investment behaviour is that the PEs continue to face the same financial constraints they faced before reform. They remain subject to the fiscal constraints imposed by governments, as well as the credit ceiling imposed on the public sector in general. It is also justified by the increased government dividends due to increased profitability, which reduces available retained earnings for expansion (Galal, 1996:8-10). This argument would not be valid if the government left all the constraints on the public sector, allowing it to perform according to the same constraints and regulations as the private sector, and providing its management with more autonomy. Tax system could also neutralise the effect of paying more dividends to the government.

In the case of Egypt, a study based on the assumption that privatisation would increase productivity and investment by 1.5 and 20 percent respectively per annum, and commercialisation would only increase only productivity by 1 percent annually, assuming that 50 percent would be privatised while the other 50 percent would be commercialised in a sample representing only one third of the PE sector in Egypt, it concluded that there would be additional expected savings of about 2.4 percent of GDP (Table 4.3).

**Table 4.3 Estimated Increases in Savings from Reforming the PEs**

	Total Increase in Savings (Millions of 1995 LE)			Annual Increase in Savings (Percentage of 1995 GDP)		
	GOE	Private sector	Total	GOE	Private sector	Total
50% privatisation	-17751	59967	42216	-0.9%	2.9%	2.1%
50% commercialisation	7937	0	7937	0.4%	0.0%	0.4%
50 % privatisation & 50% commercialisation	-9814	59967	50153	-0.5%	2.9%	2.4%

Source: Galal, A. 1996. Savings and Privatisation. Cairo: The Egyptian Centre for Economic Studies. Working Paper No. 8.

Although the study promises more, the savings rate could be up to 7 percent if we consider the total PEs. Based on the following comments, these results must be taken with cautions.

- Not all the PEs are eligible for privatisation, most of them need financial and/or technical restructuring. Privatisation does not happen at the same point in time.
- The assumption that commercialisation will not increase investment while it increases productivity can be challenged using the same argument, mentioned in the study, that productivity will generate more resources that can be used for investment. Increase in investment can also happen in an indirect way if the proceeds of privatising part of the PEs is used to increase investment in the commercialised companies.
- The assumption that the level of increase in productivity in both privatisation and commercialisation is built on single cases related to a certain activity and cannot be generalised for a group of companies with different activities.
- Most gains go to the private sector and if the price paid to the government for the privatised companies is less than £E 17 billion, privatisation impacts negatively on the treasury (*ibid*,:12).
- Privatisation has a negative impact on government savings, while commercialisation has a positive impact. It is a matter of preference for the government and whether it is able to provide other sources of revenue or not. It also depends on the way both the government and private sector utilise these savings.
- Sensitivity analysis proves that savings are most sensitive to changes in investment. This means that gains from increases in investment can be huge and the government must assure that privatisation will lead to increases in investment (*ibid*,:13). This is more likely when the PEs are sold to an anchor investor where it is conditioned to

increase investment a certain amount and where there is a particular mechanism to assure the realisation of such a condition.

### *Private Sector Investment Environment*

Empirical studies have proved that private investment in Egypt is a function of public investment, interest rate, debit ratio and the real exchange rate. In addition to these economic variables there are other important conditions to stimulate private sector responses- see chapter two above. Much legislation has been introduced in this respect, although we cannot investigate in detail the contents of each law. It is to be noted that there have been many amendments in these laws, taxes, and in the capital market which reduce the credibility and predictability in the investment environment. However, the GOE has failed to enact many important laws e.g. the law to regulate the market against the monopoly, labour law, and unified companies law.

It seems that Egyptians lack of entrepreneurial skills. The total sale of private enterprises was won by foreign entrepreneurs. The stock market attracts small household savings, foreign capital and companies working in the security market. The GOE is still taking the initiative in establishing big companies with considerable contribution of capital by public banks. Egyptian entrepreneurs are risk avoiders and seem to avoid involvement in big deals. Nasser's era created generations of bureaucrats who lacked experience and were not risk takers. This was evident from the youth projects introduced by the SFD, where they failed to pay their debt instalments. The crisis in the agency for industrial craft loans which was financed by the SFD to the tune of about £E 60.32 million, where the young investors failed to repay 60 percent of the loan revealed their lack of vocational training and managerial abilities. The loans were disbursed to projects in the absence of visibility studies. Practice revealed the multiplicity of problems concerning the high price of equipment and inputs, lack of infrastructure, high administrative fees and marketing problems (Ahram 13/3/98). While the governmental organisations helped in marketing by organising regional and central local markets for their production, supply could not match the demand needs, due to excess production of some bad quality products. Technical advice and support were greatly needed at production, financial and managerial levels.

### Investment Responses

The share of both public and private investment as a percentage of gross national income decreased in the SAP era compared with the previous period of the second half of the 1980s as can be seen in table 4.4. While the public investment share continued to decline during the reform period, private investment recovered slowly starting from 1993/94. However it did not reach pre-reform levels. This meant that the reform measures failed to increase private sector participation and the fall in public investment was not replaced by private investment which suggests that the crowding out hypothesis does not apply in the Egyptian case. Two empirical studies on private investment in Egypt proved the complementary relationship between public investment, especially in infrastructure, and private investment (Shafik, 1992; El-Khawaga, 1995: 144). This low response of private investment in Egypt raises question about the determinants of private-sector investment in Egypt. Shafik's study (1992) revealed that the factors with a positive relationship with investment in Egypt are those of public investment in infrastructure, available credit for the private sector, growth in total demand, and the profit rate. A more recent study by El-Khawaga (1995) revealed that the main economic variables that affect private investment are public investment in infrastructure, its share of credit, the real exchange rate, and the level of external debt.

**Table 4. 4 Investment and Savings during 1986/87-1995/6**

	198 6/87	198 7/88	1988/ 89	1989/ 90	1990/ 91	1991/ 92	1992/ 93	1993 /94	199 4/95	1995 /96*
% of GDP%										
Gross Domestic Investment	26.1	35.9	32.6	29.1	21.9	18.2	16.2	16.6	16.3	16.6
GN Savings	19.9	31.8	27.4	24.9	20.7	24.7	23.0	15.4	15.9	15.5
Foreign Savings	6.2	4.1	5.2	4.3	1.1	-6.5	-6.8	1.2	0.5	1.1
% of GNY										
GD Investment	23.4	31.9	29.3	26.7	20.1	17.0	14.8	15.8	15.5	16.0
Public Investment**	15.5	20.7	13.6	13.6	12.5	10.0	8.2	7.5	6.6	6.5
Private Investment	8.8	11.3	15.7	13.0	7.6	7.1	6.6	8.3	8.9	9.4
GN Savings	17.8	28.3	24.6	22.7	19.1	23.1	20.9	14.7	15.1	14.9
Public Savings	-0.7	-2.9	-0.8	-0.2	-1.3	3.1	2.5	3.3	3.7	3.7
Private savings	18.5	31.1	25.4	22.9	20.3	20.0	18.4	11.4	11.4	11.2
Foreign Savings	5.5	3.6	4.7	3.9	1.1	-6.1	-6.2	1.1	0.5	1.1

\* Estimates

\*\* The Public Sector includes central and local government, public authorities and public enterprises. Source: World Bank, 1997. Arab Republic of Egypt; Country Economic Memorandum. Egypt: Issues In Sustaining Economic Growth. Main Report. Report No. 16207-EGT.

### *Growth rate*

Cuts in public investment outlays in addition to the increase in the interest rate and the assigning ceiling on credits led to contractionary effects on the economy, hence on the growth-rate. Government reduction in investment expenditure was assumed to crowd in the private sector, however with the increase in the interest rate, the tight credit policy, and weak improvement in the investment environment, the private sector response could not compensate for the decline in public investment. Total investment as a percentage of GDP continued declining from 23.3 in 1990/91 to 16.7 in 1995/6. As a result the real growth rate declined to 1.9 percent in the first year of the reform, 1991/92, and recovered gradually to reach 4.9 percent in 1995/96 and was estimated to reach 5.3 percent in 1996/97, according to the figures of the MOP. The recent report of the World Bank adopted the same high figures of the MOP (WB 1997:1) in spite of a debate between the IFIs and the Ministry concerning the real rate of growth. The IMF's earlier estimation of real GDP growth were 2.3 percent and 2.8 percent for the years 1991 and 1992 respectively, then the fund provided a revised estimation of 1.1 and 4.4 percent for the two mentioned years respectively. According to the World Bank (1993), the real GDP growth rates were 2.3 percent (1990/91), and 0.3 percent (1991/92). The EIU estimate for 1992/93 was 0.5 percent (as cited in Ibrahim & Lofgren, 1996:171-72). The World Bank report for 1996 estimated the GDP growth during 1990-94 was only 1.1 percent.

The ability of the programme to enhance growth on a sustainable basis is in question as it lacks a clear mechanism for growth. There is no evidence on the direct relationship between outward directed policies and trade openness and growth. Even if trade openness could increase the flexibility of the economy and provide a greater ability to absorb external shocks, financial openness could considerably reduce this ability to adjust to such shocks (Bromley, 1996:63).

Estimates of the final effect of the reform measures on per capita income varied and in the best estimates improved slightly. However, these improvements were not evenly distributed between different socio-economic categories, as I discuss below.

#### **4.2.3. The Distributional Impact of Economic Reform**

Structural adjustment has distributional impacts upon various socio-economic groups. It can affect their cost of living, their incomes or both. As a result some

groups benefit and others lose in what Abdel-Khalek has called a zero sum game (Abdel-Khalek 1987: 20). In fact we do not consider it a zero sum game if the losers outweigh the gainers or if the final result is a clear deterioration in income distribution.

### *Employment*

The decade of the 1980s witnessed an increasing unemployment rate. That was due to many factors which were accelerated in the second half of the decade by the stabilisation measures which caused a stagnationary effect and because of government policy to stop employing new graduates. During the 1977/78-1981/82 and 1981/82-1991/92 periods, the average annual growth-rate of employment dropped from 3.8 to 1.8 percent. If we exclude the agricultural sector, public recruiting used to be the main source of employment amounting to 33.1 percent of total employment in 1986/87. This decreased to 30.9 percent in 1992/3 (INP, 1995: 60). The unemployment rate was officially estimated in the 1986 Population Census to reach 10 percent. The labour force sample survey (LFSS) which provides the annual source for unemployment rates, refers to increasing trends of the rate. Both estimates of unemployment are biased downwards. The LFSS is further underestimated, in addition to the change in the definitions of unemployment used over time (for more details see, Fergany, 1994, 1995; Korayem 1996; & NPI, 1995). In 1992 the LFSS estimated unemployment to be between 9 and 10 percent. A corrected estimation, which considered the phenomenon of those who became discouraged from searching for work because of the high level of unemployment in addition to the imperfection of the labour force, raised the rate to 17 percent (INP, 1995) while Fergany's estimation is higher: 20 percent (Fergany 1995: 5). It should be noted that the burden of unemployment falls more on low-income groups, thus increasing the degree of human deprivation (INP, 1995:62)

### *Social services*

Education and health are the two main services that affect human development. In Egypt expenditure on these two sectors is low compared with developmental needs. During the SAP, allocations for both sectors deteriorated. In Education, one study estimated that government expenditure on education as a percentage of total public expenditure fell from 16.7 percent in 1970/71 to 10 percent in 1989/90, while expenditure as a percentage of GDP was estimated to have fallen from 3.9 percent to

3.3 percent (Nassar, 1996:137). Another study estimated the fall of educational expenditure as percent of GDP to have fallen from 3.6 percent in 1989/90 to 3.2 percent in 1992/93 (INP, 1995:37). The investment needed to achieve educational targets during the last five-year plan was estimated to be worth £E 14 billion, however it was finally trimmed down to £E 7 billion (*ibid*). This reduction was reflected in a deterioration in the capacity and quality of the service provided (for more details about the deterioration in schooling capacity and quality (see Fergany, 1994, 1995; Nassar, 1996). Girls and the poor are the most affected groups as they suffer greater deprivation of the service than others on account of social issues. The result is that education seems to have become a tool to increase social discrepancies between different social classes (Fergany, 1995:20).

Health experienced the same bias in expenditure and a deterioration in services and facilities. The percentage of expenditure on health to total expenditure declined from 4.8 percent in 1970/71 to 1.9 percent in 1989/90, while the percentage of expenditure on health in relation to GDP is estimated to have declined from 1.2 to 0.6 percent during the same period (Nassar, 1996:137). Another study estimated the percentage of expenditure on health relative to GDP during 1989/90 and 1992/92 to be stable at 1 percent (NPI, 1995:38). Both estimates refer to a wide shift from the level recommended by the WHO which was 5 percent. The result was a deterioration in the quality of service which resulted in turn in a deterioration in the health status of the people, as health indicators refer to Egypt's position as being the worst compared with other countries in the Middle East and Africa (for more details about the health situation in Egypt, see Nassar, 1996 & INP, 1995).

### *Poverty*

Available data on poverty revealed that the percentage of poor people who were on or below the poverty line<sup>3</sup> has increased in Urban areas from 30.4 percent in 1981/82 to 35.9 percent in 1990/91, and in rural areas from 29.7 to 54.5 during the same period (Korayem, 1996:41). In other estimates the percentage of the total population below the absolute poverty line increased from 29 percent in 1981/82 to 35 percent in 1990/91. For urban and rural areas it increased from 30 and 28 percent to 36 and 34 percent respectively (INP 1995:63).

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<sup>3</sup> Poverty line was defined as the minimum income that allows a household to buy enough food to meet biological needs plus a minimum level of non-subsistence goods and services to satisfy non-material needs.

The characteristics of the poor confirm our above analysis about the most affected groups under the reform measures. The poverty of the head of the household was more wide spread in some occupational categories than others. An analysis of the survey data regarding income and expenditure research shows that the “unclassified” category, the marginalised, if taken into account, represents the majority of the poor in both the urban and rural areas (INP, 1995: 63). This group is followed by those whose household heads are “outside the labour force” in both areas. Then in the urban areas, come those who are engaged in services, if we are considering both the incidence and intensity of poverty. However, the contribution of the production and transport workers to overall poverty is high because of the relatively large number of households in this occupation. Meanwhile in rural areas, households designated as headed by “self-employed” (mainly small land owners) come next. Both those “outside the labour force and those who are self employed” contribute more to national poverty than their share of the total number of household, which means that these categories suffer severe poverty problems. The category of agricultural workers, ranks third in terms of the incidence of poverty, however it is the largest group in terms of its share in the number of households in the sample (El-Liathy & Kheir El-Deen, 1996:494-5).

Distribution of income deteriorated between 1981/82 and 1991/92 as the Ginni coefficient increased from 0.32 to 0.38 in urban areas, and from 0.29 to 0.32 in rural areas. In the following years there is evidence that the gap between the poor and the rich had widened. It is clear from the above that cuts in subsidies mainly affect the poor as they spend more on subsidised goods, the burden of unemployment falls more on low-income groups and so does the cut in government expenditure on social services. Data based on a survey by CAPMAS and the Social Fund for Development (SFD), revealed that the income shares of the poorest 20 percent of the population and that of the lowest 40 percent, declined from 7.4 and 19.5 to 5.9 and 17.0 percent of total income respectively between 1991 and 1993 (INP, 1995:63-4).

### ***4.3. The Debate about Economic Reform***

This part analyses different views, perceptions and attitudes about the Egyptian main political actors, political parties and academics towards the reform policies, their nature, pace and components. It illustrates what were the different views concerning



the main cause of Egypt economic problems? What were the different available alternatives of the different ideological and political attitudes? How did these views change over time? How far were representatives of different views and parties able to influence government policy?

#### 4.3.1. Characterisation of the Problem

There has been a wide consensus on the main problems of the Egyptian economy, yet different explanations have been expressed to clarify the causes behind these problems. In the early 1990s a new trend was crystallised with the World Bank explanation of the problem. This trend which consists of some liberal as well as more conservative academic with intellectual ties to the USA or the World Bank (see EL-Naggar 1991, 1997; Shihata 1993, 1995; Handoussa 1993, Soliman & Kheir El-deen 1992) put government intervention in a central place in their analyses of the causes of the problems. The liberal economist El-Naggar (1991) blamed the economic system adopted which was based on central planning and state control over a considerable part of economic activity in addition to massive bureaucratic control over the economic decisions. He thought that this system had not changed even during the period of *infitah*. He criticised those who saw *infitah* as responsible for the problems and thought that it was not successful due to the partial nature of liberalisation and the continuity of bureaucratic control. He also refused to blame external shocks or population growth as responsible (El-Naggar, 1991:16-24). El-Naggar blamed the public sector for most of the structural problems of the economy. He argued that public-sector losses led to budget deficits which in turn were covered by printing money leading to inflation. He also argued that while public investments received 70 percent of total investment, their efficiency was very low and this failed to generate job opportunities, hence deepening unemployment. As the public sector was responsible for 80 percent of Egyptian exports and imports, exports were falling drastically and imports increasing, resulting in an increasing deficit in the balance of payment. As a result he considered the public sector responsible for 40 percent of Egypt's external debt (*ibid*,:38-42).

Handoussa (1993:4) argued that "the sources of failure can be found in the nature and scope of state intervention, in the set of closed economy macro policies pursued (albeit in a diluted form after the *infitah*), and in the poor management of state institutions and planning." Soliman & Kher El-Deen (1992) believed that

“Experience has shown that distortions can result from government interventions as much as from market failures. A system of deliberate intervention in resource allocation through direct control and commands may conceivably create more inefficiency in production, investment and growth than would result from a given economic policy under a market system.”

El-Naggar's views were fully adopted by the Wafd party and officially reiterated in the party's political report considering the public sector the main entity responsible for all economic ills (Mossaad, 1996:83). The National Progressive Unionist Party (NPUP) thought that the problem was structural in nature rather than a trade-off between public and private. Abdel-Khalek argued that profit was theoretically independent of the ownership type. As evidence for this the NPUP stated that until 1990 the number of loss-making companies in the private sector was 600. The NPUP also refers to the experience of private sector in the open door policy as they use their capital in speculations, financial and commercial activities and light consumer industries (*ibid.*:86,94). Abdel-Khalek diagnosed the crisis as a Dutch disease. This was where the tertiary sector has grown massively while production sectors had diminished. This situation had implications on the economy as it complicated economic management, affected the equal distribution of income and wealth, employment generation, and on economic relations with the foreign world. Abdel-Khalek blamed the adopted policies for their failure to deal with the crisis. From his point of view, they weakened the productive capabilities while developing consumer possibilities and attitudes. He emphasised the importance of expanding the commodity-producing sectors and blamed the food deficit for structural imbalances in the economy (Abdel-Khalek, 1987:18; 1997: 138-39).

The labour party agreed to a large extent with the NPUP views and accused the government of lacking “a clear vision” in assigning strategic national goals and methods of implementing them (Mossaad 1996:83). Hussein also stressed the dependent relationship between the Egyptian economy and international economy developed during the past and which continued to prevail and which hindered any attempt to achieve real development. In addition to this views concerning the relationship between the Egyptian and the international economy, he argued that corruption and waste in the internal arena were responsible (Hussein 1993 as quoted in Ibrahim, & Lofgren 1996:186). The national feeling regarding the need for a

national vision or project that united public hopes and through which they could tolerate the immediate costs of the reform for future gains was increasing. This vision which the government failed to provide was one of the shortcomings of the reform (see Ibrahim & Lofgren 1996:160). The Muslim Brotherhood stressed the mismanagement of the economy and the socio-political environment. They thought that all the factors needed for production were available to the Egyptian Economy; land, finance (as proven from the experience of the so-called Companies of Islamic Employment of Money) and the labour-force. In their opinion, people needed freedom merely to stimulate them to produce and participate in political life, hence in the economic decision-making process, and to abandon negative behaviour of participation (EL-Ghazali, 1991:72-73).

Shihata itemised five main causes for Egypt's problems. First, the massive increase in population with limited arable land, and spontaneous growth in urban areas. Second, the poor strategy for human resource development. Third, the irrelevant economic policies which encouraged consumption and importation while discouraging production and exportation; expanded the public enterprises units and constrained private sector expanding; where subsidies were unlimited to the poor and where the exchange rate and interest rates were unrealistic and discouraged savings in favour of capital-intensive investments; and which showed increasing dependence on unsustainable sources of foreign currencies. Fourth, inefficient resource allocation where little attention was given to the protection of agricultural land and the environment. And finally, due to some negative cultural aspects of the public concerning consumption habits and the work ethic. In general, Shihata argues that most economic policies were issued to satisfy people- for political considerations- than for economic rationality which considered the medium and long-term effects (Shihata: 1993: 44-7, 104-6).

In my opinion state intervention in the economic policy is not the only factor to blame. Some aspects of the policy of state intervention were harmful. The setting of mandatory prices for instance for the agricultural sector resulted in negative internal terms of trade between the agricultural and the industrial sector. In this case the need to correct the prices was for economic and equity reasons as well. Other aspects, such as subsidies and the public sector, played a social role in supporting the poor. However, as Shihata pointed out the problem with subsidies was that they did

not differentiate between the rich and the poor. The poor management of state institutions which was referred to by Handoussa, was related to the state's capacity rather than to the applied development model. The need to improve administrative performance and to control corruption, cronyism and patronage networks remained with all types of development models.

On the other side of the equation the official political discourse of the state accused people of being responsible for Egypt's main economic problems. The rapid increase in population in addition to their extravagant diet, increased consumption massively and caused a food shortage. It also led to a strained infrastructure and finally was responsible for increased borrowing from foreign sources (Wahba, 1993:53-54). This view of course is one-sided and ignores the role of state policies in reshaping consumption patterns through an undifferentiated subsidies policy, the sudden openness of the economy and the applied trade policy, and the effect of stimulation and imitation which were enhanced by advertisements. It also ignores the effect of state policies on the supply side which was the main cause for a deterioration in production. This study will discuss in detail the role of such policies in the agricultural sector, and the food deficit.

#### **4.3.2. The Role of the State**

The role of the state occupies a central place in the debate about reform. As Egypt underwent a state-led development in the past, now, it is moving towards a neo-liberal development model with the support of International Financial Institutions, in which the role of the state diminishes considerably. In delineating this role many other important issues follow. It means, at the same time, a matter of reshaping the roles of the two other actors in society: the individuals, especially the entrepreneurs, and civil society. It also decides the nature of the reforms needed in other areas rather than the economic sphere, in which areas the state has to strengthen its capacity, in which areas it has to be left to civil society and what are the social commitments and political ambitions of the new entrepreneurial class. In short, the reforms needed in the political, legal and regulatory areas all related to the anticipated role of the state. It must be agreed that the role of the state relates to a great extent to its role in the past and how successful it was in performing it. It also relates to the changing nature of this phase of development very much closer to changes in the international arenas.

Egypt's experience with state-led development and the different results of the assessment of this experience shaped the views of the debaters for its anticipated role in the new era of liberalisation. The increasing dominance of the ideology of liberalisation and globalisation in the international arena has its effect in shaping these views as well. A general area of agreement in discussing the role of the state is the effect of the type and nature of the current socio-economic system and its relative level of development compared with the developed countries; and the direction and speed of change in the developed countries concerning liberalisation, globalisation, and technological change and innovation, a point which has been noted by most debaters, however, with different degrees of emphasis (see for instance, Abdalla, 1989; Beblawi, 1989, 1996; & Handoussa, 1994).

Abdalla (1989) stresses the variations in the state's role according to: the resource base of society -e.g. oil, irrigated agriculture- ; the socio-economic system which varies at different historical stages; the position in the international system, as the role of the state in the advanced core countries differs from that in developing countries; and variations in cultural characteristics and the attitude of the ruling elite. His analysis is valid for Arab countries in general and is not exclusive to Egypt. He thinks that the state in Arab countries played a dominant role in the pre-colonisation era as a tool for recovering resources from foreign control. He develops his argument by relating the role of the state to the targeted type of development in the Arab countries which, in his view, should be independent development dominated by a coalition of labour, farmers, intellectuals and national capitalists. He delineates seven areas where the government should have an effective role: controlling and exploiting the mining resources; mobilising and allocating resources; developing human resources; supporting technological development; building an infrastructure; redistributing wealth; and economic management of the economy. I will elaborate on the most debatable issues which are the role of the state in resource mobilisation and the allocation and the distribution of wealth. He argues that as the state controls a considerable part of the revenues of oil rents, it is responsible for converting these resources from depleted resources or wealth to sustainable productive assets. He further argues that the behaviour of the Arab capitalist is biased towards investment in housing, in the commercial, financial, and tourism areas more than in manufacture and agriculture. These two considerations apply, to some extent, for the first and to

large extent for the second, in the Egyptian case. He thinks that market forces cannot be used to decide the investment size or components. It is the state that should play the fundamental role in resource mobilisation and allocation. Productive public investment is important to balanced development and for society to control the strategic industries, in addition to Arab national security. At the same time he accepts the participation of the private sector and realises that the state is responsible for providing stability in the economic environment, and for safety and incentives for private capital. While Abdalla is in favour of central planning he realises that it should be indicative of prospective growth and its components. It represents the economic policy of the state which regulates economic activity through market forces. In his view, public enterprises should have a financial and administrative independence, where the market is the tool to check the validity of decisions and plans and the efficiency of management. The opinion of Abdallah reflects the realisation of the drawbacks of intensive government intervention in economic activity, which impedes efficient management. However, the notion of using central planning - even in an indicative way- with market forces, raises many questions about their compatibility, and indifference to the notion of the participation of public and private enterprises in economic activity. Abdalla encourages an effective role for the state in the distribution of wealth and income as he sees the income and wealth gap increasing. He believes that market forces cannot achieve equitable distribution. Nevertheless he is against nationalisation and public ownership, except in extreme cases of reducing the power of big monopolies. Rather he believes in coherence policies of production and resource allocation, technological choice, taxes, subsidies, providing public goods and distributing them equally, distributing economic activity between different areas and regions, a targeted programme for backward and poor areas, and social insurance networks. It is the responsibility of the state to provide the legal framework which enables the establishment of civil organisations to advocate the interests of vulnerable groups. The most important point is that Abdallah realises the dynamic role of the state which could change according to the needs of society. In the case of the availability of mature public organisations which can defend the interests of the poor and vulnerable groups the state can give up its responsibility, or part of it towards these groups (*ibid.*:316-317).

El-Emam (1995) the former Minister of Planning is still the main supporter of the government's intervention in economic activity. His view is related to "social efficiency". When the private sector increases the polarisation of wealth and unemployment he does not consider it an efficient system at all. El-Emam explains that capitalist states developed the societal system under which the market operates. He conceives the state as responsible for two main issues: continuous management of the economy- whatever the management method- and long term development. Where the market fails to direct decisions for long-term development, he refuses the notion of indicative planning, and favours comprehensive planning, as the market could move in the opposite direction, then the plan would be useless, and he argues that the market should not be the leader, rather than an effective indicator. Using the same argument of El-Emam one would ask here about the conditions necessary for the private sector to work in accordance with the comprehensive plan. Would this require more regulations and intervention in private activities which in turn would suppress the private sector. The main question is related to the extent of state intervention needed and the form of intervention, how the state manages economic activity in a way so as to achieve suitable mix between public and private.

Nevertheless, the debate about the role of comprehensive central planning would not be valid if we accepted the argument of the former Minister of Planning Dr. Abdel-Rahman (as quoted by El-Said & Othman, 1993) that planning was not used effectively and was mainly concerned with the distribution of investment for certain projects and provided some estimation about macroeconomic variables, which implied that the planning did not include detailed economic policies. The Ministry of Planning was also not allowed to deal with the public budget which meant that it dealt with financial resources without having control over them. EL-Naggar (1993) suggested that planning and planning institutions should be replaced by economic policy and economic policy institutions. While these views were partly acceptable for some academics and planning experts in the light of the already existent limitations of the planning process, they added still more needed functions under the market economy. Abdel-Khalek (1993) asked for a restructuring of the state to reduce its size and increase effectiveness. In addition to the macroeconomic policies, he believed in the need for a role to deal with the long-term aspects. This could be by estimating the prospective developments in the economic and political

spheres, deciding areas of potential competitive advantage and then deciding according to them the targeted change. Othman (1993) added the supervision of the investment programmes both public and private.

The above discussion reveals that there was more acceptance of the need for the state to reduce its intervention in economic activity, more acceptance of the role of the market in resource allocation. However, there was still no agreement on the distribution of roles between the state and the market, but there is a realisation that they were not absolute alternatives rather they complemented each other.

In defining the role of the state, El-Beblawi (1996) distinguished between three actors: the state, individuals, and society. He related each actor to a certain tool, state/politics, individuals/economy, and society/ethics. The state had the political power, the individuals were the main users of the market, while society contained values and ethics. These three groups were complementary, the state had to use its power, which was legal power, to provide the institutional framework to arrange between politics, economy and ethics in order to support the market system. According to Beblawi, state power was important to maintain the market economy and not to replace the market or ethics. He was biased towards the market economy which he saw as a part of a globalisation trend, however, he realised that globalisation should consider the national interest. In the economic sphere he conceived state role as responsible for providing public goods as markets work according to the rule of exclusion and did not accept free riders. Public goods included a wide range of public services as well as institutions: justice, defence, communications, transportation, education, health and scientific research. However, providing public goods should not be limited to public companies. The second economic job was to achieve social justice by providing decent living conditions to vulnerable groups and to reduce inequality. The problem of whether or not free competition provided social justice as claimed by liberalism and the limit of state intervention to achieve social justice could be solved, from his point of view by a democratic regime. The third job was to plan and apply macroeconomic policy in order to achieve stability, provide conditions for economic development, free competition, and employment opportunities.

Handoussa (1994) believed that the state's role exceeded the neo-classical views of stabilisation, regulation, redistribution and correcting market failure in



order to maintain the incentive structure for resource allocation. Based on her reassessment of the competitive nature of global markets, the dynamic implications of growth and the increasing importance of knowledge and organisational dimensions of development she concluded that the state had a vital role to play in the process of catching up. This role was to promote innovation and change through education, science and industrial policies. This emphasised the previous views concerning the role of the state in long-term development.

Eliwa (1998) believed that the fast technical, economic and social changes which distinguish this era effected morals and human values and increased public tension, conflict between the masses and the elite and between the political elite and the ruling elite. New characteristics which appeared in modern states were responsible for these tensions. Excessive privatisation and bureaucratic dismantling, dismantled the state while competition and market values created consumption ambition and the desire for possession so as to be conspicuous, which increased conflict between different social groups. Meantime the increasing transparency which uncovered the luxurious life of the ruling elite increased the feeling of deprivation for the middle-class and the poor. In his view, the state had a role in public tension management which was part of the crisis management depended on an early warning mechanism (Eliwa, 1998).

What Eliwa mentioned applied to the Egyptian case to some extent, when the income gap between different groups increased and consumption of luxuries was the subject of comment in some national newspapers, which urged some social scientists to discuss it in the newspapers. The role of the state here was protective of the social coherence by monitoring the income gap between different groups and by using the media to encourage productive values and a work ethic.

The above discussions about the role of the state and that of the market emphasises the need for an effective state. However, there is an increasing acceptance of the role of the market and the complementary nature of the role of the market and that of the state. While there is no consensus about the appropriate mix between state and market we can conclude several themes. As central planning was not applied effectively in the past we can not ask for it now, but the long-term perspective of development should be considered. This should not prevent the state from planning and implementing macroeconomic policy for stability, free

competition, and fair distribution. It should be concerned with setting long-term strategies for education, science and technology, and the environment, as well as in their implementing (as part of the process of catching up referred to by Handoussa). This does not exclude the private sector from participation. For the market economy to work under free competition conditions and from long term perspective of development the state is responsible for providing the necessary information and directing activities to areas of competitive advantage. The state has to enhance its capacity concerning the provision of the legal, regulatory, and organisational framework, as well as in implementing them. The role of the state could change with progress in both the economic and political arenas. With the increasing pace of democratisation and development of civil society organisations the state can relinquish some of its tasks to civil society organisations which can defend the interests of various groups. This matter will be related to the degree of democratisation and the morals of society, which determine the social role of the new emerging capitalist class.

#### **4.3.3. Privatisation Debate**

The argument to justify the need for privatisation in Egypt is based on the efficiency issues and the international orientation towards privatisation. While there is nothing intrinsic in the public sector that makes it less efficient, experience tells that the private sector is more efficient using financial criteria. This was also true for the Egyptian public sector (see Abdel Rahman and Abu Ali, 1989). Moreover, it was also argued that the increase in the size of the public sector was the cause of the deterioration in its management. This is the same as in the case of the small projects which they benefited from the economies of scale which increases with the increase in their size but beyond a certain size their efficiency decreases (Abu Ali, 1989:377). This could be true to a certain extent from the fact that it is centrally controlled while the increase in the varieties of activities needs more flexibility in response to changes in market conditions. It has recently been argued that it can increase savings either because of an increase in productivity, as claimed with the experience of privatisation in developing countries, or by attracting savings from abroad, which may not be possible without privatisation (Galal, 1996:1). For this justification the question might be how much savings? and is it possible to achieve this without privatisation? Is there other ways to attract savings from abroad rather than from

privatisation especially for the flight savings? Ayubi's (1995) view of privatisation is that it is "not a result of careful evaluation of either the contribution of public sector to development, or the managerial efficiency of the public enterprises. Rather it is a response to the fiscal crisis of the state, reinforced by pressures from agencies of the international capitalist order and encouraged, to some extent, by international fashion" (p4).

The argument of Ayubi is true to a large extent as the effect of the global orientation towards privatisation and of the financial crisis driven from the development of the argument about privatisation. In the early 1980s many academics and politicians still thought that the public sector, in spite of its losses, had a strategic and crucial importance for the Egyptian economy. In the late 1980s there was a realisation of the need for a partial privatisation or liquidation of public sector in order to increase its macro efficiency and to reduce financial constraints. During the 1990s there was a greater orientation towards privatisation of most public sector units. We can say that privatisation was treated as a goal rather than as a means because the criteria for privatisation put greater emphasis on profit-making companies as they seemed more feasible for privatisation. This criterion is at odds with the justification of the privatisation process, which is that of improving efficiency.

In 1989, Abdel-Rahman and Abu Ali wrote "Privatisation does not mean the abolition of the public sector. It is one of the facts of life that the public sector is here to stay, regardless of ideology and the prevailing social system" (p13). The contribution of the public sector to the economy even under the policy of *infatih* was significant. Handoussa estimated in 1990 that the public sector contribution to law no. 43 concerning joint ventures was a share of about one third of the total investment cost of the projects approved. This significant contribution prompted Handoussa to comment that "...the large public sector that had spread its weight across the economy was here to stay.." (Handoussa, 1990:146). Handoussa blamed the high degree of centralisation and rigid legislation regarding finance, pricing, and wage determination as responsible for making investment decisions of low priority for the economy. To relieve financial constraints on public enterprises and to attract savings into high priority public investment Handoussa suggested that they should be allowed to sell their shares on the stock market (*ibid.*:172). In a different study

Handoussa (1991) praised the increased autonomy given to public enterprises in the late 1980s which in her view led to significant improvements in their financial and economic performance. Handoussa called for the selective privatising or liquidating of some areas where the PEs operated. At the same time, she realised the importance of productive enterprises in the development process and asked for financial support from foreign donors and creditors (Handoussa, 1991:15).

Abdallah (1989) agreed about the privatisation of loss-making companies. He agreed with reorganising, incorporating or liquidating public units if keeping them would lead to a loss in wealth and income instead of an increase. He was driven by public interest which conditioned the privatisation by using the proceeds to provide public investment in other needed activities (Abdallah, 1989: 317).

During the 1980s, the official political discourse also assured the continuity of the public sector and the emphasis on its central role in the development process. However, this does not mean that there was a consensus in the ruling party or even the government. The decision for major changes in economic policy seems to have been taken at the presidential level. President Mubarak's speech to the Fourth Conference of Egyptians' Working Abroad in 1987 referred to the losses in the public sector (about 11 percent of its companies were loss making). However he asserted that this did not mean that it should be sold. The president confirmed that he would not allow any violation of the public sector because it was the only grantee for the poor. Meantime the president refused the idea of the public sector opening restaurants or even managing hotels (as quoted in Issawi, 1989:326). In 1988, the Prime Minister Dr. Sedqi insisted that the Public sector was the balancing factor in economic and social life, so it could not be given up (*ibid*). The Minister of Industry, Mr. Abdel-Wahab also confirmed that encouraging the private sector did not mean the sale of the public one. It meant only an increase in the share of the private sector in economic activity and the public sector had to intervene when the private sector gave up a certain strategic activity. On the other hand, Dr. Sultan adopted the idea of selling part of the public sector's successful units either in the Egyptian, Arab or the foreign stock market (*ibid*,:326-37). However, in May of 1990, President Mubarak for the first time announced that privatisation was to be undertaken on a significant scale, including state-owned shares in 200 joint-ventures.

Emphasis was given to the privatisation of local enterprises (as quoted in Handoussa, 1993:6).

For the political actors privatisation was one of the most controversial issues and the debate took an ideological turn, which the government tried to use against those opposing the SAP. The Wafd party was the main supporter of privatisation among the different parties. El-Wafd was “in favour of the monarchy more than the king” as it accused the government of bias against the private sector and constraining it by restrictions. They took an antagonistic attitude towards the January 1985 decrees, for instance (see Mossaad, 1996:93). El-Wafd went further and thought that the existence of the public sector limited the opportunities for the private sector to expand. They thus repeated the neo-classical view that the public sector crowded out the private sector (*ibid*). It was the same thought emphasised by El-Naggar that monetary policy with a low (negative, due to inflation) interest rate and credit policy enabled the public sector to have access to credit which crowded out an efficient private sector (El-Naggar 1991:130). On the other hand, the NPUP was the strongest defender of the public sector and the right of its employees. Opponents of privatisation based their argument on three grounds. First, that the public sector had an important social and economic role. Second, that the public sector had a role in national security especially for large strategic companies. Third, that profit was theoretically independent of ownership type. As evidence of this the NPUP stated that until 1990 the number of loss-making companies in the private sector was 600 (Mossaad, 1996:86). The NPUP also referred to the experience of private sector in the open door policy, as they used their capital in speculation, financial and commercial activities and light consumer industries rather than productive activities (*ibid*,:94).

The way that privatisation took place was also subject to criticism even by those who favoured the process. They thought that the programme was launched without public or even parliamentary participation and that there was no public censorship. It was forgotten that the sales were a means rather than an end in themselves (Wahba, 1994). Wahba also warned that the Egyptian economy was a monopolistic rather than a competitive economy and warned the decision-takers not to hand over this monopolistic structure to the private sector, especially if it was

foreign (*ibid*). Sales to foreigners were one main criticism of those who opposed privatisation and some of its proponents as well.

#### 4.3.4. Debating Structural Adjustment

In 1990, while negotiations with the IMF were at a critical stage some economist and political actors with different political perspectives explained their caution concerning the effectiveness of the IMF package and its ability to solve Egypt's economic problems. They thought that it was only an emergency, short-term remedy and that while its effect was also limited it is very harmful as proved in some African countries (see Abou-Ali; Basheer; Hussein 1991:28-31). Meanwhile they agreed on the need for fundamental changes to increase production and improve productivity, changes that could lead to long-term development. They also realised the need for other measures rather than the pure economic ones such as improving the education system, adopting and developing new technologies, in addition to political reform (*ibid*).

In searching for a suitable economic strategy or alternative to the proposed policy some accused the opposition of not having any real alternatives and that their suggestion did not in fact differ fundamentally from those proposed by the IMF. They only attacked the reform because it was proposed by the IMF which they saw as an instrument of imperialist power (Abu-Ali 1991:28). The Muslim Brotherhood, the most active opposition, for instance was accused by some writers of not providing a clear economic vision concerning economic reform and that their views were limited to some aspects of banning usury or usury and liquor; substituting *Zakat* for the current taxation system and internalising the Islamic work ethic and value of compassionate mutual help "*Takaful*" throughout society (Mossaad, 1996; Ibrahim & Lofgren, 1996:187). These views were limited to scattered articles in the Labour Party newspaper "El-Shaab". However a review of the writings on Islamic thought about economic activities provides more views about the role of the state and whether it has the right to interfere or not, and the state's role in regulating markets against monopoly, cheating, and unfair pricing. The role of the state and society was to provide a level of "Kfaya" that is one that provides the needs of people to live at an average common standard which is above the level of basic needs. It also regulates the relation between the employers and the employees (Saker 1990). The Muslim Brotherhood emphasised that they had a vision to deal with all

aspects of economic problems including inflation, unemployment, debt, subsidies and so on, and that the Islamic economy was not only established to prohibit usury and that some investing companies of employing money had misleadingly used the Islamic banner. They thought that the Islamic method was comprehensive and had only been implemented in the era of Khalifa Omer ben Abdel Aziz (EL-Gazali, 1991). The activity of the Muslim Brotherhood was legally banned. It was logical for them to stress political reform in order to gain their political legitimacy and to be able to explain their economic views. They suggested some practical actions to deal with Egypt's economic and political problems. They called on the intellectuals to agree upon a clear programme with clear and necessary changes during a specific time-frame to be submitted to the decision-takers. To force the government to respond positively they called on all parties to withdraw from the People's Assembly as its legitimacy was questioned by many political actors. The need to call for civil protest was suggested not in the cause of anarchy but to force the government to respect the people's will (*ibid*). However, in 1994, the request for a national debate was initiated again and the Muslim Brotherhood was set aside. In order to gain legitimacy and in a search for legitimate channels to express their views some members declared their separation from the group and tried to form a political party in coalition with some Christian members. Those who initiated the call for establishing a political party were arrested and imprisoned after a trial accusing them of forming an illegal organisation.

In the search for a suitable political and economic strategy many forces emphasised the need for a development strategy with an Egyptian, or Arab, identity (Abase, 1991:39) which does not exclude the need to benefit from the experience of other countries (Shihata, 1993:21,48). The notion of independent development was conceived and completely adopted by many parties and thinkers that opposed the liberalisation and openness of the economy. In this respect both the labour party, the NPUP, and the Muslim Brotherhood shared almost the same views (see for instance the writings of Hussein, 1981 and El-Essawy, 1989, 1996). Their critics were directed mainly at the increasing dependence on foreign aid and its implications in both the economic and political arenas and on the selling of public enterprises and some joint venture banks to foreigners during the privatisation process.

Among the authors who argued for a completely different view of reform was Abdel-Khalek. He was the economic spokesman of the NPUP. He expressed his views concerning three main issues which were the core of the Orthodox recipe. These issues related to the role of the state; price mechanism versus planning; and the relationship between the national and the international. Abdel-Khalek called for the activation of the state's role, not by enlarging it, as he saw that the debate should not be about its minimum or maximum size, but its optimum role. He also asked for a balanced combination of market forces and a price mechanism, versus planning and direct control. He warned not to depend on international prices as these did not reflect the competitive market because competition did not exist in reality in the international market. In the relation between the domestic and international economy he added to the issues of pricing and economic blocking the importance of having certain measures to deal with external shocks, and with international commitment in this respect. Abdel-Khalek also drew attention to important elements which should be considered in the reform process; first the need to use more policy instruments than were already being used to allow better achievements and to have balanced measures to deal with both the increasing of supply and the controlling of demand. The sequencing of reform measures was also another important issue. He argued it was harmful to start with trade liberalisation before restructuring and developing both the public and private sectors. Finally he emphasised the need for regional reform measures which enhanced Arab integration (Abdel-Khalek, 1996:54-56 , 1997:144-47). The view introduced by Abdel-Khalek balanced between the role of market and the role of the state and represented a development in Egyptian socialist thought.

Further analysis of reform came from Shihata (1993) and El-Naggar (1991, 1997) while they supported the liberalisation policy they were dissatisfied with government performance. Shihata was able to provide a comprehensive view of the total reforms needed not only in the economic arena but he also stressed the need for political reform; for legal, judicial and administrative reforms; and the need for reforms in the area of human development (Shihata 1993).

#### **4.3.5. The Political Reform**

One of the areas of debate was the role of political reform that might accompany economic adjustment. The need for political reform was the only fact that all



political actors from different attitudes and ideologies agreed upon. The Muslim Brotherhood asked for a comprehensive political reform primarily to provide the right environment for the economic reform. They asked to abolish what they called “bad reputation” laws like the continuing state of emergency. They also asked for real democratic life.

The new liberal trend led by El-Naggar which advocated more liberalisation both in the economic and political spheres resulted in the establishment of the new civic forum that emphasised the political reform in five main areas: more freedom in forming political parties; an end to the emergency law; abolition of the job of social prosecutor; an end to the combination of public employment and parliamentary membership; and finally the removal of the statement that 50 percent of parliament members should come from farmers and workers. From their point of view, the necessary political reform was a constitutional one that removed what they called the old concepts of the socialist era that the public sector was the main stance of development, and the reference to the united forces of working groups.

The Wafd Party stressed changes on four main issues: taking decisions on individual bases; the public expenditure behaviour; bad economic choices; and corruption and administrative weaknesses (Abase, 1991:39).

In relation to the policy environment, many economists and intellectuals stressed the need for transparency in policy formation. Sunbul referred to the absence of public awareness of the real dimension of the economic problems. He indicated that before 18/19 of January 1977, the public knew nothing about the problem, and after the riots the reform issues were not for open discussion. The reform file only reopened with President Mubarak’s first speech in the presence of the People’s Assembly, people still did not understand the real meaning of reform and thought of it as an increase in prices. He asked the government to abandon the policy of silence (Sunbul, 1991:27). This silent policy of the government was subject to much criticism from different quarters especially to answer the accusations of corruption relating to some senior public-sector managers and even to some current and former ministers.

The government ignored the calls for constitutional reform for a number of reasons. The change of constitution favouring liberalisation might have meant that the government could not retreat from a policy of liberalisation. The government for

example might have wanted to intervene if political stability was challenged or economic development seriously damaged, as in the case of the fertiliser problem where the government had to become involved to confront the severe shortage which threatened the entire agricultural production. While the probability of reversing the liberalisation policy decreased over time it was still valid. The state needed room for manoeuvre in case this had severe effects on social and political stability. The state really thought that a change in the constitution in the way that was claimed by liberal forces would threaten social and political stability, if it matched the economic losses of farmers and labourers by overt political losses. Another important point was that the debate about constitutional change needed open and comprehensive discussion between different levels of political power in society. Such debate required an increase in the democratic space available for them. The debate also raised very sensitive questions between those in favour of Islamic legislation and those who were opposed even to the mention of Islam as a source of legislation as in the old constitution which was not really implemented. The expected public response would be in favour of Islam as a source of legislation and the liberal powers in society who made up the main support for the government would lose their credibility among the public.

The government ignored the constitutional reform and found it completely out of question at this stage. It also believed that there was enough political openness available and any further openness would harm the economic reform process. We can say that the state saw the public as ignorant with little political awareness and unable to understand the complexity of the negotiations concerning the reform measures. As Tobar commented in a seminar held to discuss the reform issues, in response to those asking for a reform programme to arrive at a political consensus and to implement political liberalisation, the political consensus does not mean the freedom to form parties, political liberalisation should cope with and be balanced by political awareness, something which is difficult in Egypt because of the high illiteracy rate. He confirmed that the political consensus does not mean political liberalisation (Tobar, 1991:43).

The debate about the reform measures revealed three important facts: first, the lack of political consensus about the reform. Second, the severe shortage of governance in both the economic and political arenas. In addition to the absence of

the debate about social reform. While this was not on the agenda of the state, only few of the debaters mentioned it. However they received a very weak response.

The absence of a political consensus about the reform was clear from the views discussed above. This absence of a majority view was not exclusive to the opposition. In the early stages of the reform the rivalry between members of the NDP and inside government itself was clear. As Tobar mentioned, the debate among the NDP's economic committee was fierce and there was only a few chances that the committee's views would be implemented due to the weak channels of communications between the ruling party and the government, on one hand, and the weak channels between the ruling party and other parties, on the other (*ibid*). Differences in views, concerning reform and privatisation in particular, between the cabinet ministers were very clear in the early stages of the reform. Dr. El-Ganzuri himself, when he was a Deputy Prime Minister and Minister of Planning, was considered by some reporters as one of the opponents of liberalisation. This was then thought to undermine his power. There was a tendency at a certain stage of the reform to abolish the Ministry of Planning, reducing its administrative level, hence power, to a High Council of Planning. It was even reported in the newspapers, but never implemented. Ibrahim and Lofgren compared two sets of statements from four Ministers in 1993 and the two previous years, when the Minister of Industry Mohammed Abdel Wahab, and the Minister of Labour Assem Abdel-Haq at that time argued that only losing (lame duck!) companies would be privatised and none would be liquidated. Two others, Ahmed Sultan the Minister of Tourism and Atef Ebeid the Minister of Administrative Development advocated the adoption of privatisation as a strategy for all public sector companies (Ibrahim & Lofgren, 1996:183). Ahmed Sultan the former Minister of Tourism was the main proponent of privatisation in the cabinet, together with Dr. Wali the Minister of Agriculture. He led the privatisation process in the Tourism sector mainly by privatising the administration and renting it to foreign companies. This was met by severe criticism as these used to be the most profitable public companies. After he left the cabinet, Sultan criticised the process of privatisation by the selling small shares to the public. He considered it as a way of publicising the process rather than privatising it, which meant he was in favour of a total sale and fast privatisation. It was not the party's policy that guided the government, it was more the government's response to

changes in the internal and external environment which was later adopted as the party's policy.

There have been two attempts to achieve consensus about suitable reforms. The first was the economic conference at the early stage of president Mubarak's regime. The second was the national dialogue in 1994. Both attempts failed because they focused only on economic matters and ignored any talk of political reform and in addition some political actors were put aside. Moreover, the ideological choice was already chosen from the beginning. In the first case, the economic conference, there was a tendency to keep the mixed economy with cautious steps towards liberalisation. At that time there was no political will to make fundamental changes in the economic system and the new regime was anxious to retain its constituencies, while some analysts thought that that was the right time to adopt reform measures. In the second case the liberalisation policy had already started earlier.

In addition to the call for political reform, legal and administrative reforms were initiated as well. However, the need for social reform has been completely ignored until very recently. The social impacts of reforms were also limited to the economic effects on the poor. However, the consequences of these social impacts, in view of urban violence and terrorism, were frequently mentioned by some analysts yet the state did not implement any policy to avoid their dangerous consequences.

In reviewing the debate about the reform *the missing actors were the public*. There is no sound evidence about how people accepted the reform programme. No surveys have addressed this issue directly, but in a national survey which was conducted in 1993 more than half of the respondents felt that their life had deteriorated during the previous year; two thirds said that it had worsened compared with five years earlier (Ibrahim & Lofgren, 1996:159). Although there was no doubt that the standard of living of the majority had deteriorated and the number of the poor has increased, little public protest was witnessed, except on a limited scale, among the directly affected classes (e.g. public sector workers & tenant farmers). The ruling party interpreted the overwhelming majority that they managed to obtain in the 1995 People's Assembly election as an indicator of the people's satisfaction with government policies and took it as a reflection of the success achieved in the economic sphere (although over 200 of the NDP's seats in parliament -about half of

the total seats- were disputed in court and the administrative court nullified the results of the election in these areas. However the Assembly maintained the right to keep its seats). On the other hand, if we follow the previously explained view of the state concerning the ability of the public to understand the complexity of the programme, or to enjoy enough political awareness, we can say that the vast majority believed the official promises of expected gains in the long run. One could say that the official media was to some extent successful in promoting the policy at least to the illiterate half of population, and it seems that the NDP was quite aware of the fact in formulating his policies. We can say that Egyptians were used to the protracted austerity in their economic lives, they were busy looking for second part-time jobs and satisfied with the limited scale of freedom of speech which they exercised by making jokes, responding to jokes about the economic situation in some movies and plays or even just by reading opposition newspapers. Public protest about the public policies implemented in Egypt took the negative turn and was clearly reflected in the extremely low level of participation in political life, as has been widely confirmed by many studies.

#### ***4.4. The Impact of Economic Reform on the State-Society Relationship***

Although the Egyptian state is based on a central authority supported by a large bureaucratic apparatus where interventions and regulations permeate many aspects of political and economic life, it has been described as a soft state (see Waterbury, 1985; Ayubi, 1995) due to its limited capacity to implement its laws and regulations and because of weak political and societal institutions. Mubarak was faced with both a political and economic crisis in the early 1980s and showed his early concern to deal with the economic crisis, considering it responsible for most of the ills in social and political life. However, the early years of his presidency witnessed gradual, but limited, political openings with increased credibility in the regime, while economic problems continued to intensify. At the time the economic reform was implemented both political and economic capabilities were deteriorating. Changes in the economic function of the state, in addition to changes resulting from the redistribution of gains and losses between different groups, entailed a corresponding change in the state's capacity and role and were related to a new role for civil society. These changes were to differ during the phases of initiation and

consolidation of the reform. We can now examine how the state managed to undertake the reforms in a way that was able to reduce social and political instability. Was it able to change its support base successfully during the reform? Was the state able to increase its power during the course of economic reform? and What was the effect on the balance of power between the state and civil society?

#### 4.4.1. Civil Society

This part reviews the impact on civil society. Was economic liberalisation able to enhance civil society in the form of initiating new associations, and solving the existing ones? Particular emphasis was directed on the Businessmen's Associations and the General Federation of Labour Unions as they represent the two main actor groups in economic activity and the most influenced by the reform programme. The debate about the increasing role of the Business Associations and their influence on the government was one of importance during the reform process. Labour Unions' reaction to privatisation was considered by the government in the early stages. Were they able to protect the right of their members? All these were issues and questions that need to be discussed.

##### *Business Associations*

Many business associations were established as a result of the economic open-door policy in the 1990s. As the main beneficiaries of liberalisation policies they were the main constituency for the free market and privatisation policies. Businessmen were in favour of the liberalisation policies as a main policy. However, they were very critical of the government's minor policies and they opposed some measure and policies when they clashed with their interests. In the meantime they were quite convinced that their interests were linked to the survival of the government. While the Egyptian Businessmen's Association (EBA), one of the most prominent BAs, declared that they did not practise or were not involved in political activities, they worked actively to strengthen their links with the government. The association, which comprises the business elite, seeks the membership of ex-Ministers and national bank managers. The EBA tried to project a neutral political attitude and to gain autonomy and not to be part of the ruling party, yet later some of its members became members of the NDP. Another prominent business association was clearer in its desire for government support. They were established through a semi-official organisation, the Chamber of Commerce of Alexandria, and this was thought to give

them more legitimacy. Their members were quick to join the NDP and in 1987 17 of them were members of the ruling party. Two prominent BAs tried to strengthen their links with the government in other ways. The first was careful to appear as an autonomous association and tightened its unofficial links through friendship, thereby attracting government officials not the opposite. This gave it more leverage in negotiations with the government. The ability of such associations to influence government policy was debatable. It was common to hear about meetings between the President, the Prime Minister and /or the Ministers and Businessmen. Businessmen became part of the official delegations which accompanied the president or the ministers on their visits abroad. Yet only a limited number of the business elite enjoyed these privileges. This should not be generalised to the broad and varied categories under the term businessmen. Their influence was limited to facilitating some measures related to exportation, importation and so on. Businessmen tried to strengthen their links to achieve personal gains in their transactions or for some protection. The impression of their increasing role was also aroused from the increased tendency of businessmen to join or nominate themselves to the People's Assembly. But in total we can say that they were only able to influence minor policies while the major policies were still dominated by the IFIs.

Businessmen also showed an increased interest in taking part in the People's Assemblies in particular. The number of businessmen who nominated themselves during the election of November 1995 was higher compared to previous ones and reached 50 nominations. The increased interest in the membership of the Assembly was related to different reasons, the leading one being that of the economic benefit they could gain for their business. It also meant an increased role for them in the process of decision making and an increase in their power. However, businessmen did not represent a homogeneous independent group with a clear agenda to promote productive values and the positive morals of the competitive market economy, instead the campaign witnessed the utilisation of money in a primitive way (Menisi, 1995:83). Most businessmen nominated themselves either through the NDP, 18 persons, or as independents but related to a particular section or elite in the state, 21 persons. Other opposition parties which were in favour of the liberalisation policy made fewer nominations, 10 for El-Wafd and 1 for the liberals, due to the already small number of their members. The result was in favour of 36 businessmen, in

addition the ten appointed members, including one businessman, Mohammed Abou El-Enean (*ibid*:85). While the number of businessmen represented only 8.15 percent of the total seats, their influence increased far greater than this suggests. This was the case if we consider their participation in specialised committees inside the Assembly which were concerned with discussing economic laws regulating the private sector and the market economy. The economic committee involved 14 businessmen out of a total number of 39, an increase of 8 businessmen compared with the last parliamentary session. The planning and budgeting committee included 11 businessmen out of a total of 27 members. The committee of industry and energy had 11 businessmen from a total of 46 members.

### *Labour Unions*

The Egyptian General Federation of Labour Unions (EGFLU) is the umbrella under which about 22 general unions of different types are gathered. It has between 3 to 4.5 million members according to different estimates. However these numbers represent only one fourth of the total number of labourers (Awad 1991:278, Kandil 1994:263). During Nasser's era the EGFLU made unprecedented gains. The constitution of the unions requires the government to obtain their views on all draft laws, regulations and decisions related to labour and workers. Their views are also considered for laws with relation to their living standards and conditions (Awad 1991:278). In the early 1960s, a separate Ministry of Labour was created and from then up to 1987 the head of the EGFLU became the Minister (Khandil 1994:263; Ibrahim & Lofgren 1996:184). With the system of political pluralism many members of the EGFLU boards and its distinguished figures were drawn to the NDP and through it they became members of parliament (Awad 1991: 278). This might give the impression that labour unions have great leverage on government policies which is not true, as Labour unions and their leaders have always been tied to the state. Restrictive laws on the political activities of labour unions have never been lifted. Both concessions and restrictions were used to grantee their political acquiescence and obedience .

The EGFLU gains in the socialist era seemed to be endangered by the launching of the open door policy in the mid-1970s. Nevertheless, the head of the union at that time Mr. Saad Mohammed Ahmed expressed his support for the policy on condition that "it should be a productive policy, that might provide new job



opportunities.” They gave assurance that both the public and private sectors should be treated equally. On another occasion they pledged that the public sector was not for sale and should not be open to private participation (See Kandil 1994 :263; Gomma 1996:155-56).

Before officially launching the SAP, the government facilitated the passing of the Labour-Business accord, trying to achieve a conciliation between both views and interests. The accord included the acceptance from both sides of the role of both the public and the private sectors and a recognition of the need to develop both sectors and to free them from bureaucracy. The agreement did not discuss the details of privatisation and ignored this controversial issue. Individual unions rejected privatisation and considered the agreement a betrayal of the interests of the labourers (Kandil 1994:264). Since then and during the course of the economic reform the conflict of views between the leaders of the EGFLU and individual unions increased. The ways of expressing their oppositions and defending their rights were different at the leadership level, compared to the individual union level. The EGFLU leaders continued to defend the workers’ rights, keeping them however in line with state policy. They could not challenge the state shift to a liberal economy and privatisation. Their strategy was to try to minimise or reduce the workers’ losses in a peaceful way.

The issue of law no. 203 of 1991, though it did not mention privatisation explicitly, raised fears among the workers and tensions in their relations with the authorities. The leaders of the EGFLU conducted intensive meetings with high officials to discuss the law and its implications for the workers. Attention was given to workers’ rights, policies of vocational training, and retraining to guarantee stability and the provision of new work opportunities. The individual general unions had other thoughts, as 1991 witnessed an increased number of strikes, sit-ins, and demonstrations compared with previous years. These forms of rejection continued during the following years of the programme and were usually carried out by individual unions as a response to direct encroachment on the workers’ rights. In general the labourers’ demands included the right to be represented on the boards of their companies, the rights of workers concerning wages, and hiring conditions under the new labour law, the right to peaceful strikes and a support fund for the striking workers (see Gomma 1996:168; Ibrahim & Lofgren 1996: 184). In addition,

there were some individual demands related to the interruption of their wages and rewards. Were these different kinds of protests effective? The state's direct response to strikes and demonstrations was the use of police oppression and the Central Security Forces were used with increasing frequency. No-one was killed however, many were wounded (Ibrahim & Lofgren 1996: 185). However, on some occasions the authorities had to accede to the workers' demands. In the case of the mining workers' strike in 1994, which was organised by the mining workers' syndicate, the persistence of the workers in continuing the strike forced the Prime Minister and Ministers of Interior, Labour Force, Finance and Public Sector to meet to discuss the problem. The problem was concerned with the suspension of the workers' rewards and allowances due the cut in subsidies to that industry by the Minister of Finance so as to cope with the privatisation programme. The Holding company for Mining had to provide the mining companies with a loan to pay the workers' allowances. In the same year the state has to respond positively as well to the strike of the Kafr El-Dawar workers. The strike was a series of stoppages organised by the workers in the preceding years, this time they were directed against the new regulations which imposed severe punishments on the workers. The head of the company claimed it was at the behest of the Ministry of the Public Business Sector, while the investigating committee accused the company of making the wrong decision and avoiding the real problems. The event resulted in three committees to discuss and confront the problems.

On a macro basis the state had to adapt its privatisation policy to reduce the labourers' protests. The contracts of companies that was sold obliged the new owners to keep the work force for at least three years. Workers were given the right to buy ten percent of the shares with concessions, some companies were sold completely to the workers and workers who wished to leave the company were compensated. However, public sector could do much more if all its leverage were used. No collective action was taken by the EGFLU. Strikes were called on in individual basis.

In the 1990s the state succeeded completely in neutralising the leaders of the general trades union, on the sense that they accepted privatisation as an ongoing process, though they were not convinced with it. The current situation of the EGFLU was made clear by Dr. Nassar, the secretary for the economic affairs of the

EGFLU. In a seminar of 25/5/95 discussing the effect of the reform in, he confirmed that they disagreed before with the selling of the PEs and that there was nothing in Law 203 about the selling. It only referred to incorporation or liquidation. He mentioned that it was not an issue of ownership, public or private, it was concerned how to increase efficiency. In his opinion, the problem of management was not limited to the public sector. It was in both the public and private sectors. But in the public sector those who destroyed the PEs were back again to reform it. This statement reflected the lack of credibility of the labourers in the reform process which resulted from the previous failures of several attempts to reform. If corruption and patronage were there in an explicit form, the labourers could not be expected to cooperate, nor the reform to succeed. He referred also to the constitution where it stated that the public controls tools of the production and that employees share the administration of the companies where they work. However, he was very negative about defending what he thought the were labourers' rights. He refused to offer a case for the non-constitutionality of the privatisation process. Even if he had, the public sector would have been sold off before decision was reached because of the long and protracted legal procedures in Egypt. He also mentioned they were realistic in this era of change and that they confronted the risks by "thought"( corrected to "reflection"! ). They arranged seminars and tried to educate labourers about these changes through the workers' university. Although he did not mention the nature of the educational programmes, were they to increase the labourers's awareness of their rights? or to convince them that these changes were happening all over the world so they were inevitable? or both?

What Nassar stressed was that through the unified labour law they tried to guarantee the rights of labourers by making them a third partner with the government and the employers. The principle they fought for now was that they were working in the national interest and they had to be the main pillar of the reform process. He referred to the lost rights of workers in the private sector in the new industrial city the Tenth of Ramadan where the worker had to sign a resignation form before he even signed his contract. Khamees, a prominent businessman -the head of The Industrial Federation who used to be the head of the Investors' Association in the Tenth of Ramadan- thought that workers in the private sector in the Tenth of Ramadan were well paid, on average £E 1200.00 per month, and some companies

gave allowances from 12 to 16 months in addition to the social security system. He added that they tried to build an understanding of the mutual interests of the workers and the factory (Khamees, 1995). At the same time Tobar, secretary of economic affairs in the NDP, defended the private sector saying that labourers in the private sector were subject to Labour Law no. 137 which provided every guarantees to the workers. He believed that the higher income of private sector workers replaced other grantees provided by the public sectors (Tobar, 1995).

### *The New Civil Society under SAP*

The most distinguishing feature of the new civic society associations act up in the 1990s was their academic nature. Several associations were established and directed by university academics mostly to defend the political and civil rights of the citizens and/or to promote for liberal views -The New Civic Forum, the Ibn-Khaldoun Centre, the Egyptian Human Rights Association and The Egyptian Centre for Economic Studies (ECES). Most of these associations were established in spite of the National Association Law no 32 of 1961 which limited their ability to participate in political activity as they set themselves up as corporate companies. Their academic nature was also clear from their periodical publications and organised seminars. These new types of civil society associations attempted to fill the vacuum in political life where the political parties failed to do so. They also reflected the increased interest of the Egyptian intelligentsia in participating in the process of reshaping the future of Egypt's new political and economic system. The external finance of most of these associations was one of the sources of criticism as their thinking was believed to be shaped by foreign interests rather than real national concerns, while, in fact they contributed to both foreign and national thought. In the case of the New Civic Forum, its director occupied a senior position in The World Bank where he acquired liberal views and could be considered the representative of the move progressive view of liberalisation in the Arab countries. This again reflects the role of linkages between liberal developed countries and the intellectual elite who gain their knowledge and form their thought through such foreign associations.

El-Naggar's views contributed to the basic manifesto of the Wafd party. While the Wafd party is the main advocate for liberalised thought among the Egyptian parties, it can not represent a comprehensive, well-articulated, liberal

policy. As a political party the Wafd competes for political power and tries to widen its support base it can not openly represent extreme liberal views which threaten the gains of the masses represented by the labourers and farmers rather do they call for some liberal reforms in certain areas. El-Wafd party programme was prepared in 1984 and could not contradict the main principles of the constitution. It refers to the Islamic *Sharie'a* as the main source of legislation, meantime stressing the importance of national unity and the equal rights of Muslims and Christians. They support the importance of a strong public sector to participate in financing development but they call for it to be managed in the right way in the right economic environment. They review the relative size and role of the public and private sectors, while the public should rid itself of some irrelevant activities, the private sector's role should be increased. El-Naggar's views are more progressive than that. He calls for fundamental changes in both the economic and political systems. He would like to deprive the workers and farmers of the fifty percent of People's Assembly seats, which are divided among them. He also rejects the participation of the public sector in production and trade and sees overall control of the economy by the central government as the main cause of the failure of the open-door economic policy of the *infitah*.

The Ibn Khaldoun Centre calls for a strengthening of civil society organisations and the activation of their role and as part of the democratic transformation. They issue monthly reviews to promote their views. They also organise seminars and conferences. One of their conferences about the rights of the minority had to be called off because it was criticised on the basis that the Egyptian Copts could not be considered a minority. This raises questions about what kind of civil organisation is needed and who can assess their views? How personal or foreign views can direct national work? Who should supervise their work? Are the ethics of the work of these civil organisations is it civil or private associations? While financial independence is good from one point of view as it provides autonomy from the state, how much autonomy is needed?

One interesting event was the establishment of The Egyptian Centre for Economic Studies in 1992 by members of Egypt's private sector. The centre conducts economic studies of an academic nature and does not target public opinion in a direct way as do the two other organisations. It is rather more concerned to

influence the decision-making process through its studies. The declared objectives of the centre are to promote the economic development in Egypt by assisting policy makers and the business community in identifying and implementing reform. From the founders of the centre and its declared objectives it is not difficult to conclude that the centre adopts neo-liberal thought and promotes a freer economy. The executive director and the director of research -Dr. Ahmad Galal- is a close collaborator with the World Bank, and the deputy director of the Middle East Department in the IMF is one of the members of the centre too. Prominent neoliberal economists contribute to the working papers of the centre - Jeffrey Sachs for instance- and these papers in turn contribute to the World Bank's official reports of Egypt's economy (see the World Bank Country Economic Memorandum for Egypt, 1997). The foundation of the centre by members of the private sector, while it reflects their support for a liberalisation policy, is one step forward to contributing to a think tank in Egypt as part of its social commitment. However, the studies of the centre can go further than the private sector expects as it is in favour of more free trade (Sachs, 1996) the issue which the private sector is most reluctant to accept in the liberalisation programme. This raises questions about the influence of World Bank ideology by way of the centre's research director and the contributors to the studies. The role of private sector members in selecting the required areas of study is unclear. They should try to play a more effective role in directing studies towards empirical areas where they need assistance. One of the major contributions to such a centre might be to investigate new profitable areas for investment, areas of competitive advantage and studies for the external market. In brief, it should assist the private sector to expand its participation to economic activity and promote export rather than assisting its decision-making process in the direction chosen by the World Bank.

In contrast to the previous organisations, which were set up under the umbrella of liberal thought, there is the case of the Land Centre "*Makaz El-Ard*", a centre which was founded in 1996 to defend the human rights of farmers in rural areas by creating awareness and providing legal support and assistance to tenants in the Egyptian villages. It also conducts studies concerning agricultural land and employment conditions in the agricultural sector. The centre played an active role in defending farmers' right to access land during the period the new land tenure law

was implemented under which the tenant farmers had to leave their lands to the landlords. The centre publicises the drawbacks of the law and tries to create public opinion to support the farmers in order to urge the government to find reasonable solutions for the farmers' problems.

#### **4.4.2. The Political Management of the Reform and State Capacity**

This part assesses the state's management of the reform and how it managed to improve its capacity during the reform. Was it able to keep the balance of power with civil society. I assess in brief the three authorities: the executive (government), the legislative (the People's Assembly) and the judiciary. Then I evaluate the performance of the state as complementary unit.

##### *The Reform Team*

The GOE was criticised on the basis that it is controlled by some old bureaucrats who continued in office for many years. Performance was slow and routine. When the new cabinet came to power in 1996 the public was more optimistic. The new government expected to push forward the reform programme. Although criticised for the limited changes in personnel the new cabinet was praised for the new rearrangement of the Ministries. The new setup was thought to facilitate performance and provide more co-ordination. The main changes related to foreign trade which was combined with internal trade in one Ministry which was thought to have better control over the supply side of the economy and the Ministry of Foreign Cooperation was joined with the Ministry of Economics. The rationale for joining Foreign Cooperation with the Ministry of Economics was not clear, at least to the public! In the following reshuffle the Ministry of Foreign Cooperation was separated again from the Ministry of Economics although the new Economic Minister was well acquainted with it as he used to work as Minister of State for Foreign Cooperation in the previous Cabinet of Dr. Atef Sedki. The Ministry of Foreign Cooperation was put directly under the supervision of the Prime Minister.

The new Prime Minister was responsible for the Ministry of Planning for a long time and resisted the dismantling of the Ministry or reducing its status. As a person responsible for planning in Egypt, he believed in central control, as appeared in his later actions. The new Prime Minister continued his control over the Ministry of Planning, however, and appointed a State Minister for planning. The Prime Minister showed an increased interest in the concentration of his power, as we can

be seen from several examples. According to law, the Prime Minister of Egypt is responsible for the Higher Council of Youth. The ex-Prime Minister because of his responsibilities rarely intervened leaving the executive responsibility to the executive Manager. On the contrary, the new Prime Minister exerted his power over the Council as soon as he received his authority. Moreover, the new Prime Minister gave himself new powers with almost every new law. In the new law of Investment Incentive he arrogated to himself the right of final approval on activities not mentioned by name in the law, ignoring the executive head of the GAOI who used to have this authority. The same was the case with the new Companies Law which regulates the issue of newspapers where approval should be obtained from the Prime Minister himself despite there being a High Council for the Press. The Suez Canal Authority was independent for several decades, however, the Prime Minister eventually assumed authority over it. This reflects his belief in central control over the economy and/or lack of trust in the competence of his team. This concentration of power is unable to cope with this stage of the reform which requires a greater distribution of power and participation in the decision-making process. If rivalry for power still exists among government bureaucrats at the higher level, there is little hope for a greater share of power with other political powers or civil society groups which defend the interests of the public.

### *The People's Assembly*

The People's Assembly is the second authority of the state which is concerned with legislation and monitoring the cabinet's performance, yet its effectiveness is subject to much criticism. Critics start with the credibility of the election process itself, then the credibility of its members on a personal level, finally on its performance and the limits of its authority. The last election of the Assembly in November, 1995 was considered by the government as a massive victory due to the overwhelming majority, 409 seats, for the ruling party while the opposition won only thirteen seats from a total of 443. The opposition had a different view. It represented 950 appeals, about double the number of seats, to the Court of Cession. The court's decision implies that the appointment of 250 deputies will be invalidated. The People's Assembly did not accept any on them on the basis that the Assembly is the only entity responsible for their membership. This view is based on Articles 93, 96 of the Constitution, Art. 20 of the People's Assembly law, and Arts. 347-355 of the



internal regulation of the Assembly. The matter is debatable between legal specialists whose argument is based on other articles of the Constitution as well. In addition, the administrative courts issued writs to overturn the results in 109 constituencies, the matter which created a dispute between the Ministry of the Interior and the courts, which seemed to be left to the Assembly's decision as well (the Arab Strategic Report, 1996:290-92). These violations of the election process are not a new phenomenon. The previous elections of 1987 and 1990 were followed by 200 and 260 appeals to the court respectively. The low participation rate in elections is a sign of low credibility and has its justification. A study conducted by the Democracy Development Group in Egypt in seven constituencies revealed that only 42 percent of the sample participated in the election process. The non-participants justify this by expressing their belief in the futility of their participation, as the government did what it liked and they expressed their distrust in the election process (as quoted in the New Civic Forum, 1997:10). Another study of a limited number of Egyptian postgraduate students in one of the British Universities revealed that only 37.5 percent of them had an election card. However not all of them participated continuously in the process. The low rate was related mainly to the low participation of women as none of the female students had an election card or ever took part in the election process. Participation was also considerably higher among those who lived outside Cairo compared to those living near the decision-making process in Cairo. This also relates to family relationships which are more effective in small towns and villages (El-Gaafarawi, forthcoming).

Members of the People's Assembly were subject to criticism mainly for using their power to achieve personal advantages, especially in business. Criticisms and accusations were not limited to the opposition. The national newspapers were part of it as well. From their point of view the elections facilitated the entrance of the so-called members of the loans and drugs, in addition to other practices of taking over state and public land (Addle Hashish, *Ahram*, 21/2/98). El-Bad wrote in the *Ahram International* (11/7/98) describing members of both the People's Assembly and the Shoura Council as opportunists. He wondered if it was right that some members of the People's Assembly have mediated between the construction authorities and some landlords who violated the law, to be forgiven. Others attend the Assembly merely to use it as pass-word for business and have succeeded in

accumulating massive wealth though they never did business before. While the Shoura Council election of witnessed those who nominated themselves with great enthusiasm, then suddenly withdrew. They were accused of receiving benefit from this and probably bribes. Such accusations in the national papers must have at least some truth, which reduces the credibility of such councils and legislative and monitoring authorities.

The weak performance of the People's Assembly as a controlling mechanism of the government was evident and tended to deteriorate over time. The hegemony of the ruling party over the Assembly was the main cause of the decline in effectiveness. The new legislation gained majority approval whenever it was introduced. However, to avoid public reaction important legislation was launched at the end of the parliamentary year when there was insufficient time to discuss it. Others which needed to be consulted about by the institutions concerned were introduced by stealth, as was the case with the decision to appoint the deans to the different schools in the universities instead of electing them, as was formerly the case. The last contraction in the monitoring function of the People's Assembly was the elimination of its authority over the Central Agency for Auditing. The reports of the Agency are not available to or discussed by the Assembly.

### ***Judicial Authority***

The only authority that remained independent was *the judiciary*. *The higher* constitutional court together with the administrative court has played a particularly vital role in Egyptian political life. With the increasing encroachment of the Constitution much legislation was denied its constitutional basis by the Constitutional Court. Its role was vital regarding the People's Assembly elections, as referred to above. While the Assembly did not apply the court's decisions, it made the election violations clear to the public and reduced the credibility of the state. The judicial system also played another important role in the development of pluralism in political life as all parties which were created after the first phase of pluralism were established by court decisions.

Yet, the judicial system has also had its limitations which were responsible for its low public credibility. These limitations related mainly to the available set of laws, the slow and complicated judicial procedures and corruption, especially among low-level bureaucrats. The legal system in Egypt is crowded with thousands of laws

which are estimated by the head of the lawyers's syndicate to amount to 60,000 laws. Some of these laws were enacted to confront emergency crises or temporary situations (as in case of the law of money utilisation which was promologated to meet the crisis in what was called the Islamic Money Employment Companies) while it should have been proclaimed for long-term needs (Shihata, 1996:165). Every new batch of legislation brings new constraints and results in a restricted legal system. This made the investment climate in Egypt non-competitive and averse to the spread of new ideas until very recently. These numerous laws were not matched by an institutional capability to implement them or the financial resources to apply them in the right way. The result was a partial or distorted application which reduced respect for the law and increased the role of personal and/or corrupt relationships (*ibid*). Recent improvements have been introduced in the judiciary system, yet it still lacks efficiency and suffers from protracted measures, as it needs 3-6 years to deal with a civil or commercial case. It is also expensive and includes exhaustive measures on account of the wide range of administrative personnel who may lack efficiency and/ or honesty (*ibid*,:168-69).

In the late 1990s few years as other tools became limited and restricted by the state, the decisions of the High Institutional Court have become central for opposition political parties and civil society groups to fight against the encroachment on economic and political rights. The state has directed its attention to limit it. In 1997 an NDP member of parliament proposed its abolition to the People's Assembly. This suggestion was attacked by many members, political and public figures and intellectuals. The Assembly threw out the suggestion and the NDP declared that it was not responsible for the proposal, claiming that it was introduced on an individual basis. A year later another amendment was announced which restrict the validity of its decisions. Change by stealth is still the policy of the state to control both economic and political life.

### ***State Performance and Capacity***

The state's role and performance changed throughout the course of the reform. In the early stages of the reform the state had to reduce or neutralise the opposition, whereas when the reform went ahead the state has to build up a coalition of beneficiaries and to carefully manage changes in its support base. In the period of reform consolidation the state had to give up its control over political life so as to

allow more participation in the decision making. Civil society should grow to fill the gaps in political and social life where the state has withdrawn and to defend the interests of different groups, especially the vulnerable ones.

### **The Political Management of Reform**

The state used different techniques to persuade the public about the necessity and the effectiveness of the reform. Direct persuasion was used by the higher level of the presidency in official speeches of President Mubarak. An awareness of the serious situation and the real dimensions of the crisis was the first step. In analysing the causes for such a crisis the blame was placed on the public itself because of its bad consumption habits, matched by excess consumption. Examples were given about the consumption of sugar and meat. The public was blamed for the rapid increase in the population and the efforts expended by governments to provide cheap food and public services: schools, hospitals, transportation and communications, etc. The feeling of guilt was thought to be one of the motives for accepting the impending austerity. Marginalising the opposition was another method, as the government had failed to neutralise the opposition. It sought to marginalise their role in political life by restricting the democratic margin available for them. Professional syndicates law was changed so as to control the influence of the Islamists who represented the main source of criticism. These managed in the meantime to enlarge their constituencies through their social services and were able to provide for society and they started to gain increased credibility which was evident from their control of some major professional syndicates. The marginalisation of the Islamic movement was sought in many ways. Their efforts in several major social events like the earthquake were ignored by the official media. The participation of individuals and the PVOs in efforts to help those injured by the earthquake had to be diverted through official channels or they had to withdraw. The Muslim Brotherhood had also been excluded from the national dialogue in 1994. Some terrorist events were blamed on the Islamists without distinguishing between different groups or thought. The Muslim Brotherhood, the more effective group, was accused of playing a role in the terrorist attacks. Their candidates in the last People's Assembly elections were thought to be discriminated. Finally, there was the arrest of some Muslim Brotherhood members. There was a noticeable retreat from the previous trend to increase the political freedom available to opposition parties, to intellectuals and to the public in general.

Famous examples are the decrees appointing the *Umda* in rural areas and Deans of Universities. The committee responsible for approving new parties did not grant this right to any of the proposed new parties and the few who did manage to establish themselves had to go to court to obtain approval.

### **State Capacity**

Aggregate capacity is measured by the state's ability to achieve its declared development goals (Ayubi, 1995:450) and to pursue its role effectively according to the needs of the developmental phase. As is clear from the above, the state was able to achieve the short-term objectives of the reform programme of stabilisation. However, for social and economic goals which were envisaged as long-term goals, performance was weak and slow. As the long-term goals were not related to timetable performance, this gave the state some area of manoeuvre regarding this long-term time-span.

Another approach for ascertaining the state's capacity was the analytical approach to its components which included according to Ayubi (1995) the allocative, regulatory, and extractive capacity. We can add political capacity as an important area related to managing the reform. At the beginning of the reform the state improved its extractive capacity in a few ways. By liberalising the prices of agricultural crops the state gave up the semi-coercive method whereby it used to expropriate economic surpluses from rural areas. This semi-coercive method was considered to be a characteristic of a "fierce" state by Ayubi (*ibid*,:453). The state also succeeded in reducing the foreign debt at difference phases, the last of which was delayed. In addition the state managed to attract flight capital through changes in the interest rate. Yet it was unable to direct it to investment channels, which reflected feeble allocative and regulative capacities. The extractive capacity of the state also remained weak in other important areas. The state's ability to collect taxes did not improve as most of the increases in taxes were achieved through rises in indirect taxes, which do not distinguish between rich and poor and could still be considered a semi-coercive method. The state's capacity to collect direct taxes had even deteriorated, due to lack of qualified personnel. Some private-sector companies complained about the late estimation of taxes on their activities which was to be calculated every three years instead of every year, which disturb their accountancy.

The state's ability in collecting taxes was of most importance in the era of liberalisation as the state lacked other sources which it used to have in state-led development where it used to control resources through nationalisation and the manipulation of prices. In a liberal economy taxes become the main source of government revenues, where state failure to collect it effectively forces it to shift to indirect taxes which are socially costly. State extravagance in granting tax concessions to attract new investment reflected another weakness of the state where it failed to provide the appropriate regulatory framework to attract investment.

An increasing competence in direct tax collection with an enlarging of national income needs a sophisticated system with a greater tendency towards democracy. Where semi-coercive means are not valid in a strong state, there is a bargaining for power between society's representatives and the state. This needs state involvement in civil society on the basis of integration rather than coercion. It is also argued that increasing direct taxes requires compliance and cannot co-exist in the long run with authoritarian rule which in turn requires more public participation and control over public policy. This process of bargaining between the state and civil society is more feasible in a market economy than in controlled economy where the tax base is less elastic. The elasticity of the tax base expands with the increase in the role of the market where it is easier to avoid tax. Thus the greater the elasticity of tax payment the greater the need for bargaining (see different arguments in Ayubi, 1995:454:55). In Egypt different tax concessions, valid for five, ten and sometimes twenty years, were offered by the government for new investment without direct bargaining with the civil society. However, bargaining applied with different degrees to other kinds of taxes, such as sales tax, and the level of tax on commercial and industrial activities. This was done mainly through business associations which represented the interests of the investor elite and was more likely to be biased towards big business. Small business were not representative in the bargaining process between the state and civil society in many other matters because of the incomplete democratisation process in Egypt. The analysis above indicates that the greater the percentage of direct tax to total revenue the greater the state penetration in society. If we examine the tax composition in Egypt, we find that indirect taxes had the highest percentage, a matter which continued during the reform. Indirect taxes accounted for more than 60 percent during the 1970s and most of the 1980s,

while income tax improved only temporarily during the 1988/89-1990/91 period from 39.8 to 48.8 percent respectively, to fall again in the two following years to 41.2 and 40.7 percent, respectively (El-Samalouti, 1995:255). The composition of the direct taxes reflected the uneven nature of distributing the tax burden between different groups. While corporations contributed to the highest percentage of direct tax, most of it came from the contributions of public economic corporations (especially the Suez Canal and the Public Authority of Petroleum) as they contributed about 55-60 percent to direct taxes during 1982/83-87/88. Taxes on individual incomes refers to an increase in the contribution of the fixed salary group compared with those of free professionals during the 1982-1990/91 period. It is clear that was because of the low administrative capacity of the tax authority, where it was easier to identify those on fixed incomes. The result of this low administrative ability was a bias against the low-income strata (*ibid.*:234).

The political capacity of the state can be assessed by the state's ability to consolidate the reform in different ways, among which: building a coalition of beneficiaries and managing change in the support base, distributing power and increasing public participation in the decision-making process, providing transparency in state policy, and fighting corruption and the patronage networks.

The state achieved a limited success in managing its support base. While it failed to add substantial groups of winners, it succeeded to a certain extent in neutralising the opposition of the losers. The main direct losers who were organised and able to take collective action was the public sector employees, as we explained earlier. The state managed to neutralise the leaders, while responding to the pressures from different individual unions which was limited and did not oppose the privatisation policy as a whole. However, the state was unable to build a new strong support base and was due to lose another part of its old one. This came as a result of the economic outcome of the reform which had achieved very limited gains up till then. Potential winners were not certain about their gains till then. Egypt built a new coalition of elite businessmen. However, this group was limited in size and was still costly to manage. The government had to induce them to participate in the compensation of the social cost of privatisation. The state still relied on the silent majority which it tried to approach through the media to turn them into supporters.

The state failed to distribute power and maintained its political centrality till then in both the economic and political arenas. In the economic area, state responsibility for managing the reform and the slow building up of the necessary institutions in addition to weak response of the private sector kept the central role of the state. This centrality did not mean that the state was able to strengthen its capacity to the necessary level. The institutional power of the state was still limited if we realise that it failed to provide the legal and regulatory framework for the market economy. While the state enacted many laws and regulations. These laws needed change to overcome their short-comings. The state failed to promulgate two key laws to regulate the market economy: that of a unified labour law, which was still disputed by Business Associations and Trade Unions and that of a law to protect the market against monopoly, in contrast to rural areas where state control over economic life had considerably declined due to the diminished role of the cooperatives and village banks in providing agricultural inputs and crop marketing. The state tried to replace this economic control with direct political control by new regulations which allowed the government to appoint the “*Umda*” which used to be elected, it thus bureaucratized a part of civil society in rural areas.

The state could not provide transparency in the decision-making process or build credibility in the government’s ability to guide fair competition in the market. An example of the way the laws were introduced and the lack of transparency and consistency in government decisions was that of the introduction of new Law of Investment Incentive. Following changes in the economic environment, the turn to a market economy and the encouragement of private activity, a need for unified law to regulate private companies’ activities emerged. As private companies were working under different laws, regulations, and dealing with different authorities. A committee was assigned for this purpose, however the committee was surprised that the government has introduced a new and completely different law which dealt with incentives and guarantees for private companies. The committee prepared a unified law which combined the legal system with an incentive system. The government wanted to introduce a new law quickly in order to improve its image and encourage more investment. While it was meant to improve the credibility of the government and investment environment, the way the law was introduced and the content of the new law undermined credibility in the decision-making process. The new law



dismantled the General Authority of Investment stating that the administrative authorities of the governorates would replace it. However, under a certain amount of pressure, the GAI remained, a decree was issued to establish the GAI. Although it existed, the people and the investors wondered about it, as it had not been announced clearly that it was abolished. The new law gave the Prime Minister the powers which used to be assigned to the head of the Authority, which undermined his authority. Above all, a specialist accused the law of having many deficiencies. While the new law only has four new articles, compared with the old one, 230, 6 or 7 articles were modified. The new law also curtailed 18 positive aspects and incentives in the old law, the worst being that the new law contained 14 violations of the constitutional articles (Fahmy, Seminar about the law in the Association of Political Economy, Statistics and Legislation, 3/11/1997). These violations against the constitution allowed any person to call on the court to abolish it. The matter which undermined the credibility of the new law.

The state also failed to deal with corruption cases in a way that kept its credibility among the public. The labour party's newspaper *El-Shaab* led a campaign against corruption for many years. The government's best response to this was silence. The way in which the accusations against the former Minister of the Interior's sons were treated reduced the credibility of the government even, if we assume that they were innocent. The two sons, together with senior officials of their father's Ministry, were subject to different kinds of accusations of corruption for more than a year. Only then did their father, and not them, start to take legal action against the newspaper. Later on, all newspapers were denied the right to follow up the investigation. The court imprisoned the editor of the campaign in respect to some accusations, while others were still under investigation by the courts. During this period there were calls for conciliation and it was explicitly published that the higher levels of the decision-making apparatus gave the order for a reconciliation. Many prominent writers, including Heikel, were in favour of this reconciliation. Later, the editor was set free and the court continued investigating some accusations against the former Minister.

#### **4.4.3. State versus Civil Society**

State-society relations can be assessed in the light of changes in performance, power and credibility. The main civil society associations that gained momentum during

the reform were those of Businessmen's Associations. They increased their links with the decision-making centres using various devices many of them made available by the state itself, which used political gains as incentives. Many joint meetings and committees were held between Businessmen's Associations and high officials, including the President himself, the Prime Minister, Ministers and Members of People's Assembly to discuss economic policy. They were only able to influence minor policies related to the implementation of the reform measures, while the major policies continued to be influenced by the IFIs. The Businessmen's Associations were unable to emerge as a strong pressure group because most gains were granted by the state. As we mentioned, these gains were shown by appointing representatives in the People's Assembly, the Shoura Council and to some joint committees. The purpose of these gains were incentives more than to seek their acquiescence.

The Credibility of the businessmen was rather low. The negative view of the private sector who seek to maximise its profit through speculations and parasitic activities which was created during Infitah is still there however with less extent. Their view in the press was rather negative, they have been criticised in several occasions as in the people assembly election where money were spent in primary way. They have been criticised for their way of spending in their private life which was challenged to the poor. The illegal ways of accumulating wealth is also subject to comments by famous writers in the newspapers. Most recently Ussef Gouhar wrote in El-Ahram (11/7/98) an article under the title: Businessmen and thieves. The article mentioned an incident of two businessmen who imported four Mercedes cars using the names of some foreign diplomat in Egypt to avoid paying the customs which were estimated with four million Egyptian pounds. They have been convicted as the cars were found in the Villa of one of them. The writer wonder how they steel they own country just to satisfy their luxury habits or did they intend to sell them in other illegal ways to gain more money without paying taxes? How these businessmen could be trusted to provide their workers with fair wages or to produce non-cheated products with fair prices. The writer asked for strict punishment as a forgery case where the sentence could reach 3-15 years. Although this exciting title Gouhar emphasis at the end of the article that the majority of businessmen are straight. Such stories affect the public opinion towards businessmen. The absent of

social insurance for workers in private sector in the new industrial cities which referred to by the Trade Union representative is another reason for the lack of credibility.

The social commitment of private sector businessmen was limited to those donations stimulated by high public authorities or as a respond to appeal from the wife of the president as in the case of the project of the one hundred schools or to rebuild the villages who have been damaged by floods. These initiatives also limited certain prominent businessmen with contacts with decision makings authorities where they can gain more privilege from it. Some other businessmen refrain to join businessmen associations as they think that they force them to donate in such occasions while the privilege goes to the board members who dominate the association and use it for their interest. The straggle over power between businessmen themselves is also new phenomenon which reduce their credibility, which the president himself draw their attention to the importance of reconciliation.

#### ***4.5. Conclusions***

While the state succeeded in stabilising the economy, as the reform goes forward it failed to achieve real economic progress. The productive capacity of the reform has not been increased. Private sector response was weak and could not even reach the precedent levels before reform. Private activities were biased towards housing and luxury goods against productive and tradable goods. The challenge to socio-economic problems is still there; high unemployment rate, increased poverty and low domestic saving rates.

The state kept its centrality in managing the economic activity, however it extractive, and institutional capacity are still limited. The political capacity is deteriorating, the democratic margin is diminishing rather than increasing, the control over civil society associations is increasing rather than decreasing. Minor changes has occurred to the support base, with limited advances in building new coalition of beneficiaries which was limited to businessmen elite.

The analyses above proved the importance of some cultural and political aspects which need to be revived. The ethical and moral aspects in human development was stemmed again as important factors. Productive human resources do not only need high education, training and health care, they need self dignity and respect, freedom and to have feelings of national belonging and a positive value

system. This could only be achieved through democracy which allows them to express their views freely; participate in decision making and provide respect to human rights. It also entails the existence of a national project to revive national feeling which seems to be eroded under the feeling of oppression. In case the state fails to promote democracy, protect human rights and provide national project to unify the masses and revive the national feeling, the alternative is possible increased activity and support to the Islamic tendency where the public replaces religious values with political ideologies. It must be realised that some of the Islamic movements have different interpretations of Islam and they pursue a range of different interests, some of them are far from Islam.

## Chapter 5 Egyptian Agriculture and Structural Adjustment

### *5.1. Introduction*

The agricultural sector has played a historical role as an engine for growth for the Egyptian economy. It used to provide the main share of GDP, to absorb a high share of the labour force and to contribute greatly to exports. During the 1970s and 1980s, its performance has deteriorated considerably in comparison to its historical contribution and with the increased needs of the economy. There has been increased recognition of the need to improve its performance and to increase its average annual growth-rate from around 2.5 percent achieved throughout the 1980s, compared with the population growth-rate of 2.6 percent, to reach around 3.0 percent per annum in the 1990s (World Bank, 1993:11). The need to accelerate its growth rate to around 4-4.5 percent in order to contribute to a higher growth-rate at the national level was recognised later (JMA, 1995). As the agricultural sector used to be subject to intensive government intervention and control, government policies and control over the sector was considered by IFIs as the main source of its weak performance. A massive shift in development strategy was launched in the middle of the 1980s. Structural adjustment policies were first introduced to the Egyptian economy through this sector and since 1987 liberalisation of the agricultural sector has started gradually.

The cornerstone of such policies emphasised during the experience of Egypt's agricultural history, is that eliminating price distortion and 'getting the prices right' will rationalise the utilisation of resources and will lead to increases in production and income in rural areas on an equitable basis. The main argument in this chapter and the following two chapters, is that on the one hand such a strategy is irrelevant to the Egyptian rural situation and on the other, it is not conducive to sustainable growth nor to an equitable one. In the short run, the benefits which are witnessed seem to be limited to individual crops as they are from the "once for all" type and have not been on an equitable basis (Richards, 1995; Bush, 1996). This study further argues that the full effect from the policy of "getting the prices right", as set by the World Bank, might not be achieved because of other factors. First,

there is no direct relation between international prices, which are set as a standard and domestic production costs. Thus changes in prices will change the way in which resources are allocated, however, it does not ensure changes in the same direction and/or level as proposed by the strategy makers. In the Egyptian case there are other factors rather than the level of profit, which affect the way in which resources are used at the farm level. This study also argues that big farmers benefited more from the reforms, while small farmers and agricultural labourers have suffered, or achieved limited benefits according to their farm size, crop pattern and sources of income. To enhance and sustain development in the long run, more attention should be directed to the role of investment and technological change (Sarris, 1994; Richards, 1995) and socio-political conditions should be reconsidered. Although the proposed strategy from the World Bank covered some of the other necessary complementary measures it seems to be a mere 'lip service', as stated by Bush (1996), and the Egyptian view has completely overlooked the importance of socio-political conditions in rural areas in shaping the outcome of liberalisation.

This chapter examines the impact of structural adjustment policies on the agricultural sector. The first part discusses the experience before SAP. It sheds light on the institutional set up, the applied policies and the developments in the role of public and private sectors. It then assesses the outcome on resource allocation, productivity and income. The second part reviews the proposed and the implemented reforms and discusses their rationale. The third part assesses to what extent the proposed reforms were successful in achieving the objectives of the reform: Was it able to improve resource allocation and to increase production? Has this increase been achieved on a sustainable basis? Who has lost and who has benefited from the reforms? Were benefits distributed on an equitable basis? The analysis has been conducted at both national and household levels in order to account for the differential impact between different categories of rural areas.

## ***5.2. Egyptian Agriculture: Policies, Institutions and Performance before SAP***

The government of the 1952 revolution showed great concern towards rural areas. During first few months in power the RCC issued the first land reform. While the main goal was to eliminate the power of the old political elite, equality issues in rural areas were not far from consideration. The land reform was not limited to the

redistribution of land; it also set the basis for fair relationships between landlords, and tenants and established a minimum wage for wage labour. Their policies also aimed at increasing agricultural production and the welfare of the rural population. Policies adopted in Nasser's era also established the bases for the relationship between farmers and the government of Egypt. These policies have continued to have a profound impact on productivity, production relations and the living conditions of the rural households into the 1990s. The main policies adopted were: land reform to achieve more equal access to resources; government intervention in agricultural production (through defining cropping areas, crop mix and crop rotation, providing agricultural inputs, pricing, marketing); introducing co-operatives to assess both farmers and the government; building the High Dam in Aswan and the expansion of perennial irrigation; land reclamation; and providing basic health, education, water supply and electricity services.

After Nasser no substantial changes were made. Land reform laws continued to be valid and the rent was fixed to seven times the land tax, however, periodical assessment of the value of the rent was undertaken every ten years. The official value of rent increased from £E 23.3 a feddan per annum in 1971/72 to £E 73.7 in 1981/82 and £E 250 in 1989. The relationship between farmers and the government continued on the same bases. Farmers were subject to the same regulations, government continued to regulate production by controlling cropping patterns, marketing of inputs and outputs and prices. The aim was to extract surplus so as to finance development in other sectors and to provide cheap food for the urban sector. The discrimination against rural areas through control of terms of trade increased. The agricultural sector's share in public investment declined considerably. During the period of *infitah* the private sector was allowed to participate on a larger scale in the form of private companies, however, its participation and contribution to total production was limited. In the following part I describe the set of policies and regulations affecting the agricultural sector before SAP and to the outcome of these policies.

With the elimination of the big landlords in the rural areas, this class was replaced after the land reform by the upper class, the middle-size landowners who tended to dominate the local committees of both the NU and ASU in the countryside during the 1960s (Binder, 1978 as cited in Hansen, 1991:111). The influence of the

rural middle class was limited to the countryside and the Egyptian elite did not originate from them or represent their interests. The urban bias and the price policies discriminating against agriculture are strong evidence that in rural areas the middle class did not have even a small influence at the national level either under Nasser or Sadat. On the contrary at local level their influence was seen in some aspects of agrarian life such as the distribution of irrigation water and some agricultural inputs (Binder, 1978:207,372 as cited in Hansen, 1991: 112).

### **5.2.1. Policies and Regulations**

#### ***Land and Land tenure***

After the 1952 revolution three land reform laws were launched in 1952, 1961 and 1969. The main objective of these laws was to reduce the unequal distribution of land and to correct tenancy relations. They put an upper limit on individual land ownership at 200 feddans, reduced to 100 then to 50 feddans respectively. Meantime family ownership was restricted to 300 *feddans* by the first law, and reduced to 100 *feddans* by the third law.

The land reforms introduced extended to tenancy regulations, as 60 percent of Egypt agricultural land was cultivated by tenants (Radwan, 1977:15). According to these laws leases had to be in writing and for a period of not less than three years. Cash rents were fixed at seven times the land tax. In the case of share cropping, both costs and crops were shared equally by the tenant and the owner (Richards 1982:179).

Although Egypt's arable land is very fertile; its area is limited. Effective reclamation of new land started as early as the first five-year plan of 1960/61-1964/65. The average amount of reclaimed land during this period was about 107.28 thousand feddan per annum. This rate deteriorated gradually to reach 49.45 thousands feddan per annum during 1965/66-1969/1970, while the following years of the seventies experienced an even slower rate, as during year 1970/71 only 21 thousands feddan were reclaimed and in the following years up till 1979 only 1.99 thousand feddan per annum were reclaimed. With the increase in population growth and the food gap the GOE accelerated the reclamation rate during the five-year plan of 1982/83-1986/87 where the rate reached 127.43 thousand feddan per annum (INP, 1992: 44-47). These lands used to be managed mostly by the state with small areas allocated to individual farmers. Starting from 1976 there has been a plan to expand



private ownership of reclaimed land which was distributed to university graduates and the families of the victims of the war, then a few agricultural projects were established on some of the land, such as that for a company for improved seeds, another for sugar beet and animal production. In the 1980s the state started to limit its role to reclamation and left plantation to the private sector (*ibid.*:48-50). All reclaimed land was subject to privatisation, while during the early years, land was distributed free. Starting from 1980 this was no longer the case. About 40 percent of reclaimed land was allocated to peasants and graduates while the remainder was auctioned or sold to private companies. Nevertheless, the price of reclaimed land was extremely cheap compared with the prices of old land. While the price for the old land was about \$22,000 per an acre, the reclaimed land could be bought at an auction for 3,500 an acre. Areas allocated for graduates were even cheaper. This policy of low pricing continued to the late 1980s, where the price of the feddan was not allowed to be higher than £E 400 (Sadowski, 1991:110).

Although land was made available at low cost, the high cost for reclamation and plantation of new land, in addition to the needed technology, urged the government to introduce more facilities to encourage the private sector to participate on a large scale. This was by providing concessionary loans, tax exemptions and custom facilities for imported agricultural equipment (INP, 1992:58) and a new law to regulate land ownership in desert areas. Law 143 of 1981 increased the upper limit for land ownership in these areas according to sources and methods of irrigation. In the case of using ground water or advanced irrigation like drip pipes or sprinkling irrigation the upper limit of land ownership is as follow:

- a- 200 feddans for individuals, 300 for the family, including the wife and young unmarried children.
- b- 10,000 feddans for co-operatives with a limit of 30 *feddans* per member.
- c- 10,000 feddans to individual and companies of partnership by shares with an upper limit of 150 feddans per person.
- d- 50,000 feddans for joint-stock companies.

In case of surface irrigation and/or dried land from lakes, the upper limit of ownership is half the above-mentioned cases (Mustafa, 1994:10). The same law also entitled farmers and investors to concessionary loans. The PBDAC provides loans up to 80 percent of the cost of reclamation and farming at an interest rate of only 3

percent. Investments enjoyed tax exemption for five years, extended in 1984 to ten years. Poor farmers were intended to enjoy more concessions, while farms with more than five hundred feddans were not supposed to enjoy the tax holiday and some other facilities. However, large investments enjoyed more political influence and were able to extract more rents (Sadowski, 1991:112).

Small farm size has dominated agricultural land in Egypt. This is due to two main factors: old land reform laws and the inheritance law. In 1987, 22.25 percent of landholders held less than one feddan, more than half of them, 57.51 percent, held less than 2 feddans and 97.11 percent held less than 5 feddans. In addition farmers usually had spread holdings, which contained more than one plot scattered in different locations. This was due to the multiple sources of holdings and also to avoid cultivating all the land with the same crop according to the compulsory crop pattern.

#### *Land use regulations*

The government of Egypt's policy towards the agricultural sector aimed at using indirect taxes to extract the surplus from this sector and use it in financing other sectors especially industry. The GOE aimed as well to provide cheap food for the urban sector as part of its policy to build wide constituencies. To achieve these two goals, full control of the agriculture sector was imposed. First of all it imposed a compulsory crop mix and rotation, requiring farmers to grow certain crops to insure their availability in the needed amounts. This meant that small farmers had to plant all their land with cotton one year, with clover the next, and cereals the next, rather than have a little cash crop, fodder crop, and food crop each year, which increased their need for credit. A fine system was imposed on those who violated these rules. Farmers with less than five feddans were prohibited from planting highly profitable fruit trees, unless they were able to co-operate with their small holding neighbours. Only those with more than fifteen feddans could acquire selected seeds. Thus the law was biased towards big farmers. At the same time they were able to avoid the regulations concerning area restriction as they were better able to pay the fine (Richards, 1982: 182-184).

Price mechanism and market controls were the government tools for extracting agricultural surpluses. Imposed prices and control of both input and output trade were used. The government subsidised the prices of inputs and

distributed them on a quantitative bases. On the output side, a system of compulsory delivery with low prices was developed in the early 1960s. The required amount to be delivered varied from one crop to another. Cotton, sugarcane and soybeans were required to be delivered in full. Peanuts and sesame were required to deliver in full except for seeds. Each crop of rice, wheat, onion, beans and lentils was required to deliver a certain quota per feddan. Compulsory delivery of wheat was abolished during the 1976-1984 period and was imposed again in 1985. Maize became subject to compulsory delivery only after 1985. Fines of varying sizes were imposed on farmers who violated these rules and it was forbidden for crops to be transferred between governorates. Due to the low prices imposed on the delivered quotas, farmers tried to escape planting these crops, preferring to plant other more profitable crops, or escape delivering the required quotas preferring to pay the fine (Nassar, 1992: 3-4). The compulsory delivery quotas with mandatory prices continued in force until 1986/87. Then they started to be phased out under SAP.

The control of input and output prices resulted in net transfers from the agricultural sector to the non-agricultural sector. These transfers were estimated to reach about 5-7 percent of total agricultural income during the period from 1952-1970. Although the revolutionary government was responsible for launching such policies, its other contribution in the provision of social services, such as education and health balanced the situation. Harik thinks that "the revolution was positively inclined toward the peasantry and contributed more to it than had any other regime during the entire history of Egypt." (Harik, 1997: 62). This is true if we also consider the benefits of land reform laws that increased farmers' access to agricultural land and provided them with stable tenancy relations. Table 5.2 below, which indicates changes in both farm and international prices, shows an increased gap between farm prices and international prices over time which suggests that transfers out of the agricultural sector increased during the 1970s and early 1980s.

### *The Role of Co-operatives*

The co-operatives were the government's instrument in implementing its policy and in delivering its services. The co-operative controlled crop patterns and rotations, provided subsidised inputs on credit bases and controlled quota delivery of different crops. It was responsible for transferring new technology and extension works in addition to the maintenance of irrigation and drainage. The efficiency of the co-

operative in operating such functions was under clear debate. Lack of resources, and poor wages to the supervising personnel were some of the reasons behind the initial debate.

Three different types of co-operatives were available:

- a. Agricultural co-operatives for land reform: all beneficiaries of land reform area, which represent 10 percent of the cultivated area, were required to join.
- b. Agricultural credit co-operatives: The co-operative system was extended to the non- land reform areas in 1963 (Richards 1982:180) and all farmers all over the country (owners, renters and sharecroppers) became members. This is the most prevalent type. In 1991, the number of co-operatives reached 5,319, almost one co-operative for each village, and the number of total members reached three million.
- c. Agricultural co-operatives for land reclamation: served farmers in the reclaimed land. In 1986 there were 465 of them at village level, and 23 at both district and governorate level (Abdel Aal, 1996: 3-4).

The co-operative is run by an elected council of five to seven members assisted by a supervisor (*Mushrif*) who is usually an agricultural engineer appointed by the MALR. In many co-operatives the government provides a clerk and an accountant (Hansen, 1977: 58). Before 1969, 80 percent of the board members were supposed to be owners of less than five feddans. In 1969, the ceiling for board members was raised to 15 feddan and illiterates were excluded. Such regulations ensured rich peasants the dominance of the board (Richards, 1982: 182).

In 1976, the Principle Bank for Development and Agricultural Credit (PBDAC) was established and the credit function was transferred to it from co-operatives.

### ***The Role of PBDAC***

The PBDAC was not the first formal organisation for agricultural credit. In 1931 the Agricultural Credit Bank was founded as a response to the world depression. Its capital was shared between the government and commercial banks. The main purpose was to provide short-term credit, to eliminate selling agricultural land to foreigners as a form of loan payment, to moderate fluctuations in farm prices and to provide soft finance to co-operatives (Abdel-Fatah, 1994:6). The bank was renamed and organised in 1948 and again in 1964. In 1964, it was named the General Organisation for Agricultural and Co-operative Credit and the governorate Banks for Agricultural Co-operative Credit became share holders in the general organisation,

and farmers obtained bank credit through the co-operative. A main advantage achieved at that time was that crops were considered as collateral enabling tenant farmers to deal directly with the bank, something which it was limited before to landowners. The overlapping between co-operative activities and bank activities initiated conflicts and a lack of confidence among farmers and led to severe loan-recovery problems (*ibid*; Adams & Kamel, 1996:254-55).

In 1976, the PBDAC was founded and all credit functions were transferred to it. The PBDAC, which encompasses 17 governorate banks, expanded its coverage to enhance farmer accessibility. In 1996 it had 164 branches all over the country and 806 village banks with more than 4000 *mandoubia* (retail outlets) (Khedr, 1997:7). While the bank expanded its lending to cover all agricultural activities, its role was not limited to financial intermediation. The bank used to play an active role in providing agricultural inputs, including managing importation, sale and distribution; and receiving mandatory crops from farmers. Therefore, the bank owns and operates agricultural warehouses in almost every village and employs large numbers of employees (Adams & Kamel, 1996:255).

### **5.2.2. Agricultural Investment**

Agriculture's share in total investments has been deteriorating over time. In the first five-year plan in the Nasser era, 1960/61-1964/65, investment directed to agriculture and irrigation accounted for about one fourth of the total investment. Most of these investments were directed to the High Dam in Aswan and to land reclamation. Most investment directed towards agriculture used to be public. During 1970/71-1975 investment in agriculture and irrigation accounted for 9.9 percent of total investment and public investment contributed 96 percent of total agricultural and irrigation investment. During 1976/77- 1981/82 its share was 9.2 percent of total investment and public investment contributed about 71 percent (INP, 1990:57). During the first five-year plan of 1982/83-1986/87 the agricultural and irrigation share of total investment dropped to 5.6 percent of total investment and public investment accounted for 69.3 percent of total investment, about two thirds of it directed to irrigation (MOP, 1992).

Public investment in agriculture proved ineffective in managing to promote sustained agricultural growth. Public agricultural investment is usually divided between the administrative apparatus and the servicing and economic authorities,

and agricultural economic units (40 units), which include agricultural development companies (15 units), poultry and animal production companies (7 units), fishing & a fishing equipment company (1 unit) and agricultural development and credit banks in different governorates (17 units), in addition to two public-sector authorities for agriculture development and animal and poultry. It is to be noted that most economic units are mainly located in the Nile Delta (Lower Egypt). During the first plan of 1982/83-1986/87, 67.7 percent of investment in agriculture was directed to economic units and the rest went to administrative and economic authorities (Hafez, 1992:8-14). The performance of economic units was weak; they were characterised by high levels of non-productive capacity, especially for agricultural development companies, and high reliance on long-term loans. Some companies achieved low nominal profits through accountancy measures by reducing the level of reserves or capital by the rate of real deficit. While others, especially those working in poultry and animal production, suffered massive deficits. The policy of mandatory prices that forced the companies to sell for low prices was always the first to claim responsibility (*ibid*:29-31). In fact the economic units suffered technical and managerial inefficiencies, in addition to corruption and some questionable deals between public officials and private importers and dealers.

During the *infitah* private national and foreign capital was encouraged to participate in private projects according to a new investment law. However, investment projects in agriculture were the least attractive projects for investors in spite of the fact that they required low capital and investment costs compared with other activities.

The investment authority divided agricultural activities under the investment law projects into four main areas: Land reclamation and plantation; Livestock and poultry; integrated agro-industry projects and Fisheries. During the 1974 to 30/6/91 period total agreed agricultural projects reached 153 representing 9 percent of total investment projects. About one half of these projects were introduced during the 1974-1981 period and the high ratio of agricultural investments continued till 1984. (El-Saadani, 1992:44)

In spite of this classification, projects can have diversified activities. For example, the law used to oblige land reclamation projects to produce crops for industrial purposes, and they were able to have integrated agro-industrial activities,

seed production and animal production. Also livestock and poultry can participate in activities for producing animal food or veterinary materials. The most preferred agricultural projects were those of livestock and poultry as they represented about 63% of the total agreed projects. Land reclamation projects scored second and accounted for 16% of the total agreed projects, followed by integrated agro-industry projects and then fisheries with about 15% and 6% of the total respectively. (*ibid.*: 36-37).

It can be seen that projects of livestock and poultry achieved the highest capital and investment costs £E 190.6 million and 139.8 million respectively. However, due to the high return rate on investment and the short capital cycle investors prefer it more than the others. The capital needed for land reclamation and plantation projects was rather low compared with other types of activity, as the required capital reached £E 38.0 million and investment costs reached about £E 22.3 million. However, this project needs a long capital cycle and received low returns for invested capital, in addition to the problems of obtaining land. The unpopularity of projects of integrated agro-industrial activities was due to its high needed capital and investment cost which reached £E 129.9 million and £E101.6 million respectively. While for fisheries projects, a main problem was in acquiring the required land for its expansion.

### **5.2.3. Sector Performance**

#### ***The Effect on Resource Allocation***

The total cultivated area in Egypt is estimated at 6 million feddans. The increase in land through reclamation was matched by land encroachments on the most fertile land in the Delta and Valley. After building the High Dam in Aswan in the 1960s the use of perennial irrigation increased and land was used for two and some parts for three seasons. The cropped area increased from 10.7 million feddan on average for the period 1960-1966 to 11.7 million in 1987-1990 due to the increased intensification of land use. The intensification ratio increased from 1.85 to 1.95 during the two mentioned periods respectively (INP, 1992).

Government intervention in the agricultural sector affects the process of resource allocations. The low prices of some crops encouraged farmers to violate the crop pattern imposed by the government. They preferred to pay the fine if they were caught-usually around £E 20 per feddan (Harik, 1997: 66). The cereals group

dominates the crop area of Egypt. During 1960-1966 the total cultivated area of cereals accounted for 43.2 percent of total area and decreased to 40.8 percent in 1981-1986. Areas of clover, vegetables and fruits increased between the two periods from 24.4, 6.0 and 1.5 percent to 27.2 and 10.8 and 4.0 percent respectively (INP, 1992:11). Table 5.1 represents changes in the cultivated area of main crops during the two periods. The changes indicate that there has been a continuous increase in the cultivated areas of fruits, vegetables and clover which are not subject to government mandatory pricing, while areas for rice and cotton have diminished. Cultivated areas for wheat showed a slight increase only during the 1970s<sup>4</sup>. Cotton and rice areas decreased gradually due to the unfair prices for these crops, as shown in table 5.2, the gap between the farm prices and the export prices was increasing. Changes in the crop pattern starting from the second half of the 1970s were also related to a decreased supply of agricultural labour force where the emigration rate of farmers increased. This created an increased preference for crops with a low requirement of labour, especially berseem, which at the same time generates high returns through livestock production which in turn is related to women's work.

**Table 5.1 Average Annual Cultivated Areas of Main Crops** (thousand feddans)

Main Crops	1960-1966	1967-1973	1974-1979	1981-1986
Wheat	1334	1353	1404	1330
Maize	1689	1620	1866	1944
Rice	810	1213	1110	1087
Cotton	1784	1577	1309	1060
Sugar Cane	123	185	248	268
Clover	2523	2996	3100	3289
Vegetables	563	765	1030	1247
Fruits	156	264	344	481

**Source:** INP. 1992. Etaharer El-Eqtisadi wa Qita' Asera'a. "Economic Liberalisation and the Agricultural Sector" (Qadaya Atakhteet wa Tanmya fi Misr, No.77). Cairo: INP.

The result of these changes in cultivated areas with a sluggish increase in productivity and a rapid increase in population resulted in an increasing food gap in some main food commodities, as shown in Table 5.4. Food imports increased while exports of agricultural products declined, this resulted in an increasing deficit in the agricultural trade balance, starting from 1975, of US \$ 1299.6 million, reaching about US \$ 4427.5 million in 1985 from a total deficit in the trade balance of US \$

<sup>4</sup> This increase was due to the increased demand on hay as fodder, the price of which was higher than for grains.



2532.3 million and 6237.3 million respectively, thus the agricultural sector was mainly responsible for the persistent trade deficit.

**Table 5.2 Farm Prices and International Prices for Main Crops** (Egyptian pounds)

Crop	Cotton (Qantar)		Wheat (Ardeb)		Rice (Ton)		Sugar Cane (Ton)		Onion (Ton)	
	FP	EP	FP	IP	FP	EP	FP	EP	FP	IP
1971	18.24	26.08	5.00	na	34.67	na	2.57	5.60	19.00	na
1976	32.00	46.55	7.00	9.09	50.00	99.25	8.00	25.60	33.00	89.19
1981	58.09	90.10	11.50	24.46	85.00	332.2	16.00	61.50	52.00	236.3
						0				6
1986	96.86	173.87	25.00	19.23	165.0	na	30.50	65.60	100.0	222.2
					0				0	2

na = not available

Figures for Cotton prices are for the year 1985 not 1986

Source: MARL, Central Agency for Agricultural Statistics as cited in INP. 1992. Etaharer El-Eqtisadi wa Qita' Asera'a. (Qadaya Atakhteet wa Tanmya fi Misr, No.77). Cairo: INP.

It should be noted that the policy of state control over the agricultural sector was problematic because it was biased towards big farmers. Big farmers were more able to violate the crop pattern and to pay the fine. They also had better access to selected seeds and credit. Farmers with holdings of less than one feddan were only entitled to short-term credit (for agricultural inputs) not medium and long term. On the other hand, subsidy inputs were available to all farmers regardless of their farm size. That meant that a high percentage of subsidies went to big farmers who allowed the amount of subsidies to inflate and burden the public budget. Area, price and trade control were not the only obstacles for the agricultural sector. Extensive intervention was applied through poorly-trained and too many bureaucrats.

### *The Effect on the Macroeconomy*

As a result of the applied policies and the low investment levels, agricultural growth was sluggish. While the average annual growth rate in the 1960s was 2.7 percent, it rose to 3.5 percent during the 1970s and fell to its lowest in the 1980s to reach 2.5 percent (World Bank, 1993:5). Other estimates for the agricultural growth rate during the 1970s and early 1980s thought that it was below 2 percent (Harik, 1997:74). These low rates of growth affected the sector's historical contribution to the economy (See Table 5.3). Its share in GDP fell from around 30 percent in 1974 to about 19.3 percent in the mid-1980s. Employment in this sector declined from 47 percent of total employment to 35.8 percent in 1985. The sector's share from exports declined as well from 25 percent in 1974 to 17.7 percent in 1985. In spite of this deteriorating performance, transfers out of the agricultural sector in the form of

indirect taxes continued. Net transfers out of agriculture tended to be at their highest during the 1970s, while they reached 6.6 percent of GDP in 1965, jumped to 19.2 in 1975, then showed a decreasing trend to reach 6.3, 3.8 percent in 1980 and 1985 respectively (Dethier, 1989, as cited in Sarris, 1994:84). This decreasing trend was still high in absolute terms. In 1980, transfers out of agriculture due to price differentials were £E 987 million and net transfers after conducting subsidies reached £E 580 million (Nassar & Mansour, as cited in Harik, 1997:63).

**Table 5.3 Share of Agriculture in the Economy**

	1974	1980	1985	1990	1991/92
Share of Agriculture in GDP a/	30	25.4	19.3	19.9	16.5
Share of Agriculture in Exports b/	25	22.5	17.7	20.3	
Share of Agriculture in Employment	47	36.7	35.8	na.	33

a/ in 1987 constant prices, at factor cost.

b/ Data relates to 1981, 1985 and 1989, respectively

source: World Bank, 1993, p. 5. Data for 1991/92 from Egyptian National Third Plan.

The weak performance in the agriculture sector resulted in a severe food deficit. Total domestic production of food commodities were not only much less than domestic consumption, but also food exports were much below food imports. This meant that the agricultural sector could not provide self-finance to cover domestic food needs, to achieve the proposed new concept of food security which replaced the old self-sufficiency notion. Table 5.4 explains the development in self-sufficiency of the main food commodities.

**Table 5. 4 Self-Sufficiency for Main Food Commodities (percent)**

Crops	1960	1974	1980	1985/86	1987/88
Wheat	53.0	40.0	24.0	21.0	29.0
Maize	99.0	87.0	74.0	60.2	68.4
Rice	138.0	112.0	107.0	103.8	105.8
Broad Beans	97.0	73.0	69.0	94.8	109.5
Lentils	100.0	73.0	70.0	51.8	19.3
Red Meat	100.0	84.0	71.0	73.9	81.8
Poultry	95.0	85.0	64.0	90.6	91.4
Fish	93.0	92.0	62.0	66.8	68.7*
Edible Oil	na	na	na	21.6	27.6
Sugar	97.0	83.0	52.0	49.8	62.5

\* Figures for the year 1989/90

Sources: For 1960, 1974 & 1980 INP, 199

For 1985/86, 1987/88: Mustafa, M. S. 1994. *Esyasat El-Eslahya le-Qita' Asyra'a wa El-Ghesa' wa Atharaha ala El-Awda' El-Ma'shaya lel-Sukan fi Misr*. Cairo: INP. p4.

The food gap was covered by imports. The massive dependence on food imports increased the economy's vulnerability to changes in international prices. It also helped to push food prices up, a matter which increased the food subsidies given by the government. This in turn increased the burden on the budget. Because of the massive increase in food imports compared with food exports, the agricultural trade balance suffered an increased deficit from US \$ 360 million in 1975 to US \$ 2,091 in 1985/86. Thus Food deficit was in turn claimed responsible of many macro imbalances, and had sensitive results on social equity, national security and price stability. Table 5.5 shows some indicators for the relation between food security and macro balances. It shows that the food deficit features are very much in evidence in both the fiscal deficit and the trade balance. It is also a crucial factor in the cost of living, hence price stability (Abdel-Khalek, 1994:51).

**Table 5. 5 Food Deficit and Macro Balances**

(US \$ billion)

	1988/89	1989/90	1990/91	Period Average
1- Food Imports(FI)	2.5	2.5	1.9	2.3
2- Commodity Imports (CI)	10.6	11.4	11.4	11.1
3- Commodity Exports (CE)	3.2	3.1	3.9	3.4
4- Trade Balance (TB)	7.4	8.3	7.5	7.7
5- FI/CE (%)	77	80	49	69
6- FI/TB (%)	34	30	25	30
7- Food subsidy as % of Gov. Expenditure				20
8- Share of household food expend (%)				56
9- Wheat self sufficiency ratio (%)*				29

\* Average for the period 1985/86 - 1989/90.

Source: Abdel-Khalek.1994. "Egypt's ERSAP: The Orthodox Recipe and the Alternative." In Abdel-Khalek & Kheir El-Din (eds) *Economic Reform and its Distributive Impact*. Cairo: Dar El-Mustakbal El- Arabi. p50.

An econometric study of the structural causes of inflation in Egypt illustrated as well that the main structural cause of inflation during the studied period of 1974-1987/88 was the slow growth-rate in the agricultural sector. This was through the direct impact of the deficit in the food supply and the indirect impact on the insufficient supply of raw materials of agricultural origin and its effect on the slow growth of other sectors. This was explained by the increased demand on agricultural products due to an increase in the population and in income during this period which led to a massive increase in the price of some food commodities (e.g. vegetables, fruits and meat). Insufficient agricultural raw materials lead to unused capacity in some industries, which led in turn to a shortage in its supply. On the other hand, unused capacity increases production cost hence increased prices. The sluggish performance of the agricultural export led to a decline in the export of food commodities such as rice and sugar and in agricultural commodities in general, while food imports increased. However, did the decrease in exports and the increase in imports help in controlling the price increase? In fact it led to a massive increase in the balance of payments deficit and to a reduction in non-food imports which led to an increase in their prices. Food subsidies helped to limit the increase in food prices, however the increased amount of subsidies accelerated the budget deficit. This in turn led to a more inflationary pressure on the general price level. In addition, both the compulsory delivery system and the pricing system limited the increase in prices though it led to increased supply bottlenecks in agricultural goods. In sum, as proved by the econometric results too, the slow growth of agricultural sector was the main cause for inflation (Kheir El-Din, 1991:79-83).

### ***5.3. Policies and Performance of the Agricultural Sector during SAP***

#### **5.3.1. The Strategy of the Reform**

Agriculture reform was introduced to the agricultural sector as early as 1987 with the encouragement of the World Bank and USAID. Detailed measures and different phases of the reform were agreed between the two international financial organisations and the Ministry of Agriculture. Although the main outline of the strategy is the same, there are few differences according to each partner's views and interests.

*The official national reform strategy*, official publications provide us with the main outlines. The third national plan, 1992/1993-1996/1997, delineated four main goals

for the agricultural sector: to modernise Egyptian Agriculture; to achieve the most possible level of self sufficiency for staple crops; to increase the efficiency of resource use in such a way as to help increase agricultural production, income and pre-capita share; to increase agricultural exports of goods with comparative advantage in order to restore the balance of agricultural trade (MOP, 1992:252).

The main strategy to achieve these goals, which started in the late 1980s, was built on freeing market forces; increasing private-sector participation in economic activity and the decision-making process; limiting the role of the state to prepare plans and programmes to increase and enforce private-sector participation in the agricultural development process in addition to its role in agricultural research and extension, economic studies and providing information and statistics (*ibid*). Some more detailed, though still general, policies were stated in the national plan which were more focusing on general goals without clear explanations as to the way to achieve them, their priorities, or time-span.

The agricultural strategy for the 1990s developed by the MALR with the consultation with IBRD, UNDP, FAO, WEP and UNEP, was discussed by the Shura Council, and claims to have been discussed by the political parties. The main objectives of the strategy are:

- Ensuring the optimum allocation and utilisation of agricultural resources (particularly land and water) together with conserving, improving and developing these resources to achieve sustainable agricultural development, i.e., increasing production and income (efficiency or growth) as well as with attaining equity and combining with environmental aspects.
- Better Utilisation of comparative advantages to increase exports and to contribute to the overall food security of the country.
- Creating new opportunities for gainful employment in rural areas (Nassar, undated: 2-3).

The above strategy highlights three main themes: growth in the agricultural sector should be built on efficient resource allocation, resource use should be sustainable and equitable; and food security is achieved by enhancing exports of crops of comparative advantage to finance the import of other deficit crops (as was stressed in the National Plan as well); finally employment creation is stressed.

The new proposed strategy for the period 1997/98 up to 2016/2017, indicated imperatives of achieving an annual growth-rate of 4 percent. It puts more emphasis on sustaining cereals production through price policy and using high yielding varieties. At the same time, it aims to maintain rice acreage around 900,000 feddans

a year. This is to cope with the World Bank recommendation to constrain crops with high water-usage. Within the same line the strategy encourages the expansion of sugar-beet crop and projects to promote efficient use of irrigation water. It also encourages soil improvement and maintenance projects. Improving the efficiency of horticultural crops marketing and post harvest treatment to increase exports. Encouraging cotton production for domestic needs and exports main factor in this concern is providing mechanism to safeguards producers against the risk of price fluctuation. Allowing recent graduates to own part of the reclaimed land and allocate the rest to small farmers and investors. While encouraging the production of animal production, providing support for agricultural research and marketing extension, mobilising role of women, creating conducive environment for private investment, Egyptian, Arab and foreign (See Nassar, undated: 8-10).

Although the declared strategy tried to cover most aspects of the agricultural sector, it reflects a static and unintegrated view. It does not identify the sources of growth within the agricultural sector, how this increase will be achieved and what the policy impact will be on equity in rural areas. It does not delineate the role for the public and private sectors, or explain how to create a favourable environment for the private sector and what is its expected role. The need for institutional reform is absent. A targeted strategy for the new lands is also needed. In the broader sense, it fails to integrate the dynamics of rural areas, the social structure, distribution of power and the political role. It ignores the relationship between land and population, between big farmers and small farmers, between farmers and labourers and finally between traditional farmers and new investors. In general it is important to emphasise again that equity issues were referred to without any real concern about how the dynamics of the reform would really affect farmers differentially. This is because in some cases the means for reform were considered a target while real objectives were neglected. Emphasis was directed to increasing prices, cutting subsidies and limiting the role of the PBDAC in distributing inputs, thus making way for private merchants. The new reform of land tenure was rarely mentioned within the dynamics of the reform especially in the early writings about this subject (see for example objectives of the reform programme as quoted in Khedr, 1992).

*The World Bank and USAID*, The World Bank reports on agricultural strategies for the 1990s represent a comprehensive strategy for the rural sector. The strategy targeted a growth rate for the agricultural sector of 3 percent during the 1990s (WB, 1993:11). Then by the middle of the decade it was realised that a 4 percent growth rate in the agricultural sector was needed to raise the national rate to 5 percent per annum (USAID, 1995:i). Other estimates for USAID, based on the experience of low and middle-income countries, estimated the needed growth rate in the agricultural sector to be between 4-5 percent per annum, that is a more than 2 percent per capita of the total population (JMA, 1995:5). It was thought by both the World Bank and USAID that Egyptian resources, land and water, are not efficiently used and that there is a potential to accelerate growth through the reallocation of resources in favour of the highest value crops, taking into consideration the utilisation cost of land and water and ecological sustainability. This means to 'increase the productivity of the unit of land and water, reduce unit cost of production, and thereby increase national output and farmers' incomes' (WB, 1993:11). Although it is agreed between the two agencies that better utilisation of resources is needed there is a slight difference about the most efficient use of resources, as we will see later. The World Bank referred to equity issues and poverty alleviation through the growth process. There is also a belief that although crop yields are high there is more potential to increase them, considering the quality of the available resources (JMA, 1995:6). In addition, an export-led strategy was thought to help in accelerating the growth and achieve national and food security. The proposed strategy of the World Bank was built upon five main principals as follows;

- The need for measures to ensure efficient use of important natural resources, i.e. water and arable land;
- The use of the free market, and the promotion of the private sector, in resource allocation;
- A comprehensive look at rural development including better involvement of women, diversification of rural activities, and provision of essential social programmes for health and education;
- The recognition of social and political issues;
- The initiation of institutional reforms (WB, 1993:xii).

The proposed strategy by the World Bank is more integrated and comprehensive than that of the GOE and the USAID and reflects an awareness of rural needs. However, the real implemented policies failed to a large extent to encompass some of the objectives or to achieve the relevant results. In this respect

Bush (1996) considered the expression of concern with issues of equity, the position of women and the landless as not being seriously pursued. Bush also pointed out that the characterisation of the Egyptian countryside employed by both the agencies failed to integrate the dynamics underpinning the relations of power and politics and the issues which are currently affecting the rural poor during the period of adjustment (Bush 1996:76).

***Rationale and Dynamics of the Reform in Agriculture***

The World Bank strategy aims to achieve a more efficient use of Egypt's limited resources, land and water, through increasing agricultural productivity per unit of land and water, and reducing the unit costs of production. This will lead to other objectives to be directly achieved, as it will increase national output and farmers incomes. It will lead as well to divergence of resources to the production of more competitive crops, increase exports and achieve national food security goals. This could be achieved from the World Bank point of view through three main policies: the free market economy (an increased role for the private sector); cost recovery; and land tenure changes.

Both GOE and USAID agreed to the above policies with only a few differences. The main dispute between the GOE and the World Bank concerns the cost recovery programme. On the other hand, all partners agree upon the need to adopt an export led strategy to achieve food security from its broader context and to improve the balance of payment deficit. It was thought that the three main policies above would lead to divergence of resources and to the production of more competitive crops and increased exports. In addition, there was a recognition of the need to improve technology, and to undertake administrative and institutional reforms; yet the reform programme did not provide practical policies in this respect.

***Free Market Mechanism and Private Initiative***

The orthodox view of Egypt's agricultural decline was blamed on state intervention, and price control in particular, for working as a disincentive to farmers to grow certain crops and for creating deficiencies in resource use. Price liberalisation was seen to provide more incentives to farmers to grow and invest in crops with real high value added i.e. in competitive crops. International prices were used to compare the distortion in prices at the national level and the target was set to increase prices at there international levels. Analyses done by the World Bank which take into



account the value added and the resource use of different crops, show that Egypt has the greatest advantage in cultivating horticulture products (fruits and vegetables), cotton and wheat, a disadvantage in producing water-intensive crops, rice and sugarcane, and is moderately competitive in some relatively low water-consuming crops such as maize, beans, potatoes, long berseem and oil seeds (World Bank, 1993:37-38). The study is not in favour of expanding the cultivation of long berseem and suggests the substitution of some of its present demand by non-traditional feeds. It is also not in favour of expanding the production of livestock and prefers to expand the production of poultry and fish, as they are less resource demanding (*ibid*:42). This strategy involves increasing importation of non-traditional fodder, which places a greater burden on the balance of payment. On the one hand, the study recognises the other benefits of growing livestock as in maintaining soil fertility through the provision of manure, and in providing proteins in the local diet. It was also unable to ignore the social and economic consequences of the division of labour inside the family. Livestock production, which accounts for one-third of the gross agricultural production, relies heavily on women's work (*ibid*). As for the cultural aspects, it must be noted that the reduction of livestock production does not mean that all women work force will be diverted to other activities. This is because livestock activities can be carried out inside the house, working in the field even on the family farm is constrained by many social factors and is relatively correlated to the economic and /or the social level of the family. On the other hand, it is true that fishery resources are under utilised in Egypt and need further consideration especially with the increase in population.

In contrast to the World Bank's view, an expert house working for the USAID suggested the importance of giving priority to horticulture, cotton and livestock and that these three subsectors need to grow at a level of 6.5 percent, while maintaining a growth rate equal to population growth level for the basic food staples in order to achieve growth rate of 4.5 percent per annum for the agricultural sector (JMA, 1995:5-6). The three sub-sectors were selected because they contribute over half the value added to the sector; a substantial increase in their growth rate will contribute greatly to the growth rate of the sector. Both cotton and horticulture are export crops, while livestock depends on domestic demand. Such an expansion in livestock production will entail an increase in the import of fodder. It must be noted

that the proposed strategy of the JMA considers the commercial interests of US, which explain the replacement of wheat with livestock. The Egyptian government view concerning crop patterns and the priority of the sub-sectors is not completely clear, however, it agrees with what is proposed by the World Bank concerning increasing wheat production. In general it is concerned with rationalising the use of irrigation water, and not expanding the areas of rice and sugarcane and in maintaining their high level of yields; raising the self-sufficiency of cereals, especially wheat, and planting corn to support the poultry industry; improving productivity of cotton and horticulture without increasing its area (Nassar & Khedr, 1997:14-15).

The validity of more than one strategy to accelerate the growth rate in the agricultural sector refers to the limitation of the price policy alone to achieve the efficient use of resources and that there is a need for a more targeted policy to provide incentives for farmers. On the one hand, there is no direct relation between international prices and real domestic cost, so there is no guarantee that the provision of international prices will direct production toward crops of high value for unit of land and water at the lowest production cost. On the other hand, there are factors other than profit which direct the allocation of resources and the choice of crop pattern at farm level, which render the price policy not completely effective in achieving its target. An empirical study of an Egyptian village that was not subject to a compulsory crop pattern proved that other factors such as the availability of family labour, size of farm, availability of off-farm activity and household self-sufficiency consideration have impact on the choice of crop pattern (El-Gaafarawi, 1991). There is also the effect of the habit of growing traditional crops, which are expected to be more responsive to the increase in prices as farmers become more aware of the farming techniques. This point will be examined further in the study on the impact of the reforms.

The increase in prices affects production 'once for all' as it reallocates the resources towards the most profitable, and it is unlikely that the profits achieved will be sustained. This is because the withdrawal of the PBDAC from distributing inputs increases the levels of middlemen and increases the transaction costs and creates uncertainty about prices and a state of asymmetric information. Big producers will have better access to market information, know-how and technology as well. There

is the risk of a further increase in agricultural inputs with the withdrawal of the bank, especially with the absence of a relevant legal infrastructure to regulate the market, which Egypt's market still urgently needs. While merchants used to sell at similar prices to those of the bank and give concessions to farmers in payment to compete with the bank (see El-Gaafarawi, 1991; Abou Mandour & Siyam 1995) the complete withdrawal of the PBDAC will deprive farmers of sources of information about price levels and will give merchants more control over prices. There is also the potential for further increases in the cost of production with the increase of rent after the full application of law 896 of 1992 in the relationship between landowners and tenants.

In a liberalised economic environment market signals are supposed to direct farmers to investment in these competitive crops. This encourages exports and enables them to achieve food security targets on the basis of external trading of high value foodstuffs with staple deficit foods. In addition to the direct effect of the liberalisation of agricultural prices, the liberalisation of exchange rates and initial devaluation are expected to have some impact on agricultural production as well. The prices of export decrease and the prices of import increase, this is expected to increase demand on exports and reduce it for imports. However, this is related to elasticity of demand for imports which is low for cereals as a staple food. USAID anticipated a shift towards production of these high-value foodstuffs such as: strawberries, fine green beans, peppers and tomatoes, as well as grapes, peaches and other citrus crops to yield as much as US \$ 100-150 million a year up to 1996 (as cited in Bush, 1996:83).

Other issues need to be considered when discussing exports. First, there is the increasing competition in the global market, and the willingness of importing countries to open their markets to Egyptian exports. Egyptian Agricultural exports have their biggest market in the Arab countries which are completely free markets open to different countries, with increasing competition in the world market, Egyptian exports will suffer more competition there. The European market is the second market for Egyptian exports as Egypt has a joint economic co-operation agreement with EC countries since 1977. According to this agreement some Egyptian exports are custom free, others have low custom rates compared with other countries. According to the GATT agreement these countries are obliged to reduce

their customs on agricultural products by 36 percent during six years. This will lead to the elimination of the Egyptian exports privilege (Kheir El-Din, 1997:7). A new economic co-operation with the EC has been under negotiation for years. Agricultural aspects remain the principal obstacle to the concluding of an agreement, as Egypt cannot reach an agreement that compensates her for the GATT losses. Studying the effects of free trade on Egyptian crops after the Uruguay Round reveals increases in the international demand and price of rice, which encourages Egyptian exports. The failure of Egypt to satisfy its quotas in the quota system of the EC of some food products like potatoes, oranges, onion and green beans is due to its inability to meet EC goods standards. This underlines the internal constraints on Egyptian exports and the need to improve product quality, packing, and preserving facilities (*ibid*,:17-18).

The direct effect of reducing custom duties on Egyptian imports is a decline in the prices of imported goods, which increases their competition with local goods. However, with the elimination of subsidies on agricultural goods in the international markets, this increases their price and reduces their penetration in the local market. However this does depend on the elasticity of demand which is high for staple food where the substitutes are limited. In this case, the effect of a rise in the international markets will increase the burden on the balance of payments. Consequently it is in Egypt's interests to increase the production of such import-substitute goods such as wheat - a matter which Egypt is already considering. Another aim of price correction is to reduce the tax burden on farming, hence improving incomes and stimulating the supply-side response. Ending such transfers is only macroeconomically sustainable if either government expenditure is reduced or an alternative source of revenue is found (Richards, 1994:19). However, although the "right prices" and the elimination of indirect tax can achieve efficiency gains in reallocating land from lower to higher value crops, these gains are what Richards calls a 'once for all' type (Richards, 1994: 3 & Bush, 1996: 116). It is also argued that price liberalisation of agricultural crops would improve terms of trade between agricultural and non-agricultural goods which in turn would encourage more investment in agricultural projects (Abou Mandour, 1996:185).

Another element of market economy in agriculture is privatising input marketing, which is claimed to promote more timely delivery of farm inputs

(Richards, 1994:19). The Egyptian case reflects a clear failure in this respect and will be discussed in detail in the following chapter. With the withdrawal of the PBDAC from marketing and with liberalisation, the PBDAC intends to convert completely to a commercial bank. As the role of the bank in distributing agricultural inputs is eliminated, so is the in-kind credit, and subsidy on interest rates. The new policy aims at the bank providing its own finance and reducing its reliance on loans from the banking system. This needs an active policy from the bank to collect deposits and to offer a near market interest rate. Lending within the deposit range is thought to enhance the efficiency of resource allocation among rural firms and households (Adams & Kamel, 1996:257). Although the bank's deposits increased substantially between 1984/85 and 1993/94 from £E 574 million to £E 2949 million (*ibid*) it covers less than two thirds of the bank's loans and its possibility to accelerate its growth-rate is limited, given the low income levels and saving rates in rural areas. To achieve this policy the bank needs to absorb savings from urban areas, which in turn need the bank to be competitive with commercial banks as regards its deposits and lending incentives. The fact that PBDAC is a government bank constrains its lending policy as it relies heavily on collateral.

#### ***Cost Recovery Programme***

Water resources seem to be a major limitation on agricultural expansion in the future. The shortage of water is estimated to be in the range of 2 to 6 percent of total requirements if the proposed land reclamation programme is to be implemented at the presently proposed scale of about 1.4 million feddans; the shortage would be more severe under drought conditions. The availability of water could be increased through the completion of the Jonglai canal, more effective in farm irrigation practices, changes in cropping patterns in the direction of less water consuming crops and the introduction of an improved irrigation system in the old lands (World Bank, 1993:24-25). While the completion of the Jonglai canal is related to the external factor of the civil war in Sudan, the World Bank and the USAID thought the other goals could be achieved through a cost recovery programme which would allow for the recovery of O&M costs and if possible recover a contribution towards investment costs. In justification of such a programme, the World Bank pointed out that indirect taxes in the agricultural sector, which could be argued as a source of finance, has been removed, in addition to the need to increase the current level of

spending in order to ensure the required adequate levels of maintenance. The World Bank thought that the necessary charges to recover O&M costs would not have a significant impact on net farm incomes. The fee covering present O&M would only be in equivalent to 3 percent of net farm revenue for representative farms of 3.5 and 2.2 feddans in the Delta and Upper Egypt respectively, while a fee covering present O&M and capital costs would be equivalent to 5-6 percent of net revenues. This seemed to be bearable considering that real net farm incomes have risen by about 40% since 1984, according to the World Bank estimation (World Bank, 1996:26-29). This says nothing about the non-representative farms, those of less than one feddan. It also ignores the unequal effect of the reforms on income according to farm size and crop mix. It overlooked its own recognition of the steep fall in agricultural wages since 1985 which shifted income towards land holders and reduced it for those without access to land and the near landless (Bush, 1996:82).

From the World Bank's point of view the cost-recovery programme would rationalise the farmers' decision concerning crop mix and would shift the crop pattern towards crops with low water requirements. According to their studies, the value added per m<sup>3</sup> water, excluding the cost of water, is high for tomatoes and wheat, cotton, beans, and oranges respectively, while it reaches its lowest for sugarcane and rice respectively. It is estimated that about 35 percent of water is used by sugarcane and rice which together account for 13 percent of agricultural value added (World Bank, 1993:28).

While the government of Egypt agreed to apply cost recovery programmes on the new reclaimed land, on the old land there are social and political difficulties surrounding the implementation. The national plan referred to the need to encourage crop patterns that achieve the highest possible level of food security taking water into consideration in the economic accountancy, without giving in-depth view of this matter. On the other hand, one of the Egyptian academics and a prominent actor in the reform programme in agriculture announced in an interview that there is no intention to implement this part of the programme (Bush, 1996:81). This suggests that the Egyptian government manipulates the World Bank and the farmers and it can change its decision in case of severe pressure from the Bank.

### *Land Tenure Arrangements*

Under the old land tenure-law, tenants enjoyed land rents with tenancy contracts in perpetuating the ability to pass them on to their heirs. This meant that tenants enjoyed legal protection against being dismissed from the land. Rent was equal to seven times the land tax, re-valued every ten years and reached around £E 250 per feddan in 1989. In 1992, a new law was revised (law 96), which provided a transition period of five years during which rents were increased to 22 times the land tax and the owners were able to buy back the tenancy contracts. At the end of the five years, rents were to be determined freely on market bases; in addition, owners are now able to terminate current contracts.

When the new land reform was launched it was justified on equity issues, improved productivity and land property rights (see National Plan; Mustafa, 1994:11). Mustafa drew attention to the relative stability at the amount of rent in the same time of increasing land productivity, crop prices, hence land returns. In addition, due to many socio-economic changes many beneficiaries of the tenancy contracts moved to other occupations while keeping the rented land or rented it in turn to others which led to inefficient or weak utilisation of these lands (Mustafa, 1994:11).

The World Bank emphasises the importance of land tenure issues to maximise the returns from land. They believe that the low level of rents acted as a disincentive to rent out land and in combination with law 116, which prohibits the leaving of land fallow for more than a year, encouraged insufficient use of resources. This is because they are forced to cultivate it in a suboptimal manner in order to retain their ownership rights (World Bank, 1993:33). The World Bank still expresses dissatisfaction at the current levels of taxes, and calls for more frequent reassessments. They also call for bringing farmers owing less than 3 feddans within the purview of the land tax system. This is at odds with the equality issues which the Bank called for earlier. Holding of three feddans for farm size indicates a minimum holding of land for average family size to avoid poverty (see Kishk, as cited in Bush, 1996).

When the time to implement the law was due, the government had to face an increasing number of violent acts in many governorates where there were high levels of tenancy, namely Dakhalia and Kalubia. Initial government response was the use

of oppression by the police force. While the law tried to secure some fairness for the owners it created an unfair situation for the tenants. In fact the government had done nothing during the transition period of the law to find a solution for the tenants who rent all the land they cultivate. Even data about the exact number and the total area that is rented is not available and certainly equity issues not addressed. Any assessment of the problem of the relationship between tenants and owners should integrate the long-term dimensions of the problem. These are the long term relationship between resources (land and water in particular) and population as stressed by Abdel-Fatah (1997:32) and the resulting problem of land fragmentation.

The relationship between the population and resources is important and begins with several issues. The relationship between land and population is not balanced and the average size of holdings is diminishing. In the meantime, there is an increasing challenge facing the agricultural sector in the near future to increase its production to meet increases in population. On the other hand, land and water are the main constraints on agricultural expansion and the fact that the new land has low productivity compared with the old land that is still the main contributor to agricultural production. Bearing this in mind, it is important to point out that due to the small size of farms and with the large size of households in rural areas, the relative importance of agricultural assets has changed considerably. Land is no longer the main source of income, as farmers have developed different types of investment, the most important is in agricultural machinery where the income from renting them out exceeds the revenue on land, in addition to the increasing importance of non-farm income (see Abdel-Fatah, 1996:32; El-Gaafarawi, 1991; CACS, 1994). While land fragmentation had a negative impact on the efficient use of resources, since could affect productivity, increase in water wastage, in some cases it encourages the use of agricultural lands for urban purposes, which is more profitable (El-Gaafarawi, 1991). Thus land consolidation may prove useful if equity issues had been taken into consideration.



**Table 5. 6 Number and Areas of Holdings by Feddans in 1989/1990**

	Total Holding Areas			Completely Rented Areas		
	Number of Holdings	Holding Areas		Number of Holdings	Holding Areas	
		F	Q		F	Q
Less than Fed	1050900	508144	17	173130	87335	16
1-	1215869	2078541	8	170969	279095	19
3-	350222	1250949	17	29632	103509	8
5-	198926	1250038	23	9147	57078	11
10-	60932	793707	13	2470	31288	13
20-	27288	770403	3	1135	31552	23
50-	4520	287585	4	371	23128	2
100+	1622	909803	4	316	65080	16
Total	2910279	7849173	17	387160	677069	13

F = Feddan

Q = Qirat

Source: MALR, 1989/90 Agricultural Census, Volume of Total Republic p 15.

It is important to study the holding structure in rural areas to assess the impact of the law on equity on the one hand and productivity and efficiency on the other. Table 5.6 shows the last available data on the distribution of land holdings. There are different kinds of holdings: those who own the whole area of their holding; those who rent for cash the whole area of their holdings; those who rent the whole area as share cropping; and those whose holding is a combination of two sorts or more of the above-mentioned. There are also different kinds of landowners, those who hold their whole land, those who rent out all their land, and those who hold part and rent an other part. The problematic categories of tenants are those who rent all their lands and who are threatened with landlessness. These amount to 387,160 tenants, who represent 13.3 percent of the total number of holders and hold 8.6 percent of the total area. There are also those who own part of their land and rent another part. They account for 16.2 percent of the total holders and rent 7.6 percent of the total area. Most of those with mixed holdings are concentrated in the smallholdings: 66.6 percent hold less than three feddans, and 26.8 percent hold five feddans and less than seven. It is also of note that in these two categories about half the holdings are owned and the other rented. Losing the rented part increases the suffering of those who own less than three feddans, which moves the holders in the second category to the edge of poverty. Another group are land owners who rent out their land, partly or completely, and do not get a fair rent, especially those small owners whose standards of living is low and some of whom work in agriculture but cannot obtain access to their land.

The last year of the transition period of the land reform witnessed some violence and the police force was used to control the antagonists. In some cases the police clearly supported the interests of the landlords. To contain the situation, the government offered three suggestions:

a- to establish a land fund to provide soft credit for farmers who want to buy the land.

b- to give reclaimed land to farmers who have to leave the land.

c- to postpone the implementation of the law in land owned by the state (Abdel-Fatah, 1997:34). The provision of finance is subject to many conditions which are completely irrelevant to the small farmers. Among these is that in which the upper limit to a loan is 70 percent of the land value repaid over 7 years at an annual interest rate of 13 percent. Abdel Fatah compares this to housing loans for university professors which are repaid over 40 years at an interest rate of 5 percent; while some farmers who obtained contracts for reclaimed land discovered that the same piece of land was allocated to more than one farmer. This is a false solution merely to calm the farmers during the transition period (for more detailed discussion of the validity of the solutions offered see Abdel-Fatah, 1997: 33-7).

### **5.3.2 The Actual Reform Measures in Egyptian Agriculture**

The reform programme was divided into two phases. The first phase, 1987-89, reduced price and marketing controls and delivery quotas for 10 major crops, reduced subsidies on inputs and increased farm-gate prices of fertiliser by 75 percent, (See Table 5.7 for changes in the direct subsidy for agricultural inputs). The PBDAC reduced its involvement in input marketing and private sector participation was encouraged.

During the second phase, 1990-94, a complete liberalisation of the sector was brought about. This included increasing cotton procurement prices to 66 percent of the economic price in the early 1990s and complete liberalisation of its prices were achieved in 1994. Government control of prices for different crops was completely abolished. Procurement quotas for all crops including rice were removed, except for sugarcane, as the government still controls this industry. The compulsory cropping pattern was removed. In addition, there was the limiting of the role of the PBDAC to providing credit for agricultural activities; the elimination of all subsidies on inputs and the restricting of subsidised credit; liberating of seed production and marketing;

the introduction of a new law to regulate the relationship between landlord and tenants -Law 96 for 1992 ( Khedr, 1994: 52; Kheir El-Din, 1997: 3-4).

**Table 5. 7 Changes in Subsidies for Agricultural inputs during 1988/89-1991/92**

Years	Fertilisers	Insecticides	Seeds	foddor	Interst rate	Total
1988/89	182.60	114.70	3.60	na	na	na
1989/90	175.80	118.90	1.70	229.70	112.00	638.1
1990/91	193.80	116.70	3.50	170.60	92.00	576.6
1991/92	62.10	131.70	4.00	104.40	65.00	367.20

Source: Othman, M. A. 1993. El-Athar El-Mutarateba Ala Elgha' Eda'm Esyra'i fi Itar Barnameg Etakayouf El-Haykali fi Esira'a El-Misrya.

Privatisation programmes in agriculture were also encouraged. This took two forms; first, to limit state ownership of assets and second to encourage private initiative in new activities which used to be the monopoly of the public sector.

One of the aims of the privatisation programme was to encourage the private sector to replace government ownership to land both in agrarian reform and reclaimed land. The agrarian reform authority planned to sell 10,000 feddan to the private sector at current market prices. It also planned to sell 84.2 thousand feddans of rented land to tenants and holders. 36.5 thousand feddans have already been sold (Khedr, 1993:53).

The GOE encourages private sector participation in land reclamation and plantation on the new land. The role of the state in the reform era will be limited to the infrastructure, exploratory studies to choose the most suitable areas for reclamation and to provide finance and the needed facilities for the plantation process. The state is encouraging private sector ownership for reclaimed land and trying to limit public ownership through three kinds of policies:

Selling land under the control of public agricultural companies to investors, workers, and graduates. The revenues are planned to be used to finance the reclamation of new land. About 384 thousands feddan have already been sold and have been planted.

Selling land after providing the infrastructure, This is the policy since 83/84. The plots sold to the private sector's investors were between 3 and 10 thousand feddans. Selling or renting land suitable for reclamation to the private sector and encouraging it to participate in land reclamation. This policy started in 1987.

In all, the total area under privatisation, according to the three types mentioned above, is about 808 thousand feddans. In addition, the private sector is investing

about £E 700 million to reclaim and develop 150 thousand feddans of non-reclaimed land. The total amount under private sector effort for reclamation is about one million feddans (Khedr, 1993:56).

### 5.3.3. Reform Impact

In this section we study the impact of reform at the national level, then particular emphasis is given to the effect on farmers, as this is the most debatable part. I study the effect on farmers' access to resources (ability to invest) and utilisation of resources (investment type) then the farmers' welfare and living conditions. Those in the agribusiness will be assessed in the following chapter.

#### *Utilisation of Resources*

Several changes have occurred in the crop pattern during the reform. These changes cannot all be attributed to changes in prices alone. Other factors affected these variations, among them changes in productivity. Table 5 shows changes in both crop areas and productivity during the reform.

Table 5. 8 Cultivated Areas and Productivity of Main Crops (1985-1995) (area=thousands of feddans)

Crop	Cultivated Area				Productivity*			
	1985	1990	1992	1995	1985	1990	1992	1995
Wheat	1186	1955	2092	2512	10.53	14.56	14.72	15.19
Maize	1914	1975	1967	2133	14.92	17.40	18.41	17.79
Rice	926	1037	1216	1401	na	3.01	3.40	3.60
Cotton	1081	993	840	710	6.79	5.21	7.15	7.27
Sugarcane	250	274	267	301	na	902.40	967.75	1020.93
Clover	1865	2620	2542	2430	---	---	---	---
Vegetables	1018	945	904	1043	---	---	---	---
Fruits	429	866	907	954	---	---	---	---

\* Productivity per feddan: Ardeb for wheat and maize, M.Qantar for cotton, Dariba for rice, and Qantar for sugarcane.

Sources: For 1985 CAPMAS as cited in Kheir El-Din, 1997:9, For 1990-1995, CAPMAS. 1996. Statistical Year Book 1990-1995. Cairo.

While changes in prices, hence in the incentive structure, aimed to increase the areas of wheat, cotton, and horticulture, only wheat and fruit areas have increased. While cotton and vegetable areas showed a downward trend and only the vegetable area revived in 1995. Changes in prices aimed also to reduce or maintain the area of rice as a crop consuming high quantities of water. The areas of rice were increased. The figures show that the highest response was for wheat. This was high due to the coincidence of increasing prices and productivity. The increase in productivity cannot be wholly attributed to the effect of better incentives for farmers as it is related mostly to research efforts in previous years. On the other hand, there

is a belief that part of the increase in the cultivated areas is only statistical as before SAP farmers used to underscore their wheat areas to avoid compulsory delivery. There are also indications that the increase in the acreage of wheat was not part of the increasing role of the market rather it was a response to the self-provisioning needs in the market era where access to flour in the market was becoming more expensive (see Mitchell, 1998: 22-23). Mitchell uses evidence for the farmers' behaviour in one of Qina's villages where small farmers were the ones who responded by increasing their cultivated areas of wheat (*ibid*).

Figures for berseem show a decreasing area during the adjustment. Cotton followed a decreasing trend in area and yields in the pre-reform period, although the increase in productivity starting from 1990 which was related to an increase in prices. Area response was negative. Land was taken from berseem-cotton rotation and used for wheat and rice rotations (Nassar, 1996). This reveals that an increase in price does not always lead to increases in the area cultivated and that there are other factors that affect the crop area. In the case of cotton, the increase in productivity compensates for area reduction, as cotton is a relatively risky crop which can be subject to severe pest attacks in some years, and with the increasing trend towards preferring self-provisioning crops, especially by small farmers, reduces the area of cotton in favour of staple crops, including rice.

*Crop production responses.* We can now ask how these changes in crop patterns and productivity affect production. A study of the reform impact on 23 major crops on old land revealed that significant changes in production did not occur at the same time for all crops (Nassar *et al* 1996). Also many policy initiatives that were crop-specific occurred at different times. The years 1980-1986 are considered the pre-reform period and 1987-1993 the years of reform. Overall production grew at 2.7 percent a year from 1987 to 1993, compared with 1.1 percent before the major reforms began (*ibid*:90). The data shows a major increase in tomato production after 1984, which the authors related to non-policy factors. The four main crops: wheat and maize production increased massively after 1986, rice production increased after 1988 and cotton only shows increase after 1991. The writers relate the changes in these four main crops to changes in policies, particularly price policies (Nassar *et al*, 1996:86). However, the increase in production cannot be attributed to increases in price alone. It was clear that great improvements in

productivity happened especially for wheat due to investing in improving new varieties. The increase in productivity per unit, in addition to an increase in prices, was the main incentive for increasing the cultivated area from wheat, hence an increase in total production. The result of these increases in self-sufficiency was positive. Self-sufficiency from all major crops increased except for lentils, as can be seen in table 5.9 below.

**Table 5. 9 Self-Sufficiency from Main Crops**

Commodity	Self-Sufficiency Ratio	
	1990	1995
Wheat	43	53
Maize	76	74
Rice	113	118
Broad Beans	91	96
Lintels	17	11
Edible Oil	14	18
Sugar	59	83

Source: MALR, Central Agency for Agricultural Economics, as cited in Kheir Eddin, H. 1997:11.

How did these changes in crop patterns, productivity and production affect tradable goods in the agricultural sector? Was it able to the competitiveness of the agricultural crops? Figures refer to the fluctuating performance of the agricultural exports during the period 1991/92 to 1995/96. It reached its lowest in 1992/93, £E 976.7 million, and it highest in 1994/95, reaching £E 2088.4 million (MOP, 1997:59). These variations in the value of exports are related to the usability of the exported crops. It was mainly affected by fluctuations in the exports of cotton, which was still the major agricultural export. Its export value dropped to its lowest point in 1992 and 1993 at £E 175.2 million and £E 146.7 million respectively and increased in 1994 at £E 691 million. It was affected also by variations in rice, the second major crop. In general, most exported crops, potatoes, refined sugarcane, and oranges, experienced major fluctuations during that period though in different directions (see CAPMAS, 1996: Table 11.13). The impact on the agricultural trade in general was positive, as its deficit decreased due to the decline in imports, especially those of wheat (Kheir El-Din, 1997:12).

*Utilisation of resources at farm level;* It is important to understand which classes of farmers increased the areas of which crops and why, and what were the other determinants of resource allocation other than nominal profit. This will enable us to assess the effect on income distribution and equity issues. An empirical study

conducted in five governorates: three in the Delta (Sharqya, Daqahlya and Munifiya); one in Middle Egypt (Bani-Suef); and one in Upper Egypt (Aswan) (see Abou-Mandour & Siyam, 1995) examined the relationship between structural adjustment and agriculture. The study revealed that farm size and crop pattern were related and that middle-size and big farms (2-less than 5 feddans, and more than five feddans respectively) had a more diversified crop pattern. Their study recorded that small farms allocate a higher percentage of their land to growing cereals (wheat, maize and rice) compared with the two other groups. As the study considered those crops that benefited from the policy of reform, it concluded that SAP has a positive sign concerning equity, provided that small farmers have better chances to access agricultural machinery, high-quality seeds and credit to enhance their benefits. The study also revealed that rental contracts discourage the cultivation of cereals and that ownership of tractors is an important factor in encouraging the cultivation of such crops (*ibid.*;132-34).

Meanwhile horticultural cultivation increased considerably with the increase in holding areas. Big and middle-size farmers were able to benefit more from these crops which used to be associated with big farms because of the need of large investment and to the difficulties in accessing the markets. High percentages of farmers in the three different groups show a preference for cultivating berseem, which is related in turn to the ownership of livestock. Ownership of livestock increases with increase in farm size but not by the same portion. The differences were significant between the small and middle-size farmers but not between the middle and big farmers. Potatoes achieved minor advantages during SAP, and cultivated areas were independent of farm size and holding type. Nevertheless sugarcane cultivation were related to large holdings and ownership of land in particular, and the availability of agricultural credit played a vital role as well, while it had a negative relationship with rental contracts due to its long duration on the land. As for cotton, which was still under control when the study was conducted, its area expanded with the increase in farm size and was more related to rented land (*ibid.*;134-38). Findings at farm level confirm Mitchell's view mentioned above that small farmers are motivated by self-provisioning in selecting their crop patterns.

### *Access to Resources*

A recent empirical study in two Delta villages revealed uneven access to resources, land and input production, in addition to the spread of poverty. The study admits that poverty is not new and can not be attributed to SAP alone, however, the strategy introduced does not address the problems of the majority of the poor. In fact it concentrates attention, and resources, upon peasants with more than 5 feddans of land holding and owners rather than tenants (Bush, 1996: 121-122).

There is no definite data at the national level about how SAP affected farmers' access to resources. However, there is some indication about the direction of change. While there is no recent and comparable data about changes in land during SAP, the last two agricultural censuses of 1981/82 and 1989/1990 show that the number and percentage of tenants who rent all the area they hold compared to the total holders has declined from 18 percent in the former census to only 13.3 percent in the later one; so did the area they hold and its relative importance to the total area, which declined from 11.9 percent in the former census to 8.6 in the later one (Hassan, 1997:23). While this happened before the introduction of the law of relationship between the landowners and tenants, it is important to note that the debate about it started earlier and some tenants searched eagerly for solutions before the introduction of the law which was thought to be in favour of the landowners, hence more harmful to them. It also emphasises that landowners were keen to recover their land and were trying hard to do so. There is no data to explain whether this shift from tenancy to ownership was in favour of the old tenants or not. However, if we know that most of this category of tenants are small farmers, of whom 95.6 percent in 1981/82 and 96.6 percent in 1989/90 held less than five feddan, it is more likely that they could not afford to buy the land. Furthermore, the increased percentage of tenants of smallholdings suggests that the big tenants were more able to buy the land.

There is empirical evidence that during the transitional period of the land-reform law some small tenants had give up their tenancy contracts. In one village about five or six farmers had to leave the land due to the new law (see Bush, 1996:143). The last year of the transition period witnessed more confrontation between tenants and farmers due to the landlords' attempts to recover their land and the failure of the government to provide real solutions. As I discussed earlier, credit



terms to buy land were difficult, and those who received reclaimed land had problems of access, as it was allocated to more than one person.

Access to credit, total short-term credit for crop production increased in nominal terms from £E 676.6 million in 1986/87 to £E 2204.9 million in 1995/96 (PBDAC, unpublished data). However, in real terms, if we consider the inflation rate, this amount did not undergo any real change as the real amount for 1995/96 was equal to £E 679.5 million. In the meantime, the interest rate subsidy was reduced from £E 111.1 million in 1989/90 to £E 7.4 million in 1995/96 in nominal terms. The decline is much greater in real terms. As a result, the interest rate increased by about 50 percent over two years starting from 1991 (Khedr, 1997:22, 23, 29).

The farmers' accessibility to credit has decreased considerably due to the new land tenure system. Local banks refrain from giving credit to tenants due to lack of guarantees as they might be dismissed from the land according to this law within five years. Their access to credit reached its minimum during the last year of the transition period. The privatisation of the input markets reduced the farmers' accessibility to credit as well. Farmers complained that in addition to the increase in input prices, there was a lack of flexibility in credit terms and repayment methods (Bush, 1996:134).

So far water for irrigation is still under the same rules, and except for the usual complaints from some of the old and new land owners about the unavailability of water. Trade liberalisation and a decrease in custom duties on capital goods might provide more advanced technologies at a cheaper price. On the other hand, there might be more restrictions on the transfer of technology.

As for input accessibility, input markets were liberalised, subsidies were eliminated and prices allowed to rise to reflect market levels. The prices of fertilisers, which represent 50 percent of the input costs, have increased three-fold, while the prices of crops have not increased by the same proportion (Khedr, 1997:22).

In the empirical study quoted, farmers complained not only about the increase in fertiliser prices but also about the inflexible credit terms. Some of them developed their own ways of coping with the new situation. Some of them increased the use of organic fertilisers and reduced the use of chemical fertilisers. Other used nets with hormones instead of chemicals. Nevertheless most of them referred to the

increase in the use of fertilisers and chemicals in spite of the increase in prices. One farmer mentions that there is an increased tendency to use chemicals for all crops while it was restricted to vegetables before (Bush, 1996:134,137). However, it seems that this farmer was referring to a general trend before SAP or to personal experience. Official figures show continuing declining trends in the use of fertilisers and insecticides at national level. Insecticides used in agriculture decreased from 15,099 tons in 1989/90 to 5,835 tons in 1994/95. This rate was even worse in the previous two years reaching just 4,360 ton in 1992/93 and 3,298 in 1993/94. Between 1989/90 and 1994/95 azot and amonia fertiliser use decreased from 5,007 tons to 552 tons, for phosphate fertilisers from 1,101 tons to 46 tons, and for potassium fertilisers from 44,142 tons to 25,706 tons (CAPMAS, 1996, Table 2.12).

The decreasing trend in the use of fertilisers was not only because of the increase in prices; it was sometimes due to lack of availability. The privatisation of marketing channels was responsible for this, as fertiliser exports increased. There was a severe shortage of fertiliser in the summer of 1995, which became a crisis in some areas and threatened the production of some of the main crops. A clear example is an empirical study in 335 villages in the two Upper Egyptian governorates of Qena and Aswan from April to September 1995. As a result of the severe shortage, the prices went up from £E 26.00 to 50.00 per sack (190% increase) and continued to increase until it reached £E 80.00 per sack (350% increase) around the end of September 1995 (Abdel Aal, 1996:6-7). The more dangerous effect was on the productivity of the main crop in this sugarcane region; farmers had to start planting and irrigating the crop without adding any fertiliser, as it required. Many farmers expected a considerable drop in production; the most desperate farmers expressed their intention to remove the crop (*ibid*).

The other possible effect of liberalisation on the input trade is that on the availability of better quality inputs, which means the provision of improved varieties of seed, there may be the more effective use of less environmentally-harming fertilisers and chemicals. In this respect it is difficult to separate the private effort from the public. There were considerable improvements in the yields of many crops. For wheat for instance the massive increase in productivity was due to the protracted efforts of research institutes. Private sector efforts may be seen in the production of vegetables, where it was responsible for providing seeds. Tomato production

increased massively however this was not sustainable as there were dramatic falls as well. This refers to the importance of the complementary services needed in the agricultural sector, namely, the need for better extension work to explain the right way to use it. In case of tomatoes, the new hybrid varieties of seeds introduced were highly productive, however, this character does not have the ability to pass from one generation to another. This means that farmers can not use the new product to grow their seeds, the seeds they received do not possess the same qualities. This was the cause of a massive drop in production for some farmers (interview with input distributor in early 1996). Trade liberalisation could help to provide more advanced farm machinery either through importing new technologies or through the combination of foreign technology and capital to produce machinery (see below in the empirical study, examples of importing advanced technologies for water treatment, and the production of farm tractors)

### *Effect on farm Income*

Income from crop production: Prices of inputs increased during the reform because of subsidy elimination. At the same time crop prices increased as well. What was the total result on income? The cost of production for the main crops doubled many times over during the reform. This was mainly due to an increase in input prices as the cost of input as a percentage of total cost increased during the reform (Nassar, 1993:27-32).

To assess the total impact of the changes on the input and production prices, a percentage was calculated for the unit production costs for the farm-gate price of the major food crops under investigation over the 1975-1992 period. The value of by-products per feddan was deducted from the total costs in order to obtain the total cost of the major products (Nassar, 1993:32). In the second half of the 1970s, the percentage was relatively high while it tended to fall throughout the 1980s. Following the application of the reform, the percentage increased for most crops with indicates that income decreased. During 1989-1992, the percentage increased from 15 percent to 30 percent for wheat, from 39 percent to 58 percent for faba beans, from 19 percent to 28 percent for summer rice and from 54 percent to 60 percent for sugarcane. It was only for cotton that the percentage fell from 60 percent to 34 percent, which meant an increase in income generated by this crop (Nassar *et al*, 1993:32-33). These results are consistent with what another study referred to as a

decrease in the income of the different mixes of a three-crop rotation during the agricultural year, except for the one including cotton. It also drew attention to the fact that the increase in income was not because of price liberalisation but the administered price for cotton (Abou Mandour, 1996).

Another study estimated the agricultural resource income (ARI) for 11 main crops. The ARI is defined as the difference between the gross value of agricultural crop production and the costs of current inputs purchased from outside the agricultural sector. It concluded that the real ARI value in the reform period (1987-1994) was 19 percent higher than its average value in the pre-reform years (1980-86) (Rady *et al* 1996:145-55). These estimated increase is modest, and part of it is attributed to an increase in yields, as referred to earlier. The costs were also underestimated as they were calculated only for inputs only from outside the agricultural sector. Examining the figures in the same study, the annual estimate of real ARI (*ibid*, Table 7.2, p115) reveals that it reached its highest in 1989, 1990, then there was a general downward trend between 1991 to 1994. This proves that the increases were not sustainable.

Income from crops is only one source of income for rural families; it is also differentiated according to farm size and hence crops pattern. From the above discussion concerning crop patterns and farm size it is noticeable that big farms allow farmers to adopt crop patterns that allow them to increase their benefits. Big farmers receive many more benefits from the increased revenues of some crops, such as cereals, horticulture, sugarcane, and dairy products; in contrast to small farmers, who are likely to achieve their highest benefits from cereals. However, the benefits achieved by middle and big farmers from the same crops are higher. This is because the previous study revealed that big and middle farmers had the same and higher preferences respectively towards cultivating these crops, if we consider the percentage of farmers who cultivated them in each holding group. Although small farmers cultivate a higher proportion of their total area. In absolute terms, the cultivated areas of these crops by middle and big farmers are likely to be higher (see Abou-Mandour & Siyam, 1996: Tables 4/7, 4/8 pp.128,130). If we consider that small farmers usually devote an even higher percentages of their products for self-provisioning, this means that their benefits are limited to part of the marketed produce. The empirical study of Abou-Mandour and Siyam (1995:147-50) revealed

that small farmers sell only 13.7 percent of their wheat, 19.1 percent of maize, 50.7 percent of rice, 7.0 percent of fine maize, 87.0 of potatoes, and 26.5 percent of berseem. These ratios rose with the increase in farm size and recorded 58.6, 42.0, 85.2, 11.9, 96.4, and 66.3 percent for the aforementioned crops respectively. This supports Mitchell's view (1998) that market reforms supported self-provisioning of staple foods.

It was also observed that livestock products contribute a relatively high percentage of income to small holders, as demonstrated by other empirical studies (see Richards, 1995: 41). As livestock products were protected until recently the impact of removing such protection on livestock products during SAP was anticipated to reduce prices and the attractiveness of cultivating berseem (see *ibid*; WB, 1993:42). Richards expected that in the short-term small farmers who relied heavily on sales of dairy products were likely to lose (*ibid*). Abou-Mandour and Siyam's study (1995:135) refers to a loss relating to livestock but not for dairy the products. Abou-Mandour and Siyam's view is more likely as dairy products face less competition from imported goods and have less near substitutes compared with red meat. This means that small farmers are likely to achieve minor benefits from dairy products.

It is noticeable that the rural poor- the landless and small holders- rely on their labour force as a main source of income. It is estimated that even for farmers with between 3 and 5 feddan the income raised from the labour market is about one third of their income; this percent for smaller farmers is even higher. In all cases off-farm wages are higher than agricultural wages. Both agricultural and non-agricultural wages are likely to decline. Agricultural wages declined by 40 percent in the late 1980s. As 2/3 of rural off-farm employment is in non-traded goods, devaluation reduces the prices of such goods, which in turn reduce the demands for their labour in the short run (Richards, 1995:39-41). On the other hand, the decline in agricultural waged labour means that the cost of production for big farmers has declined as they rely more on waged labour.

The same study for 11 crops showed an increase in hired labour per feddan in the reform period (Rady, 1996:156), this was due to a decrease in the hired labour wage as shown below, which encouraged the hire of more labour. The study drew attention to the role that can be played by the agriculture sector in creating

employment through linkages between agriculture production and non-farm employment. The increase in production increases employment arises from manufacture and distribution of agricultural inputs and the processing and distribution of agricultural output (*ibid*). Although this is true in general, it should be noted that the ability of the agribusiness to create employment is low, as proven from the empirical study (see next chapter)

Another empirical study proved that working days in agricultural decreased in 1991/92 compared with 1986/87, while increased for non-farm work (Abou Mandour, 1996: 195)

There was general agreement that real wages for agricultural workers decreased during reform (see, Rady *et al*, 1996; World Bank 1993; Abou Mandour, 1996). This refers to the uneven effect of reform on rural people; waged labour is usually one of the categories that lies below the poverty line (see Kuraim, 1994). The World Bank's report in 1993 referred to the decline in real wages in 1991 by 60 percent compared with the 1985 level. Official data reveals that real wages decreased in 1992 by 50.8 percent compared with 1986 (Abou Mandour, 1996: 195). An empirical study estimated a 50.5 percent decline between 1991/92 and 1986/87. The study revealed that there was a greater decrease in the wages for women than for men, which meant that the programme harmed the opportunities for women in work (*ibid*).

Structural adjustment increases the cost of production because of increased prices of inputs. An empirical study revealed the undifferential rates of using fertilisers among different farm-size classes. This means that any increase in the prices of fertilisers will lead to equals effect on different farms, however, the relative increase in cost compared to the small farmers' income will be higher (Abou-Mandour & Siyam, 1995:140).

The differential effect on income in rural areas related not only to farm size and hence crop pattern, it also related to the different sources of income. In conclusion, we can say that wage labour and farmers with less than two feddan stand to lose, while with those having 2-5 feddan the effect is indeterminate, those with more than five feddans are likely to gain.

#### ***5.4. Conclusions***

While state intervention was blamed for the poor performance of the sector, one major drawback of the policies of state intervention was that it was not differentiated between the poor small farmers and the big farmers. This resulted in the rich benefiting more than the poor and the burden on the state budget increasing.

The reform policies were biased in favour of big farmers as well. At the national level, changes in crop patterns were not consistent with the intended policy changes. Increases in wheat and cotton for example cannot be attributed to changes in prices only. Food security was improved, but agricultural exports did not increase as expected, and individual crops did not follow a consistent trend.

At the farm level the landless and small farmers stood to lose while big farmers obtained gains. The type of changes in farmers' access to resources and utilisation of resources undermined their ability to invest at farm level and the sustainability of resources for the future. As their access to agricultural inputs and credit was undermined, the poor experienced greater impoverishment. Increases in crop areas were achieved through greater intensification in the cultivated areas. The crop patterns increased from 11.2 million feddan in 1982 to 14.4 million in 1995 due to an increase in intensification (Nassar & Khedr, 1997:9). While this was considered a positive indicator it overlooked two facts. First, that the intensification was a result of changes in relative prices where big farmers won and small farmers lost. The big farmers intensified their production to increase their profits while small farmers increased their intensification as a survival strategy. The overall impact on the environment and the sustainability of resources were overlooked.

The effect of privatising marketing channels of input distribution failed to provide inputs at the right time, as was anticipated, and fertiliser prices increased massively. The reinvolvement of the PBDAC in the distribution of fertilisers undermined the credibility of the government programme.

While the state withdrew from some areas of production and trade, it did not enhance its capacity in other areas; co-operatives stood idle. The institutional reform also lagged behind.

## **Chapter 6      Agribusiness and Liberalisation**

### **:Assessing the Evidence**

#### ***6.1. Introduction***

This chapter examines some of the possible impacts that SAP has had on the agribusiness community in Egypt. I also assess the relationship between the declared intentions of the reforms and the actual outcome of the policies on agribusiness. I ask how successful have been the reforms in encouraging private sector participation? How successful was SAP so far in overcoming obstacles facing agribusiness? And to what extent has the state succeeded in providing policy transparency and credibility in SAP? In this chapter I use empirical evidence to examine some of the theoretical and conceptual issues raised in chapter two concerning the role of the state and that of the market. Was the intensive intervention of the state the only constraint on private sector revival? And does rolling back the state mean that the private sector will automatically take over? What are the other constraints that impede private sector revival? This chapter argues that reforms were incomplete and inconsistent and that institutional reforms lagged behind stabilisation liberalisation measures of exchange rate, interest rates, and reducing state intervention. The state also failed to perform its new role in the free market economy.

<sup>1</sup> This chapter and chapter 7 drew on empirical work conducted on the agribusiness community in Egypt. The study used structured questionnaires prepared for qualitative analysis. The valid responses represent 36 companies typifying most agribusiness activity in Egypt. The responses indicate a prevailing view of investors in the agribusiness community between December 1995 and mid-April 1996. Most major business groups were represented in this sample, six of them being businessmen not restricted to agricultural activities. Data is supplemented with other evidence from secondary sources. The data available provides good indicative views, assessment, and policy implications rather than anything definitive.



## *6.2. Sample Profile*

The sample covered companies from different activities, it included those who were involved directly in the process of production and exports, land reclamation, and those with backward links with the agricultural sector i.e. those who undertake manufacturing or trading activities in agricultural inputs. Table 6.1 provides a distribution of the sample's companies according to their main activity. There were no strict boundaries between activities. Most companies practice complementary activities simultaneously the most common shared activity was consultation services. The two land reclamation companies had different types of activities in addition to land reclamation; these were firstly, well drilling services and equipment provision, and secondly agro-industry and livestock production. One of those trading in irrigation systems also designed the networks involved. The reason for diversifying the activities was the high competition and/or the lack of experience. It was observed that more experienced well-established companies in the market had complementary activities in separate companies rather than in the same company. For instance, it was seen that some traders had their own farms to experiment with new types of seeds, fertilisers and/or pesticides. This was of the benefit to their clients as they were able to give the right advice to them. Some of them started in different sector(s) and found a good expanding opportunity in the agricultural sector. Agricultural activities were sometimes complementary to industrial activities as in the case of chemical industries or completely different to them. Nine of the sample, one fourth, belong to investment groups, four of them practised varied activities and five were only restricted to agricultural activities. Another example of complementary activities was that of one of the respondents who managed to set up four companies between 1977 and 1988. He succeeded in attracting finance by seeking a foreign partner for the third company and by establishing a joint stock company for his last one. He was experienced to select new kinds of activities with a high demand and low competitiveness. While he started with input trading his last two companies dealt in the shipment and unloading of cereals in two Egyptian ports.

Table 6.1 Distribution of the Sample's Companies According to their Main Activities

Activity	Number	Percentage
Agro-machinery	4	11.1
Well Drilling	2	5.6
Poultry	2	5.6
Animal feed	2	5.6
Animal feed and poultry	2	5.6
Agricultural producers and exporters	3	8.3
Bio-Plantation	1	2.8
Manufacturing Irrigation systems	3	8.3
Trade of agricultural inputs & irrigation systems	2	5.6
Trade of agricultural inputs	4	11.1
Manufacturing & trading in fertilisers	3	8.3
Manufacturing bio-fertilisers & pesticides	1	2.8
Land reclamation & others	2	5.6
Agro-industry & input trade	1	2.8
Producing seeds, herbs, trees nurseries	3	8.3
Fighting pests & seed production	1	2.8
Total sample	36	100

Companies in this sample were established between 1936 and 1994 and none of the companies were established between 1967 and 1976. This is because of the low participation rate of the private sector at that time, during the war period from 1967 to 1973. The types of activities were not strictly related to certain dates, however, we can say that activities like poultry, animal feed and well drilling started during the *infitah* period. This period was one of technology transfer, as was clear from the inception of bio-plantation activity in 1979, yet this activity does not spread to the following period. Activities related to the SAP period are more related to trading in agriculture materials, drip pipes irrigation systems, bio-fertilisers and pesticides and plant growth regulators. It should be noted that the last two activities were related to new technology introduced into Egyptian agriculture, while the first related to the new regulation of free marketing of agriculture inputs.

Private sector companies in Egypt work under different laws: law number 159 of 1981<sup>5</sup> known as the private sector law; the investment law number 230 of 1989<sup>6</sup>; and the new communities' law number 59 of 1979. It should also be noted that during the *infitah* period companies preferred working under the investment law than working under the private sector law. This was due to the greater number of

<sup>5</sup> To encourage Egyptian investors law 159 of 1981 replaced law 26 of 1954.

<sup>6</sup> Law 230 of 1989 replaced the investment law 43 of 1974 for Arab and foreign investment and free zone (amended by law 32 in 1977) which was issued during the *infitah* period to encourage Arab and foreign investment and then allowed Egyptian investors to work under the same law if investments were undertaken with foreign currency.

concessions available under the investment law. This preference does not continue in the later period starting in the mid-eighties.

Capital size in the sample seemed to increase in the period of *infatih* when more companies were established as Joint Stock ventures under the investment law. Where it allows local capital to share with international capital, 37.5 percent of them had foreign partners. Companies established in the period of SAP had little capital compared with the period of *infatih*. This may relate to the type of activities and the characteristics of the new investors of that period.

*Investors' characteristics;* Most investors were concentrated in the 40-50 age group. Access to investment needs time to accumulate the needed capital, the youngest of our group was the son of a well-known investor, where the whole family worked in this kind of business, and the young investor helped the father. He did not have his own business. However, we have an example of two young partners one of whom left his government job and the other left his work in the private sector and used their experience as agricultural engineers and sales managers to acquire their own business with the help of an SFD loan.

Nearly all the sample had received higher education except one who had 20 years' experience in his career in the private sector<sup>7</sup>. Most of them had the relevant education as 44.4 percent of them studied agricultural science, while about a quarter studied business, commerce and economics. They were in other words formally qualified to run this business technically as they studied agricultural science and some of them were senior officials of the MALR. They expected to be able to identify the problems of the agricultural sector, to help select and provide suitable technology or to improve the existing provision.

About half of the sample used to work in the private sector and a few others were university professors or university staff and all except one still kept their jobs. Two used to be senior officials of the MALR and there was another who was a university professor and used to be a senior official in the MALR as well. The others used to work as PE managers, bank managers, and officers. However, the latter group had some family ties with people experienced in agricultural activities in one way or another or had partners with agricultural experience, thus combining agricultural with market experience.

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<sup>7</sup> He is not Egyptian, there are two cases of non-Egyptian investors.

University professors and those with a PhD in agricultural science are more likely to participate in activities with advanced technology especially in bio-plantation, bio-fertilisers and pesticides, and plant growth regulators. There is no specific time horizon for their participation, nor for the MALR officials whose time horizon covers the eighties and the nineties.

Although a previous study about the private sector in Egypt revealed that most firms in the sample were dominated by individuals and families even those which were registered as joint stock companies so as to maximise autonomy and achieve control over management (Shafik, 1989 as cited in Shafik, 1992:71). In our case it should be noted that large firms whose activities were not limited to agricultural production, that is those managed by what may be called professional businessmen, as opposed to technocrats who lately entered the field, were managed by families. New investors in the era of reform were technocrats who obtained their experience in universities and the MALR, who in management rely on elements from the private sector's managers and sales managers, former MALR officials, and in one case family-based management was also evident. It was clear that government officials received benefits from the liberalisation policy by establishing their own businesses or through working in private companies. It was plain that they represented urban interests more than rural. As my study focused on the formal sector of the agribusiness, its image is quite different from Sadowski's description of the traditional rural businessmen wearing the *galabya* who emerged during the period of *infitah*. They are still represented in cattle-breeding activities, or working as middlemen, small distributors and merchants in rural areas.

### **6.3. Barriers to Entry**

Routine issues and bureaucracy were always blamed for distracting investors. This study tries to distinguish between the effect of rules and regulations and that of the bureaucrats who implement them. One third of the sample believed that the steps for establishing new activities were lengthy and complicated and half of this percentage believed that government bureaucrats add extra routine and obstacles for investors. See table 6.2. below.

Table 6. 2 Establishment Obstacles

Obstacles	Number of Respondents	Percentage
Funding	9	25
Government officials adding extra routine and difficulties	6	16.6
High Registration Fees	6	16.6
Lengthy and complicated steps	12	33.3
Lack of information about market	1	2.8
None	11	30.6
Some companies practise market monopoly	6	16.6
Some companies seek illegal ways	6	16.6

\* Total percentage is more than 100% as most companies mentioned more than one obstacle.

Funding was a problem for one fourth of the respondents. A smaller number complained of market monopoly and others complained about the illegal practices of other private sector companies. It is interesting to note that the types of problems that were reported varied and changed over time. Four companies were established during the 1936-1967 period. Three of them did not mention any obstacles, as it was probably difficult to remember. One complained about government officials increasing the routine and difficulties; and of lack of information about the market. It was clear that the problem of bureaucracy is deeply rooted in the Egyptian administration. In the era of *infitah*, 1977-81, about half the established companies identified no obstacles. One investor believed that the real facilities were only given by Dr. Abdel Mageed, when he was Deputy Prime Minister for Economic Affairs, in 1980-82. Still, more than one third of the companies set up in this period suffered from lengthy and complicated government procedures. Other complaints were not emphatically mentioned and it is interesting that during the *infitah*, businesses that often belonged to the old class of businessmen colluded with foreign capital and used those ties to facilitate funding (Said, 1986:56). About 37.5 percent of the sample in that period had foreign partners. At that time people preferred to work for the government and only those who had experience and money started productive private activities.

In the following period, 1982-86, between Sadat's era and the start of the implementation of SAP measures, 50 percent of companies complained about lengthy and complicated measures, 30 percent complained about market monopoly, 20 percent about funding, and 20 percent about high fees, while 20 percent mentioned that they faced no obstacles.

Between 1987 and 1990 when reform measures started to be gradually implemented, one third of the companies complained about lengthy and complicated

bureaucratic procedures. These complaints were combined with complaints about government officials being obstructive and access to funding was also identified as a similarly difficult problem.

Companies founded after 1991, when the economic reforms became official in all sectors of the economy, seemed to have major problems with funding, as 80 percent of them complained about it, this was in spite of the decline in the capital size of these companies. The next problem in this period was that some producers sought to use illegal methods as 60 percent complained about it.

In general the most prominent constraint was the complicated and lengthy procedures for establishing new business activities. In addition investors were frustrated by the attitudes of government officials. Complaints about lengthy and complicated practices were joined most of the time by additional routines and difficulties from the executives. This meant that both the regulations and performance of government officials had to be improved and developed.

This complaint was confirmed by investors who set up their companies at different times, which meant that this problem was deeply rooted in Egyptian bureaucracy, and which made it a far from easy task to overcome. Even in the era of *infatih* when fewer obstacles were experienced (half of the sample recorded no obstacles at all) this problem was there. The problem underwent a slight improvement in the SAP period, as it scored only 20 percent of investor complaints at that time.

In general, funding was the second notable problem, but it was the first during the period of SAP. While the *infatih* era encountered no funding obstacles at all, the following periods underwent increasing difficulties. This could be due to various causes, among them the nature of new investors during this era. Most of them were technocrats who had the required experience but lacked finance, or people who used to work for the private sector, and the new environment encouraged them to have their own businesses after they had gained the needed experience, or sometimes young ambitious graduates, who worked for government for short periods, who found governmental work unrewarding or had no chance to find work at all. The second cause, but not in terms of importance, is that appropriate credit facilities were unavailable. This will become clearer in the following analysis.

Investors tried to overcome the problem of funding through a combination of people with technical experience and those with capital. About half the investors obtained loans when they started their activities, and one fourth attracted foreign investors to join with them.

Investors in the SAP period encountered new types of obstacles. The problem was that some companies in the private sector practised illegal ways to dominate the market. Complaints shifted from government regulations and the performance of their employees, to the complaints about other private producers. This refers to the new important role of the government in the market economy, which was to provide the legal framework for private transactions and to be applied effectively. This is not an easy task. It needed a great deal of effort from government to restore its prestige and ability to enforce the law and its regulations, to move from a soft to a hard state, and to control corruption and patronage networks in order to enforce the law.

#### ***6.4. Agribusiness Activity Profile***

##### **6.4.1. Agro-Machinery**

The use of mechanisation in Egyptian agriculture has grown steadily since the 1970s. The shortage of labour due to emigration starting from the mid-1970s, in addition to the policy of subsidisation of machines, fuel and credit encouraged this trend. The increased demand encouraged importation rather than domestic manufacturing. This was partly because of the overvalued exchange rate and technical difficulties, such as lack of materials. The majority of the machines used were imported. Domestic manufacturing provided mainly tractor attachments such as wagons, scrapers, simple ploughs and threshers. Public companies dominated local industry and were able to manufacture some machines in addition to assembling imports. They were relatively larger in size compared with private ones. There were private dealers which were also able to manufacture, in addition to small workshops who gained experience from repairing and were eventually able to copy simple machines (Kerr, 1994:878-79).

Public sector agricultural machinery has been operating in Egypt since the 1950s. Private dealers criticised it for using advanced high technology capital-intensive equipment to manufacture simple products which the private sector built in its workshops. However, public companies were able to provide tractors and small

machines, but could not compete in price with the cheap imports from the Eastern bloc. The private sector had also relatively large, with 20-50 workers, well-established firms located in Delta towns particularly in Tanta city (*ibid*). It seems that the private sector is as old as the public sector or even older, as two of the sample located in Tanta City were established in 1936 and 1952 respectively, which means that the agricultural machinery industry was less restricted by public regulations compared with other agribusiness activities. The two companies managed to expand their size and activity during the latter period. Both can be categorised as big companies if we consider the number of workers, more than one hundred, or the amount of capital, £E 300,000 for one and more than £E 4 million for the other. This large amount of capital was essential for the types of activity and the products of the companies which were not limited to importing and trading. It also encompassed manufacturing. Both companies managed to export their products although their exports were limited to various Arab and African countries. Finance and marketing were the main two constraints limiting this activity. The large capital sum needed for such companies was one of the barriers to entry and the high value of the products compared with individual capabilities drew attention to the need to provide adequate credit for both producers and consumers. The PBDAC played an important role, especially as regards distribution.

Although these were specific barriers to entry, our sample includes two companies which were set up during the reform, in 1992 and 1994 respectively. One of them complained about a market monopoly while both complained about the manipulation of other competing companies. The two companies represent different cases- one with limited capital, £E 30,000 and three workers- found difficulties in providing finance and obtained a loan from the SFD. In spite of its small size it was based mainly in manufacturing. The second was large in size- £E 4 million and 50 workers- and managed to share with a foreign investor in the provision of finance, new technology and at the same time in opening new markets for export, however, up until then its export was limited to Arab countries. This type of activity is capital intensive as the average Capital\Labour ratio among the four companies in our sample was £E 26,047. The smaller company which was established according to the private sector law complained about the extended and slow procedures of establishments, the bureaucracy and the routine. The other was set up under the



investment law and while not suffering from administrative obstacles complained about high fees.

Production in such activities was competitive, as most of them experienced high competition in marketing and admitted that they found high degree of competition from local producers when marketing their imports. In contrast, a local producer complained that consumers preferred the imported machinery. Another complained about the general sales tax that increased its cost, which did not apply to small workshops. In spite of intense competition half of them were optimistic about the local market as they expect demand to expand due to the expansion of land reclamation. Half the investors complained about the heavy duties of imports, on inputs and about the complicated import procedures. Two out of our four sample companies found the interest rate very high and one thought it was appropriate.

The companies however, could not agree in their views about the general assessment of the SAP. One found it had limited utility. Another considered it did limited harm and another believed that it had no effect, while the fourth did not express a view. In general, we cannot say that investors in this subsector were in favour of the reform. However, as reviewed by one of them, the reform could overcome some of their problems. The reform facilitated some procedures by abolishing the need for permission from the armed production to import agricultural machinery or its components. It also stabilised the exchange rate and facilitated its availability by allowing private exchange companies. On the other hand, the stabilisation of the exchange rate was achieved mainly for the US dollar while other currencies which are needed for imports did not enjoy the same advantage, raised and destabilised production costs. While customs duties were revised, a need for more revision was still considered important by them, in addition to complicated import procedures. The general tax on sales was subject to many complaints especially because it was imposed suddenly. Hastily introduced procedures were also criticised for destabilising the market.

It seems that this sub-sector still relies heavily on importation both of raw materials for manufacturing or machinery parts for assembly. Manufacturing is still limited to simple machinery and equipment. Finance is not the main problem for it as some companies have already managed to work on a large scale. But it is still a barrier to entry for some new companies, and credit facilities for manufacturing

firms should be made easier. The main constraint to the expansion of local manufacturing is the availability of materials as it relies heavily on imported inputs. For agricultural machinery manufacture to expand, it is important to develop other activities with vertical links to it. The emphasis on the land reclamation project in the South provides a good opportunity to further expanding this industry and there is an opportunity for new activities or outlets in upper Egypt to be made more accessible for land reclamation projects.

The members following this activity have an association to unite them: The Businessmen's Association for Agricultural Machinery Development. Two of the sample were members. The association does not seem to play an active role as one of them overlooked its activities. The other believed it provided technical assistance and discussed economic policies with the government. The new investors were not members, but one of them who practices various economic activities is a member of the Egyptian Businessmen's Association, so it seems that he is satisfied with its activities and has no need to joint small associations.

#### **6.4.2. New Irrigation Systems Industry**

The industry providing new irrigation systems is relatively new and is related to the revival of land reclamation in the 1980s. It is related to the new technology of water-saving irrigation, using sprinklers and drip-pipe irrigation, which is relevant to sandy soil. It is set up independently or as an extension of the plastic industry. However, this industry is relatively simple compared to the agro-machinery industry and it mainly manufactures pipes with drips, and fittings. Our sample included three manufacturing companies and one trader in agricultural materials who is a designer of irrigation networks and used to produce its materials until he stopped. Most of producers complaints about the manipulation of some other producers. One of the three companies was founded in the second half of the 1980s while two others were established in the 1990s. This industry requires a relatively smaller amount of capital compared with the agro-machinery sector. The size of companies in the sample varied between £E 20,000 and £E 1.5 million. The number of employees ranged from 20 to 122 employees with an average Capital/Labour of 16,689 or 15,366 if we consider temporary employment. The reforms have been useful to investors in this type of activity. The most useful measures concerned the availability of foreign currencies and stability of their prices. However, their have been some

problems with custom duties as they do not take into consideration company receipts for the price of imported inputs. Most producers' complaints were about the manipulation of other producers. Some producers used cheap, low-quality or recycled materials and were then able to compete with low prices. These caused one of the sample to cease production and to focus on other activities.

### **6.4.3. Poultry**

The poultry industry gained momentum during the *infatih* in the mid-1970s which encouraged food security projects by both the public and private sectors. The industry enjoyed concessions in the form of low interest and tax rates, and direct subsidies for animal feed and medicine. The industry relied heavily on imports for chicken feed (85 percent) and veterinary products and failed to build strong backward linkages for local industry. The industry made considerable progress and was able to achieve self-sufficiency in eggs and to cover a high proportion of the domestic needs of chickens. Between 1975 and 1987 the invested capital increased from £E 200 million to nearly £E 3 billion (Harik, 1997: 79-80).

However, it was vulnerable to changes in economic policy or circumstances due to its reliance on subsidies and imported inputs. Unavailability of foreign exchange in the early 1980s affected the ability to import chicken feed and the local market suffered severe shortages which more strikingly affected the private sector. The public sector had priority in accessing the feed but it had to deliver a certain quota from its production to the MOS. The private sector was the more affected and in 1987 it suffered another blow when the corn subsidy was suddenly removed while the public sector continued to enjoy it. As a result, about 80 percent of the farms suspended their operations. The effect on the industry was enormous if we recognise that the private sector constituted 90 percent of the poultry farms and produced about 75 percent of the poultry products. However, the closure of private farms was also due to several internal factors of inefficiency and lack of managerial skills. Low-interest loans were diverted to other uses (*ibid.*;80-82). In spite of the favourable treatment of public sector companies compared with private ones they suffered huge deficits. The mandatory prices for selling products and the shortages of corn, as well as the MOS policy to import cheap chickens in 1987, were blamed for this deficit (Hafez, 1992:31); while the policy of importing cheap chickens indicated a lack of co-ordination and a government competing with itself, Harik (1991:81) points that

the effect was mainly on the private sector as the public sector already had to deliver its products to the MOS at control prices and its share of the market was very small. At the micro level, the public sector also lacked efficiency, enjoyed soft budget constraints concerning loans, and corruption and patronage where networks were spread among public sector managers and private importers. Harik quotes the case of provincial officials of some public sector farms discriminating against private local producers of baby chickens by making tenders available only to importers. Public officials were accused by private producers of corruption and the gaining of commission.

Our study sample includes two private companies working in the poultry industry and two others working in poultry and animal feed production at the same time. They were founded between 1978 and 1985 and none was established during the reform period. The industry in general was characterised by large-scale operations; capital was relatively small in one partnership company -£E 250,000-; in the three other companies capital accounted for between 7 and 10 million and was established on the basis of investment law as joint stock companies, where commercial banks were the main share holders in two of them.

The liberalisation policy for this industry started in 1987 by removing the corn subsidy. While this policy greatly damaged the industry at the time and had far-reaching effects on the industry as a whole, as we have seen, the liberalisation of feed imports in 1988 improved the availability of feed, and the devaluation of the Egyptian pound in 1991 increased the cost burden on the imported inputs. However, the stabilisation achieved in the exchange rate provided greater stability in the availability of inputs. Poultry producers were satisfied by overcoming the bottleneck in the supply of imported feed. However, the government still controlled some elements of the feeds, and producers still experience difficulties in obtaining the local component '*Nukhala*' from local mills. While the rapid increase in the price of imports before the SAP -estimated by one producer as a five-fold increase between 1982-1990- was controlled due to the exchange rate stability, importers enjoyed more freedom to manipulate prices. The benefit achieved from exchange rate stability was offset by the deregulation of the local market. Producers complained that interest rates for operational loans were high and some of them suffered from being in arrears. The total debt owed to banks by poultry producers was estimated at

£E 1 billion (Harik, 1997:82). The interest rate for operational loans decreased from 1994 dropping from 20 and 18 percent to 13 percent which was considered reasonable by one producer if there were no administrative charges which accounted for an additional 2 percent. Other producers considered it very high. Producers were finally able to reschedule their debts. One producer blamed the PBDAC for encouraging people to borrow, while loans were diverted to other purposes, some of them consumptional. This reflected the weak monitoring system of the bank in the utilisation of the loans. One drawback of the reform was the rise in the cost of electricity, gas, kerosene and wages which increased the production costs. In general, one producer found the reform very useful, another found some parts useful and others harmful. Two found it had no effect.

The market for poultry products is oligopolistic and a few merchants control the prices. There are an insufficient number of slaughter houses, and although the government provides some their capacity is limited and payments are always two months late which hurts producers who need to maintain liquidity. One of the sample preferred to deal with public slaughter houses and asked the government to increase its capacity and facilitate payments. Only 4 percent of the private produce of broiler farms goes for slaughter in private sector slaughter houses, while about 56 percent of the market live through wholesalers who seek to maximise their profits. Oligopoly has been extended to the retail trade where there are, in many cases, agents working for the wholesaler. Only about 6 percent of poultry meat is marketed through supermarkets (De Boer *et al*, 1996:119). Liberalising external trade led to an opening up of the market for imported frozen chicken which hurt the local producers. These complain about the instability of the supply which in turn affected the prices. Some producers complained about unused capacity. This problem was more severe in the past, as egg production was estimated at 40 percent in 1985, increasing to 60 percent in 1988, due to shortages of raw materials (Harik, 1997:82). However producers were optimistic concerning local demand. They expected it to grow because of an increase in the population and a shift in demand from red to white meat following the to BSE crisis. Nevertheless, this effect was not as long-term as one producer expected.

In sum, the poultry industry enjoyed a good market in Egypt and a fair opportunity to expand vertically and horizontally. Although some projects achieved

vertical integration between the poultry and feed industry, in order to overcome the problem of shortages of feeds it still relied heavily on imported ingredients. Furthermore, the market for feed imports is a monopoly with a few importers who control the prices. There is a need to promote feed components of domestic origin such as new varieties of corn to be used as fodder, as noted in the new agricultural strategy, in which steps for real implementation should be taken. There is also a need to promote industries with forward linkages for processing and marketing, such as slaughter houses and refrigerating and packing plants to shorten the marketing chain and to overcome the oligopoly of the wholesalers and to improve prices for producers to be able to compete. Vertical expansion will facilitate horizontal expansion by utilising full capacity and encouraging new investments. Vertical expansion will also help to promote exports, as seen in the sample. None of the companies was able to compete in the international market. In this respect the Arab countries could provide a suitable market. Finally, the study revealed the weak legal infrastructure of the market where oligopolistic powers prevailed in both input and output markets.

#### **6.4.4. The Animal Feed Industry**

The animal feed industry has relied heavily on imported ingredients. Before reform, the government used to control importation quotas for feed mills, pricing and distribution, and feed prices were subsidised. This price control, in addition to foreign exchange shortages, created supply bottlenecks in certain foodstuffs. New entrants into commercial animal and poultry production, preferred to build their own feed mills to ensure adequate and reliable supplies of mixed feed meeting nutritional standards. Earlier capacity subsidies, particularly for poultry and veal production, encouraged this trend (De Boer *et al*, 1996:120). Most controls over the industry have now been abolished, subsidies cut, and trade liberalised. However, the PBDAC is still involved in the allocation of inputs and the distribution of outputs. At the moment, the vast majority of the annual production of 2.0 million tonnes of manufactured livestock feedstuffs are produced by public sector mills (Smith, 1994:154). Over the past five years their capacity utilisation never exceeded 50 percent and in 1993 it dropped to 31 percent.

There are 39 feed mills for the production of poultry feed. Of these, 11 are joint public/private, 4 are publicly owned, and 24 are under private ownership.

Private sector annual production is in the range of 1 million tonnes of poultry feed. Furthermore, it has its own distributional system and does not rely on the PBDAC (*ibid*). In 1989, capacity utilisation was 37.6 percent. Since then, it has increased, as the industry has started to recover, following the removal of subsidies on feeds. Still, both poultry feed mills and livestock feed mills have considerable excess capacity (De Boer, 1996:120).

Our sample included two companies specialised in all kinds of animal feed, in addition to the two previously mentioned who combine the feed with the poultry industry. All companies were created in the 1980s. Just like the poultry industry, companies operating in the feed industry were large-scale companies with capital ranging from 2-3.5 million and labour from 150 to 300, with a relatively high ratio of labour/capital. As in the case of poultry, feed industry producers were satisfied that the market was relatively free now that imported ingredients were more accessible, however, they complained about the unavailability of some local ingredients, such as *nukhala* and that derived from cotton straw, which was still monopolised by the public sector. Producers related its unavailability to public management difficulties. Privatisation policy was inconsistent as they also complained about the irregular interference of the PBDAC in its distribution. They asked for privatisation to be completed, the hesitation of the government to abandon the distribution of local ingredients reduced its credibility as regards its intentions towards the private sector. From their point of view, one of the negative aspects of the reform was the massive increase in electricity prices and the general sales tax that they had to pay on imported spare parts for their factories. The general view of the impact of the reform varied from the idea of limited usefulness to the acceptance that some aspects were useful while others were harmful.

Producers of feeds face several obstacles in the local market with regards to taxes; the availability of inputs, feed ingredients and spare parts for the factories because the high sales tax on imports which led them to shift to local products; and some MALR regulations. In general, unlike most producers, they were pessimistic concerning future demand for their products. The reason for this was related to the stagnation of livestock production, as they claimed that many producers had to abandon the market and that the importation of cattle for slaughtering was harmful to

local production in livestock and animal feeds. Only one producer was able to export his poultry and animal feeds to Arab countries. He complained that the high prices of inputs raised the price of the final product and reduced his ability to compete in the external markets. The attitude of the producers toward the PBDAC was negative. One businessman required transactions to be conformed to Islamic norms. Another producer accused the staff of being ignorant concerning banking transactions, which meant that it needed to upgrade its staff's capabilities in order to compete on a commercial basis.

#### **6.4.5. Fertilisers and Insecticides**

The use of modern inputs in Egyptian agriculture is well established. Nitrates were introduced from Chile in 1902, while domestic production of Phosphate fertiliser and nitrogen fertiliser began in 1936 and 1951, respectively. Egyptian farmers use high concentrations of fertilisers compared with the rest of the world. Nitrogen fertilisers represent about 80 percent of total fertiliser use in Egypt. The use of potash has increased since the 1980s. Domestic production supplies about 90 percent of the nitrogen and 96 percent of the phosphate used, whereas potash is entirely imported (Goletti, 1996:167). The GOE used to control fertiliser production, importation and distribution. Distribution of fertilisers and other input was monopolised by the PBDAC. When the liberalisation policy was introduced in the agricultural sector, subsidies on inputs were eliminated and the private sector was allowed to trade in agricultural inputs including fertilisers, (See previous chapter for details). The Private sector was allowed to import up to 30 percent of total domestic demand but had to hand over 60 percent of the imported amount for the PBDAC to distribute (Khedr, 1992:51). Moreover, since 1990 the private sector has been allowed to work in fertiliser distribution with the idea that the PBDAC would gradually be eliminated from providing finance. Private sector participation increased rapidly to reach 80 percent in 1993. However, this increasing contribution came to an end because of severe shortages of fertilisers which led to a massive increase in prices and created a crisis in Egyptian agriculture.

Our sample includes ten companies that deal with fertilisers and insecticides either as producers and traders (four companies) or as traders only (six companies). Fertilisers and insecticides produced and used in Egypt are usually chemical



products. However, there is an evolving slowly growing trend towards using biological products as being more healthy and environmentally clean. Our sample includes one company that produces biological growth regulators and pest-fighting materials. Those companies that are engaged only in trade usually deal in other agricultural materials -inputs- as well, such as seeds and agricultural equipment. Few of them, two companies, also design and assemble modern irrigation systems. In spite of the PBDAC monopoly of the input trade and distribution, the business of dealing in agricultural materials is old. One of our examples was originally established in 1958 where it used to trade in agricultural equipment and a number of types of fertilisers and insecticides. The trader explained that the private sector was completely forbidden to import only between 1964-74 when he used to deal in some domestic products. Now he is able to manufacture, import and export. Another company started its activity in 1977, while the other eight companies began their operations during the period of reform, half of them were founded in the second half of the 1980s and the other half set up in the 1990s. This was the most popular type of undertaking in the agribusiness during the period of the reform and it was supported by PBDAC loans which were biased towards large companies. (This will be developed in the analysis below.) This type of activity allows for companies with different amounts of capital, varying between £E 20 thousand and £E 10 million. The capital of five companies was between £E 25 and 50 thousand, four between £E 100 and 800 thousand and one with £E 10 million. However, if we consider the number of employees, most of them were small as only three had 100 or more employees, one had 50 and others had less than 50. This was an intensive capital activity as the Capital\Labour ratio was £E 23,383.

Producers of fertilisers and insecticides suffered from the delayed payments of middlemen and merchants. They also experienced the more serious problem of commercial cheating, where other producers provided cheap and poor quality products and were able to compete in the market. The ability of committed producers to overcome the latter problem was limited. They had to explain the quality of the product and exert more effort in marketing, however, the end consumers -farmers- were not qualified to discern the difference immediately and a time lag of one season at least was needed. This problem required an effective legal framework and control by the government. Imports of agricultural materials suffered

as well from the MALR's complicated and lengthy procedures for admitting new types of fertilisers or seeds, in addition to the high fees.

### *The PBDAC and the Fertiliser Crisis*

One of the main actors in the agricultural sector liberalisation policy wrote that the problem of input shortage was one of the main difficulties in this sector in recent years. He added that domestic production was insufficient and that the gap was filled by imports. The deficit was not restricted to fertilisers but it included high-quality seeds, chemical pesticides, animal feed and especially concentrated additives. This was the reason for the GOE allowing the private sector to import fertilisers, pesticides and other inputs. The import quota allowed for the private sector was raised to 30 percent of total market needs and 60 percent of the imported inputs allowed were to be delivered to the PBDAC (Khedr, 1992:51). The private sector share in fertiliser production was limited as regards quantity, yet it helped to introduce the new bio-fertiliser technologies in the early 1990s. Three PE companies still controlled the production of fertilisers in the market. These three companies controlled the available amounts of fertilisers in the local market.

From October 1994 onwards signs of shortage in fertilisers appeared in the domestic market. Later, in the summer of 1995, the shortage became a crisis and the domestic market suffered severe shortages which led to a massive increase in prices and threatened agricultural production. Three issues were responsible for this crisis. First the technical problems in the three big production companies, (which were subsidiaries of the Ministry of Public Business Sector) which reduced production. In order to keep their records clean and to keep their production value they increased exports. The export price was much higher than the local price. A head of one of these main producing companies blamed senior officials in the agricultural sector for not providing him with data about annual consumption, its rates throughout the year, and the anticipated increases. This lack of information, in his opinion, was one of the causes of his company not having specific policies for the local and external markets (*El-Ahram* 7/11/95). Although he had not been provided with this information officially he was able to analyse the causes of increased consumption and gave a good explanation for the shortage. He thought that the increase in consumption was due to a change in the crop structure and an increase in crop prices, as well as an increase in the cultivated area (*ibid*). These three production

companies were accused of gradually reducing the PBDAC share in inputs and preferring to sell to the private sector distributors.

The second issue involves private distributors, who were accused of exporting fertilisers to other markets rather than selling them in the local markets. This was of course to realise greater and easier profits. This was clear from the growing exports, as revealed in the empirical study. Most exports were growing steadily and only decreased in 1995 because of the ban on fertiliser exports. Some traders refrained from giving information about their exports.

And finally the PBDAC had the task of providing policies to maintain a balance in the market so as to avoid bottlenecks. In fact, it was the responsibility of the GOE as a whole, as there were several ministries responsible for regulating the market: the Ministry of Supply and the Ministry of Foreign Trade, which became one Ministry in the government of 1996. It is the responsibility of the PBDAC to help co-ordination between the MOPBS, MOS and MOFT and to keep them informed about market needs so as to regulate production and trade. It is the role of the PBDAC to regulate distribution, to maintain balance for emergencies and to interfere when the signs of crisis already are evident. PBDAC inactivity was a contributing cause of the fertiliser crisis.

### **Response to the crisis**

After months of shortage, it was declared that the PBDAC had been given control of 50 percent of fertiliser production. Later on, this was increased to 100 percent which represented total control of production. This control of fertiliser distribution was intended to continue in the hands of the PBDAC, which meant a step back in the liberalisation policy. The fertiliser distributors who had organised an association headed by a reputable ex-senior official in the MALR, a member of the NDP, an ex-head of the agriculture and irrigation committee in the People's Assembly. The association's members protested against the decision and published an appeal in the newspapers. After negotiations and a meeting with the government they were allowed to return partly to the field. On the one hand, the power of the fertiliser traders' association was limited, and on the other, the crisis was sufficiently severe to threaten agricultural sector production, that the decision was not subject to negotiation. The full return of the private sector to trading in fertilisers was only achieved in 1998. At an interview with the head of the PBDAC Dr. Khedr in June

1997, he stated that he lacked exact information about the end of the PBDAC monopoly over fertiliser distribution. In a discussion with one of the PBDAC staff, he revealed his conviction that the bank had an important role to play in the fertiliser distribution and he criticised the manipulation of private merchants. While what was mentioned was true it also reflected the unwillingness of the Bank staff to surrender their power to the private sector.

Private sector companies responded to the unavailability of local fertilisers by trading in imported fertilisers. In the long-term, this can have a negative effect on the domestic product, as it can shift demand from domestic to imported products.

The second part of the solution was to import 1 million tons of fertiliser. The private sector was asked to do the job for the PBDAC. The imported fertiliser was exempted from customs duties to grant a fair price for the farmers, and the government budget lost a considerable amount of money which could have been saved if this crisis had been dealt with differently. The rush of private sector companies to buy from the international market at the same time, caused prices to rise drastically. When the fertilisers arrived in those Egyptian ports which had low capacity, ships had to wait there and to pay fees into the bargain. All these extra costs were passed on to the end consumers -farmers- and the exemption from customs had not done much good.

### ***6.5. The Role of the PBDAC in Financing the Agribusiness Community***

Since 1987, the agricultural strategy has aimed at limiting the PBDAC's role to providing finance for agricultural services. To help increase the economic effectiveness of the banks and to expand non-subsidised credit, the PBDAC was supported by an American team of specialised bankers. They worked under long-term contracts to increase credit effectiveness, reduce costs and facilitate loans (Khedr, 1992). Here I provide an assessment of the performance and the role of the banks based on the investors' views concerning the PBDAC.

#### ***The PBDAC loans***

In October 1995, shortly before conducting the field work, the PBDAC advertised in the Ahram newspaper, in order to promote the credit available for the agribusiness sector. The fund was introduced under the title of the Agriculture Modernisation Project and was supported by the World Bank at a subsidised interest rate. 60

percent of the project fund was introduced by the IDA with an interest rate of 4.3 percent (*El-Ahram* newspaper 5/7/95), the PBDAC added its commission and administrative fees. The total available finance for the project was \$100 million (*El-Ahram* newspaper 9/12/95). It covered four main areas; Marketing activities, Agro-industries, Agro-machinery and Agro-inputs (Dr. Wali statement at a meeting with investors, *El-Ahram* 15/7/95). The study aimed to assess the PBDAC's ability to reach the business community and provide it with finance. Surprisingly about 36.1 percent of them knew nothing about it. And one quarter of the sample did not need loans at that time. One received a loan from the SFD and at the moment can not seek any other loans. However, he did not know about it at that time. One of the sample mentioned that he did not want to deal with the PBDAC at all and accused his staff of ignorance and lack of banking experience. This reflected the low credibility of the Bank's efficiency. Another investor accused the PBDAC officials of being secretive concerning these special offers, and accused them of awarding them to clients who were part of their patronage networks. When it was pointed out to him that it was advertised in the newspaper, he seemed unconvinced. This reflected badly on the credibility of the bank and raised the question of the lack of transparency of the PBDAC policy and about its advertisement as an effective way to promote for such services. It should have been supplemented by other approaches, like contacting the various business associations and organisations which represent the agribusiness community and which already exist. Nevertheless, this project was discussed at a meeting between Dr. Wali and 21 investors in agricultural activities (*El-Ahram* 15/7/95). From the names mentioned in the report few represented agricultural machinery, one was from the Chamber of Commerce, another, the head of the agricultural syndicate, and others. On the one hand, the members mentioned did not represent the whole range of the agribusiness community, on the other, it seems that there is a lack of communication within the agribusiness community as a whole. It seems that the well-connected agribusiness elite work for their own interests and do not represent agribusiness associations. They were the ones who received the best offers and at the same time were able to use their political influence and connections to facilitate and overcome bureaucratic obstacles.

13.9 percent said that the terms for loans were not suitable for them. This was because of the collateral that the bank asked for, which they considered

excessive. Others stated that the kind of activity the bank offered was not compatible with their needs. One remarked that it provided finance for manufacturing cartons for handling eggs, while they did not finance the production of eggs itself. Businessmen usually choose activities which they consider profitable for themselves, and after a market study, they select one activity because there is a demand on it, and the market needs it. This is the main hypothesis of the free market introduced by the World Bank. In this instance it is not clear who set the priorities for investment, the World Bank, which participates in finance, or the PBDAC officials, and who benefits from it.

Two of the sample stated that they were negotiating a loan. One provided no details about which activity it was for or how much. The other needed a loan of one million to set up a new operation, a flour mill. The investor was asked to provide land or estate as a grantee. He insisted on examining the machines and the project as a grantee and was ready to pay 10 percent in advance. This did not seem convincing for the officials of the PBDAC. The investor found the other terms ideally suitable for him, a 10.5 percent interest rate, a 6 months' allowance with no repayment and repayment of the loan within four years. However, at the meeting of Dr. Wali with the investors a question about the grantees was raised, and Dr. Wali assured them that the development banks did not set commercial pre-conditions. He added that the project itself, its anticipated revenues and its ability to cover the project's obligations should be the grantee. In this respect he referred to the project's appraisal study and the client's creditworthiness (*El-Ahram* 15/7/95). It seems that there is big difference between what is said at a high level of policy-making and the execution of these policies. Even client creditworthiness did not seem to be useful, since one of the interviewed complained that he had dealt with the PBDAC for over twenty years with clean slate and no arrears and they still insisted on asking him for unreasonable collateral. It seems that this client enjoyed preferential treatment under the former bank regime, which he praised, now there will probably be bias against him.

Three mentioned that they had already obtained a loan from the PBDAC. One received it for the importing of agricultural inputs and outputs. Others gave no details concerning activities. It seems that they are related to the same fields they are working in (one, agro-machinery, another, land reclamation and agro-industries).

The loans came to millions of pounds. There were no comments about grantees and terms on loans. The three companies were large, well-known and reputable. another company mentioned that it did not know about the project, but it secured a short-term loan for one year from the PBDAC. Again it was large reputable company.

### *Assessment to the Role of the PBDAC*

Official figures shows that the PBDAC provides the bulk of agricultural credit, which was 74.6 percent in 1986 and rose to 78.8 percent in 1996 (CBE as cited in Khedr, 1997: table 1). The PBDAC figures show that the total credit from the PBDAC increased during the reform from £E 2,369 million in 1986/87 to £E 4,504 million in 1992/93, reaching £E 6,430 million in 1995/96. Calculating the real value, using the wholesale price index <sup>8</sup>, the real figures for 1992/93 and 1995/96 were only £E 1,680 and 1,981.5 million respectively, which means that the bank credit was decreased in real terms during the reform programme. Table 6.3 shows that most PBDAC loans were directed to short-term lending, 14 months. These were followed by medium-term loans, up to 5 years, then long-term of more than 5 years. For medium-term advances it is to be noted that Agricultural machinery received the highest percentage. This is because the banks financed both producers and consumers. Livestock occupied the second rank, while poultry loans increased massively during the early 1990s then decreased again. Since 1992/93 the PBDAC has introduced new types of loans, that is commercial loans to finance input trading. In that year, loans were £E 447.7 million and increased to £E 921.5 million in 1995/96 (Khedr, 1997:29). From 1/2/1996, PBDAC Interest rates on different kinds of loans have been reduced by 3 percent from 16, 15, 14 percent for the long-, medium-, and short-term, respectively, to reach 13, 12, 11 percent respectively, however, there is still an extra 2 percent for administrative fees. The decrease in the interest rate could increase the demand on loans.

Nevertheless, the PBDAC was not very popular among the investors in our sample. When asked for their opinion of the role of the PBDAC, one fourth of the sample gave no answer or stated that they had never dealt with it. Two showed indifference and one believed that it was not bad. Another remarked that it as like any other commercial bank.

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<sup>8</sup> Index number published by CAPMAS, 1996, Statistical Year Book. 1986/87=100, figures used are for 1992=268.0, 1995=324.5.

A quarter of the sample thought it played a useful role. In fact, one found it very good. Some of them thought of it as having a good co-operative role for farmers, especially small ones. Others found it helpful in providing inputs and asked for it to return to distributing high-quality seeds and bio-fertilisers for the private sector, however without interfering with prices, admitting their failure to reach all the governorates, as it was very costly.

**Table 6.3 Distribution of the PBDAC Loans during 1982/8 - 1995/96** (Million £E)

	1982/83	1986/87	1990/91	1992/93	1995/96
<b>Short-term Loans</b>					
Crops	310.3	676.6	1515.6	1687.2	2204.9
Livestock	92.9	781.6	1321.3	1047.3	1076.1
Poultry	72.3	168.0	161.7	123.0	156.9
Fishing	-	-	2.5	-	1.9
Cultivation related activities	-	-	29.8	609.7	1430.7
Youth	-	-	1.8	2.2	0.6
Others	13.2	17.8	16.9	2.4	79.1
<b>Sub-total</b>	<b>178.5</b>	<b>967.5</b>	<b>1534.1</b>	<b>1784.7</b>	<b>2745.5</b>
<b>Medium-term Loans</b>					
Livestock	63.8	284.3	225.1	177.4	442.2
Poultry	39.7	60.6	265.7	53.5	66.1
Fishing	1.8	0.6	6.9	6.7	4.3
Machinery	42.1	203.3	267.9	279.9	277.7
Crop production	-	-	-	9.2	12.8
Covered plantations	-	-	12.3	16.6	6.5
Cultivation related activities	-	-	315.6	411.4	516.7
Youth	-	-	-	-	32.9
Others	18.0	167.1	85.9	56.2	108.4
<b>Sub-total</b>	<b>165.3</b>	<b>715.9</b>	<b>1179.4</b>	<b>1010.9</b>	<b>1467.4</b>
<b>Long-term loans</b>					
Land reclamation & Plantation	0.6	5.1	22.9	16.5	5.1
Irrigation systems	-	-	-	3.9	5.4
Horticulture	2.6	3.9	0.7	0.9	2.1
<b>Sub-total</b>	<b>3.2</b>	<b>9.0</b>	<b>23.6</b>	<b>21.3</b>	<b>12.6</b>
<b>Total</b>	<b>657.4</b>	<b>2369.0</b>	<b>4252.8</b>	<b>4505.0</b>	<b>6430.5</b>

Source: PBDAC unpublished data.

About 16.7 percent of the sample supported the bank's role and added a few comments. Some asked for a reduction in interest rates, others complained about the collateral, one did not believe that loans were used for their activities and asked for more control and he pointed out that there were some activities that were not clear to the bank and consequently it refused to finance them. Another found the bank played a satisfactory role but should not deal in usury "Reba". The bank had already opened a few branches for Islamic transactions.

On the other hand, 27.8 percent were completely against it. 13.9 percent complained about its staff being bureaucratic and ignorant with regard banking



business, the lengthy slow steps and measures and found dealing with it not as easy or fast as commercial banks. 11.1 percent complained of the very high interest rates and one found it completely useless.

Was the PBDAC able to develop its role, enlarge its business network, and provide new services for new clients? If we observe PBDAC clients we will find out that it covered mainly two types of activities. These were; input trade and agromachinery. The first was what the PBDAC thought was its role to finance and support, that of taking over the task of input trade and distribution. The second used to have business ties with the bank for a long time before the SAP as it used to market their goods. Agricultural machinery in Egypt are expensive durable goods that take a long time to produce. Because of their high price, between 50-70 percent of machines were sold on credit. The sole source of institutional loans for agricultural machines was the PBDAC. Only firms registered with the PBDAC were allowed to sell their machines on institutional credit. All approved machines were sold through village banks (branches of the PBDAC) with the bank collecting commission on every sale (Kerr, 1994:881). These old ties between the agromachinery business and the bank were one of the main reasons behind this current co-operation. The bank employees were well acquainted with the financial and economic situation of these activities. There was no need for any new investigation and feasibility studies. On the other hand, the companies became used to the bank's routine and had probably developed a network inside the bank.

Meanwhile, the bank was unable to attract new clients with different types of activities. We can say that the bank staff were short-sighted concerning other types of operations. One of the sample mentioned that it took him a long time to convince the PBDAC about his business which comprised tree nurseries and landscaping. The work was not included in the list of undertakings in the bank. Another who was trying to obtain a loan for a flour mill had the same problem of convincing the bank to enlarge the scope of activity to consider his activity. The third example was for an investor who could not get a loan for egg production while it was allowed to get a loan to produce egg carriers. The question is who set priorities for activities and how? From the answers we can state that the bank used to rely on a list of activities which was rigid and should be reassessed according to market needs. We think that market needs were taken into account in the investors' project feasibility studies.

What the bank should have considered carefully was the project's anticipated revenue and its ability to repay the loan. As the bank's employees lacked experience they were too cautious to take responsibility for granting loans for new types of enterprises. Moreover, their overcautiousness in insisting on a high rate of loan repayments reflected an incorrect view concerning its effectiveness was the other reason.

It was evident that the PBDAC maintained the highest level of loan repayment among agricultural banks and organisations in the region, and one of the highest international levels of loan repayments (Ali, 1993:36). This was not, or should not be considered the main criterion for efficiency, as this could crowd out useful investment. However, loan repayments began to diminish from 1992, which revealed that there were other criteria for the repayment of loans, one of them was using loans in their purposes. Some investors mentioned that this was not the case with the PBDAC loans. The second related to changes in the economic environment which affected the profitability of projects, as happened with activities like poultry, as the increase in the price of inputs attendant on the monopoly enjoyed by some merchants in the market. This forced the PBDAC to reschedule the debt on these projects.

This caution was the reason behind what was observed with regard to most of those who obtained loans. These were large companies in terms of capital and the size of their transactions or had ties with the MALR and its officials because of their previous jobs or political connections. Most of them were reputed in the business market. However, their patronage network gave them the privilege of overcoming bureaucratic obstacles from the bank and they had greater access to bank credit than others. While it was announced by Dr. Wali that the concessionary loans available for this venture was meant to support farmers and young investors (*El-Ahram* 9/12/95). There is no evidence that the project had achieved its objective. In an interview, Dr. Khedr (17/6/97) stated that the bank was trying to introduce forms of untraditional collateral: as group collateral whereby the bank provided finance to five people, 100,000 for each, totalling half a million, and these five people were mutually responsible for the repayment, this type was suitable for the youth; or they used the creditworthiness of the undertaking itself and assessed it both technically and financially. The third kind was through another person who provided someone

or something as collateral. However, in the end Dr. Khedr pointed out that the bank was still a government bank and they could be accused of wasting public money; so that is why the staff was very cautious about the collateral.

As for the high overheads. Dr. Khedr justified them on the basis of its size with regard to its branches, which was spread throughout the country (17 governorate banks with 164 branches), the number of its staff (37,500 employees), the seasonality of its loans and their smallness, which entailed high overheads.

### ***6.6. The Impact of SAP upon Agribusiness***

The following part assesses the effects of the SAP on the agribusiness community, and how it responded. The study first evaluates the impact of some major measures, then the total effect of the SAP as reflected in the views and responses of investors.

#### **6.6.1. Interest Rate**

About 44.4 percent of the sample stated that their activities had been affected one way or another by the increase in interest rates at the beginning of the SAP. The effect was not related to specific types of activity; within the same activity some companies had been affected others not. It depended on the way it was managed and the size of transactions. The effect of paying high interest rates was an increase in the production costs which raised prices and caused problems in marketing. One businessman compared his situation with that of other small factories where he had to pay a sales tax in addition to the interest rate which led to a massive increase in his costs compared with theirs. 30.6 percent saw no effect on their activities. This was because they relied on self-finance, secured very low bank finance, avoided borrowing during that period, or obtained loans with US \$, with fixed interest. One investor mentioned that the high-interest rate on current accounts also caused money to accumulate in the banks which later encourage them to expand credit without appropriate grantees. This resulted in people escaping abroad with the money.

The effect of the rise in interest rates at the beginning of the SAP seems to have been mild, as it was for a limited period. Investors could control their credit during that period. Those who were not engaged in these activities were adversely affected as it crowded out new investments at that time.

In general investors were against high-interest rates as they affected their production costs. When they asked about their views concerning the current interest rate and if it was acceptable to them or not, the majority found it very high, 38.9

percent. Twenty seven percent considered it slightly too high and a quarter found it reasonable. However, one of them found it suitable in its own right, though he complained about the administrative fees which were very high, sometimes reaching 2-3 percent in the case of the PBDAC. The rest of the sample did not give any answer.

### **6.6.2. Currency Devaluation**

When investors were asked about the effects of the currency devaluation at the beginning of the reform, it was found that 44.4 percent experienced an increase in the price of imported raw materials, which had different impacts on them. Increased raw material prices meant an increase in costs, something difficult in marketing, an increase in prices in general, and a rise in wages. One investor believed that it caused an interest rate increase and one on storage prices as well; another said his export revenues had decreased; a third, that his foreign partner's share was paid in US dollars at the official rate, which affected his obligations towards him; a fourth suggested that it was a good idea to fix the rate, as he received loans in US dollars. Other investors provided no answer or assured that it had not affected them, as some of them had started after the reform. A few suffered some mild effects as their obligations in US \$ were not large. One pointed out quite correctly that the private sector never relied on the official price.

As can be gleaned from data about agribusiness imports, there were some activities that relied on imported inputs and raw materials. Others traded in imported goods. For these activities devaluation should have had a cost-push effect. In a study which relied on the estimated total requirements (direct and indirect) of imported intermediate inputs in Egyptian industries, chemicals, except oil, and machinery came third and sixth in the pecking order of industries using imported intermediate inputs. These activities, which included agro-chemicals and agro-machinery, had more important cost-push effects than others (Abdel-Khalek, 1993:107).

As we have seen Some investors blamed devaluation not only for affecting their cost, but also for an increase in prices in general (general price level) and the wages they paid. This generalisation is true for the whole economy because for Egypt the propensity to import is high. The share of imports from the GDP is

around 0.3, so the impact of devaluation on the general price level can not be ignored (*ibid.*:109)

### 6.6.3. Trade Liberalisation

The question of the effect of trade liberalisation on business was open. No specification concerning local or international trade was given to find out about businessmen's concerns. However, specific questions were asked about the local and external markets. Few took this as the end of the government monopoly of the agricultural input trade. Many took it as free international trade and for others it meant the GATT. The answer to the question also reflected a low awareness of the effects of trade liberalisation on the business community's activities or the economy. 13.9 percent of the sample gave no answer and 19.4 percent found it had no effect. One of them believed that it would not affect his operation: agricultural machinery! meanwhile it would affect textile industry, which meant that there was no international competition in his area which in our belief is not true. Another thought there would be no effect as he produced for the local market. He did not realise that foreign products could compete with him in the local market. A third thought that he would not be affected because his work was technical. He forgot that he relied on imported inputs and that the technology in his area of specialisation was developing very fast and that he could experience fierce competition, as others put it. One was frank and said that he did not know. In total 36.1 percent of the sample were not aware of the effect of trade liberalisation on them. In short there are some investors who are still not aware of the new era they will face.

On the other hand, 11.1 percent thought that it would have a positive effect without giving any explanation. One was in favour of free trade because only the strong would survive. 8.3 percent thought that it might improve the quality of the raw material and input and the price would be cheaper. Another believed that it might have good features if it encouraged imported raw materials for his activity, while it could have negative elements if it encouraged imported end products which would compete with his. Even this opinion overlooked the effect on other national producers of these raw materials. Those who saw the negative side were 8.3 percent. They thought they would encounter fierce and unfair competition. The same percentage thought it would affect local industry.

8.3 percent cared about free trade in the local market and considered it timely that they were able to compete with the government in local tenders, and they thought it best to leave price-determination and profits to market forces.

The majority of investors seemed unaware of the challenge they had to face in a free market era, especially after the full application of the GATT. They lacked knowledge about their new role not only in exerting more effort to improve their quality and produce efficiently, but also in developing their own technologies especially in bio-plantation and fertilisers. They also lacked an understanding of their obligation to encourage other national producers.

### *Local markets*

Investors' problems with the market reflect unregulated market problems: difficulties of access to the markets, oligopoly, and cheating with products. 13.9 percent found difficulty in accessing the marketing points all over the country. This was the problem of those working in the production of inputs -seeds, fertilisers, and insecticides. Some of them called for a role for the PBDAC in distribution but not in pricing. In the meantime 19.4 percent of the sample complained about dealing with their clients, merchants, middlemen and retail traders. They were not committed to payment times and some investors accused them of being greedy, trying to buy at the lowest price and sell at the highest. Another 8.3 percent complained specifically about the oligopoly of a few merchants with regard to the prices. These complaints came from the poultry and agro-industries. Another 11.1 percent complained about other producers who cheated the products and did not follow quality control directions and who were able to sell their products at low prices and compete with them. Those with forward linkages with other activities, as in the case of producers of animal feed, their operation was affected by the prosperity or stagnation of other activities. In our case animal feed producers complained about the deterioration of national livestock resources due to the importation of cattle for slaughtering.

The majority of investors were not able to overcome local market problems. A few of them tried. However, their strategies were not very successful. As for commercial cheating, two producers of agro-chemicals tried to explain the quality of the product on the bottle and exerted more marketing effort, yet one of them thought he could not overcome the problem. Another producer of irrigation systems had to abandon them completely and only work in commerce. Challenging the competition

was accomplished by reducing the price, as it appeared earlier that quality competition was not effective, so they had to use price competition. One of those who suffered from sale and retail traders stated that he tried to reach the consumer directly and failed. Another tried to diversify his activities. Traders in inputs tried to overcome the problem of local factories ceasing to deliver fertilisers to them, through importation. Those who suffered from the oligopolistic power of traders in imposing prices for their essential inputs gave no answer, as they could find no solution. One asked the government to intervene.

In spite of earlier drawbacks, about half of the investors were optimistic about future demand and expected it to increase. This was not justified by some, 16.7 percent related it to an increase in the population, 11.1 percent to progress in land reclamation and the same percentage to their marketing policy. One associated it with the advantage of being located outside the big cities. He was thus able to offer better quality and lower prices. Two input traders expected an increase in their demand. One saw that his business was less complicated and more efficient than that of the PBDAC. Another subject increased demand so as to receive all the produce of the local factories. Only one investor related it to an external factor which was the decrease in importation due to decreased demand on frozen meat because of BSE. On the other hand, only 5.6 percent of the total sample expected their demand to decrease. One arose from international competition, the other was because of an increase in domestic competition, as the local producers increased in number. 8.3 percent expected the demand to remain the same. The rest of the sample did not provide any clear answer.

### *Exports*

About 61.1 percent of the sample were engaged in export activities<sup>9</sup>. 9.1 percent of them produced only for exportation, while 36.4 percent exported 10 percent or less and 27.3 percent exported between 15 and 45 percent of their goods. Only 50 percent exported their output, 9.1 percent produced part of it and 18.2 percent hoped to produce it in the future.

The exports varied widely covering almost every kind of agricultural and agro-industry product. Vegetables and/or fruits were first with 27.3 percent of the exporters, Seeds and agricultural machinery followed with 13.6 percent for each.

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<sup>9</sup> Three cases, 13.6 percent, exported through others.

Then came animal and chicken feed, irrigation pipes or fittings, chemical fertilisers, bio-fertilisers, herbs and medical plants. Each of them was exported from 9.1 percent of the exporters. At the end of the list were water treatment units, pesticides and cotton materials. Livestock and poultry production were the only products that were not exported.

The Arab Market absorbed most of the exports as 72.7 percent of exporters export to Arab countries, most of them exclusively to it. 27.2 percent export to European markets; 4.5 percent to African countries, the same percentage to North America; and 9.1 percent to different parts of the world. Most of the exports to Arab countries were directed to the eastern part of the Arab world; Saudi Arabia, the Gulf states, then the western bank, Syria, Jordan and at the end came Tunisia and Morocco.

*Export change;* About half the investors were able to increase their exports and 9.1 percent of them opened up new markets. On the other hand, 27.3 percent of them experienced a decline in exports. However, some of them underwent more than one change. Investors attributed export increases to different causes: their own effort, government policy and external factors. 36.4 percent related this to their efforts in manufacturing new products and/or opening new markets. One related it to developments in production and improved quality and other attributed it to the availability of more facilities to the company like refrigerating and packing, price competitiveness, in Arab countries in particular. A smaller percentage gave the credit to the government, as only 9.1 percent believed that exportation had become easier and that there were more facilities. One was grateful that the MALR had stopped imposing mandatory prices on agricultural exports. Those who associated it with external factors, thought it was due to Arab conciliation, a general trend in increasing demand and to the water problems in the region which increased the demand for water-treatment units. Those whose exports declined said that it was a result of the ban on fertiliser exports for input traders, of bad weather for horticulture exports, or of production cost increases and because the products were less competitive and faced competition from Turkey. It was difficult for another whose domestic demand increased thus reducing his exports.

The investors' expectations about future external demand were rather optimistic as well. Some 54.5 percent expected the demand for their goods to



increase and only 18.2 percent to decrease. Among those in the former group 33.3 percent linked this increase to their efforts in developing their products, the facilities they provided to deliver the product in good condition and their good reputation, which built confidence in their products. A quarter of them thought that there was a market for their goods, one of them relied on the Arab market, another thought that the Chinese and Indian markets were growing, and the third thought that the demand for bio-products, his products, was increasing. The rest of the exporters gave various answers like; more information was available about external markets, there was an increased awareness among Egyptian farmers which meant that the quality of goods had improved, there were water problems in the region and one of them was aware that there was an external market but the local demand absorbed. Of those who expected their exports to decrease, half of them blamed the government for not being committed to a liberalisation policy or for the lack of an effective facility or export body to help open up new markets. The other half admitted that among the Arab countries, on which Egyptian exporters heavily rely, demand had shifted to other countries, while foreign markets were more restrictive with regard to quality control measures.

*Exports obstacles;* Only 18.2 percent of the exporters made it clear that they did not have any problems in exportation. One thought that most obstacles had been removed in the last two years. 13.6 percent gave no answer, which encouraged the belief that they did not have problems. The rest, 63.7 percent, complained about various things primarily administrative problems: 27.3 percent of the exporters. The same percentage complained about shipment difficulties, especially the high costs. 18.2 percent complained about the high price of the goods which reduced their competitiveness. From their point of view, high prices were for reasons beyond their control, as they related it to the high price of imported raw materials and customs duties and/or the high cost of electricity and shipment. Other obstacles varied. Most of them were linked to local factors, such as high fees. Two input traders complained about the unstable export policy. One of them who had links with government officials and the NDP did not want to criticise the government, but blamed the factories for not being serious about delivery. The absence of good packing facilities, bad quality, sometimes due to the use of chemicals, and corruption were on the list, but referred to by only one investor. The businessman who

exported through others claimed that a few individuals monopolised the market and accused government officials of colluding with them. He had one experience when he tried to export on his own account but his goods were refused because of unacceptable quality. Before he left the place an exporter bought them and was able to export them. Obstacles linked to external factors scored low, as only one entrepreneur complained about the competition of international companies, while others claimed that some countries like the Lebanon placed barriers to their imports.

### *Imports*

More investors were involved in importation than exportation, as 69.4 percent were engaged in the former and others relied on imported inputs and spare parts. They imported various kinds of goods for different purposes: trade, inputs, production machines and goods, and spare-parts. Agro-chemicals (different kinds of fertilisers and pesticides) topped the list of imports, as 30.6 percent imported them. 19.4 percent imported agro-machinery (or components) and equipment. 13.9 percent imported seeds while the same percentage imported other kinds of inputs and raw materials. 8.3 percent imported spare-parts. 5.6 percent imported production machinery and the same percentage imported turbine pumps and water treatment equipment. One imported irrigation systems, others imported cows' milk, packing materials for exports, and fruit receptively. The sources of imported goods varied, western Europe was at the top of the exporting countries, followed by USA, while Asian countries and Israel came at the bottom.

When marketing their imported goods, 32 percent of importers believed that there was competition from local products while 28 percent did not think so. One trader in agricultural inputs explained that most markets relied on imported agricultural materials, yet this was not the opinion of all of them, as a few thought that they had encountered competition. For the rest, the question was irrelevant as they imported spare-parts, inputs for their activities and production equipment, or they provided no answer to the question.

Importers complained about many constraints. At the top were administrative problems. 28 percent complained about routine and the lengthy bureaucracy. Moreover, they suffered a lot during the licensing process. The MALR was mentioned as adopting lengthy procedures and taking a long time to approve new products. The same percentage complained about the high customs duties. 24

percent complained about the sales tax. 12 percent complained about the extremely high administrative fees. Fees collected by MALR to examine new product before allowing in the market was extremely high as most traders in inputs mentioned. The remaining complaints varied between lengthy steps to open credit and the compulsory transfer of value even if it was free or granted.

The domestic market for agribusiness products and services was vast and expanding, promising to absorb any increase in production. Although there were many complaints about marketing in the local market, this was a result of problems in marketing capacity not market capacity. The only product which had difficulty in finding an adequate demand, was animal fodder. Many producers of livestock abandoned the market because of the importation of meat or cattle. Producers also suffered from the oligopoly of the merchants who imposed unfair prices and from the cheating of other producers. This revealed the absence of a legal infrastructure to protect property rights and to fight monopolies.

External markets was available especially for irrigation systems and agricultural inputs. The Arab countries provided the main external market for Egyptian products. These markets did not have strict quality-control conditions like the European markets, which might mean that they overlooked some aspects of quality-control. However, these markets are diminishing in the face of Egyptian products, as more countries are competing. The cost of shipment was another reason for reducing Egyptian competitiveness. Shipment to Arab countries is more expensive than to Europe. The main challenges facing Egyptian production is those of competing more in the European markets and being able to continually develop its quality. There is a need to exert more effort in external marketing. Many producers asked the government to play a vital role in this respect but they must not forget that they have some obligations in this matter as well.

Although it was observed that exportation was promising, especially where some more effort was made to improve quality and open new markets, it was also noted that most agribusiness products relied heavily on imported inputs, raw material, spare parts and manufacturing machinery and goods. They claimed that local products were of poor quality. This involvement in importation at the expense of exportation meant that any advantage achieved from the latter was offset by an even greater burden on the former.

#### 6.6.4. SAP Ability to Overcome Investment Obstacles

When investors were asked about the obstacles which the SAP was able to overcome, 63 percent of those who faced problems before the programme stated that their problems had not been overcome by the programme. One of them claimed that his problems had become more complicated. He complained that the regulations for owning land for reclamation were difficult and complicated. 14.8 percent agreed that their problems were partly solved, while only 22.2 percent mentioned that their problems had been solved.

What were the problems which the SAP succeeded in overcoming and what were those in which it failed? The list of obstacles was lengthy and varied due to the variety of activities. However, if we try to group them according to the most intractable ones, we find that; when it came to government bureaucracy and complicated procedures and regulations, only one person referred to the solving of the problem of the slow administrative procedures, another found it partly solved, while three considered it still there. The following obstacle, which was the subject of many complaints, was the monopoly of the public sector and the PBDAC. The monopoly of armed production of agro-machinery importation-licensing were the obstacles which had been solved. As for the PBDAC, while investors expressed their relief at its withdrawal from distributing agricultural input, they complained about the retreat from the liberalisation of distribution of fertilisers and some local components of animal feed, which were also publicly produced, as its policy was not consistent. They asked for the liberalisation policy to be completely implemented. Other features of the public sector monopoly were also very clear in the services offered by Egyptian ports. The obstacles which it is evident the programme succeeded in overcoming were the availability of foreign currencies and the stability of the exchange rate. These were solved for those who dealt with US \$ more than for others. Some investors who dealt with other foreign currencies complained that the price of these currencies was not sufficiently stable for them to feel secure in their dealings.

Few complained about taxes, custom duties, and unstable prices, and said that these problems were not overcome by the SAP. It is to be noted that there were a few problems that became clearer after the SAP, for instance, in addition to the problems of taxes, investors complained about the general sales tax. While some

referred to the reduction in the customs rates, there were increases in other dues related to importation. More complaints were directed against importation facilities after the SAP. This may be because investors were more involved in importation. The results of importation was also crystallised in other obstacles, as there were increased complaints about the unstable prices of imported inputs. In some industries they stated that inputs were more readily available compared with the period of public sector monopoly, while prices were more unstable. There were more complaints concerning marketing than in the period before the SAP, Some asked for the PBDAC to come back as the only distributor of Agro-chemicals inside Egypt without being involved in pricing or importing, but merely to work as an agent with them as distributor.

### ***6.7. Conclusions***

My case study has revealed that the reforms encouraged a limited private sector revival. The most common activity introduced during this period was input trading, as a result of rolling back the PBDAC from input trading and distribution. This period witnessed a greater involvement of university professors of agricultural science in the private activities of the agribusiness. They usually collaborated with private sector managers with experience in marketing. Agribusiness enterprises benefited from their experience and they were more involved in production than trading. They were also able to introduce the new technologies of non-chemical plant-growth regulators and pest control. The MALR officials benefited as well, since some of them set up their own operations and were able to persuade others to work with them. Family ties were clear in the management of few companies, however, this did not constitute a common pattern.

Finance was the main barrier of entry in this period of reform, while administrative barriers to entry were relatively relaxed. Fewer numbers of investors mentioned that they suffered from routine and the discretion of public officials. However, these obstacles remained significant in the functioning of agribusiness activities. It was repeatedly stated when discussing importation, exportation and sales tax refund measures and was emphasised most strongly when there was any deal with the MALR.

Reforms targeting the PBDAC were meant to increase its capabilities as a commercial financial institution. Nevertheless, these reforms were of limited effectiveness. Most investors in the sample refrained from dealing with it and preferred commercial banks. They described it as a government bank steeped in routine and with its staff lacking in banking experience. Its collateral policy was also strongly criticised as being unrealistic and inelastic. The PBDAC as a government bank, was very cautious in its credit policy. As a result, its loans were biased towards large companies.

The reforms were useful for those activities that used to be subject to massive state intervention, as in the case of the input trade, animal feed and poultry. However, the reforms lacked gradualism as happened in the cutting of the corn subsidy, or were inconsistent, from their point of view, regarding the irregular interference of the PBDAC in the distribution of fertilisers and some animal feed components. The most useful reform measure was that of allowing free transactions in foreign exchange. This step, together with interest rate reform, also allowed for more stability in the exchange rate of foreign currencies. This stability was useful to those who traded in the foreign markets: exporters and importers. As agribusiness activities were forced to rely heavily on imported components, one of the drawbacks of this sub-sector, stability in foreign exchange were very useful. However, this stability was achieved more for the US dollars, while other currencies were less stable. This hurt investors who used other currencies in their transactions.

The potential for the expansion of agribusiness activity was high due to heavy demand. However, administrative and institutional obstacles impeded this potential. Internal demand showed an increasing trend and investors were also optimistic about the external demand. However, some investors seemed to lack knowledge about the international and regional agreements. Both the fertiliser and poultry industries had high potential. Fertilisers had high internal and external demand. The poultry industry provided good expansion potential for complementary activities such as slaughter houses, and packing and refrigerating as there was a severe shortage of these complementary activities. This shortage was one of the reasons which paved the way for merchants of live chickens to monopolies the market and influence prices. This led to new problems which arose from the free markets.

Investors in the period of the reform not only suffered from administrative obstacles from public officials but they also suffered new problems in the market economy. Commercial cheating was one of the main difficulties which faced producers of fertilisers, insecticides, and new irrigation systems. They failed to face up to this problem completely and needed an effective legal system to protect them. Some producers of input also failed to reach consumers all over the country and asked the PBDAC to help but without interfering with prices as it had outlets available in every village which were not being used at that moment. They also suffered from manipulation and from the irregular payments of middlemen and merchants. Finally, the merchants enjoyed a price monopoly over some activities which producers in the poultry industry complained about. Some of them failed to access the external market and asked for effective help from the state to open new markets, to provide new technologies to help investors improve the quality of their products and to compete in the external market. Thus the study confirmed the private sectors need for a strong and effective state to help private sector revival.

## Chapter 7 State-Agribusiness Relation

### *7.1. Introduction*

This chapter draws on more empirical evidence concerning the effect of the reforms on the agribusiness community. I assess the ability of the reforms to build credibility between investors and encourage their participation. I also evaluate State-Business relationships in the agribusiness sector under the SAP. On the one hand, I consider how the state managed the reforms with regard to their transparency, sequencing and consistency. I ask how successful has the state been in raising the performance of its bureaucrats? And has state capacity been improved? On the other hand, I assess the impact of reforms on the political behaviour of agribusiness investors. Have reforms increased their credibility in the state? Have they encouraged more political participation? Have the economic gains achieved by investors enhanced their political power? Have they had any influence on the process of decision-making? I also identify the main characteristics of the economic and political behaviour of investors and assess their political participation and their political weight. The main argument running through this chapter is that the agribusiness community is politically weak and has limited effectiveness in the economic arena because it is fragmented and its members, with the exception of a few, lack clear vision about their role at the macro level.

### *7.2. Credibility of the Reform*

Was the SAP able to win the credibility of investors? The credibility of the reform programme is very important to revive the supply-side response, to enhance growth, and to build a constituency of beneficiaries. The evidence drawn on earlier shows that the SAP succeeded in some aspects and failed in others, but, in short, what was the investors' view, did they find it generally useful? Were they willing to support it politically? To answer these questions I draw on more evidence concerning their general assessment of the usefulness of SAP measures for their activities; anticipated expansion of their activity in future; their views concerning the new government measures; and their willingness to participate in the privatisation programme.



### 7.2.1. Investors' General Assessment of the SAP

As is clear from table 7.1, one fourth of the total sample found the SAP measures very useful, while the same percentage found it of limited usefulness. Yet, even among those who found it very useful some had reservations concerning the inconsistency of the liberalisation policy. Overall, we can say that half the total sample found it generally useful. This might give the impression that the percentage of people who opposed the reform was rather high, while this was not true. Two thought that some parts of the reform were useful and others were harmful. One thought that he could only see some improvement in the last year. Two found the reforms harmful and one found them very harmful. Together, those represented 16.7 percent of the sample. The rest, about one third, either found it had no effect or gave no answer. One of the main reasons for this relatively high percentage was that some investors did not know what the economic reforms were, They might have been aware of some of the measures taken, but they did not realise that this set of reforms collectively made up the reform nor could they imagine what was the rational and general objective beyond it.

**Table 7. 1 Investors' Assessment of the SAP**

Reform Usefulness	Number of respondents	Percentage
Very Useful	9	25
With limited usefulness	9	25
Some useful, others harmful	2	5.6
Last year, limited improve	1	2.8
With limited harm	2	5.6
Very harmful	1	2.8
No effect	8	22.2
No answer	4	11.1
Total	36	100

*Characteristics of the Reform Supporters,* Who found the reform useful? What activity benefited from the reform? We were unable to obtain a definite answer to this. Those who found it of limited usefulness or very useful came from different activities, where as within the same business some found it useful others did not. It did not relate to a particular size as well.

One common characteristic we noticed among those who found the reform very useful was that 5 out of 9, more than a half, were members of the NDP 'The ruling party'. While those who found it of limited usefulness 2 of 9, 22.2 percent, were also members of the NDP. Table 7.2, which shows the response of the NDP

members reveals that about 78 percent of them found the reform useful and only one person found it did limited harm, while another found some parts useful and others harmful.

**Table 7.2 NDP Members' Views of the SAP**

Reform effect	Number of respondents	Percentage
Very useful	5	55.6
With limited usefulness	2	22.2
Some parts useful, others harmful	1	11.1
With limited harm	1	11.1
Total	9	100

Most of those supporting the reforms gave at least two reasons for their opinion. The most common were those related to changes in the monetary policy, such as the fixed exchange rate which benefited those whose business was related to importation, either directly or indirectly, using or trading in imported inputs. One person also referred to the facility given to credits in foreign currencies, while another referred to the allowing of profits to be transferred abroad, which helped him to find a foreign partner. At the same level investors supported the increased role of the private sector and the roll-back of the state. Other reasons varied between free prices and markets, and trade liberalisation. The main obstacles to investment seemed to be that it was still valid as only one referred to the stability in tax laws and regulations with no mention at all of the stable macroeconomics environment or policies in general, and it seems that this matter still needs more time to gain investors' credibility. The other more crucial obstacle was routine and the complicated procedures of government regulations and rules. Only one case referred to the facility of some administrative procedures.

### **7.2.2. Investment Expansion**

Investors anticipated an expansion in the future and the reasons behind it were another good sign of the belief in the reform. Their expansion in the past offers a good contrasting situation to measure their anticipated response.

As for expansion in the past, investors expanded their activity in various ways, as can be seen in table 7.3 below.

**Table 7.3 Companies' Expansion in the Past**

Type of Expansion	Number of companies	Percentage
Decrease Production	1	2.8
Expand Employment	10	27.8
Expand Exports	7	19.4
Expand Capital	19	52.8
Expand Production	18	50
Introduce new Products	23	63.9
Introduce new Services	8	22.2
Introduce new Technology	14	38.9
Shifting from Domestic to External Markets	16	44.4

Most enterprises, 64 percent, expanded by introducing new products. This should be viewed with caution as this could mean that the increase in demand was merely due to an increase in population, as most answers justify their expectations of increasing demand in another question. Others also stated that they had to diversify their activities to overcome market problems, by introducing new products and services. This might mean that there was increasing competition between companies which they had to overcome by introducing new products. The next area of expansion was in capital, 52.8 percent. Only 27.8 percent increased employment. This means that increasing capital does not necessarily lead to an increase in employment, that agribusiness operations are a capital-intensive activity and do not greatly help in solving the problem of unemployment. This is clear from the ratio of capital / labour in the companies. As far as export was concerned, 44.4 percent were able to shift from domestic to external markets, while 19.4 percent were able to increase their exports. This expansion in exports was possible due to the fact that most of this sector's exports are to Arab countries where political relations improved after the elimination of the Arab boycott against Egypt in the wake of the peace accord. This means that they were expanding well before and during the early years of the SAP. However, some of the expansion was due to an increase in population or by increasing up the increased competition of the new activities which affected their share in the market, by introducing new products and services. What about the Future?

*Anticipated expansion in the future,* Most investors were optimistic. A quarter of respondents said that they sought expansion in about four ways. Only one employer thought of reducing his employment by expanding his production through new technologies.

**Table 7.4 Companies' Anticipated Expansion in Future**

Type of Expansion	Number of companies	Percentage
Decrease of Employment	1	2.8
Expand Employment	18	50
Expand Exports	16	44.4
Expand Production	24	66.7
Introduce new Products	20	55.6
Introduce new Services	1	2.8
Introduce new Technology	17	47.2
Open new External Markets	20	55.6
Start new Complementary Activities	15	41.7
Open new Internal Markets	1	2.8
Establish Research Unit	1	2.8

Table 7.4 indicates that the majority wished to increase their production, 66.7 percent. 55.6 percent thought of introducing or marketing new products and services and the same percentage hoped to open new external markets. Their expectations for expanding export were high as well. It also appeared that they had high expectations concerning improving technology and starting new complementary activities. This optimism should be viewed by care. Respondents expectations for the domestic market were based on an increase in population. Investors were also optimistic concerning external demand as some of them had more information about the external markets, or had improved the quality of their products. However, as also appeared earlier, there was increasing competition in the external markets and some of them started to lose the Arab market share.

### 7.2.3. New Government's Measures

A new government took over in 1996. It was thought to encourage investment and improve the investment climate. At that time these measures included reducing the customs duties on production machinery and equipment, facilitating ownership of reclaimed land, eliminating the police inspections of the tax authorities. When investors were asked for their opinion<sup>10</sup>, four provided no answer, which gave the impression they did not know about it. Again, few of those interviewed asked what these measures were. Three answered that they were sufficient if properly carried out. Seven, 23.3 percent, found them to be of limited effect. And 16, 53.3 percent, found them good. Some of them added the comment 'if properly executed', but other steps were needed.

<sup>10</sup> This question, and related ones, was asked only in 30 cases of the sample, the remaining six were conducted before the 1996 measures.

When investors were asked about other necessary steps to encourage investments, three provided no answers, one mentioned that he hoped that there was more. However, the list we recovered was varied and extensive. It was interesting that even those who had been asked about the difficulties they encountered before in at least two different ways, had more to add every time. Most of them, 36.7 percent, concentrated on getting rid of bureaucracy and red tape. Investors asked for measures to be facilitated, for a reduction in the number of authorisations and approvals they required to obtain every time. Some of them asked for a unified authority for them to deal with. The MALR, in particular, was subject to several complaints. Traders introducing new fertiliser, seeds and pesticides complained that they had to wait for lengthy periods, several months, to obtain its approval, in addition to the extremely high fees which they had to pay (thousands of \$).

More than a third complained about tax rates and measures. One expressed his delight in the abolishing of the police tax inspections and wondered whether it would really be carried out. Many of them considered the tax rates too high and asked for their reduction, also an increase in the tax holiday or the raising of the exemption level to £E 5,000 per annum. Tax accountancy methods were subject to criticism as well and was thought to crowd out the private sector. While 20 percent requested a reduction in customs and importation fees. 16.7 percent asked for a decrease in government monopoly, control and intervention. 10 percent wanted the expansion of new industrial towns, facilitation of land registration and a reduction in its price. The same percentage asked for more facilities and the expansion of land reclamation. Some also made it clear that it was for the benefit of their business as traders in agricultural inputs, while one asked for a drop in the price of land, electricity and water.

Some investors put forward other requests, such as those to trust investors; to stop or to regulate the importation of final products; to abolish obstacles facing exporters and to encourage exporters; and to increase quality control on inputs.

When investors were specifically asked about other essential steps to encourage exports, the list was more homogeneous and less extensive. 43.3 percent provided no answer; only one mentioned that there were no problems. At the head of the requirements of the others was their demand for easier measures. 26.7 percent asked that the necessary administrative steps for exportations should be curtailed so

that the refund of the sales tax and the temporary allowance should be easier. Of like importance was the request to provide information about foreign markets, as asked for by the same percentage. They asked about the real role of Egyptian embassies and commercial offices abroad, and for formation of exportation bodies with effective participation in external marketing. Other asked the help of the MOFT to send official delegations of businessmen to promote exports.

13.3 percent asked for exportation fees to be abolished or reduced. 10 percent requested that all burdens increasing costs be abolished as well: customs, sales tax and electricity prices. One mentioned that electricity prices had increased five times recently. The same percentage asked for financial incentives, these incentives varied from one investor to another. One asked for tax concessions, another for a low interest rate on loans and a third asked for an encouraging exchange rate. Two asked the government to increase quality control on exports and to provide good-quality goods for exportation. Two others asked the government to support the exporter with whatever possible and to remove all obstacles.

#### **7.2.4. Participation in the Privatisation Programme**

Investors showed little interest in participating in the privatisation programme. Only two had already taken part in the programme. 41.7 percent refused to join in, justifying this with their preference to expand in their own businesses, and for one it was because he could not afford it. Another investor revealed that he could not trust the management. If he could afford to buy, he would have bought a controlling share. Only 8.3 percent said that they intended to buy main shares, 19.4 percent intended to buy some shares. Some of them placed few conditions for this; to be a successful and profitable company, to study their budgets first, and to be in the same business, for the Egyptian stock market to become international.

#### **7.2.5. Credibility Assessment**

From the above answers we can see that although the SAP could not create a consensus support between investors, it was not faced with real opposition. Half of the investors found it useful. However, most of the other half were not openly hostile. In fact some of them gained. Investors supported the major policy of liberalisation. In different situations they expressed their satisfaction with the market system, free prices, and the end of government monopoly. Although they sometimes had complaints about negative aspects of the market, they resisted the

return of government control over the markets. The lack of credibility was directed towards the government's ability to carry out the needed reforms, towards the pace of reform and sometimes its sustainability.

There is a lack of credibility in some government institutions and in government officials. This was clear from investors' views about PBDAC officials and employees and the reluctance of the majority to deal with the bank. It was clear as well from their attitudes towards MALR officials. Some seemed suspicious concerning the application of what was said by the new government about the reforms. They preferred to wait and see. They believed that there was a gap between policy-making at the ministerial level and at the implementation level.

Investors thought of the government as the last resort for their problems. They were used to government intervention, now they asked for it on their own terms, to help in distribution and markets, but without interfering with prices. They also needed government help against commercial cheating, market monopoly, and in opening up the external markets.

In the end they were generally optimistic about future internal and external demand for their products and services. However, most of the time they related it to the natural growth of the market or their own efforts, at least they were convinced that their efforts would not be interrupted by government intervention.

### ***7.3. Political Participation***

This section assesses the behaviour of investors' participation in formal politics. As we have seen they did little to face up to market problems as they believed they could not. Did they try to influence government decisions? And if so, how and what were the results?

*Membership of political parties:* One fourth of investors in the sample were members of the ruling party the NDP. None was a member of any other party. This highlights the fact that a growing number of businessmen are joining the ruling party on mean to become more involved in decision-making process and to gain more benefits.

Members of the party were engaged in different kinds of activities, like agro-chemicals, producing high-quality seeds, poultry, land reclamation, and bio-fertilisers. Capital size differed as well and was not related to a particular amount of capital. The largest amount was £E 8 m, while the smallest was £E 50,000.

Investors who joined the NDP came from both Cairo the capital and from other governorates as well. More than half of them their activities located in the greater Cairo district, while the others were located in Dakahlia, Behiera and Sharkia. Some of them were university professors others were purely businessmen. They were highly educated, but this was the case for most of our sample. The majority of them, 77.8 percent believed in the importance of democracy to enforce the programme.

*The People's Assembly:* The number of businessmen nominating themselves in the Peoples' Assembly elections is increasing. Many businessmen nominated themselves in the last election of the People's Assembly which took place shortly before of the fieldwork (November 1995). According to press reports' these businessmen paid millions of pounds during their campaigns, which reflects their seek of power and participation in the decision-making process two of the sample nominated themselves in the election. For one of them it was the second time that he had put himself forward. However neither of them won. Both of them were members of the NDP and were nominated by the party. The estimated number of businessmen who were able to join the assembly was ten. One of them was a prominent agribusinessman. In addition, the ten appointed members included one businessman. The same happened in the Shoura Assembly, as another prominent businessman was appointed. This reflects not only the ambition of the businessmen to participate in political life but the interest of government to have them represented in her legislative authority. Yet we should mention that the Peoples' Assembly enjoyed greater popularity for businessmen than the Shoura. Assembly, as it provided them with more power and privileges.

*Voting in the election:* About one half of the sample voted in the elections of the last People's Assembly. One third of the sample admitted that they did not vote, while the remaining percentage provided no answer to the question.

Here, we face two different attitudes. One group seems to have tried to increase its representation and power by joining the ruling party and nomination in the parliament. On the other hand, the majority, on the contrary, did not even exercise its right as normal citizens. This might relate to the crises of political participation in Egypt in general and the low level of credence in the voting process.

*Ability to organise:* The question that arises here is; does this negative attitude towards elections and voting apply to the participation of civil society



organisations where they enjoy relative autonomy? A considerable number of the sample were members of more than one organisation. If we exclude the Chamber of Commerce as a semi-governmental organisation supervised by the Ministry of Supply where membership is compulsory, and if we exclude the Industrial Federation as its situation is virtually the same, we find out that 17 members of the sample, about a half, are members of 13 different kinds of Business Associations, as some of them were members of more than one association. While two investors were members of two '*Gamayat Ahlya*'. We define Business Association as those associations whose activities are effectively to the business of the companies, while the other '*Gamyat Ahlya*' engage in activities in a wider context, which is more related to society as a whole or other groups not strictly related to the business of the company. Both kinds of organisation were established under the regulations of the Ministry of Social Affairs.

There have been two types of business organisations, those that are not restricted to a particular activity, and specialised organisations. Three of the sample were members of the Egyptian Businessmen's Association, one of the most prominent business Associations in Egypt. A further reason for joining which all of the three agreed upon was the ability of the association to open new external markets. A further reason for one of them was consultation with government concerning economic policy, for another, it also provides technical consultation. The Arab-German Chamber of Commerce gained the membership of two of the sample. The reasons investors gave for joining it were the same as in the previous case. †

**Table 7.5 Business Associations and Number of Members**

Organisation	No. of Members
Animal Feed producers Association	1
Arab-German Chamber of Commerce	2
BAPAM	2
Businessmen Association for Agricultural Development	1
Cooperative for Fisheries Plantation	1
Cooperative for livestock development	1
Egyptian Association for Agrochemical for producers and Affiliates (EAAPA)	2
Egg Producers Association	1
Egyptian Association for Fertilisers Merchants & Distributors	2
Egyptian Businessmen Association	3
Friends of Environment and Desert Association (FEDA)	1
Federation of Producers and Exporters of horticulture	1
Sadat City Investors Association	1

The second type of Business Association comprised the specialised business associations that varied in type as shown in table 7.5. The reasons for joining them varied widely. The strongest reason in relative terms was consultation with the government concerning economic policies. There were variety of other reasons which differed from one organisation to another. Some gave general reasons, such as maintaining the interests of the members in every respect, others were more specific like; providing loans and funding facilities, technical consultations, exhibitions to provide information about new technologies and solving administrative problems. We were unable to distinguish between the important ones as they provided similar, limited services. Nevertheless, one of the organisations provided an outstanding service compared with the others and that was the EAAPA, which engaged in environmental activities and was working on awareness concerning the use of chemicals and safe ways of handling them.

Specialised associations usually contain homogenous groups with homogeneous interests. However, in our case it was rather fragmenting and created power conflicts. On the one hand, this was because of the overlapping activities of some associations which competed with each other, and on the other, the lack of a general association or federation which worked as a gathering and coordinating body. In the case of those working in the agrochemicals, there were two associations the first was the Egyptian Association of Agrochemicals for Producers and Affiliates (EAAPA). The second was the Egyptian Association for Fertiliser Merchants and Distributors. We noticed that the producers had their own association which was separate from the distributors although they experienced difficulties in distributing and there was a need for them to unit their efforts. Signs of competition were noticed between one of the sample and another outside it. The one belonging to the sample who founded an association and used to organise annual exhibitions of agricultural machinery and materials. Then another organisation competed and organised bigger exhibitions with better capabilities. However, for some time the competition tended to favour the industry.

The limited activity of the organisations might be due to the lack of real participation of their members. It was evident that some members were unable to state some of the activities of their organisations. This could have been due to lack of communication or participation in the organisation's activities as they might have

expected different types of service. For example, the researcher visited one organisation, the EAAPA, the main purpose being to gain access to those who were involved in their operations. However, it was apparent that the organisation engaged in manifest activity related to the environment and it had arranged some seminars in this area with the help of an international organisation, about safe ways to handle and deal with agrochemicals. When investors were asked about the work of the organisation none referred to it. Although one did mention it in an answer to a different question. This raises questions about their general participation and about the type of involvement? Was the reason for low participation the fact that it did not provide a direct benefit for them, but rather cared about the health of the employees?

Although about half the sample were members in one or more business organisations or in the *Gambia Ahlya*, the kinds of services they received were still very limited. The common activity they gave was consultation with the government concerning economic policy. How effective was this consultation? When they were asked about the effectiveness of the business association in shaping economic policy, nearly half of them thought that it had limited effectiveness, while 13.9 percent thought it exerted no influence at all. The same percentage provided no answer. This could mean, either they in no way believed in its effectiveness or they did not have enough information to judge, which means that they were isolated from the business community and politics. Those who thought that it had an effective influence were less than a quarter. One case related the matter to the power of the members of the association, their previous role and status in government or their relations and connections with empowered government officials. This was true to a large extent and we stress here that it also depended on how much it was in favour of certain policies and what kind of support it could obtain from domestic and sometimes external forces. It is worth mentioning here that between what we ask about its effectiveness was the Egyptian American Chamber of Commerce and we received no answer at all, except from one person who thought that it was effective and it drew its effectiveness from its name, to which here we can add no comment. Another investor mentioned a prominent name, pointing out that he knew him and he asked him to join, so it seems that it was really true that some associations gain from its name, power and then are influenced by its figures. Our question about this specific association to this businessman, together with the starring name he

mentioned proudly, seemed to incline him to consider joining so as to gain a more prestigious position and to benefit from a more extended network. So it really seems that this was one more advantage in joining these association:

*Investors' views concerning democracy,* As we discussed in the first chapter, there have been conflicting views concerning the relationship between democracy and the success of the SAPs. Some have seen democracy as an obstacle to the programme as it allows conflicting and competing views and goals. The experience of developing countries has shown that there is no relationship between the political system and the success of a programme. Reforms have been successful in authoritarian regimes and in democratic ones as well. However, there is more consensus about the importance of democracy for the sustaining of the programme. This study explored the views of agribusiness investors concerning the relationship between economic reform and democracy, trying at the same time to clarify whether or not they were in favour of democracy. Three of those questioned answered that it depended on the way democracy was practised. This meant an implicit protest about what was called democratisation in Egypt. Only one businessman found democracy an obstacle to the reform programme. This was because he believed that the majority of people did not benefit from it and investors were the only beneficiaries and more democracy would mean more protest. Apart from this very frank investor, at least in expressing his opinion, the rest of the sample were in favour of democracy as a support for the programme. For a high percentage of them the reasons for this were purely economic. They saw democracy as a means to communicate their views on the economic problems and issues. This was a purely personal attitude, only one related it to development in general. He gave an example of the developed countries and related the practice of democracy to achieved economic development. Although the first view can help in achieving economic development, this comprehensive view was not meant for their argument. The most developed views were for those that looked at democracy as providing equal rights for all citizens and as a means to control corruption and the patronage network.

*Investors' views concerning the role of the state,* Investors' views concerning privatisation reflect, to a large extent, their views on the role of the state. More than a quarter of the sample thought that all PEs should be sold, while 41.7 percent thought that large strategic companies should be kept in the public sector. This

could reflect the national feelings of the investors. They may also have thought that they could not afford it. This appears from their answers to the question about their participation in the programme. They might prefer government monopoly in this case rather than the monopoly of foreign investors or even a national one. Only one businessman thought that companies dealing with people's basic needs should be kept. This reflected a strong sympathy for the poor however, with a very low percentage. Less than a quarter thought that failing, loss-making companies should be phased out. The same percentage refrained from giving an opinion. Few of them were not able to give an opinion concerning privatisation or to answer this and the following question. They thought it was the work of economists and responsible people.

When asking about the best way to privatise the PEs, a third of investors preferred to sell shares on the stock market, more than a quarter preferred a total sale for national investors, while only three preferred a total sale of the PEs and they did not mind selling to foreign investors. Their view was that the companies would still be in Egypt and that the people would benefit from its activities, they did not distinguish between different activities. They did not think of foreign banks and the risks of controlling sources of finance or of introducing foreign employment. 13.9 percent preferred private-sector management and the same percentage preferred selling to employees. It should be noted that some investors gave more than one answer with different alternatives. However they did not specify for each type of company.

#### ***7.4. State Performance during the SAP***

##### ***Sequencing of Reform***

Gradualism was the slogan of the programme when the GOE first agreed to adopt the SAP. Protecting the poor was the reason behind it. Gradualism was to be applied to policies which affected the cost of living and peoples' ability to generate income such as; phasing out subsidies or privatising the PEs. Phasing out agricultural subsidies seemed to be done suddenly, as in the case of cutting the corn subsidy for the poultry industry or the fertiliser subsidy for farmers, as seen in chapter 5. While institutional reforms seemed to be lagging behind, they should have been given priority and pushed forward more rapidly. This would have enforced the programme

implementation and enhanced the private sector response. Meanwhile it could have helped to remedy the negative effects of the programme.

Dealing with the fertiliser problem reflected the slow response to deal with an old problem before it turned into a crisis. This slow response reflected weak capacity and performance which in turn affected the pace of reform. The government solution to the problem represented a step back for the liberalisation policy. Again, this affected credibility in the reform and affected the pace and sequence of the reform.

The legal framework needed for the market economy was absent. Laws to protect consumers and producers from commercial cheating and market monopoly were delayed. After more than eight years of official approval of the SAP the laws were still under consideration. The last period of the free market proved its need not only for consumers but for producers as well. As it was mentioned above, producers experienced commercial cheating and asked for a law to protect them. The government should have done everything to gain credibility in developing the programme.

#### *Administrative performance*

Complaints about complicated administrative measures, in addition to the poor performance of the government bureaucracy, lack of flexibility and competition for power were frequently cited. These complaints were repeated at the various stages of operating their business. As a result, the administrative reform was one of the investors' main concerns for reform. Investors were confronted with routine and administrative obstructions from their first moves to establish their companies. It was their first complaint about establishment measures. The period of the SAP showed a slight improvement. It was observed that bureaucratic measures prompted the first complaints, even for those companies which were set-up in 1936 and later, and we were aware that this problem was deeply rooted in the Egyptian administration. It should also be noted that most agribusiness companies created during the SAP were instituted under private sector law and not under investment law, which achieved better progress in facilitating establishment steps. This drew attention to providing greater consideration for companies established under this law or to provide a unified law for investment.

Many other kinds of administrative performance were subject to complaints. Tax administration was one of the main obstacles, as investors complained about tax accountancy and sales tax refund methods. The General Authority for Export and Import Control and the lengthy procedures for exportation and importation were criticised as well. The MALR was subject to many implicit and explicit complaints. Right from the beginning of the research some investors, in land reclamation in particular, claimed that research results would cause them more difficulties with ministry officials and bureaucrats, or simply nothing would be changed. This lack of credibility in the MALR bureaucrats was the result of bad experiences with their performance. Traders of imported inputs repeatedly complained about the lengthy steps and prolonged waits to have a new product approval, apart from extremely high fees. This raised questions about the capability and efficiency of the MALR laboratories and research units, and their role in advancing technology and introducing new varieties of agricultural inputs.

In addition to what is mentioned above, there is the case of the PBDAC. Its effectiveness and even the effectiveness of different kinds of support it received from outside was under question. The effectiveness of its project for Agriculture modernity, which was backed by IDA concessionary loan, was questioned. The project failed to achieve one of its main objectives: to help farmers and small investors. This was due to lack of experience, of flexibility and of efficiency among its employees. They showed a lack of efficiency in allocating the project loans by asking for unreasonable collateral aiming at reducing their risks, thus crowding out useful investment. The PBDAC failed to deal either as a developmental bank or as a commercial bank, as the USAID support project intended. It failed to reach farmers and young investors and it failed at the same time to attract appropriate deposits or to provide flexibility such as commercial banks. As for the PBDAC, the efficiency of the affiliated agency for its development, USAID, was under question as well. The question of conflicting goals between the agency and government officials was to be considered too.

Lack of co-ordination between different ministries and the lack of a long-term strategy were revealed by the emergence of and the dealing with the fertiliser problem. The fertiliser crisis revealed a failure of the government to prevent the problem of fertiliser shortage to turn into crisis. It failed as well in the first test of

the free markets. Dealing with the crisis reflected a slow response and lack of experience. The state failed to cooperate together with the private sector and to find indirect ways of regulating the market.

Solutions introduced by government were short-term, and long-term solutions were not on the agenda. While the prohibition of export and import of fertilisers solved the crisis in the short-term, no extra concessions were given to encourage private sector participation in the production of fertilisers. Increasing the production capacity of commodities for high and expanding, internal and external demand should have been given the first priority.

The government's ability to undertake its task in the free market economy was under question. It failed to regulate the market and to envisage its role in the free market economy. Different types of monopoly and oligopoly were complained about, while investors were happy to dispose of the government monopoly in some areas, complaints were directed to merchants in the private sector. There were three major market crises in cotton, sugar, and fertilisers.

### ***State Role and Private Sector failure***

The role of the state from the private sector point of view reflected' to a large extent, private sector failure to deal with certain problems or even to run some parts of their business. Whenever the private sector failed it called for government intervention.

One major failure of the private sector was in marketing, either in the internal or external markets. Producers of agricultural inputs (seeds and fertilisers) either failed to gain far-reaching marketing points and/or suffered from non-obliged private distributors and merchants. They suffered as well from unfair competition from cheating producers, who provided poor products. The complaints about the commercial cheating of other producers was not restricted to producers of seeds and fertilisers, producers of irrigation systems parts were the main perpetrators. They complained about other producers using recycled bad-quality materials and then competing with low prices. The difference between the two products could not be distinguished easily before use. One of the businessmen had to stop manufacturing and only work as a trader because of the loss to his business. In all these problems they seek government intervention and the chance to enjoy the benefits of the empty warehouses of the PBDAC and they asked for the PBDAC to return to distributing



agricultural materials provided it did not interfere with prices. Others requested a law for regulating the market and prohibiting monopolies.

In the external markets, investors' views about the encouraging of exports showed a great dependence on the government. Many investors asked the government to provide specialised companies for exportation. These companies, according to them, should have a real role in marketing to foreign countries, in addition to providing information about foreign markets. Others found it the responsibility of the government to provide high-quality commodities for exportation, forgetting that it is the role of private producers to improve production and provide competitive goods. Another individual considered the government responsible for providing information about new technologies to be able to compete in the free trade era.

These views of the private sector concerning the role of the state are the legacy of an old economic policy where the government used to play the role of producer, distributor, and regulator of the market. If we review the three areas of intervention requested by the private sector, dealing in the local markets, dealing in the external markets and market monitoring, we find that the first two jobs are not usually adopted by governments in free market economies. However, if we look at the case of the PBDAC, the available slack capacity of warehouses and the huge number of workers which the bank cannot dismiss, it might be reasonable for it to play some role in introducing these new products to remote areas. The bank could encourage and finance the setting up of a private marketing company. This private company should encompass members mainly of producers to prevent merchant monopoly. The loan could be conditional on the company rent or the buying of the bank warehouses and hire percentage of the manpower which the bank could not get rid of it.

### ***State policy transparency and private sector participation in the decision-making process***

Although private sector participation in the decision-making process has increased recently, it seems that agribusiness participation is not at the same level as with other business. Recently it became normal to hear about meetings between businessmen and high officials of the government, beginning from the prime minister, economic,

finance, and supply ministers and so on. Businessmen representatives accompany official delegations or even arrive first, especially in the case of the USA. But it also became usual to hear the word of 'big' used of businessmen when referring to the type of businessmen who were able to attend meetings or join the delegation. In this respect only the name of a few businessmen's associations were mentioned. At their head is The Egyptian Businessmen's Association, The Egyptian American Council, The American Chamber of Commerce, and to a less extent the Alexandria Businessmen's Association. The importance of these associations derived from their autonomy from the government as they relied on self-finance, and from the members it embraced as most of them were previous ministers and big businessmen so they did not lack power or connections inside the government, as in the case of the first mentioned association or from its links with the USA. Although most in our sample were members in Businessmen's Associations, they were small specialised associations compared with these mentioned earlier. And although they stated that the most important activity of these associations was to negotiate with the government concerning economic policy, they seemed to lack much important information concerning that very policy. They were ignorant about the meaning of the SAP or economic reform as it was known in Egypt, about the GATT and its effect on their business and about obstacles to signing new partnership agreement with the EC and the subsequent effects on their activity. They were also short of information about available funds, as we saw in the case of the PBDAC fund, and about the new measures taken by the new government. These referred to a great weakness in the relationship between their associations and the government. It seems that they were absent from the discussions on major economic policies and their associations were only concerned with minor problems related to their activities. Representative of these small specialised associations were not integrated into the policy-making process in a proper way. The members themselves find their associations of limited effectiveness. Finally we should mention that this dearth of basic information about economic policy, while reflecting a lack of transparency in government policy, also reflects, at the same time, the nature of Egyptian investors and their limited interest in their restricted areas of activity and their lack of a broad view of the economy and its dynamics.

### ***The Private Sector and the Development Effort***

In the following section the study assesses the capability of the agribusiness private sector to enforce development. The study only provides qualitative clues which together with official statistics can clarify the following issues:

#### **Awareness of needed reforms**

Investors in the agribusiness showed little awareness of the needs of the economy. One third of our sample did not have any view concerning the essential reforms needed for the Egyptian economy to accelerate development and increase the welfare of the people. This reflected either a negative attitude towards participating in reform efforts, even with opinions, or an unawareness of the needs of the economy and the society.

The need for a clear, stable economic policy and system came as the first requirement. However, it was recognised by only 16.7 percent of them. The removal of bureaucratic obstacles and the facilitation of measures for introducing new projects and to own land was the second request of 13.9 percent of investors. 8.3% of investors asked for free markets and for an end to the government monopoly and for the treatment of the private sector on an equal basis with the public sector. While we note that some investors referred to important issues, their views were limited to direct problems, which they mentioned before. Only a few raised the national issues needed to advance the reform. Only two referred to democracy as an important need. The same number alluded to the importance of cultural elements to create an awareness of the reform and to create an acceptable image for good investors. Another investor said that they should be treated with respect and not like thieves. Only one person mentioned the need to reform the educational system and to improve vocational training. Only one cited the problem of terrorism and only one who asked the government to encourage young investors, because he was young himself. So only a few investors obtained a comprehensive view of the reform and realised that it should be combined with cultural and political aspects. The main concern was directed towards issues with a direct impact on their activities.

#### **The Private sector's awareness of the agricultural sector's need for reforms**

Investors in the private agribusiness sector reflected a greater awareness of what the agricultural sector needed in terms of general reform than in terms of national reform. Only six, 16.7 percent, gave no answer, compared with twelve in the

previous case. Land reclamation was at the top of their interests, as 27.8 percent gave it as their concern. The issues they discussed varied and covered different aspects of the situation. They asked for land reclamation to be facilitated by ease of access to land and by providing an infrastructure and needed inputs. Some asked for reduced custom dues for reclamation machinery, others for regulations to halt speculation on reclaimed land and to assure the seriousness of the investors. The following concern was directed to inputs. A quarter of investors raised the issues of input availability, quality and prices. They were worried about the availability of good-quality seeds, fertilisers, and pesticides, yet more concern was directed to seeds. One encouraged the use of plant-growth regulators instead of traditional fertilisers, other asked for more facilities to register bio-products. As for prices, the high price of machinery was their main anxiety as they asked for subsidies and reduced excise duties especially for machinery for reclamation.

Agriculture extension and technology, and exportation were the next areas of a concern, with the attention of 19.4 percent of investors for the two of them. Investors asked for an active role in agricultural extension. To achieve this, extension workers' conditions and quality would have to be improved. Paralleled to this, more attention should be directed to R&D and its applications. For exportation, investors asked for a specialised authority or company in external marketing. They considered this the responsibility of government. They also asked for the encouraging of non-traditional crops for exportation, in addition to the regulation of the cultivation of crops for exportation.

† 13.9 percent of investors requested more effort in selling to the domestic market and asked for marketing companies. Some of them thought it the responsibility of the government. One asked for a private marketing company. Other concerns were directed to providing credits and reducing the interest rate, increasing the capacity of Egyptian ports and finding new sources of irrigation.

Investors showed considerable awareness of agricultural sector's needs. They were able to identify one of the main constraints on the agricultural sector, which was the limited cultivated area. However, they failed to identify the second major curb which was water availability; only one of them mentioned it. Another major check, not only on agriculture but on other industries as well, was the low capacity of Egyptian

ports. This problem has a great impact as it affects the cost and the quality of products in addition to its effect on market clearing. The issues they raised were essential to the agricultural sector's development and competitiveness. Nevertheless they still thought that most of these reforms were the responsibility of the government. Expressions like 'sincerity' and 'commitment' were not mentioned here as they were used before when they were directed to the government. One said that youth should exert more effort to increase production. Nothing at all was said about encouraging young investors or providing more facilities and credit to achieve better participation.

### **Improving technologies**

With the high percentage of University professors in the sample, one would expect considerable concern about introducing new technologies and following new developments in this area, which is growing fast in the agricultural sector. When businessmen were asked about investing in R&D, we discovered that seven members, 19.4 percent, of the sample did not invest in R&D at all. Most of the others invested in more than one way. More than a third consulted the government research unit. This percentage was high because they were obliged to do this. Every new input product, seeds, fertilisers and pesticides, introduced onto the market had to be examined in the MALR laboratories. This was the process which investors complained about, especially its high fees and the long time that it took to obtain final MALR approval. Seven persons, 19.4 percent of the sample, had their own R&D departments, while two did their own independent experiments. Six, 16.7 percent, consulted private sector research units. 44.1 percent used specialised magazines to improve their knowledge. 36.1 percent travelled abroad to be learn about new developments. 22.2 percent sought the help of foreign experts. Only one attended domestic and international exhibitions. This percentage is much higher, at least at the domestic level, as more than one exhibition was organised during the field work period. They probably regarded it as a marketing event and did not realise that it was a form of investment in the development of the company's products especially when there were foreign companies participating and offering different type of technologies.

The private sector played a vital role in developing the use of technology in agriculture. It was able to introduce new bio-plantation technologies as early as

1979. Activities for producing bio-fertilisers and pesticides were in operation as well. The efforts they were making were quite good if we consider the relatively recent involvement of the private sector. In this respect, thanks were due to technocrats, university professors and PhD holders. Other studies referred to the increasing contribution to agricultural research of the private sector, particularly in relation to seeds, tissue culture and agro-chemicals (Gomaa, 1995:3). However, knowledge of changes in the international market seemed to be beyond their reach. As we observed in their discussions concerning trade liberalisation, they lacked an awareness of the GATT effect on technological transfer, concerning bio-technology, which meant that they had to exert greater efforts of their own to develop an adequate technology.

#### **Awareness of environmental dimensions**

Does the pattern of investors' use of resources enhance their sustainability and protect the environment? When investors were asked about the effects of their operation on the environment and how they managed to remedy the negative effects, they showed little concern about the environment, as more than one third gave no answer. Approximately one third thought that their activities had no effect on the environment. Nearly half of them gave an explanation for this belief, as two mentioned that they regulated their production and followed quality-control instructions. One stated that he provided green areas and rationalised the use of water, another created public awareness of the better use and handling of chemicals through his active membership of the EAAPA, and a third said that he travelled abroad for exhibitions. Two asserted that their activity could have a bad effect. However, there was no alternative, from their point of view, to the use of chemicals in agriculture and they asked the government to provide alternatives through research.

A few were even more aware, since two said that they tried to limit their adverse effect, one by reducing the amount of chemical fertilisers and pesticides, the other claimed that he did not deposit petroleum waste in drainage pipes. The same number insisted that they produced no negative effect and one of them explained that he invested the waste from his poultry project in land reclamation. One admitted that in the long run the accumulation of plastic pipes for irrigation could have a bad outcome. Only four maintained that their activity had a good effect on the

environment. One of them gave no explanation; another declared that his business involved the planting of trees and plants in streets and gardens. A third asserted that he reduced the use of chemicals, while the last one explained that his manufacture of balanced growth-regulators helped plants resist diseases so there was no need to use chemicals.

### **Competitiveness in the foreign markets**

We noticed that more investors were involved in importation (69.4 percent) than in exportation (61.1 percent), and that about 52.8 percent were involved in both. This means that the advantage they gain by exportation is more than offset by importation. If we consider the type of imported and exported goods, we notice that only a half of exporters export their own products, and 9.1 percent partly produce them. These exporters relied on imported goods like water treatment units, agro-chemicals and agricultural machinery or its components. Most imports were inputs, spare parts or goods to re-export, and final consumer goods. Fruit imports ranked low, while exports of fruit and vegetables ranked first. This partly explains the continuing deficit in the balance of payments, in spite of the notable increase in agricultural exports, as most of the used inputs, raw materials, and spare-parts used were imported.

### **Job creation**

One of the main challenges facing the private sector in Egypt is that of creating new jobs for growing number in the new labour force which enters the labour market every year. Estimations of new jobs needed is about 500 thousand per year. Large capital<sup>†</sup> was the characteristic of most companies in the agribusiness sector. This was because of the nature of some activities like land-reclamation and industries like; agro-chemicals, agro-machinery and food. Some of these enterprises relied on new technologies which needed a large amount of capital. The good aspect about large capital was its ability to spend on R&D and to adopt advanced technologies.

However, its ability to create jobs was low especially if we consider permanent jobs. Its competence in creating temporary jobs were better. As for permanent jobs, we found out that the Capital/Labour Ratio was £E. 51.1 thousand. This is much higher than the average for the country as a whole which is 27.8 thousand, and higher than the ratio of industries in the Tenth of Ramadan city which was 31.8 thousand (Fawzi, 1994:77). This was due to the reliance on temporary

labour in the productive activity. If we take into account temporary labour the ratio is lower.

Their skill in providing trained labour was poor as well. An executive in the agrochemical industry maintained that he did not need trained labour at all. All he asked his workers to do was to mix things together. It is not in his interest for them to know because he wanted to protect his product.

Only one company complained about lack of trained labour, which is one of the main problems in Egyptian industry, and he claimed that he trained the labour within his company. He asked the government to pay more attention to vocational training.

The problem of the availability of skilled workers or the quality of the labour force was not on the agenda for the agribusinessmen. Only one referred to it, as we stated earlier, although it was a pressing problem. There were many explanations for this. Either they did not need trained labour, as one investor mentioned earlier, or they paid little attention to quality aspects.

#### ***Changes in state capacity and the state role and their effects on state-business relations***

The private sector showed the need for effective role for the state. While the private sector showed weaknesses concerning its autonomy, the state showed a weakness in the performance of its role in the market economy. If we look at changes in state capacity during the reform path, we cannot see any notable changes in the 4 areas of institutional, technical, administrative and political capacity as determined by Grindle (Grindle, 1996:8). The state failed to provide the effective legal infrastructure for the market economy where laws to prevent monopoly and commercial cheating were delayed. The state also showed little effectiveness in applying the available laws, as in the case of the environment law. Investors considered the state with little effectiveness concerning the protecting of the environment.

At the administrative level there was limited progress with regard to facilitating administrative measures. The problem of an over-staffed bureaucracy which is one of the main causes of the embedded routine procedures and the power conflict between the different authorities can hardly be dealt with. In this respect we find that two related indirect measures were taken. The first was to stop new



recruitment in the bureaucratic administrative staff, and rely on early retirement to gradually reduce the excess labour-force. This was, of course, a time-consuming strategy and not very effective. It could not cope with the necessary pace of reform. Another solution of direct cuts in the labour-force was considered to be politically costly. However, triggering the reform was able to provide another solution for the government which was private-sector absorption of government bureaucrats, either through their direct involvement in private-sector activities, (some might prefer to keep their jobs to benefit from their position), or through better recruitment opportunities available in the private sector.

The second method was to reorganise the ministries so as to restructure the administration while reducing the labour-force. The last reshuffling of the government at the beginning of 1996 tried to overcome this problem by reorganising and regrouping some ministries. This reorganisation or regrouping of the function of different ministries was welcomed by commentators and academics. The first of three main changes was the merging of foreign trade with the ministry of supply to ensure complete control or regulation of the availability of goods in the local market. International Co-operation was joined to the Ministry of Economics. Both Foreign Trade and International Co-operation were handicapped by a conflict between various ministries, such as; the Ministry of Planning and the Ministry of Economics. The Ministry of International Co-operation was claimed by that of Foreign Affairs but never came under its control. The third merger was between the Ministries of Agriculture and Land Reclamation. Although they were under the supervision of the same minister for a while, they were formerly two different ministries at the administrative level. In the past, the Ministry of Land Reclamation used to be subject to claims and under the supervision of other ministries, such as the Ministry of Housing and Construction. The claiming of jurisdiction was one of the main reasons for the unstable and conflicting policies, laws and regulations.

The reorganisation of the ministries was meant to achieve better stability and co-ordination in the decision-making process. It was also meant to restructure the over-staffed bureaucracy in such a way as to facilitate administrative measures and to provide greater smoothness in the decision-making process. In agriculture there were four ministries with direct responsibility for agricultural production. These were the Ministries of Agriculture, Land Reclamation, Public Works and Water

Resources, and Construction and the New Communities. There were four other ministries related to agricultural products. These were the Ministries of Supply, Economics and Foreign Trade, Planning, and Finance, in addition to the other ministries, which were responsible for providing the necessary services (Gouili, 1992). Under each ministry there were groups of authorities which were set up with different names; apparatus, centre or authority, each of them was over-staffed. One study revealed the administrative fragmentation and the weak ties between the different authorities responsible for planning and implementing agriculture policy. However, co-ordination between ministries on issues of policy-making was easier than that concerned the authorities and the division of power. While co-operation was possible in the first case through the Ministry of Planning, the Cabinet and then the People's Assembly. The horizontal ties between different authorities in the ministries involved was not enough to frame sound policy at programme level. The study linked this to four reasons; a-Sharing authorisation and co-ordination with their counterparts in other ministries, b-The surplus manpower which made each authority a semi-independent authority did not welcome interference, c-The duplication of authorities working in the same area of concern or in the same geographic area, which made duplication very difficult, d-The unsuitable criteria for evaluating performance. The main criterion used was how much was spent on investment regardless of its effectiveness or efficiency (*ibid.*).

One of the main requests of our sample was the merging of authorities that to be dealt with. One of the sample complained that for two years since he started his business he was unable to obtain final registration of land for his project. He was told secure the permission of different authorities and the last was the general authority for archaeology. The question is, if it was an industrial area and the investors were encouraged to locate their projects there, why did not the Ministry of New Communities arrange and co-ordinate with the various ministries and authorities involved and produce the necessary permission for the whole area and then allocate it to the investors? Why did it leave it to the individual efforts of the investors? Why did it invite them to invest in an area that might be of archaeological interest? It is not clear.

In the question of the fertiliser crisis, one of the main reasons for the crisis was the lack of co-ordination between the different elements responsible for

production and distribution. There were no indications in the answers of the sample members for improvements in performance of the Ministry of Agriculture in particular, as it was the subject of many complaints.

As for institutional capacity, which means 'the ability of the state to set and enforce the broad sets of rules governing economic and political interactions' (Grindle 1996:9), we could not detect any substantial improvement in its institutional capacity during the SAP. Many important laws were delayed such as the united law of investment; laws to regulate the market, to prevent a market monopoly and to protect consumers. The government's competence in collecting taxes did not improve. Any increase in revenues was related to fresh imposition of indirect taxes, fees, and stamps, while the efficiency of the tax authority to follow those who did not pay did not improve either. The judicial authority experienced greater independence. While this could imply respect for the law, it had a negative effect on the state's prestigious position with the public. The abolition of many state decrees, laws and election results revealed a weakness in state power, as discussed in chapter four. However, this independence of the judicial authority seems to be subject of many encroachments recently.

As regards technical capacity, defined here as the ability to manage macroeconomic policy and analyse economic policy options more generally (Grindle, 1996:9), on the subject of agricultural policy in particular, as a part of macroeconomic policy, it was successful in promoting policies to increase agricultural production. yet, it failed to improve the situation of the poor or even to help them maintain their relative position. This goal was not included in the ends of the set of policies related to reform, especially for the rural poor, the SFD programme was more concerned with the unemployed graduates of universities, and this was left as a long-term remedy.

It is difficult to examine the changes in the other part of the relationship between the state and business, and the relative strength of agribusiness power, or influence on the policy-making process. Indeed definitions of power are problematic but we can offer some criteria or approximations. The following criteria might give some indication; the quality or main characteristics of investors in general, investors' previous and present links with the bureaucratic system and government officials,

and/or the amount of political power they enjoy due to their links with the ruling party.

The investors in our sample referred to consultation with the government concerning its policies as one of the tasks that their organisations were involved in. They, nevertheless, thought that their influence was limited. Our study suggests that the only clear situation where investors practised some limited leverage on the government was in the fertiliser crisis and the fight to recover the right to distribute fertilisers.

The GOE might review the investment laws and regulations and try to improve and simplify the performance of its officials. One empowered investor who was a member of the Egyptian Businessmen's Association and had open channels and connections with some ministers and senior officials complained about red tape and claimed that about 90 percent of his time was devoted to solving administrative problems with government officials. He believed that high-level officials like the President and the Ministers had good intentions and worked hard to iron out any difficulties for investors. However, when he solved one problem there was another waiting. He said that he could not call on the minister at every step in his work and in his analysis of the characters of those officials at the lower levels or the executives of the investment laws and regulations. He believed that they enjoyed using their power and they resisted any transfer of power out of their hands. This meant that his connections were sometimes useless or not empowered to help in overcoming certain problems. So it seems that it was a kind of power struggle between the two groups and the investor should be convinced in the end that government officials were more powerful than he. The message was "we have more power, and you can not beat us". All the above poses the question of whether it is possible to have a real improvement in state performance and to get rid of the bureaucracy. Can reducing the overstuffed bureaucrats solve the problem? Does it mean that if power is distributed among less people it means more for those working? or the problem is different and you have to create a new mentality and new attitudes. Cutting the number of bureaucrats at least means that monitoring their activities might be easier. The weakness of the state affected private sector performance. The state showed weak capacity not only with regard to providing the needed legal framework but also concurring its administrative and political capacity. In turn it does not help this

sector to extend its power relative to the state. Sadowski refers to the private sector's need for a strong state. At present time, many examples can be found of the important functions of the state, without which the private sector can not survive. Markets are not self-regulators or have invisible hands, as Adam Smith claimed. Markets require a vast institutional underpinning. Without courts to interpret and enforce agreements, for example, commercial life would be chaotic. Without laws to define, and police to enforce them, property rights would be non-existent (Wilson, 1990:4). The government should act as a mediator between business and labour in order to promote consensus on the measures needed to achieve growth, including measures that regulate their relations. Modern industries need better trained or educated labour-force; the state can provide them by improving education and training (*ibid*,: 3-4).

### **7.5 . Conclusions**

The reform was unable to create a strong feeling of credibility among investors, at the same time it was not faced by a great deal of opposition. Half the investors found it useful, while most of the other half refrained from giving an opinion. Investors who found the reforms useful joined the others in their complaints or comment about some aspects of economic policy and about the performance of the state. They received announcements about new reform measures with some suspicion and followed the "wait-and-see" model. Although they were optimistic about future demand and were excited concerning the expansion of their businesses in the future, this was related more to the trend effect, an increase in population or to their own effort to improve the quality of products or open new markets. They were too politically inactive to form a strong support base. The gains achieved from the economic reform could not change the attitude of political indifference which was part of Egyptian culture, because of a variety of historical and contemporary reasons. This was because the gains were relatively limited due to an incomplete and sometimes inconsistent liberalisation policy that created low levels of credibility. The absence of real democratic life was one of the reasons for the low participation rate of investors. Investors showed interest in developing democratisation process and believed in its ability to enhance economic reform, although one of them felt worried about losing his gains in case "real democracy" was applied. This investor

saw private entrepreneurs as the only beneficiaries of reforms. His view confirms the idea that democracy could contribute to a more equal distribution of the benefits.

The study revealed the need for a strong capable state for the market to operate efficiently. Private investors did not show an independent ability to increase and develop and prosper their activity without relying on state regulations and facilities. The rolling back of the Egyptian government was supposed to improve its performance and capacity in other arenas. This was the promise of the World Bank that the government should concentrate on tasks it could perform effectively to have a chance to improve its potential, then to be able to expand its tasks. This did not happen in the Egyptian case as, while the government withdrew from different activities, it was unable to develop its competence in others. This was the case of the PBDAC and the MALR, as they were subject to many critics for their poor performance. That was also the case for the government as a whole, where it failed to provide the legal infrastructure to protect investors against monopolies and to protect their property rights.

Agribusiness investors proved that they were politically weak and could not lobby or influence government decisions. Investors showed a poor ability to organise. Their organisations were fragmented and lacked effectiveness. They lacked interest in political participation, however they could be persuaded to, if the government became more credible and more democratisation was allowed.

In conclusion, the state could not expand its capacity during the reform and could not change from a “soft” to a “strong” state. At the same time, the agribusiness sector could not increase its economic or political power to challenge the state. Private agribusiness realised its need for the state. In fact it needed a strong state to protect it from other uncommitted private actors. Investors showed little ability to influence the economic policy, and their organisations remained ineffective and fragmented. They could not change the balance of power from the government to their favour.

My case study has helped to emphasise themes about the risks involved in free markets and the anticipated role of the state. It also helped correct some wrong conclusions about the increasing influence of businessmen. The study stressed that businessmen were not a homogeneous group and that it is only the well-connected

elite was able to enjoy the benefits of reform. Nevertheless they even enjoy limited political influence.

## Chapter 8 Conclusion

This thesis has critically examined the changing nature of the agricultural sector in Egypt during the period of economic reform. It has particularly focused on the position of agribusiness within that sector and situated this discussion within a small survey of agricultural investors. In many respects this thesis confirms much of the experience undergone throughout Africa and the Near East. The thesis has also contributed to assembling new material for the Egyptian case.

The experience of developing countries with structural adjustment has shown an uneven outcome. African countries which were the most affected with the crisis of the late 1970s and early 1980s performed badly under adjustment programmes. Their performance during the crisis was affected by the nature of their economies with low diversification levels of economic activity and single commodity exports. The poor performance during adjustment was often related to the social and political structures, the political systems and the weak administrative and technical capabilities of the state. The experience of African countries was the main impetus that directed the IFIs' concern to the issue of good governance and its linkage to economic reform. The poor performance of adjusting economies led to a negative distributional impact of the economic reform and the need for social safety nets to protect the poor. It also led to greater consideration for long-term growth and the environment. Both the IMF and the World Bank have tried to integrate such issues into their programmes although the effectiveness is still debatable.

The World Bank has nevertheless managed to develop its views concerning one of the most debatable issues of liberalisation and that is the role of the state in economic activity. While neo-liberal thought was in favour of a minimal role for the state and saw the state as the cause of the economic crisis and decline, the implementation of the programme revealed the need for an effective and capable state to carry out the reforms. The World Bank realised that it was not the size of the state that matters but rather its capacity and effectiveness. This issue was recognised by Egyptian academics and formed part of their views concerning the role of the state. Egyptian commentators also realised the importance of an effective role for the state in the process of long-term development, which reliance solely on market



forces failed to consider. Among the issues of importance here are the need to provide a legal and regulatory framework for market forces to work; the need to support and encourage technological change and innovation; and the need for a sound industrial policy. This realisation stemmed from the recognition to the increasing gap between the developing and the developed countries and the importance of the necessary 'catching up process'.

Experience with Egypt's economic reform since 1991 has revealed little success for the GOE in enhancing its capacity and effectiveness or in providing an appropriate institutional framework for market forces to work. Administrative obstacles have remained, as this thesis has demonstrated. The necessary legal and regulatory framework remains weak and incomplete and the GOE has failed to provide a law against monopoly or a unified law to regulate private sector activities. The new investment incentive law is fragile with little claim of legitimacy constitutionality. The technical capacity to manage the privatisation programme has also been limited. This has been reflected in difficulties regarding privatisation relating to the scale of sale and questions about pricing and conditions of sale. The pricing of shares in the stock market and the regulation of the stock market is subject to frequent fluctuations.

The GOE has confronted criticism of adjustment very strongly. It has used the police force, when dealing with labour demonstrations, and they imposed new restrictive legislation and regulations limiting the ability of civil society to participate in decision-making.

There has also emerged a consensus on the need for political reform to complement and support economic reform. While academics and political parties have different views concerning the needed economic reforms they all agreed on the need for political reform; to respect human rights; to encourage an active role for civil society and to expand the space for democratisation. The argument in favour of an active role for society and more political liberalisation in order to sustain economic reforms was based on many reasons.

In the long-term the distribution of gains and losses is likely to lead to a redistribution of power among the different groups. The balance of power between the state and different socio-economic groups is another aspects to consider in managing the reform. In order to maintain the balance of power in Egyptian society,

it is important that the amount of power abandoned by the government should not to be given to one group, such as Business Associations, for instance. It should rather be distributed among a wider range of groups. This also raises the issue of democratisation and the need for a vibrant civil society to check state power in order to defend the interests especially of different vulnerable groups.

The government, under a state-led growth model used to replace or to limit public preferences of goods and services by controlling the availability, the quality and the prices of such goods and services. The public were then more willing to accept it as they traded their preferences for subsidies. In a free market economy while prices are supposedly determined by market forces, the public have the right to set their preferences and protect them through wider political and economic participation. Although the economically stronger groups also tend to be the most powerful politically.

Democratisation is also needed to monitor and enhance state performance, where the state failed to reform itself concerning some aspects of corruption, cronyism and prevailing patronage. In this respect there was a need to encourage public participation in Egypt, which has been very weak among different strata, and to change the culture of silence which grew for generations because of the practice of coercive power which reduced confidence in the state. There is also a need to raise patriotic feelings to encourage people to participate politically. While Nasser did this artificially through ideology it is now needed through a national project unifying peoples' efforts. There remains the situation of a lack of national projects and the continuing deliberalisation process that limits the opportunity to participate and reduces the available channels to express free opinion, so there is greater likelihood of the emergence of extremist views and practices.

In the economic arena, what is needed to build sustainable growth is productive investment. Investment that enhanced the productive capacity of the country as the high rates of growth of the 1970s proved fragile because these were achieved through the services sectors. A recent World Bank Report (1997) revealed that the increase in the productive assets of the Egyptian economy was zero during the 1990s if resource depletion is also calculated. The fact that oil reserves, one of the main sources of foreign currency, may to be depleted within fifteen years, which seems to be forgotten or ignored, shows the size of the challenge facing the Egyptian

economy, which looks immense. There is an urgent need to expand the productive capacity of the country, especially with its growing population. The privatisation programme is unlikely to contribute seriously to investment and growth. Such investment should also be able to create high employment opportunities to reduce the problem of unemployment.

None of Egypt's main challenges has yet been faced. Unemployment and poverty continue to be high and little has been achieved to improve the quality of human resources. The gap in science and technology with developed countries is widening. Stabilisation and restoring internal and external balances, albeit still fragile with increasing internal debt and unstable export performance, is not useful to the real economy. In such a case one would not dare to call for a minimal role for the state, waiting for private initiative to slowly revive. There is a role for the state to encourage domestic savings and to provide appropriate channels through which such savings are directed to productive activities. This could be mainly through providing the appropriate legal and regulatory framework, creating differentiated incentives to direct investments towards the targeted activities and by increasing credibility in its policies through stability, consistency, transparency and accountability. Political stability, democratic practices and availability of equal opportunities are also important elements for building credibility. The GOE needs to increase credibility in its capabilities and to improve the administrative performance of its apparatus. It is too late to be told, after eight years or more of reform efforts, that the IMF would provide technical assistance to improve the technical abilities of the Egyptian executive to carry out the reform programme.

Economic reform in the agricultural sector, which has focused on price reform, resulted in some improvement at sector level by increasing production. These increases did not meet targets. Expansion in the production of wheat, cotton and horticulture were targeted. Yet, only wheat has managed to expand together with cereal crops. Free market mechanisms were used by farmers to improve the production of self-provisioning crops rather than reviving the internal and external markets. This was due to the low living standards in rural areas and where the market economy seemed to threaten farmers' access to food in the markets.

The growth achieved in Egypt's agricultural sector has not been sustained nor equitably distributed. Focusing on price reform in the agricultural sector created

gains from the 'once for all' format. Even these gains were not fairly distributed between farmers. Big farmers were more likely to gain while very small farmers and the landless were likely to lose. Institutional reforms in that sector seem to have lagged behind. Cooperatives have been neglected and rendered jobless. Their role in extension work is nearly absent. After the complete withdrawal of the PBDAC, merchants seem to be the only source of information about new varieties of inputs and prices and are more likely to adopt monopoly prices. Cooperatives seem more suitable to take initiatives to provide farmers with information and know-how. The absence of the PBDAC is more likely to create asymmetric information where big farmers have better access to the market, market information, technology and to have better chances to bargain for better prices for their inputs and products.

Other conditions for sustaining growth in rural areas also seem to be absent. For long-term development a number of issues need to be considered. These are environmental dimensions; the issue of increasing investment and improving its efficiency; technological progress; and political participation. Rural areas have been marginalised from political participation at the national level. Farmers seats in the People's Assembly are only cosmetic and have lacked effective influence over the decision-making process, and they fail to eliminate the bias against farmers in crop pricing and availability of services. Big landlords who won the seats benefited personally and have used parliamentary membership to consolidate their power in their villages. At the local level they also dominate cooperatives and local councils. However, farmers representation in the People's Assembly is threatened to be eliminated or marginalised during the "liberal" transformation. As a result, rural civil organisations need to be initiated and consolidated in order to enhance the political weight of a historically neglected sector. Because small farmers with less than five feddan are the majority of farmers in Egypt and because the five feddan represents the frontier for poverty, these groups have to be fairly represented in any association or public organisation.

Investment is the other source for maintaining high production rates. Increasing poverty in rural areas reduces the farmers' ability to invest in maintaining their resources. Public investment is also low and little is directed to maintain the old agricultural land which is the main source of agricultural production. It seems that a high proportion of agricultural investment is directed to the projects of

horizontal expansion especially in the southern part of Egypt like Toshka where the outcome is uncertain. There is a great need to balance the allocation of resources between the old and new lands. The encouragement to apply new technologies across all categories of land holders is also needed but so too is adequate and flexible extension services.

Due to the competing uses of public investment in agriculture and because of the new policy of encouraging private sector initiatives, the agribusiness sector has been assigned an increased role. The field work study conducted on this sector exposed its limited competence and emphasised its need for a strong state to improve its effectiveness. The sector's response after the SAP was weak in terms of the number of companies, their size and the type of activities chosen. The majority of them were working in input trading. The main market entry barriers were a lack of finance, administrative obstacles, and market monopoly by some private units. The PBDAC seemed an irrelevant source of finance for most of them. It was not able to improve its performance in attracting more clients and was accused by investors of cronyism and favouritism, in addition to providing a lack of technical capabilities. The credibility of its staff is low. The PBDAC's policy to provide credit seemed biased towards big companies because of its credit policy which was based on the holding of collateral. It performed as a governmental bank which aimed to reduce its risks to a minimum not through project appraisal criteria but by depending on customers' asset holdings.

Because privatisation was a result of fiscal crisis, it was taken as a goal not a means to improve efficiency and productivity. However, it does not provide a sustainable source for public finance. Equity issues have been neglected in selecting such sources. As financial incentives for investment proved ineffective, a shift from financial incentives to policy incentives is likely to be more rewarding. Incentives should be differentiated and target oriented to specific activities. It would also encourage environment-friendly projects. For agribusiness incentives could be by providing low cost credit as finance proved to be one of the main barriers to entry in the reform era, or in form of support services and legislation. By low cost finance I mean not only low interest-rate, but also easy procedures and lending conditions. PBDAC seemed to have no clear priorities for lending to agribusiness apart from low interest rate for land reclamation. However, this type of lending was not tested

in our sample as none of it enjoyed such credit. Food security projects, such as poultry and its complementary industries and services, need greater concern. Incentives to improve technology in the area of providing environmentally safe agricultural inputs is most recommended. Industries providing non-chemical inputs, bio-fertilisers, should be encouraged to expand by providing every necessary support. Some of them suffer problems to access final consumers- farmers- in this respect the PBDAC distributing points might be of great help. The absence of an effective legal framework was another impediment to agricultural investment. Illegal practices of some private investors in the form of commercial cheating and oligopolistic practices crowded out real entrepreneurs. Appropriate legislation and its effective implementation are necessary conditions for sustaining investment revival.

Investors in the agribusiness sector seemed to lack concern about macroeconomic issues as they were short of information about some economic policies and measures, had no clear vision about the dynamics of the economy and showed a low ability to participate in the decision-making process. Their views and policies towards the expansion of their activities were built on their experience in the market in its narrow sense, where changes at the national and international level were not fully considered. Some of them lacked awareness about the effects of the GATT and free international trade on their activities. Exports were mainly directed to Arab countries, followed by European countries and they were likely to face increasing competition even in the Arab countries' markets. The failure to include agricultural products in the partnership agreement with the European Union in the late 1990s did not seem to bother them. In general they were optimistic about the future demand in the local markets and external markets as well. This optimism was built mostly on the effect of trend and an increase in the population. Those who produced for the local market were not aware that free international trade could create more competition with imported goods. There was also the opposite situation, where local market absorption could depress exports. One producer of new irrigation systems was satisfied that his products were absorbed by the domestic markets thus reducing his exports. Fertilisers also showed a high external demand. While shortages of fertilisers threatened agricultural production, such industries did not receive any favourable incentives to increase local production in order to satisfy the local market and retain the external market which was difficult to restore if lost.

Agribusiness investors showed moderate belief in the reform programme with little inclination to oppose it openly. The reform succeeded in solving part of their problems especially the monopoly of the public sector in input trading, however some of these monopolies remained. Investors suffered from the imposition of the new general sales tax which affected large companies more than small ones and which caused them difficulties in refunding. Administrative constraints remained especially concerning import and export measures and the MALR services.

The political participation of investors in this sector was very low. And while they showed some ability to organise, their organisations were weak and ineffective. They did not support the view that businessmen in Egypt were gaining more power and influence over the decision-making process. They could not be considered as an active coalition of beneficiaries or as an opposition or lobbying group. Their political weakness stemmed from their lack of interest in political participation and from weak and fragmented, sometimes competing, organisations. However, few of them showed political ambition by joining the ruling party and by nominating themselves in the People's Assembly elections. And in spite of their political indifference they were in favour of democracy and asked for more political liberalisation which encouraged the belief that they are willing to participate more in a favourable environment.

The empirical study in this thesis emphasised the needs for a strong state to promote the private sector revival. It also highlighted the problems of the market economy where public monopoly were sometimes replaced by private monopoly. Oligopolistic practices of merchants and their control over prices were very clear in the poultry industry. Complaints from merchants and middlemen were also frequent from producers of agricultural inputs. Commercial cheating was also evident. In all these cases private investors asked for government protection from such practices and admitted their failure to solve such problems. Producers of inputs also failed to provide geographical coverage in distributing their products and requested seek the help of the PBDAC. All this highlighted the need for the state to strengthen its ability to provide the necessary law to fight monopoly and to impose existing legislation concerning commercial cheating.

In short, any review to the reform programme should consider to eliminating the negative effects of unequal distribution of gains and losses between various socio-economic groups; to enhance the positive outcomes and to consider long-term issues.

Further research might examine the relationship between agribusiness associations and the state. Investors response revealed that the main task of agribusiness associations was to negotiate economic policy with the government. However, they express the view that these associations were weak. More investigation is necessary to the kind of policies or measures negotiated with the government and the reason for the relative weakness of these associations. My empirical study has not covered middlemen and merchants who work in districts and villages, yet this strata plays a pivotal role in influencing availability and prices of input. Their relation with agribusiness and farmers needs to be examined. Furthermore, there is a need for periodical assessment to investment obstacles and changes in the investment environment through research and meeting between government officials and businessman. Finally greater transparency in state policies would facilitate, among other things, opportunities for an improved policy debate.



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### **Newspapers**

Ahram Newspaper (Arabic)

## **Appendix 1 Questionnaire on the Agribusiness Community in Egypt**

Name of Company:

Name of Investor :

Address :

Date :

This information is confidential and will only be used for the purpose of scientific research. Confidentiality of respondents will be maintained at all times

This questionnaire is to be answered by one of the owners of the company as it represents the views of investors who risk their money and their participation in the decision-making process.

Name :  
 Education :  
 Age :  
 previous job :

1- When was your company established? year .....  
 - When did you start your actual activity? year .....

2- what is the legal status of your company?

- Joint stock
- Partnership
- Ltd. Partnership
- Ltd. Liabilities
- Individual Enterprise
- Other

3- Under which investment law was your company established?

- Investment law no. 230 for the year 1989
- Private sector law no. 159
- Other

4- What is the size of the company's capital?

- Authorised Capital
- Paid up Capital

5- Do you have non-Egyptian partner?

- Yes ( )ask no. 6                      -No ( )ask no. 8

6- What is his nationality? .....

7- Why do you need a foreign partner?

- To provide finance
- To provide new technology
- To open new markets

8- Did you obtain a loan to establish your company?

- Yes ( )                      -No ( )

9- What is the number of your employees? Total .....

- Permanent.....
- Temporary.....
- Seasonal.....



10-What are the company's main activities?

- 1- .....
- 2- .....
- 3- .....

11- By which of the following methods did you manage to expand your activity in the previous period :

- Increasing Capital
- Increasing production
- Introducing new products
- Introducing new services
- Introducing new technology
- Expanding employment
- Shifting from domestic to external markets
- Expanding exports
- Others

12- What were the main obstacles which faced you when you founded your company?

- Funding
- Lengthy and complicated steps
- Government officials increasing beaurocracy more ruttred and difficulties
- High fees
- Some companies practise market monopoly
- Other producers seek illegal ways in operating
- No enough information about market
- Terms for loans difficult
- Others

13- What were the main obstacles which faced your company in its operations before 1991? and how did you manage to overcome them ?

- 1-.....
- 2-.....
- 3-.....

14- Which of the obove obstacles were overcome after 1991 through economic reform policy? how?

- 1-.....
- 2-.....
- 3-.....

15- What other obstacles faced your company after 1991? how did you manage to overcome them?

- 1-.....
- 2-.....
- 3-.....

16- To what extent was the economic reform useful to your company?

- Very useful
- Limited usefulness
- Some parts are useful others are harmful
- No effect
- Limited harm
- Very harmful

17- Which parts of the economic reform were useful? why?

- 1-.....
- 2-.....
- 3-.....

18- which parts of the economic reform were harmful? why?

- 1-.....
- 2-.....
- 3-.....

19- Does your company engage in export?

- Yes (            ) ask 20
- No (            ) ask 28

20- What is the proportion of exports relative to the company's total production (operations)?

.....

21- Do you make your own products?

- Yes (            )ask 23
- No (            ) ask 22

22- Do you intend to produce them in the near future?

- Yes (            )
- No (            )

23- What are the main markets for your exports ?

Product	Country
.....	.....
.....	.....
.....	.....

24- Have any of the following changes happened to your exports during the last five years?

- Increase in exports            (            ) Year .....
- Decrease in exports            (            ) Year .....
- Opening new markets            (            ) Year .....
- Exporting new products            (            ) Year .....

25- What are the main causes for these changes?

- 1-.....
- 2-.....
- 3-.....

26- What are the main obstacles which face you in export? how do you try to overcome them?

- 1-.....
- 2-.....
- 3.....

27- Do you expect the demand on your products to increase or decrease in the future? why ?

.....  
.....

28- What are the main obstacles in the local market? how do you try to overcome it?

- 1-.....
- 2-.....
- 3-.....

29- What do you expect concerning domestic demand? why?

.....  
.....

30- Is your company engaged in import?

-Yes ( ) ask 31                      -No ( ) ask 34

31- What are your main imports and from where?

Product	Country
.....	.....
.....	.....
.....	.....

32- What are the main obstacles which face you when importing? how do you try to overcome them?

- 1-.....
- 2-.....
- 3-.....

33- Do you find competition from local products when you market your own?

-Yes ( )                      -No ( )

34- Did the rise in the interest rate in 1991 and 1992 affect your activities? how?

.....  
.....

35- How suitable is the interest rate for loans now?

- Very high ( )
- Suitable ( )
- High ( )
- Do not know ( )

36- Have you tried to obtain a loan from the PBDAC project for Agricultural modernity backed by the World Bank?

- I do not know about it ( ) ask 40
- I do not need loans now ( ) ask 40
- I obtained a loan ( ) ask 37,38,40
- I am trying to secure a loan ( ) ask 37,38,40
- Terms are not suitable ( ) ask 39
- Other ( ) ask 40

37- How much? for what activity?

38- What are the main terms?

- Interest rate:.....
- Repayment period:.....
- Other:.....

39- Why?

.....

40- What do you think of the PBDAC role in finance?

.....

41- Do you think that the devaluation of the Egyptian pound at the beginning of the reform affected your activity? how?

.....  
 .....

42- Do you think that the exchange rate of the Egyptian pound is suitable now? why?

.....

43- How will trade liberalisation affect your activity?

.....

44- Do you intend to achieve any of the following goals in the near future:

- Increase production ( )
- Introduce new products ( )
- Increase exports ( )
- Open new external markets ( )
- Modernise technology ( )
- Expand employment ( )
- Start new complimentary activities ( )
- Other ( )

45- Do you invest in R&D? how ?

- I do not invest in R&D ( )
- I have my own R&D department ( )
- I consult the government research unit ( )
- I consult the private research unit ( )
- I seek the help of foreign experts ( )
- I use specialised magazines ( )
- I travel abroad to keep informed about new changes ( )
- Other ( )

46- What is the percentage of your expenditure on R&D in relation to your total expenditure?.....%

47- What are the main countries whose technology you seek to learn? .

.....

48- Do you think that the main steps taken by the new government to promote investment and exports are sufficient ?

- Very adequate ( ) ask 51
- Good, but there are other steps needed ( ) ask 49
- With limited effect ( ) ask 49

49- What are the other main steps needed to promote investment?

- 1-.....
- 2-.....
- 3-.....

50- What are the other main steps needed to promote exports?

- 1-.....
- 2-.....
- 3-.....

51- What are the main countries in the region that compete with Egypt to attract investment capital?

.....

52- Why does Egyptian capital seek to invest abroad? what might be the main effects on the Egyptian economy?

- 1-.....
- 2-.....
- 3-.....

53- What do you think of selling public enterprises (privatisation)?

- All PE should be sold ( )
- Big strategic companies should be kept ( )
- Only failing companies should be sold ( )
- Failing companies should be phased out ( )
- Other ( )

54- Which privatisation method do you prefer?

- Total sale for national investor ( )
- Total sale for national or foreign investor ( )
- Selling shares on stock market ( )
- Selling for employees ( )
- Private sector management ( )
- Other ( )

55- How can selling of shares be encouraged and made easier?

- 1-.....
- 2-.....
- 3-.....

56- Did you participate or intend to participate in the privatisation programme?

- I bought some shares ( ) ask 58
- I intend to buy some shares ( ) ask 58
- I intend to buy amain share ( ) ask 58
- I do not intend to participate ( ) ask 57
- Other ( ) ask 58

57- Why?

.....

58- Are you a member of the Chamber of Commerce?

- Yes ( ) ask 59
- No ( ) ask 63

59- How do you benefit from it?

- 1-.....
- 2-.....

60- Are you a leading member?

- Yes ( ) ask 61
- No ( ) ask 63

61- Where? .....

62- What are your main goals?

- 1-.....
- 2-.....

63- Are you a member of any businessmen association?

- Yes ( ) ask 64
- No ( ) ask 66

64- Which one? .....

65- In what way do you benefit from it?

- Loans and funding facilities ( )
- Technical consultation ( )
- Opening new external markets ( )
- Access to land facilities ( )
- Consulting with government concerning economic policy ( )

-Other ( )

66- Do you think that business associations can influence government policy?

- Have effective influence
- Have limited influence
- Have no influence at all
- Other

67- In what ways?

.....

.....

68- How can its effectiveness be increased?

.....

.....

69- Are you a member of the Egyptian-American Chamber of Commerce or the Presidential Board? What are its main activities?

.....

.....

70- Do you think that any of them can influence economic policy? how?

.....

.....

71- Are you a member of the industrial federation?

- Yes ( ) ask 72
- No ( ) ask 73

72- How do you benefit from it?

- 1-.....
- 2-.....

73- Are you a member of any other civil association?

- Yes ( ) ask 74
- No ( ) ask 76

74- What is its name?.....

- What is its main activity?.....
- .....

75- How do you participate in its activities?

.....

.....

76- Are you a member of any political party?

- Yes ( ) ask 77
- No ( ) ask 80

77- Which party? .....

78- What kind of activity do you practise inside the party?

- 1-.....
- 2-.....
- 3-.....

79- How do you express your opinion inside the party?

.....

80- Did you nominate yourself in the last People's Assembly election?

- Yes ( )
- No ( )

81- Did you vote in the last election?

- Yes ( )
- No ( )

82- Do you think that a greater degree of democracy can enhance the economic reform programme?

- Yes ( ) ask 83
- works against the programme ( ) ask 83
- There is no relationship ( ) ask 84

83- How?

.....

84- Do you think that the partnership agreement with the European Union or the USA will affect your activity? how?

.....

.....

85- Do you think that the Middle East co-operation can expand your company's activities?

- Yes ( )
- No ( )

86- Are there any agricultural projects that can be implemented through Middle Eastern co-operation and introduced in the coming Cairo economic summit? Which are the main countries that can participate?

- 1-.....
- 2-.....
- 3-.....

87- What are the main steps you adopt to limit the negative effect of your activity on the environment?

.....

.....

88- How effective are the government initiatives to reduce pollution by companies?

.....

89- What are the main reforms that the agricultural sector needs?



