Chapter Two

The *Etatist* system in Egypt, 1952-1991

Introduction

To understand the historical development of the economic and political transformations caused by Egypt's structural adjustment program at the beginning of the 1990s, it is necessary to analyze the development of the Egyptian economy from the 1950s to today. Hansen (1991: 10) divides Egypt's economic and political transformations in the twentieth century into five periods. The first period, from 1929 to 1955, was characterized by a dependence upon private enterprise and free trade. This yielded a moderate-sized public sector. At this time, Egypt's development strategy depended upon agricultural exports, which it supported through public investment. In terms of industry, Egypt primarily focused upon import substitution, which supported Egypt's industry through tariffs and other trade restrictions.

The second period, from 1955 to 1960, which was a period of transition, witnessed no essential changes. However, the third period, from 1960 to 1965, witnessed the rise of *etatism*, a peacetime economy, an increased public sector, and Egypt's first five-year plan. Like the first period, Egypt's economy still depended upon agriculture, export promotion and import substitution. In industry, however, import substitution began to be supplanted by a growing military-production agenda.

The fourth period, from 1965 to 1973, merged *etatism* with a wartime economy, an enlarged public sector, and military-based economic growth. Finally, the fifth period, from 1973 to1991 continued Egypt's involvement with *etatism* and a large public sector, but moved back to a peacetime economy, and witnessed the development of *the infitah*, or partial economic liberalization. Egypt's economy, still dependent upon import substitution in agriculture and industry, also benefited from oil, the Suez Canal, and tourism. To support this growth, Egypt promoted export-oriented activities and allowed the migration of workers.[1]

The period from 1991 to the present has witnessed an expansion of the trends that Hansen identified in the fifth period. Egypt's economy has grown through structural adjustment and privatization. The institutional setting of this period has depended on the maintenance of the *infitah* policy, widespread liberalization, and growth in the private sector.

The most common and noticeable feature of the former periods is the dominant role of the state. In the light of these historical periods, this chapter examines the main characteristics of the Egyptian state from the introduction of the *etatist* system to 1991, when Egypt began applying its structural adjustment policy.[2] The following historical analysis will focus mainly on the state's advances in its developmental and welfare policies, the two main pillars of the *etatist* system.

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[1] See also, Harik 1997:17-22.

[2] While Hansen (1991: 10) considers 1991 the ending date of the *etatist* system in Egypt, Wahba (1994: 147) argues that 1981 represents the end of this period. In this study, I find that Hansen's classification is more veracious in regards to the historical changes, which faced Egypt since 1981. Despite the war against corruption, which followed Sadat's assassination on October 6, 1981, Muabarak has ended with the same policy of *infitah*, supporting private sector and encouraging foreign investments. The period from 1981 to 1991 witnessed no important economic changes. On the contrary, since applying the major stand by

Egypt's political and economic development can be better understood in light of the dominant role of the Egyptian state since the early sixties. Richards and Waterbury demonstrate two fundamental types of state intervention and capitalist accumulation. In the first, "the state nurtures or strengthens a private sector" (Richards and Waterbury 1990: 214). During this process, the state "provides roads, railroads, port, and electrical power to stimulate economic activity" (Richards and Waterbury 1990: 215). The essential function of the interventionist role of the state here is to try to absorb all major risks for the private sector. In so doing, the state hopes to encourage private investment in the country.

In the second process of accumulation, the state takes control of all available resources to finance its own expansion. The main goal of the state here is to dominate all aspects of the economy. The state generally characterized this process as a "socialist transformation," or as following "the non-capitalist path."[3] Egypt adopted the second process of accumulation with the Socialist Decrees of 1961, but gradually dropped it after 1974 (Richards and Waterbury 1990: 215).

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agreement in 1991 with the IMF, Egypt has witnessed dramatic economic changes, mainly in regards to the welfare and social policies, which have affected the majority of the poor and middle class in Egypt.

[3] Harik calls this pattern the "patron state." He contends that "the patron state is made up of a set of rules in which the provision of livelihood of citizens and the management of business enterprises fall within the public domain as a responsibility of the government" (Harik 1997:5-6).

Egypt on the Eve of the 1952 Revolution

Before the 1952 revolution of the Free Officers, the private sector dominated almost all Egypt's economy. While the public sector provided public services, such as electricity, water supply, railways and civil administration, the private sector was responsible for 87% of Egypt's economic production and employed 95% of its civilian workers (Mohieldin and Nasr 1996: 32-33).[4] One of the major factors that contributed to the dominance of the private sector is the fact that a small group of people owned or controlled most of the farmland in Egypt. According to Whaba (1994: 48), 0.1 % of the total number of landowners held nearly 20% of the total farmland, while 94% held 35% of the area. This reflects the extreme wealth concentration and rampant inequality in Egypt before 1952. This monopoly of wealth and power combined with the extensive dependence of these oligarchs upon foreign capital to produce a truly explosive social and political situation on the eve of the 1952 Coup.[5]

The dominant role of the state is the main characteristic of the majority of the Middle Eastern regimes which have no effective interest groups or significant social classes. Hourani (1991) divides the ruling classes of Middle Eastern countries into two groups: royal families, and those who were elected or seized power. Countries ruled by royal families include Saudi Arabia, Kuwait, Oman, Morocco and Jordan. Countries

[4] Aoude (1994: Online) states that "industry, agriculture, domestic and foreign trade, transport, banking, electricity and water were all part of the private sector." This means that the private sector dominated every aspect of the economy in Egypt before 1952.

[5] For more details about many riots which happened in Egypt before 1952, particularly in the rural areas, see Wahba (1994: 49) and Vatikiotis (1980: 390-391), in which he demonstrates that much of the financial power was in foreign hands and state intervention was limited to irrigation and railways.

ruled by the second group include Egypt, Syria, Iraq, and Libya. Other segments of the upper classes that directly rule or influence the governments of Middle Eastern states include military officers, governmental officials, and businessmen (Cockerham 1995: 13). Richards and Waterbury argue that other classes, including the middle class, working class, and lower class, are so weak and fluid that they lack the cohesion and self-definition necessary to effectively manipulate their governments (Richards and Waterbury 1990: 38).[6]

Egypt in the Wake of the 1952 Revolution

Since the late 1950s, the state has been the main actor in Egypt's political and economic development, even after the introduction of the structural adjustment program in the 1990s (Waterbury 1983: 134; Harik 1997: 1). After the 1952 Revolution, the Nasser's regime adopted what became known as "state-led growth policies," which implemented import-substitution industrialization, highlighted the importance of agriculture, and reduced inequalities through land reforms.[7] Nasser's regime did not

[6] James Bill says that "in the Middle East these classes traditionally have been the following seven: the ruling class, the bureaucratic middle class, the bourgeois middle class, the cleric middle class, the traditional working class, the peasant class, and the nomadic class. The twentieth century has witnessed the appearance of two new classes: the professional middle class and the industrial working class" (in, Richards and Waterbury 1990: 40-41).

[7] Ibrahim (2000) explains that Nasser's model of the state was common and widespread in other Arab countries. He states that "following Egypt's example under Nasser, peoples of the Arab world were led to believe that the state would grant or provide consolidation of newly obtained independence, achieve rapid economic growth (through industrialization), institute social justice, march toward Arab unity, liberate Palestine, and maintain cultural authenticity. All of this would be achieved in return for suspending liberal Western-type democracy, at least for a while. Public policies, central planning, and command economics became the order of the day. State organs multiplied. State bureaucracies grew in size ten-times, on average, between 1950 and 1980."

adopt these policies immediately. In fact, according to Mohieldin and Nasr, the free officers did not begin implementing its “Egyptianization” laws and effective nationalization until after the 1956 Suez crisis, five years into the revolution. The nationalization, in fact, began with Egypt’s sequestration of properties formerly held by British and French concerns (1996: 33; see also Harik 1997: 13; Aoude 1994).

At the beginning of the revolution, the Free Officers did not threaten to nationalize private property; on the contrary, they encouraged the private sector to participate in national economy. The Free Officers focused on demolishing feudalism; to this end, they instituted agrarian reform in September 1952. The main aim of this land reform was to limit personal ownership to 200 feddans. This improved income distribution in Egypt, even if it did seem to contradict Nassar’s socialist agenda (Oweiss 1990: Online). Although Land Reform reduced the inequality of land distribution, its only radical component was its deliberate attempt to weaken the landed aristocracy. The Land Reform law effectively destroyed the landed aristocracy, replacing it with a new agrarian rich peasant class, while simultaneously supporting Egypt’s traditional peasant underclass (Aoude 1994: Online). Just prior to the agrarian reform, the 0.11 percent of landowners having 20 or more feddans (one feddan equals 1.038 acres) owned 45.0 percent of all cultivated land; by 1965, a similar proportion of landowners (0.12 percent) owned 20 or more feddans, but their landholdings constituted only 25.2 percent of the total (Oweiss 1990).

The July Revolution promptly forged a sociopolitical coalition of three social classes: the petite bourgeoisie middle class, the urban working class, and the rural poor. The target of this coalition was Egypt's upper-class landed bourgeoisie (Ibrahim 1994: 27). Because of the nature of this coalition, many scholars classed Nasser regime as a populist system. According to Farah, populist regimes depend on "'import substitution' to stimulate internal industrialization, coupled with welfare measures such as land reform, free education, and subsidized health care, etc., designed to effect a more equitable distribution in the interest of political stability" (1994: 138). While all of these components can be seen in Nasser's regime during the 1960s, the full expression of his populism lies in his political and ideological discourse, not in his economic policies.

The populist period of Nasser's government formed the first phase after independence, and was followed by the second phase, bureaucratic authoritarianism. In the second phase, Nasser's government moved toward more liberal economic policies and a place in the world capitalist system (Farah 1994: 139). To do so, however, it had to reduce the political and economic power of the labor force, which it had previously enfranchised, and scale back governmental expenditures on social welfare services. This required repressive measures and dramatic reconsideration of its social agenda (Wahba 1994: 16-17; Harik, 1997: 5; Brumberg1995: 256; Bianchi, 1989: 20).

The 1952 Free Officer's attempt to support and encourage the private sector to share and participate in economic conditions met with very limited success. The 1952 law was an attempt to stimulate industrial and commercial economic growth, funded by the landed aristocracy (Aoude 1994: Online). Despite governmental support and encouragement, the private sector was reluctant to contribute to these economic investments. In fact, as Zaalouk (1989: 25) points out, “most capitalists were panic-stricken. Many emigrated abroad. Most did not abide by the state’s plans; instead, they continued to do business and to accumulate and consolidate their own wealth and economic power.” Private sector investment fell from 112 million Egyptian pounds in 1950 to only 39 million Egyptian pounds in 1956, whereas gross public investment increased from 22 to 66 million Egyptian pounds over the same period (Wahba 1994: 55).

Under the wide nationalization of 1960s, the Egyptian state adopted and depended on a public-sector-led and inward-oriented development strategy. The government nationalized almost every economic segment, including “most private enterprises in industry, manufacturing, trade, insurance, finance, and other services” (Harik1997:18). The state-owned enterprise sector was the central key to achieving the economic development of Nasser’s regime (Waterbury 1992: 198).

After Nasser’s regime proclaimed the so-called Socialist Decrees of its extensive nationalization in July 1961, the public sector greatly expanded.[8] Thus, by 1963, all financial institutions, transportation, and all significant manufacturing concerns were owned by the public sector. External trade and a significant amount of internal trade remained under the control of the state. Agriculture and urban real estate were the only sectors “outside complete government ownership, but they were overwhelmingly regulated by laws and decrees” (Mohieldin and Nasr 1996: 33; see also Rivlin 1997). By adopting a policy of State Owned Enterprises (SOEs) in the wake of the1956 Suez War, the government organized public firms under the aegis of a holding company, which it named the Egyptian Development Organization. By 1959, the government had created two more holding companies, which controlled firms nationalized from the private sector or greeted by the government (Waterbury 1992: 198).

The extensive nationalization of July 1961 and the establishment of the SOEs allowed the Egyptian state to dominate the essential economic sectors, including textiles, metals, engineering, chemicals, and trade (Waterbury 1992: 199). These sectors were supervised and controlled by the General Organizations, which belonged to the state and were “charged with preparing sectoral plans, developing budget projections, procuring raw materials and financing, and identifying senior management” (Waterbury 1992: 199). Waterbury outlines the impressive growth of the public sector:

> By 1965 the public sector had been expanded to its greatest extent to date, and Egypt’s economy as a whole grew at remarkable rates. Never before had such investment ratios been achieved. The public sector accounted for nearly 40 percent of total output, 45 percent of domestic savings, and 90 percent of gross domestic capital formation (1983: 81).

The laws enacted by Nasser’s regime enabled this impressive move toward nationalization, and led to inclusive state control of the economy (Whaba 1994: 82-83). With the July Socialist Laws, the Egyptian state cemented its dominance over the

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[8] For more details about the effects of declaring the laws of July 1961, particularly on improving the living

economy. For example, “Law 117 nationalized all banks, all insurance companies, and 42 large industrial, commercial, financial, transport and land reclamation companies in both provinces of the UAR (Egypt and Syria). The following day, Laws 118 and 119 were published. Law 118 provided for the transformation of 82 Egyptian and 11 Syrian companies into Arab Joint-Stock Companies with 50% government ownership” (Baynard 1995: 311; see also Wahba 1994: 82-84).

This expansion of state ownership strengthened its control over Egypt’s economic resources. After 1961, the state controlled almost every aspect of society. The public sector was supported by the division of three large General Organizations of the public sector into thirty-eight smaller ones. These were allocated to various ministries by virtue of Presidential Decree 1989/1961 in the proportions. For example, the Ministry of Industry has nine organizations, Ministry of Defense has one; Ministry of Agriculture has one, Ministry of Communications has two, and Ministry of Economy has five (see, Wahba 1994: 86).

The *Etatist* System of Nasser’s Regime

One of the main aims of Nasser’s *etatist* system was to develop the Egyptian economy with a focus on industrial growth. The first five-year plan, which ran from 1960 to 1965, witnessed a period of economic stability and the economic apex of the Nasser regime. “Growth rates averaged 7.2%, unemployment was virtually eliminated

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conditions of the labor class and ameliorating their wages, see Wahba 1994: 85-88.

among workers and intellectuals, and per capita income increased by 19.1% by the end of the plan's period" (Aoude 1994: online). For this Five-Year Plan, the Egyptian government coined the slogan "From the needle to the rocket," which highlighted its industrialization agenda. This slogan reflected the wide range of activities of the first plan, which aimed at the end to achieve what the government called a "self-reliant strategy of development," a goal not only in Egypt, but also in the majority of newly independent countries. This became the main characteristic of the Nasser regime: creating a strong industry that was mainly dependent on the Egyptian raw materials.

The Egyptian state during 1950s and 1960s attempted to address a group of what it saw as broad obligations to the Egyptian people, including basic human needs. To this end, it subsidized food, health care, and housing, offered free education up to the university level, and guaranteed employment (Ali 1994: 185; The Economist October 25, 1997). All of these regulations and social policies made the revolutionary government of the 1950s and 1960s widely popular. In addition, the Egyptian state established wide-ranging welfare policies, aimed at subsidizing the majority of the poor. As McDermott notes, Nasser tried to "provide a cushion" against poverty by subsidizing the essential needs of his people. As time went on, these subsidies expanded to include energy, transport, public utilities, financial services, and public-sector companies (McDermott 1988: 80-81).

There is a wide debate about how best to label the Nasser regime. Harik notes that the leaders of 1952 Revolution preferred to use the term "Arab socialism" instead of "patron state" (1997: 6). Their regime was inspired by different sources, including Marxism, Islam, and the experiences of socialist regimes of the nonaligned movement of the Third World. On the other hand, Waterbury (1983) characterizes the Egyptian system since 1957 as existing in a "state capitalist mode." He bases this term on the role of government and its use of a dominant and wide-ranging public sector as a means of accumulating national capital. Many post-colonial states have expanded the role of the government in economic and social life; because of this, many scholars argue that such states take on a capitalist role.[9]

Although this system has some elements of state capitalism, such as "a nationalistic reorientation of economic resources through agrarian reform and a wide nationalization of basic industries" (Cooper 1982:16-17), one cannot easily and inclusively label it as a form of state capitalism. Harik argues against labeling Nasser's regime state capitalist. For him, the absence of competitive relationships between active actors in a free market, combined with the Nasser's government's role as sole provider of basic needs and general welfare are two main reasons that this label is inaccurate (Harik 1997: 8).

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[9] Cooper (1982:16-17) states that scholars seem to agree on a number of characteristics of state capitalism at the descriptive empirical level. He says that:
"1. The origin of state capitalism lies in weak national economies at the periphery of the international economy with weak national bourgeoisies and disorganized popular classes.
2. State capitalism involves a nationalistic reorientation of economic resources through moderate agrarian reform, nationalization of basic industries, centralization of finance and an expansion of social services.
3. There exists a state-centered interest group which is grounded in this reorientation of economic activity and which attempts to dominate society through essentially bureaucratic means.
4. The societies remain capitalistic, in spite of the expanding role of the state. In fact, the expansion of the state is seen as a buttress to capitalism.
5. State capitalism fails to transform the society in its fundamental structure and is quite unstable."

Nasser's regime followed the general trend of countries that have gained their independence since the 1950s. This model has a variety of integrated components, including its tendency to reduce the private sector without abolishing it, nationalize economic resources, and control a great deal of economic activity while maintaining earlier economic relations. Waterbury (1982: 17) describes the Egyptian economy under Nasser as, "a form of semi-populist, state capitalist, developmentalist nationalism - a common form in the Third World. In that form, the state dominates the economy, but is unable to transform it either into a non-capitalist form or into a dynamic capitalist one." Because of these contradictions and difficulties, which confound any attempt to label and characterize the Egyptian state under Nasser's regime, this study adopts the concept of the *etatist* system to untangle this problem.

The *etatist* concept accounts for economic development and the expansion of welfare programs, the two main roles of the Egyptian state under Nasser. Skidmore (2000: online) contends that, "the particular forms of state economic guidance varied considerably: comprehensive economic planning and direct state ownership in the socialist bloc; import substitution in Latin America and state-allocation of credit toward growing export industries in East Asia." Nasser's regime was a mix of the socialist and import-substitution systems, with a strong inclination toward social programs. Because of this contradictory nature, this study classifies Nasser's regime as an *etatist* system.

During the fifties and sixties, state-led development/growth achieved considerable success in stimulating economic growth and industrialization in many developing countries. However, since the seventies, *statist* development strategies have failed in two respects. First, as Skidmore points out, they "failed in fostering the transition from extensive to intensive economic development" (Skidmore 2000: online). Second, state-led modernization was self-defeating; it empowered social groups who later challenged its dominance (Skidmore 2000: online). Kanovsky mentions many reasons for the failure of the state-led-growth in Egypt not only during Nasser's era, but also during the later Sadat and Mubarak governments. He (1997: online) says that:

> The state-owned industries, especially in manufacturing, suffer from gross inefficiency, over-manning and very low productivity and profitability. The loss-making state-owned firms are a serious drain on the treasury. Nasser guaranteed jobs to all university graduates, as well as demobilized soldiers, in the civil service or state-owned enterprises a policy continued by Sadat, and by Mubarak during the 1980s. Subsidies were expanded under Sadat and maintained, for the most part, by Mubarak. Price controls, foreign exchange regulations, including multiple-exchange rates, wage policies, and other measures added more distortions to the economy.[10]

In other words, state involvement in the economy, while a short-term solution for unemployment and poverty, ultimately led to a sprawling, overburdened state structure that slaved under the weight of its own inefficiency.

The *Infitah* and the Absence of the Developmental Role of the State

As mentioned before, Egypt explicitly adopted the slogans of "socialist transformation" and "the non-capitalist path" with the Socialist Decrees of 1961, but gradually dropped them after 1974. The import-substitution industrialization that had characterized the economy turned toward export-led growth, in which the state acted "as catalyst to and partner in alliances with foreign private capital and technology, and, on occasion, with the Egyptian private sector" (Waterbury 1983: 8). This does not mean that the Egyptian state entirely disregarded its socialist slogans; on the contrary, "in ideological terms, the socialist legacy was maintained, at least in name. At the same time, the private sector was encouraged, and Egypt moved toward closer economic links with the Arab oil states and then with the West" (Rivlin 1985: 5). Thus, Egypt continued to use the popular rhetoric of socialism, even as it began supplanting it with more capitalist structures.

Because of the difficulties, which resulted in the state-led economic growth policy, and the burdensome 1967 war,[11] the Egyptian state adopted the *infitah* policy in the 1970s, beginning widespread economic liberalization.[12] This policy did not start abruptly; on the contrary, the Egyptian government began instituting it in 1968, increasing its implementation in the years preceding its official announcement in 1974. President Sadat issued the October Working Paper in April 1974. It "contained ideas that

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[10]For further information on state-led growth and its cumbersome interventionist role, see Mohieldin and Nasr 1996: 34-35 and McDermott 1989: 80-81; for information on the difficulties which faced this model of development in the third world, see Waterbury 1990:257-258.

[11] For more information on the difficulties which resulted in the 1967 War, see Mohieldin and Nasr 1996:33-34.

[12] In the 1970s, many other Arab countries, including Syria, Jordan, the Sudan, North Yemen, and Tunisia, followed the direction that Egypt took with its *infitah* policy. Kerr states that, "despite considerable variations of detail from one country to another, *infitah* has everywhere included measures to relax central controls over the economy so as to facilitate the entrance of foreign capital, the productive investment of

had been worked out by ministers over the preceding six years… Ministers were chosen for their technical skills and political loyalty to the policies of the day" (Rivlin 1985: 14). The transformation from Nasser's non-capitalist path to Sadat's *infitah*, reflects the weakness of the former, particularly in the political domain (Rivlin 1985:1-10).[13]

The *infitah* policy made the private sector the engine of economic growth, lowered tariffs on imported goods, removed restrictions on foreign investments, and increased exports. "The open-door policy consisted of modest measures intended to relax official constraints imposed on management of the public and private sectors, particularly with regard to construction, tourism, and finance. An open invitation to foreign capital to invest in Egypt was made and sweetened with tax holidays" (Harik 1997: 19; see also Sonbol 2000: 153-154; Mohieldin and Nasr1996: 34-35). The most important law in the October Paper is Law No. 43/1974, which aimed at attracting Arab and foreign investment capital. An Investment and Free Zones Authority was created to deal with foreign investment.

The outstanding issue here is that from the beginning of the *Infitah* the political system in Egypt elected to depend upon foreign investments and aid. Therefore, Abdel-Khalek (1982: 261) states that the *Infitah* means, in the conception of the October Paper, that Egypt decided to open its economy to direct private investment, both Arab and non-Arab. Some scholars have suggested that, by opening itself up to outside involvement in

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domestic capital, and the movement of domestic labor out to the oil producing neighbors" (Kerr and Yassin 1984: 4).

[13] Sadat was vice-president in two periods, 1964-66 and 1969-1970. With Nasser's death in 1970, Sadat was elected as a new president.

its economy, Egypt demonstrated two elements underlying its rationale for *the infitah*: finance and technology. However, this "finance and technology" argument requires gross abstractions of social elements in the development process, and virtually equates economic growth with development. In reality, development is a much more fundamental task, involving aggressively pursuing the eradication of poverty, unemployment, and inequality. The main laws underlying *the infitah* are 1974's Law 43, and its amendment, 1977's Law 32. According to Abdel-Khalek (1982: 256), these were the most important steps on the road to *the infitah.* The main stipulations of this law are:

- Opening the Egyptian economy to foreign direct investment in almost every sector, including manufacturing, mining, energy, tourism, transportation, development of desert and barren lands, housing and urban development, banking, finance and insurance. The law left no protected sectors national investment.
- Outlawing nationalization or confiscation of privately-owned enterprises in which foreign investments were made. .
- Exempting foreign-invested enterprises from taxation for periods ranging from five to fifteen years.
- Declaring foreign-invested enterprises to be private companies that are exempted from laws and regulations that apply to public sector enterprises

The government hoped that reducing restrictions on foreign exchange would help the upper class, including government officials, and businessmen, who were engaged in construction, import-export, and consumer-goods, and had significant connections to the multinational corporations and international capital. In so doing, they hoped to further stimulate foreign investment; in fact, it increased corruption in the government. Rivlin (1985: 6) contends that, "liberalization did not replace the state with the market or even significantly reduce its role. It did increase the area of interaction between badly paid bureaucrats and rent seekers. The bureaucrats therefore acquired rent in their transactions."

The private sector did not immediately respond to the state's attempt to involve it in economic investments. On the contrary, the private sector did not become extensively involved in the economic process until the early 1990s (Harik 1997: 20).

There are many explanations for the *infitah* phenomenon in Egypt. Some of them, like Amin (1994:13), focus on the role of external agents[14] and the power of international capital:

> A very strong case can be made for the view that changing international conditions were the dominant factors behind the shift in Egypt's economic and foreign policies…after 1970. Although domestic conditions obviously play a role, including the personal inclinations of individual rulers, not to mention the underlying economic, social, and demographic conditions, the decisive factor in the case of countries like Egypt seems to lie in the international context (See also Amin 1982; Hussein 1982; Ayubi 1982).

The *Infitah* policy reintegrated Egypt into the capitalist world market, bringing it into the Western sphere of global influence. According to Ayubi (1982: 350), it pleased the capitalist world to see a country like Egypt, "with great culture and geo-political importance in the region shift to a position of close alliance with the United States of America in particular and with the West in general."

[14] Richards and Waterbury (1990: 259) illuminate that, "these external agents were (and are) the major international agencies (especially the IMF), bilateral donors, and foreign multinational corporations, especially multinational banks. The IMF has been a critical "player" in policy outcomes in Morocco, Tunisia, Egypt, Sudan, and Turkey. Arab donors have played important roles in Iraq [after the war against Iran began], Syria, Jordan, and Sudan, while multinational banks have played an important role in Turkey."

Another interpretation argues that the *infitah* was the result of Egypt's internal class structure. Mursi (1976), for example, believes that the *infitah* was an outcome of the class bourgeoisie. He proposes that a "parasitic private sector, fat with the profits of doing business with and for the state, pushed Egypt's state capitalist regime toward economic liberalization and an open-door policy. *The infitah* produced some millionaires, but it did not provide Egypt with foreign investment" (in Richards and Waterbury 1990: 410). The point here, according to Richards and Waterbury (1990: 259), "is not whether 'internal' or 'external' forces were more important; it is simply that the interaction of these forces with domestic difficulties not only created a sense of urgency (and often, a very palpable crisis) but also increased the leverage of external agents." On the external side, the bilateral donors like the United States and other Arab Gulf states had their own interest in establishing and maintaining political stability in Egypt.[15]

The Rentier State of the *Infitah* and the Extensive Policy of Subsidization

Although *infitah* moved Egypt toward economic decentralization, the Egyptian state continued its ascendancy over the economy in the 1970s, increasing the importance and centrality of its bureaucratic apparatus (Rivlin 1985: 3). Moore (1986), for example,

[15] "After the Egyptian peace agreement with Israel and its new alignment with the West in general and with the USA in particular, Egypt "has received more than $55 billion in aid over the past quarter-century from Western governments, international lending organizations such as the World Bank, the oil-rich Arab neighbors… Ironically, this aid-motivated by a desire for stability in the Middle East- helped the Egyptian government maintain a system whose failings are now recognized as a source of the alienation that may stir unrest worldwide" (Blustein 2002: A01).

argues that this privatization and decentralization was primarily “a political tactic for sustaining authoritarian regimes rather than a set of reforms for stimulating free enterprise or markets.” The reform efforts of the seventies and eighties were not real changes in the main pillars of the Egyptian economy; on the contrary, they were formal and superficial. The decision making power remained authoritarian and centralized (Harik 1997: 27). Moreover, in spite of its emphasis upon privatization and an open door policy, the bureaucratic apparatus continued to expand, offering new jobs for those who could not absorbed elsewhere. Between 1970 and 1978, government employees increased from 15 percent of the labor force (1.2 million workers) to 22 percent (2.1 million workers) (Rivlin 1985: 21).[16]

In addition, the Egyptian state continued to subsidize many necessary goods for its poor people. Unlike Nasser’s regime, the *etatsit* system in the 1970s and 1980s focused mainly on social welfare programs, not on economic development. The subsidization process during the seventies and eighties was helped by income from many external resources, as mentioned earlier.[17] Therefore, the main concern, which the *infitah* policy carried over from the *etatist* system, was Egypt’s extensive welfare system and subsidized programs. For example, in 1979 the estimated cost of governmental food and energy subsidies was £E2.9 billion. In 1980/1, subsidies consumed as much as 13% of

[16] Wahba (1994) considers state policy toward employment as an implicit subsidy. At this time, both the administration and the public sector suffered from what is called “bureaucratic inflation.” According to Wahba (1994: 150-151) “estimates of over-employment in the government administration sector ranged from a low of 20-25% according to a *Shura* Council report, to a high of 40% in 1976 according to an ILO report, while official sources give the number of employees with a ‘non-specific job description’ as 31%.”

the national income.[18] This percent was astronomical compared to former periods. For example, the GDP spent on subsides in 1948/49; 1953/4; 1962/3 and in 1973 were 2.32; 1.70; 2.32; and 3.51 respectively (Harik 1997: 93; Wahba 1994: 151; for more details about the governmental expenditure on subsidies, see Wahba 1994: 149).

Despite the dominant discourse of the *infitah*, which largely focused upon the importance of the private sector, the public sector continued to play an effective and wide-ranging role in the Egyptian economy until the early 1990s. It "remained responsible for 70 percent of investment, 80 percent of foreign trade, 90 percent of banking, 95 percent of insurance, and about 65 percent of value added" (Harik 1997: 20). The main question here is that why the public sector continued to flourish despite the rhetoric surrounding the *infitah*? There are many reasons why Egypt retained its extensive public sector until the beginning of the 1990s. The most important is that "many public-sector companies provided consumer products, including food, textiles, and medicines, at very low prices that the people could afford" (Sonbol 2000:164). In addition, the public sector was the main source of employment, and employed the majority of Egyptians; particularly within the middle class (Sonbol 2000:164). By the early 1970s, the Egyptian economy was suffering from extensive problems, including

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[17] Harik (1997:198) asserts that "the rentier economy helped Sadat stay the course, for he did not have the will, the knowledge, or the conviction to abandon Nasser's legacy."

[18] In his 1974 October Paper, President Sadat stressed that: "The public sector has paid the full amount of its transactions and contributed to the stabilization of the prices of goods." Rather than limit subsidies, the president actually emphasized them: "The state spends 150 million EL. [Yearly] to make sure that a loaf of bread does not exceed 5 cents, despite the fact that its real price is 22 cents. The state spends 7 million EL. to stabilize bus fares, although the price of one bus has shot from 5,000 to 20,000 EL" (in Sonbol 2000: 164).

slow growth in the industrial and agricultural sectors, weak performance in the public sector, a large fiscal deficit, and a prolonged trade imbalance. In stark contrast to this situation, from 1975-1979, the early years of the *infitah*, the real growth rate of the GNP averaged 8.6%. This was considered remarkably high by international standards. Most of this growth was related to the external sector, which included oil revenue, Suez Canal duties, tourism, and remittance of Egyptian workers abroad (Mohieldin and Nasr 1996: 34-36).   Thus, during the *infitah*, the Egyptian economy depended mainly on external sources, which Harik (1997: 21) calls the "rentier system."[19] Rivlin (1985: 9) affirms that, "these funds created what might be called a parallel economy; they did not bring about changes in the domestic economy (industry and agriculture) to any great extent." Rivlin calls these sectors the "rentier" sectors, because they depended on natural resources or decisions made abroad.

At the same time, the real growth rate in other sectors, such as industry and agriculture was extremely low during this period. For example, it was 1.9% in the agricultural sector. This disparity in economic growth between different economic sectors, as well as the relative decline in the non-booming sectors, i.e., agriculture and manufacturing, was symptomatic of a Dutch disease problem in the economy (Mohieldin and Nasr 1996: 34-36).

In addition, since the mid-1970s, Egypt, like many other developing countries, has suffered from the negative effects of the debt crisis. It has been crippled with heavy

[19] About the role of rentier state in the Arab countries see Luciani (1995: 211-227).

foreign debt, and suffered from servicing these debts. The loans that Egypt is currently servicing were given as a reward for attending the Camp David Accords (Hopwood 1993: 193).[20] At that time, interest rates were high (Rivlin 1985: 177); consequently, the debt crisis has continued to affect the Egyptian economy to the present day. McDermott states that in 1981, the IMF estimated that Egypt's debt was $21.18 billion, with a debt service ratio of about 25 per cent (McDermott 1989: 79). He adds that "by the end of June 1986, the World Bank was reporting debts of $35.8 billion for mid-1985, with a debt service ratio of 35 per cent" (McDermott 1989: 79). By 1987, Egypt's debts were estimated to be $42.6 billion, and constituted 29 percent of the total Arab debt of $147 billion (McDermott 1989: 79).

The *infitah* policy depended heavily on unsecured sectors and over borrowing from creditor governments. Unfortunately, this was accompanied by high interest rates and severe conditions.[21] Therefore, when the price of oil, Egypt's main export, declined by 50% between January and June 1986, the economy was not prepared to absorb this external shock. Mohieldin and Nasr (1996: 36-37) state that:

> The real GDP growth slowed down to 2.7% per annum in 1986-88, and the economy rapidly [encountered] serious difficulties. The [fiscal budget deficit] reached 23% of the GDP in 1986, excluding debt amortization and

[20] "The Camp David meeting between Menachem Begin, Jimmy Carter, and Sadat in September 1978 produced an agreement between Egypt and Israel, followed by a peace treaty in March 1979. In the treaty, Israel undertook to withdraw from the Sinai within three years. It [normalized] trade and diplomatic relations, [allowed] Israeli ships to pass through the Suez Canal, allowed the U.S. to monitor the Sinai, and limited the freedom of Egypt's activities in the Sinai. In February 1980, Israel opened an embassy in Cairo, and Egypt was ostracized by the rest of the Arab world" (Aoude 1994: Online).

[21] El-Mahdi (1997: 17) called this policy "an expansionary fiscal policy" which "relied on the expected massive current inflows of oil revenues in addition to workers' remittances, and was assisted by an era of 'easy lending' in the international capital markets during the seventies."

> the current account deficit exceeded 10% of the GDP. The external debt [reached] 119% of the GDP in 1987, with a debt service ratio of over 40% of total exports. Inflation accelerated to 25% in 1978 from an average of 17% during the preceding five years.

The Egyptian economy started the 1980s with several structural problems, Including a weak economic structure, inefficient public sector companies suffering accelerating losses, and a growing need to subsidize several production sectors, products, and wage earners. "As a result, Egypt suffered from growing fiscal deficit, escalating inflation rates, worsening balance of payment deficits, and declining international reserves" (El-Mahdi 1997: 17; El-Laithy 1997: 147-148; Mohieldin and Nasr 1996: 37).

The Economic Problems at the End of 1980s and the Beginning of the Agreements with the IMF

These economic structural problems reached their peak in May 1987 when the Egyptian government started its macroeconomic reform program with the IMF, aimed at reducing external and internal imbalances. According to this first stand-by agreement with the IMF, the essential aim of the Egyptian government was to reduce the budget deficit[22] through severe regulations, including significant cuts in consumer subsidies, increases in the price of goods and services to bring them to parity with real international prices, reform in public sector enterprises, private sector encouragement, and the

[22] In the early 80s, most structural adjustment programs focused on a narrow range of policies aimed at reducing the budget deficit.

rescheduling of part of Egypt's external debt service obligation. The Egyptian government, remembering the bread riots of 1977[23], which were caused by an increased in the cost of many essential goods, was cautious in its implementation of the 1987 reform program. Consequently, it was short lived, as the IMF terminated it after a few months, refusing to advance further drawings against the stand-by agreement after an initial disbursement in May 1987[24] (Mohieldin and Nasr1996: 38; El-Mahdi 1997: 17-18; Waterbury 1992: 184-185; Ibrahim 2000).

The regional and international context also affected the Egyptian economy in the 1990's, when Iraq invaded Kuwait. This invasion resulted in a massive influx of Egyptian workers from Iraq and Kuwait, accompanied by a concomitant loss of workers remittances, a decline of tourist revenues, and the deterioration of the investment climate. However, because of its distinguished role in the international coalition, "Egypt received significant financial assistance from the Gulf States and the USA which cancelled US$ 13 billion of its total external debt of US$ 51 billion. Egypt was also granted, in 1991, a debt/debt service relief by the Paris Club creditors equivalent to 50% of the outstanding

[23] These riots took place on January 18 and 19, 1977. The 1977 budget brought a severe reduction in subsidies, which affected many staple goods used by poor people. This reduction resulted in a 16% rise in the price of sugar, a 31% rise in the price of gas, a 12% increase in the cost of cigarettes, and a 46% rise in the price of cooking gas. The announcement of these price increases led to widespread, bloody riots. The press reported that 73 people were killed and 2,000 arrested (Rivlin 1985: 178).

[24] Harik (1997: 104) states that, "Egypt, like some other LDCs, tried to respond to the IMF's suggestions in the mid-seventies, and the officials who took that step were burned out by the destructive riots that followed. Since then they have become very careful of, and indeed resistant to, the IMF. In those cases when Egyptian officials responded to IMF recommendations, the situation had reached the disaster point, as was the case with the devaluation of the pound that followed depletion of foreign exchange reserves in 1987" (Harik 1997: 104).

debt over three phases through mid-1994 conditional upon implementing an IMF agreement" (Mohieldin and Nasr 1996: 40).

This financial assistance and debt cancellation helped recover Egypt's balance of payment and net international reserves, improving the capacity of the Egyptian government to embark on its comprehensive 1991 Economic Reform and Structural Adjustment Program (ERSAP). According to Mohieldin and Nasr1996: 41)

> This reform program has been supported by a stand-by arrangement from the IMF and a structural adjustment loan from the World Bank, in addition to the bilateral debt forgiveness/debt service relief of the Paris Club. The primary objective of ERSAP is summarized by the IMF as 'to create, over the medium term, a decentralized, market-based, outward-oriented economy, where private sector activity will be encouraged by a free, competitive, and stable environment, with autonomy from government intervention. For this purpose, controls on economic activity and investment were to be dismantled, and primary reliance was to be placed on market forces for resource allocation' (see also El-Mahdi 1997: 18-19).

The main aim of applying the economic reform and structural adjustment program in 1991 was to shift from a planned economy to a market-based economy. The essential components of this program were:

> A major reduction in the fiscal deficit, initiation of financial liberalization; including decontrol of interest rates and unification of Exchange Rate system, establishment of treasury bill market, liberalization of most prices and adjustment of energy prices to come closer to their opportunity costs; real and financial sector reforms, as well as privatization and public enterprises reforms. The aim is to deepen the structural reforms in order to put in place an economic environment conductive to a strong and sustainable supply-side response from the private sector (El-Laithy 1997: 148; see also Weissman 2001: 85).

After applying the structural adjustment policy in an extensive and intensive way in Egypt in 1990s, the *etatist* system of Nasser and Sadat has lost its two main components: its developmental and welfare agendas. In short, the *infitah* policy resulted from two pressures upon the Egyptian state: (a) external demands of international institutions and foreign investment and (b) Egyptian neo-interest groups, such as that sector of businessmen who were integrated with the international capitalist market. [25]

[25] Richards and Waterbury (1990: 257) believe that "the *infitah* phenomenon must be understood as, at least in part, arising from the exigencies of the development process itself, as well as from the international economic conjuncture." Similarly, Stallings (1992) does not believe that international variables can provide a total explanation; domestic variables continued to play an important role, even in the 1980s. His "argument is that international factors are crucial in explaining broad shifts in policy, both in contrasting the 1980s with the 1970s and in explaining changes within the decade of the 1980s. They are also useful in accounting for variation across countries, but for that purpose, domestic factors are essential too" (Stalling 1992: 43). For Mohieldin and Nasr (1996: 34) the 1967 War was not the main reason for putting new pressure on the government to change the socialist economic orientation of the 1960s. "The *infitah* policy was a response both to internal economic problems related to the heavy state intervention and to major changes in the international economic and political environment." Sonbol (2000: 153-154) asserts that the *infitah* policy came in response to both national and international pressure.