Conference Proceeding: Egypt's Current Economic Features and Policies

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Bearing in mind the difficulties of making predictions, one could expect the recent agreements with the International Monetary Fund (IMF) to reduce fiscal and external deficits as well as public debt without addressing the structural difficulties of the Egyptian economy that affect the creation as well as the distribution of wealth. The 2016 three-year extended fund facility loan of US $ 12 bn was unlikely to contribute to sustained economic development based on inclusive growth, an increase in total factor productivity, and a shift towards high value-added products and services. The same applies to its successor, the 2020 stand-by loan of US $ 5.2 bn, mainly supposed to alleviate the effects of the current Corona virus epidemic. Reducing jargon to a minimum, recent economic policies, which are supported but not entirely defined by the IMF, will probably neither enhance 'social justice' nor transform Egypt into a high-income country. According to the World Bank classification a lower middle income country (defined by GNI per capita between current US S 1,036 and 4,045), Egypt with a GNI per capita of US S 2,290 in 2019 may even find it difficult to turn into a higher middle income country.

Earlier Agreements with International Financial Institutions

Such reservations are confirmed by the effects of earlier agreements that Egypt had reached with the IMF and the World Bank (that is the 'Bretton Woods' or 'international financial institutions'/IFIs) as well as by the effects that similar such agreements governed by the successive iterations of the Washington consensus have shown in other countries.

No doubt the most telling precedent is the 1991 agreement on macroeconomic stabilisation reached between the Mubarak administration and the IMF that was accompanied by an agreement on structural adjustment with the World Bank. Ultimately an effort to cut government expenditure and raise revenue (in particular through indirect taxation), the austerity measures entailed by stabilisation considerably reined in budget and balance of payment deficits and reduced foreign public debt. However, improvements were temporary and fragile; the current account deficit soon rose again and public debt remained high, partly because external debt shifted towards domestic debt. Moreover, the improvements were heavily influence by events outside the scope of the agreement, in particular the reduction and rescheduling of a large part of foreign debt as a reward for Egypt's participation in the 1991 Kuwait war.

Historically, programmes of macroeconomic stabilisation have helped to produce the intended effects on budget and external balances, though at considerable social cost and primarily in the short and medium term. However, structural reforms as defined by the Bretton Woods institutions have generally failed to initiate or strengthen economic development in the sense defined above. Emphasis on the growth of the private relative to the public sector (through the privatisation of state-owned companies and other measures to encourage private businesses) and on associated forms of deregulation (which in actual fact is a form of re-regulation) is no generalisable recipe for development. Frequently the ‘retreat of the state’ has not shown such effects but rather produced the opposite.

For instance, deregulation has often come at the expense of functioning markets that henceforth are supposed to govern the allocation of resources in lieu of government decisions. In Egypt, the reforms launched in 1991 led to the growth of the private sector without the commensurate growth of markets in the sense of level playing fields on which buyers and sellers negotiate the sale of commodities, services or factors of production. No doubt all markets are politically constructed and thus biased towards the interests of certain actors, be it only because regulations or their absence strengthen the position of the ones or the others (for instance, minimum wages may work out in the favour of workers rather than employers while low corporate tax helps the latter).

In Egypt, however, the lack of appropriate regulations combined with the de facto power of market players close to the authoritarian government entailed the emergence of highly truncated markets that are characteristic of ‘political’ or ‘crony capitalism’. Put more simply, public monopolies and oligopolies were replaced by private monopolies, oligopolies, and rent-seeking. Another example is deregulation in the area of foreign trade, which prevented the imposition of (however temporary and decreasing) protective tariffs that could strengthen nascent industries. Moreover, the growth of the *formal* private sector has not led to the creation of the number of jobs it was supposed to create, neither in the 1990s nor since 2016. As a result, income from work has not replaced cuts in social benefits including subsidies.

The structural reforms after 1991 had no major effect on the sophistication of commodities and services produced in Egypt. The focus remained on relatively low value-added services and products and, depending on the period, on oil or gas. Investments were concentrated in the hydrocarbon sector which by definition creates little employment. The ratio of various forms of rents to domestic and national income remained considerable. Unemployment, underemployment, inequality and poverty remained salient features of the Egyptian economy, and most likely reached proportions that are only in part reflected in official government and internationally (re)produced figures.

Current Policies

In line with IMF statutes and ultimate priorities, the 2016 loan agreement and preliminary measures requested from the Egyptian government were primarily concerned with macroeconomic stability. In addition to fiscal and monetary measures, the package included so-called structural reforms focusing on private sector development that were supposed to ensure macroeconomic stability in the longer term. Fiscal measures themselves as usual sought to raise government revenue and cut expenditure. On the revenue side, they included the introduction of a fully-fledged VAT (replacing the sales tax levied since the 1990s) which like all indirect taxation in the end was regressive rather than progressive. Interestingly, the measure more or less coincided with the reduction of the maximum income tax level for high earners. On the expenditure side, they included cuts in food and especially in energy subsidies as well as in the public wage bill. Monetary measures included the floating and devaluation of the Egyptian pound from roughly 8 to 18 to the US dollar.

Finally, the agreement itself also emphasised inclusive growth, job creation, and social protection, in particular for women and young people. These concerns were broadly shared by the Country Partnership Agreement that Egypt had signed with the World Bank in 2015 for the period ending in 2019. The agreement with the IMF allowed Egypt to obtain additional loans of some US S 3 bn from the World Bank and US S 7-8 bn from other bilateral and multilateral donors.

Nonetheless, economic policies under President Abdel Fattah al-Sisi's administration cannot be reduced to programmes and reforms conducted under the aegis of the Bretton Woods institutions, even though the latter have considerable impact. More so than they did in the 1990s, economic policies have openly relied on government intervention in areas other than the restoration of budget and external balances. 'Government intervention' refers to measures decided and implemented not only by the government in the sense of the council of ministers or the president of the republic but also by actors that in principle should be subordinate to them.

The main actor in this respect are the armed forces which themselves include partly autonomous sub-units that in some cases reflect functional specialisations (army, navy, air force, procurement services, etc) and in others fiefdoms that officers could create for themselves and their allies. Far from being the 'agent' of a 'principal' called the state or the government, the armed forces are the informal principal of the state which covers and legitimates their activities. Under the current constitution (but in practice already since the 1950s), the budget of the armed forces is removed from civilian oversight, and many other decisions concerning the military are made by a restricted number of high ranking officers or bodies which they control. President Sisi himself is an army officer. The inverse relationship was strikingly illustrated when the armed forces publicly offered a loan to the government.

The armed forces and secret services own or control numerous companies whose contribution to GDP has been estimated to reach up to thirty, possibly forty, per cent. Like the armed forces themselves, these companies escape any parliamentary and civilian accountability. Some of them are classical military industries that produce or at least assemble tanks and other weapons. However, others produce non-military capital and consumer goods, largely but not only for the domestic market. Yet others play a considerable role in services, including in the financial sector. Since 2013 they have increasingly established joint ventures with domestic and foreign investors in order to raise capital and benefit from the transfer of technology and skills. Such involvement in the production of goods and the provision of services, including the media and therefore the formation of public opinion, is difficult to reconcile with the IMF and World Bank policies that - in principle – seek to reduce the size of the public sector.

Simultaneously, the economic activities of the armed forces have reshaped the private sector which may increasingly be subdivided into two components, the one closely related to the military, the other not. The former is part of the broader crony capitalist sphere where private capital is not exposed to competition or market forces. For instance, government procurement contracts may no longer be challenged in court. Though a broader issue, corruption cannot be disassociated from these developments that are intimately tied to the authoritarian character of the political regime. In a parallel development the businesspeople closely associated with the Mubarak administration, and especially with Gamal Mubarak, have lost part but not all of their clout. According to the World Bank, the public sector in the financial year 2017-18 received 69 per cent of domestic credit, households 8 per cent and the private sector 21 per cent; the figures do not show the share of companies connected to the government including the military in these 21 per cent.

Above and beyond the production of commodities, government intervention in the broader sense has also been highly visible in the planning and coordination of new infrastructures, not least the 'mega projects' such as the new administrative capital near Cairo and the 'new' Suez Canal. More easily reconcilable with IMF and Bank policy (though within limits), government planning and coordination have nonetheless gone hand in hand with an active, even dominant, role of public sector and crony capitalist private companies in the implementation of the projects concerned.

To an extent, government intervention at the current scale has been made possible by the revision and redefinition of IMF policies over the past two or three decades. At the same time, however, it reflects the ability of the current Egyptian government to influence, even shape, foreign perceptions of its action. Considered to occupy a 'strategic' geographical location, Egypt at various moments in its history has benefited from foreign support – even though the same 'strategic' location had earlier led to British occupation. Using Egyptian participation in the 1991 Kuwait war, Mubarak managed to renegotiate conditions applying to IMF and World Bank and support. In the late 1970s his predecessor, Sadat, had already managed to do the same. As for Nasser, he obtained over more than a decade Soviet military and development aid alongside large quantities of US wheat that were heavily subsidised by the American taxpayer. In the 1960s Nasser also twice obtained IMF support, even though the second agreement remained *letter morte*.

Increasingly, over the decades, Egyptian leaders have also succeeded in depicting themselves as a major bulwark against Islamists whom Americans and Europeans consider a major threat. Yet more than its predecessors, the Sisi administration has emphasised its contribution to the global fight against terrorism, conveniently extended to all Islamists of the Muslim Brotherhood variety and even all human rights defenders. Simultaneously, the current, increasingly multipolar, international environment offers Egypt a growing choice of partners. If support from Russia and China cannot at present replace support from the US and the EU, it may nonetheless fill gaps and serve as a bargaining chip.

Only occasionally and temporarily glossed over by initiatives such as Nasser's five-year-plan in 1960, the return to macroeconomic stability in the late 1990s or the hydrocarbon-dependent growth after 2004, economic fragility combined with continued demographic growth has created the wide spread and officially promoted perception that Egypt is too large to fail. The IMF and its major shareholders in North America and Western Europe seek to avoid the functional incapacitation of a state with more than 100 million inhabitants, ensuing social conflict, and large-scale emigration, even though beyond the very short term their policies may expedite rather than arrest such outcomes. More than its predecessors, the current Egyptian government has managed to extract from its foreign allies and supporters not only a 'positive' strategic rent for the services it renders, but also a 'negative' strategic rent derived from the chaos that it pretends to prevent.

In actual fact, recently the IMF was called in when the transfer of major amounts from Saudi Arabia and the United Arab Emirates as well as Kuwait decreased. By 2016 the three governments, especially Saudi Arabia, heavily reduced their aid, which over the three years following the military coup had reached US S 25 bn or more. The oil price and thus their own revenues were an important variable, but also Egyptian foreign policy that, while overall aligned on Riyadh, failed to satisfy Saudi expectations first in Syria, then in Yemen, and more generally vis-à-vis Iran.

Rents of various sorts have nonetheless remained a key factor that provided the government and the country with a however limited breathing space; helped to address the macroeconomic imbalances targeted by the IMF inspired reforms; and that in the short term mitigated their socially disruptive effects. Royalties from the Suez Canal (stalling in spite of the 'new' canal) that end up in the treasury are one example, remittances from the many Egyptians working in major oil and gas producing countries are another. In the longer term, however, rents prevent the transition from the mere 'allocation' of resources to the actual 'production' of wealth. Apart from more specific negative side effects such as Dutch disease, rents are also a precarious source of income as they are all subject to developments beyond the control of the Egyptian government.

Effects of Current Policies

In the short term

According to figures released by the Egyptian government, the IMF and the World Bank and various more or less reliable assessments of these figures, macroeconomic stabilisation has been partly successful. The budget deficit decreased from more than 12 per cent after the fall of Mubarak to 8.1 per cent in the financial year 2018-19. The current account deficit has been reduced from 6 per cent in the financial year 2016-17 to 2.4 per cent in 2017-18. The ratio of public debt to GDP has decreased from some 107 per cent to some 97 per cent. Much of itis domestic debt which - at some 78 per cent to GDP - does not move with the exchange rate but possibly crowds out the private sector. Inflation which, after the devaluation of the Egyptian pound had reached more than 30 per cent and still stood at 15 per cent in mid-2018, decreased to about 12 per cent in early 2019, though at the price of driving up interest rates and thus reducing investment. Real economic growth, which amounted to a little more than 2 per cent in 2011 and 4.3 per cent after 2015, reached

5.3 per cent in 2018-19. The currency reserves of almost US $ 44 bn in 2019 cover roughly six months of imports.

There seems to have been far less progress, and indeed compliance, with regard to the other objectives of the 2016 agreement. Figures quoted above show that access to credit remains difficult for the private sector. Conditions that would allow women to find decent employment have not improved as far as one can judge. Independently of these –sadly secondary - objectives, no real progress has been made to shift output towards higher value-added services and products (apart from products that rely on imported high tech components) that could replace the (future) export of hydrocarbons and many of the low value-added products in which Egypt can no longer compete (many of the textiles sold in Egypt today are produced in East Asia). As a matter of course, any such change would take far more time to materialise than the current preoccupation with 'hardware' such as new roads and bridges, the new capital and the 'new' canal. They would also involve investment in human development, in particular education, higher education and therefore critical thinking.

Nor have current policies enhanced the material welfare of ordinary Egyptians any more than in the 1990s. So far, Egypt is far from creating jobs for the roughly 700 – 800,000 new employment seekers every year. Recent annual growth of some 5.3 per cent is lower than the 9 per cent generally assumed necessary for creating such employment. However, even higher growth would not necessarily translate into lasting higher employment creation. Capital intensive investments in hydrocarbon industries in particular create little employment. The same applies to the 'mega projects' cherished by the government but launched without serious feasibility studies. Unemployment and underemployment rates are far higher than the roughly 10 - 12 per cent shown by official figures that are based on restrictive definitions and ignore the large informal sector. Even these figures, though, are particularly high for women and young people. Figures since the 1990s also show that attempts to limit or reduce public employment particularly penalised women and young graduates.

Insufficient job creation has not been compensated for by other policies that would reduce poverty and inequality. Rather the situation has been aggravated by the cuts in food and energy subsidies; in practice these cuts may have been less far reaching than announced but at the same time the introduction of smart cards to access subsidised goods seemed to have perverse effects. Food allowances and other, partly recent, targeted benefits for those officially recognised as poor fail to help those who may fall through the cracks. The only consolation for many Egyptians lies in official figures that apply an unrealistic poverty line and thus reduce the poverty headcount from about 70 to 33 per cent of the population. Poverty indicators, like other economic and social indicators, continue to show an important divide between the better off parts of the country including Cairo and the Delta on the one hand and Upper Egypt to the South of the capital on the other.

In the long term

As already in the past, the advocates of macroeconomic stabilisation concede that austerity has negative short-term effects on welfare but consider it a necessary precondition for improvements in the longer term. As a matter of course, such long-term improvements remain largely hypothetical at this stage. On the basis of earlier experiences in Egypt and elsewhere it seems nonetheless unlikely that recourse to the IMF will result in any general welfare gains. Even if economically speaking there was a long term link between stabilisation and welfare, authoritarian rule such as in Egypt comes at the expense of transparency and accountability, two major conditions for more inclusive economic and social policies.

Most likely, therefore, IMF inspired policies - in spite of the potentially mitigating effects of rents - will not alleviate the unequal distribution of income and wealth or significantly reduce poverty. It is more likely that they will contribute to widen the gap between the upper and lower deciles, which already in the past was probably much higher than reflected in official statistics and a relatively low Gini coefficient of about 29-32 (0 corresponding to maximum equality and 100 to maximum inequality). Nor is there any reason to believe that they will encourage the private sector to create more and better jobs than in the past. Neither in the 1990s nor later has job creation in the formal private sector compensated for the loss of public sector and government jobs. If at all there was compensation, it was in the informal sector which, depending on estimates, accounts for anything between 30 and 50 per cent of the economy (with the obvious caveat that the size of the informal economy is by definition impossible to measure and difficult to estimate).

Inequality, poverty, and other exclusion mechanisms (like highly controlled market access and the marginalisation of politically non connected owners of capital) may continue to fuel widespread sentiments of social injustice. The results may be either similar to those that culminated in the 2011 protests or a combination of endemic frustration, disaffection and emigration. As ‘loyalty’ through co-optation and participation ceases to be an option, the Hirschmanian options will be increasingly limited to ‘voice’ and ‘exit’.

If and when the current nationalist discourse of the valiant military protecting Egypt against the ‘terrorist’ Muslim Brotherhood loses its popular appeal, the government may have to depend on repression even more than it does now. The question then is to what extent repression permanently pre-empts or defeats protests such as the ones in September 2019, or prevents them from spreading and intensifying. Defunct for decades, in actual fact an illusion from the outset, the much vaunted ‘social contract’ would be definitely exposed as repression in disguise.

Conclusion

Events and developments suggest that Egypt is continuing its balancing act between crises and attempts to overcome these crises. Collapse is not excluded but unlikely as long as foreign support continues to flow. However, except for macroeconomic indicators there is little hope for improvement, and even these indicators may - once again - only temporarily improve. Considering the recurrent balance of payment, budget and debt crises in the past, Egypt may be in for another round of stabilisation in a few years from now, provided donors consider further transfusions useful and justified.

Nonetheless, one needs to remember that previous governments have not come closer to putting Egypt on a sustainable development path. Shortcomings and failures today have numerous precedents; though partly the result of failed or inadequate policies, they are also intimately related to the constraints, including external constraints, under which policies in Egypt and other ‘developing’ countries are formulated and implemented.

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About the Author

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