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The Political Economy of Reform in Egypt:

Understanding
the Role of Institutions

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Introduction

Egypt's economic reform was initiated in 1991 within the context of stabilization and structural adjustment programs. And since the appointment of Prime Minister Ahmed Nazif and his ministerial economic team in 2004, reform has been pursued more intensely, apparently taking new directions. The government has implemented a number of reform measures and has announced concrete plans to restructure the financial sector, adjust regulations, enhance trade liberalization, and privatize most state-owned enterprises.

As a result of reform efforts, and over the past three years, Egypt has managed to stabilize the economy, increase foreign currency reserves, and achieve steady growth. Reform programs have introduced effective amendments in the social contract between the state, market, and society. Yet little if any progress has been made in the fight against corruption and in creating an enabling and competitive business environment. The current institutional environment poses critical questions about the capability of the Egyptian economy to sustain growth; to create decent jobs for the unemployed, the underemployed, and new entrants into the labor market; and to alleviate massive poverty. These failures to address socioeconomic problems and curb the side effects of economic reform are proving key impediments to accelerating the reform process in Egypt.

The reform process in Egypt suffers from the lack of a consensus on the meaning and ramifications of reform among key national stakeholders. Debate with the state over economic reform is more or less limited to major private-sector actors, who are often close to the regime or part of it. This debate centers on the costs and benefits to these actors. The majority of the private sector, represented by small and medium-sized enterprises (SMEs) and members of civil society, especially workers and grassroots organizations, is excluded from the debate with the state over Egypt's economic reform strategy.

This paper demonstrates that Egypt needs to make a greater investment in building efficient, transparent, and dynamic institutions in both the public and private sectors, as well as in civil society, to more effectively coordinate economic reform with a wider scope of ownership and stronger ties to social policies. Such dynamic and transparent institutions are crucial for sustaining strong economic growth while promoting equity, facilitating employment expansion, and encouraging a rise in productivity. Such institutions are also necessary for enhancing social partnerships between the state, the private sector, and civil society. Developing these collaborative partnerships—enforced by a new social

contract that enjoys consensus among the various sectors and actors—will be conducive to advancing economic reform in Egypt.

The paper examines the state of the Egyptian economy before the reform era and the various generations of policies implemented as part of the country's economic reform programs. In exploring the extent and limits of these programs, the paper highlights the different parties affected, including the winners and losers as well as the supporters and opponents of reform. It is hoped that the combination of areas covered in the paper will contribute to a comprehensive assessment of the achievements and challenges pertinent to reform in Egypt, shedding some light on what can be done by the Egyptian government to promote a better-coordinated reform process, which, as mentioned above, will allow for an expanded scope of ownership while effectively addressing the country's social and economic challenges.

Paradigm Shifts in Economic Policy

Egyptian economic policy witnessed three paradigm shifts during the period extending from the second half of the twentieth century to the start of the reform period in 1991. These shifts affected the role played by the state in the Egyptian economy and the economy's position in the international market. The first shift followed the end of the British colonization era, marked by the 1952 revolution. At the time, feudal and semifeudal relations ruled over rural areas, while the private sector dominated commerce and small industries. Direct government intervention was limited to protecting national industry and controlling foreign currencies.¹

From 1952 until 1973, the Egyptian economy experienced a process of transformation through a state-led industrialization model. The public sector was developed to be the main engine of growth and was responsible for the major part of new investments and employment. The state spent heavily on public infrastructure and social services, and engaged in land reform. The Egyptian president, Gamal Abdel Nasser, nationalized the Suez Canal in 1956. Further large-scale nationalization in 1961 effectively restricted private-sector activity to agriculture, real estate, and the informal economy. Even these sectors were subject to centralized controls over prices, marketing, raw materials, and foreign exchange. State-owned enterprises (SOEs) monopolized the banking sector, the manufacturing sector, and foreign trade, as well as the bulk of the transportation sector. In addition, the government exercised high protective measures over the economy and pursued import-substitution policies.

State control over the economic sphere was officially institutionalized in the National Charter of 1962. The state introduced policies to secure government employment for those with a secondary school diploma. In addition, the state provided subsidies for a variety of goods, including basic foodstuffs, utilities, electricity, and water. The state's large military expenditures and the effects of

the wars of 1967 and 1973 weighed heavily on the economy, and the country was not able to sustain high rates of economic growth. According to World Bank data, average growth declined from 7.52 percent during the period from 1959/1960 to 1964/1965 to 2.85 percent during the period 1964/1965 to 1973.

The second paradigm shift in the Egyptian economic policy took place in 1973 with the launch of the *Infitah* or Open Door Policy. The Egyptian president, Anwar al-Sadat, presented the October Paper, which called for opening up the Egyptian economy to foreign investment and inter-Arab joint investment projects, as well as promoting the role of the private sector in the economy. Based on these guidelines, Law No. 43 of June 1974 was promulgated; it allowed tax concessions for foreign private firms in the form of tax holidays, exemptions from labor laws, import/export licenses, and exchange rate control regulations. The law distinguished between foreign investments in the Free Zones (for example, Port Said), where tax holidays were indefinite and joint ventures with local firms were not required, and inland projects, in which setting up partnerships with local firms was required.

Between 1974 and 1985, the economy grew at an average rate of 8 percent a year. However, this seemed to be encouraged by a series of windfall rents: high oil prices; Israel returning the Sinai oil fields; the reopening of the Suez Canal; and remittances from Egyptian workers in Arab countries, which created a large influx of foreign exchange. The state redistributed its increased revenue. For the lower end of the income distribution, it increased its subsidy payments and continued the guaranteed employment scheme initiated under Nasser. For those at the upper end of income distribution, the state created conditions for lucrative investment opportunities in imports. An overvalued exchange rate, coupled with the creation of the Free Trade Zone of Port Said, led to the exponential growth of imports and luxury goods. Competition from imported goods reduced the demand for domestically produced goods, leading to underutilized capacity in domestic industry.

Financing took place mainly through costly short-term credit and at the very high commercial interest rates prevailing at the time. Imports soared and exports fell, mainly due to a fourfold rise in the price of U.S. wheat imports during the period from 1973 to 1976. At the end of 1981, Egypt's foreign debt had amounted to more than 100 percent of its gross national product. External indebtedness would leave the state vulnerable to its creditors and to geopolitical instability, consequently threatening its social and political legitimacy at home. In January 1977, under pressure from the International Monetary Fund, the government proposed raising food prices; in response, popular riots broke out in Cairo. Due to these riots, the government abandoned these procedures and decided to remove subsidies gradually, while avoiding publicly announced reductions and the phasing out of subsidies.

The third paradigm shift in Egyptian economic policy took place in the aftermath of the boom decade that ended in 1986. Since the mid-1980s, Egypt has accelerated the policy of opening the economy and continued fiscal expansion. These policies had coincided with the crash of oil prices in 1985–1986. This crash had a dramatic impact on the Egyptian economy, because its main sources of revenue—the Suez Canal, petroleum exports, tourism, and remittances from Egyptian workers abroad—shrank sharply and were no longer able to sustain the economy. The boom that Egypt had witnessed in the previous decade, since the government launched its Open Door policy in 1974, had encouraged the expansion of public-sector expenditures, in particular through public employment and subsidies. Consequently, fiscal deficits rose, averaging about 15 percent of gross domestic product (GDP), and debt accumulated.² As a response, an expansionary monetary policy was adopted, leading to a rate of inflation close to 20 percent. Exports dropped, and the current account witnessed a deficit of around 8 percent of GDP in 1989, constraining the servicing of external debt and leading the government to resort to exceptional financing of about \$14.1 billion from 1987 to 1991. Confidence in the economy dropped, and the need for reform became clear. This led to the arrival of the IMF and World Bank in Egypt and thus to the country's adopting their stabilization and structural adjustment policies.

The Post-1991 Reforms: Three Generations

Three generations can be identified in the current economic reform process that began in 1991 with the main objectives of stabilizing the economy and generating sustainable economic growth. To achieve these objectives, the government has adopted reform programs based on reducing the role of the state in the economy (including liberalization and privatization), adopting market-based economic principles, increasing the global integration of the Egyptian economy by opening it to outside competition, encouraging exports, and increasing the economy's dependence on domestic revenue.

The first generation of reform, from 1991 to 1998, started with the launching of a successful stabilization effort. In January 1991, the interest rate on Egyptian pounds was liberalized; and in February 1991, the government decided to liberalize the foreign exchange market and to establish primary and secondary markets. In October 1991, these two markets were merged into one market. In 1991, foreign currency exchange became no longer limited to commercial banks, leading to stability in the currency. The government signed an economic stabilization program with the International Monetary Fund in May 1991 and a structural adjustment program with the World Bank in November 1991. This period witnessed the successful stabilization of the economy and serious privatization efforts, which resulted in about one-third of all SOEs' assets being privatized between 1991 and 1998.

In June 1995, Egypt joined the World Trade Organization. In 1997, it signed the Greater Arab Free Trade Agreement. In 1998, the country graduated from its third IMF program, with a record of successful macroeconomic stabilization and partial privatization efforts.

The second generation of reform, from 1998 to 2004, focused on trade and institutional measures. Several external and internal factors had pushed for this reform. External conditions had become more difficult after the global financial crises that many countries witnessed during the period 1997–1999. Internal factors that lessened confidence in the economy included the 1997 terrorist attack in Luxor, which resulted in the killing of 62 people, including 58 tourists, and the “loan deputies” financial scandal. This scandal involved five former members of the People’s Assembly who were accused of using their political positions to get about LE 1.5 billion in loans from corrupt officials in state-owned banks. These internal events had repercussions for both the growth path of and trust in the Egyptian economy.

During this period, efforts to introduce new legislation intensified. In 2001, a Real Estate Mortgage Law was enacted. The year 2002 witnessed extensive economic reform measures on the legal level. Laws were promulgated pertinent to Special Economic Zones, export promotion, intellectual property rights, chambers of commerce, and money laundering. These were followed by a unified banking and Central Bank Law in 2003.

In January 2003, the exchange rate was liberalized. As the currency depreciated, the prime minister issued Decree 506 binding exporters to sell 75 percent of the foreign currency they received to banks in Egypt. But this decision was canceled at the end of 2004 because it was deemed unconstitutional, and the currency has since depreciated.

During the same period, Egypt signed a number of trade agreements, including the Trade and Investment Framework Agreement with the United States in 1999; a free trade agreement with other countries belonging to the Common Market for Eastern and Southern Africa in 2000, and the Agadir free trade agreement with Jordan, Morocco, and Tunisia in 2004. The EU Association Agreement came into force in June 2004, after trade-related issues came into force on a provisional basis in January 2004. Egypt’s participation in the World Trade Organization, combined with the various trade agreements it has signed, has pushed the country to reform its trade policies and to be more sensitive to international standards, especially in the agriculture and industrial sectors. Dobronogov and Iqbal demonstrate that the Egyptian economy became more sensitive to growth in countries belonging to the Organization for Economic Cooperation and Development (OECD).³ They show that in the period 1988–2003, GDP growth rates in high-income OECD countries had a simple correlation of 0.70 with GDP growth rates in Egypt, 0.53 with the growth of gross domestic fixed investment (GDFI), and 0.69 with the ratio of GDFI to GDP.

Finally, Egypt has been witnessing the third generation of reform since Ahmed Nazif became prime minister in July 2004. Since his appointment, the reform process has intensified. Between 2004 and 2005, many laws were introduced, including laws on e-signatures, new investments, customs, antitrust and competition, a unified corporate tax, and antidumping; in addition, export-import regulations were amended. A new Consumer Protection Law was passed in 2006. In 2004, the weighted average tariff was cut from 14.6 to 9.1 percent. In February 2007, it was further reduced to 6.9 percent. In December 2004, Egypt signed the Qualified Industrial Zone Agreement with the United States and Israel. In December 2005, Egypt signed a free trade agreement with Turkey.

In addition, the pace of privatization was accelerated during this period. Between mid-2004 and mid-2006, a number of public-sector companies, joint ventures issuing public stock, and public land areas were privatized, valued at about 16 billion Egyptian pounds. In addition, in July 2006, Egypt granted its third mobile telephone network license to a United Arab Emirates–Egyptian consortium for \$2.9 billion.

The government launched a comprehensive financial sector reform plan in September 2004. By late 2006, more than half the banking sector had become privately owned. In June 2005, banks began to be required to have a minimum of LE 500 million in paid-up capital. Since the launch of the plan, most joint-venture banks have been sold to the private sector, with the most notable sale being that of the Bank of Alexandria to a foreign bank in December 2006. As a result, the majority of banking assets have been placed in private ownership. In addition, over half of private-sector nonperforming loans (NPLs) were restructured by mid-2006, with public-sector NPLs being cleared with a capital infusion by the government since 2005, mostly from privatization receipts.

The government has also worked to make the Egyptian economy more open by setting up an interbank market in 2004 where banks could freely trade foreign exchange and removing the surrender requirement on export proceeds. Many steps were taken to improve the fiscal position of Egypt. Prices of subsidized fuel were raised in September 2004 and July 2006, and prices of electricity were increased in December 2004. The Income Tax Law was modified in 2005, with the aim of simplifying the rate structure, broadening the tax base, cutting down personal and corporate income tax rates, and setting a higher minimum threshold. The stamp tax was broadened and streamlined in August 2006. Public expenditure management reforms have been ongoing since 2004, with a focus on upgrading budget classifications, establishing a Treasury Single Account, and rationalizing financial relations among general government institutions. In addition, the government launched tax administration reforms, established a large taxpayer unit in 2005, and merged its income tax and indirect tax departments in 2006.

A number of other changes have also been introduced at the institutional level. In August 2006, the Ministry of Planning was abolished, with the minister

of state for economic development assuming the duties of the minister of planning. To improve the transparency of economic policy, Egypt subscribed to the Special Data Dissemination Standard in January 2005, and since 2005, following monetary policy meetings, it has published a monetary policy statement and communiqués.

The Rewriting of the Social Contract and the Elites Behind It

The process of reform initiated in 1991 has resulted in significant changes in both the Egyptian economy and the nature of the social contract between the state and society. The nature of the old social contract was defined in the Egyptian Constitution (adopted in 1971 and amended in 1980). The Constitution stated clearly that the economic system in Egypt was a socialist democracy that places a significant emphasis on socialist principles and central planning (articles 1 and 4). Employment was considered “a right, a duty, and an honor guaranteed by the state” (article 13), social and health services were also guaranteed by the state (article 16), and state-sponsored education was free (article 20). The Constitution also gave the state the lead role in managing and allocating resources by giving the public sector the dominant role in the economy and focusing on central planning to achieve development in the country.

The various generations of reform since 1991 have contributed to introducing changes in the social contract. These changes were affirmed, in writing, when the Egyptian Constitution was amended in March 2007. Some of the most relevant modifications are found in article 4, which deals with the nature of the Egyptian economy and social equity, and in article 24, which deals with the role of the state in the economy. These articles, in their amended format, give market forces a major role in the economy while assigning the state the responsibility of regulating the economy. This contrasts sharply with the old social contract, under which it was primarily the role of the state to allocate resources, manage the economy, and determine its outcomes, as well as guarantee the provision of social welfare services, including securing employment for the masses; offering social services, especially health and education; and providing citizens with income support—subsidies—without imposing high taxes on them.

Understanding the significance of this shift requires looking more closely at the actors and process that led to the recent written changes in the social contract. In effect, the Egyptian government’s acceleration of the shift from a state-dominated economic model to a market economy since the early 1990s has generated support among certain sectors of the Egyptian population while at the same time alienating other sectors.

The political elite and state officials were in general skeptical about reform, especially the privatization of SOEs. They feared losing political and economic patronage options and rents as a result of reform. Nevertheless, they had to succumb

to the prescriptions of the international financial institutions at a time of financial crisis. It is important to emphasize that their hesitancy did not indicate genuine and effective opposition to reform. On the contrary, the Egyptian political elite recognized the desirability of reforms but were concerned that these reforms, if conceivably taken too far, could undermine their own power. This hesitancy, which dictated the speed, breadth, and depth of reforms, was held by the political establishment itself and thus did not represent a form of opposition.

The regime has struggled to maintain the support of state officials and the political elite on the one hand and to push—to a limited degree—the reform agenda on the other hand. The regime was aware that fundamental changes in the structure of the public sector and a fast privatization process would threaten its support base. Hence, it opted for a postponement of important privatization steps to avoid threatening the established relations with those elite members who had been supportive of the regime. But the regime also invested much effort in removing obstacles and reducing hesitancy about the implementation of the reform agenda. A good example in this regard is the replacement of Minister of Trade Ahmad al-Guwaily and the merging of his portfolio with that of the pro-reform Minister of the Economy Youssef Boutros Ghali in 1999.⁴ Prime Minister Atef Ebeid, along with his reform team and their allies in the business community, supported acceleration in trade liberalization, whereas Guwaily had introduced restrictions on imports the year before to curb Egypt's trade deficit. Similarly, it was reported that former prime minister Kamal al-Ganzouri was removed from office in 1999 because he was not clearly in support of privatization.⁵ However, it should be noted that a major reason for the reluctance of government officials to support reform is the priority given to political and regime stability, which could be challenged by new groups gaining power as a result of market reforms.

Given the nature of Egypt's public sector, which plays a major role in employment and providing privileges to senior officials, it was expected that public-sector managers would be the most opposed to reform out of fear of losing their jobs in case of privatization. Although this was indeed true in many instances, not all managers reacted this way. In fact, many used their access to public money and networks to establish their own private companies or purchase other SOEs. For example, throughout the early 1990s, leading government officials of the Holding Company for Public Works actively cooperated with the majority of their employees in privatizing company affiliates.⁶

Support for economic reform policies—and, crucially, for their implementation—came from and was shaped by two main sources: those actors whose economic opportunities and influence would be increased by the reform, and those groups that are politically loyal to the regime because they are close to it or are already part of the establishment. A further important determinant of the situation is the limited role of formal business and labor representative institutions in shaping economic policy, an issue explored in greater detail below. Indeed, a

direct link with the regime has proven more beneficial for business and union leaders than institutional channels such as membership in business associations or labor unions.⁷

The main support for reform efforts comes from the well-connected and very wealthy business elite, who are often close to the regime or even part of it. They are, therefore, very influential in both the political and economic realms, which is a reflection of the close association between wealth and political power in Egypt. A good example of this kind of relationship is Ahmed Ezz, the chairman of El-Ezz Steel, the largest company in the country's steel industry, which it dominates with about a 70 percent share. Ezz is a high-ranking member of the ruling National Democratic Party (NDP) and also the chairman of the People Assembly's Budget and Planning Committee. He is also a close associate of Gamal Mubarak, President Hosni Mubarak's son.⁸

A recent trend signaling the increasing political power of the business elite has been the appointment of major businesspeople to key government posts. To list a few, Minister of Foreign Trade and Industry Rasheed Mohamed Rasheed was the president of Unilever AMET (Africa, Middle East, and Turkey); Minister of Tourism Mohammed Zoheir Wahid Garana was the owner and managing director of Garana Travel Company, one of the largest companies of hotels, floating hotels, and travel companies; and Minister of Agriculture Amin Ahmed Mohammed Osman Abaza founded Nile Cotton Trade Company, "which became the no. 1 cotton-exporting company."⁹

Business circles have influenced the way reform policies were implemented. In general, men with connections to the Egyptian government or military institutions benefited from favorable business terms, and the implementation of Egypt's privatization program favored the wealthy business elite—or the "whales," as they are known locally. An example is the sale of Coca-Cola in 1993 to businessman Mohamed Nosseir. According to Sfakianakis, Nosseir's relations with the then-minister of the public business sector, Atef Ebeid, allowed him to make the purchase with little competition. Nosseir would go on to sell the company after two years at more than triple the acquisition price.¹⁰ Another example was the move in the late 1990s to involve the private sector in the state cinema industry. Only two families were allowed to bid for and to operate the cinemas, due to connections with Egyptian politicians. The lack of a competitive environment has also led to distrust of the aims of reform. An important example of making large gains in an uncompetitive environment is the case of the Zayat family in the beverage industry.¹¹

The business elite had in the past lobbied to preserve high import barriers and state contracts. As networks grew and state bureaucrats and businesspeople grew wealthy, they worked to slow down reform—or at the least redirect its path to advance their own interests. The business elite also opposed movement toward increased transparency and competitiveness that would open more space for competing actors. It is important to highlight that the reluctance of

the business elite was less toward reforms per se; it was rather motivated by a desire to preserve the early benefits of reform and to maintain their influence in the economy. It should be noted, as well, that many business groups appeared to be opposing reform in the beginning but then adjusted their approach as reform measures looked increasingly unavoidable. Thus, they have attempted to adapt to the changes created by reform policies and reap the benefits of the new economic opportunities before they went to others.

Although the business elite has been very influential in shaping reform efforts, as well as determining the outcomes and reaping the rewards, SME businesspeople have been too weak to have any influence on the reform process or its outcomes. This situation is related to two main factors. The first is their lack of participation in the reform process. The debate surrounding the nature and means of reform as well as reform plans and their implementation has been limited to a small group of technocrats, members of the Cabinet, and high-ranking members of the NDP. The second factor is the lack of representation of SME businesspeople in the People's Assembly, and hence in committees that deal with reform issues, in contrast to the significant representation of the business elite. A report published by Al-Ahram Center for Political Studies shows that the number of businesspeople in the People's Assembly grew from 31 out of 350 in 1995 to 77 in 2000. The current People's Assembly includes 68 businesspeople, the majority of whom are from the banking and commercial sectors. The report also indicates that to gain seats in the current Assembly, businesspeople spent between LE 3 million and LE 15 million on the 2005 parliamentary campaign, in addition to substantial grants offered to the NDP in the form of donations. For example, Essam El-Din argues that Ahmed Ezz funded President Mubarak's presidential elections campaign and Hani Sororo spent more than LE 6 million in 2005 refurbishing the NDP's office in Cairo's downtown district of Al-Dhaher.¹²

Social and Economic Outcomes

Although, as shown above, Egypt's various generations of reform have led to deep changes in the social contract, have these generations also helped the country address its major socioeconomic problems and improve the living conditions of its citizens? There is no doubt that Egypt has engaged in a reform process that has been serious though slow, especially in public-sector reform, and at the same time uncoordinated with sectoral policies targeting socioeconomic problems, including various economic sectors, the informal economy, and SMEs. The evidence suggests that the outcomes of reform have been mixed. Egypt has managed to stabilize its economy, achieve steady growth, and increase foreign reserves; but the country still faces almost the same major social and economic challenges, including widespread poverty and unemployment, high inflation and a large public debt, and dependency on remittances and aid. In addition,

little if any progress has been made in the fight against corruption and in creating an enabling and competitive business environment. Finally, the question of the sustainability of growth is a serious concern, given that the country's current economic boom is largely attributable to external factors.

The Egyptian economy has registered strong growth in recent years, with real GDP growth rates of 4.1 percent in 2004, 4.5 percent in 2005, and 6.8 percent in 2006. In nominal terms, exports grew from \$7 billion in 2001/2002 to \$18.4 billion in 2005/2006, or by 160 percent. As a proportion of GDP, exports more than doubled from 7.6 percent to 17.3 percent. After registering deficits, ranging from 1 to 3 percent of GDP between 1997 and 2000, the current account has picked up since 2001, registering a surplus of 5 percent in 2003 and 2004, and 2 percent in 2005, in large part because of increased exports of petroleum products. The overall investment level reached 18.7 percent of GDP, and foreign direct investment grew to 6 percent of GDP (\$7.2 billion). The country's balance of payment account registered surpluses of \$1.8 billion in 2005 and \$1 billion in 2006, which has helped the Central Bank increase its foreign reserves, which reached \$22.7 billion (excluding gold) at the end of October 2006.

The budget deficit decreased from 9.6 percent in 2004/2005 to 8.2 percent in 2005/2006, before rising slightly to 8.5 percent in 2006/2007. Privatization and corporate taxes were the main contributors to curbing the public deficit. The public debt stood at 77 percent of GDP at the end of 2006/2007, compared with 81 percent in 2005/2006. In the previous few years, the public debt had risen from 71 percent of GDP in 2000/2001 to 93 percent in 2004/2005. One should welcome such macroeconomic results. The main challenge for Egypt is to sustain this performance.

Egypt's current economic performance has been fueled by external factors that represent important elements of recent growth: the improved prices for the country's subsoil assets, the increase in Gulf oil revenue resulting in higher investment in the country, and the rise in remittances from abroad.¹³ The recent positive trend in remittances has been driven by the rise in oil prices and the increasing income from expatriates in the Gulf region, which rose from \$3.3 billion (4 percent of GDP) in 2004 to \$5 billion (6 percent) in 2005. In the past, workers' remittances reached an all-time high of \$6.1 billion (15 percent of GDP) in 1992, before falling to \$5.7 billion (12 percent) in 1993; they averaged \$3.2 billion (4.3 percent) over the period 1994–2003. Despite their recent rise, remittances remain much lower than the level of services exports, estimated at \$14.6 billion (17.5 percent of GDP) in 2005, thanks to the soaring tourism industry and revenues from the Suez Canal.

Egypt also receives significant flows of aid, mainly from the United States and the European Commission, due to its political and strategic importance. Net development assistance to Egypt reached \$926 million (1 percent of gross national income, GNI) in 2005, compared with \$1.46 billion (1.9 percent

of GNI) in 2004 and \$987 million (1.2 percent) in 2003. The biggest donor to Egypt is the United States, which contributed \$397 million in 2005, \$705 million in 2004, and \$442 million in 2003, followed by the European Commission, which contributed \$183 million in 2005, \$184 million in 2004, and \$59 million in 2003.

In addition to these factors, a closer look at Egyptian export growth shows that it has been shaped by natural resources and energy-related factors more than labor-intensive manufactures, and the larger registered foreign investment has benefited from the sale of the third wireless telecommunications license.

Another issue to be raised in evaluating economic reform programs is the limited reduction in the size of state employment. Private-sector employment accounted for 70 percent of total employment in 2005, compared with 67 percent in 1990. Though the share of employment in SOEs declined during this period from 10 to 5 percent, the share of government employment actually increased from 22 to 26 percent, after registering a decrease in recent years. The Egyptian state is caught in a quandary. On the one hand, it wants to pursue reform efforts because its current economic conditions and external pressure from international financial institutions do not permit it to pursue expansionary measures and policies of granting subsidies. On the other hand, the social and political price of abandoning this role and public spending programs has been greater than what could be borne by the Egyptian state; it has been faced with resistance from people who are negatively affected by these measures, as is shown below.

So far, the government has succeeded in maintaining a delicate balance by proceeding with economic reform—to a limited extent—without alienating the business and political elite that is close to the regime or part of it and while keeping in check popular resistance to reform. From 1990 to 2005, the compensation of employees decreased from 31 percent of public expenditures to 24 percent, after having fallen to 19 percent in 1992. During the same period, goods and services expenses fell from 26 to 7 percent of total expenses. Interest payments' share fluctuated during this period, going from 19 percent in 1990 to 18 percent in 2005 (having reached a high of 36 percent in 1994), before rising again to more than 23 percent in 2006. Subsidies and other transfers increased from 12 percent in 1991 to 33 percent in 2005. This was mainly the result of rising food and oil prices. Drastic subsidy cuts remain a politically sensitive issue. On the revenue side, the share of other taxes in total revenue fell from 13 to 3 percent; the share of taxes on goods and services rose from 16 to 26 percent; and the share of taxes on income, profit, and capital gains increased from 23 to 25 percent—while the share of taxes on international trade dropped from 17 to 12 percent.

The overall impact of labor market reform has been mixed. Official statistics show that unemployment decreased from 11.7 to 8.3 percent between 1998 and 2006. New entrants into the labor market face the greatest difficulties in

finding jobs. Therefore, unemployment is mostly concentrated among youths in the age range of 15 to 24 years, with university graduates being the only education group that witnessed an increase in unemployment during the period. It should be noted that many graduates typically wait for years without looking for work in the private sector in the hope of finding employment in the public sector, where the work conditions are better, particularly for women. However, it seems that expectations are being modified as the chances of securing state employment are decreasing.¹⁴

Although it is obvious that more jobs have been created during the reform era, the evidence shows that these jobs have been created in sectors with low productivity. Indeed, while the share of agriculture in total employment declined from 40 percent in 1990 to 30 percent in 2003, the share of manufacturing also declined from 14 to 11 percent. In contrast, the share of trade and tourism rose from 9 to 13 percent, and the share of services rose from 22 to 27 percent, with an important role for the informal economy. A closer inspection of the sectoral composition of GDP at constant prices reveals that agriculture contributed to 15.5 percent of GDP in 2005/2006, compared with 16.5 percent in 2001/2002. Manufacturing contributed to 18.9 percent in 2005/2006, in contrast to 19.8 percent in 2001/2002. In contrast, over this period the contribution of gas increased from 2.9 to 4.7 percent of GDP, the contribution of restaurants increased from 1.8 to 3.3 percent, and the contribution of the Suez Canal increased from 2.3 to 3.4 percent. In other words, the recent growth pattern is not in productive sectors with the potential of enabling sustainable employment growth. A related feature is that Egyptian exports have become less diversified during the reform period, because the top twelve export items constituted 59 percent of total exports in 2003 compared with 37 percent in 1992. In addition, the new exports introduced during this period are of low value.¹⁵ Because the diversification of the export structure is associated with economic development, this should be a matter of concern for policy makers.

At the social level, Egypt still faces severe challenges. Reform efforts have failed to adequately address the issue of high inflation. In fact, high inflation has been partially created by the reform measures. Consumer price inflation registered a rate of 11.3 percent in 2004, 4.9 percent in 2005, and 7.7 percent in 2006. The main factors influencing it are higher food prices, especially for meat, as a result of avian influenza fears, rising domestic demand after the cut in income tax rates, and the reduction in subsidies of oil products. As a result of rising costs of living, the government has to take more carefully into account the higher social and political costs linked to furthering subsidy cuts.

In addition, poverty is widespread in Egypt, affecting 41 percent of the population, or about 28 million people in 2005, slightly less than the 43 percent noted in 2000. However, *absolute* poverty increased during this period from 17 percent in 2000 to 20 percent in 2005. Rural areas had a poverty rate of 52 percent, almost double the rate of 26 percent in urban areas, with rural Upper

Egypt home to 51 percent of Egypt's poor population. One reason for increased poverty is high inflation, especially after the devaluation of the currency, because the relative price of food increased by 10 percent. In 2005, transfers represented 11 percent of incomes for the poor and 22 percent for the nonpoor. The reason is that about two-thirds of social transfers came from pensions, and 85 percent of pension spending goes to the nonpoor. Thus, social safety nets did not significantly benefit the poor, who relied more on remittances and subsidies in their spending.¹⁶

There is also a regional disparity in the level of economic development in Egypt. The rural regions, mainly in the south, have shared fewer of the benefits of economic growth than the north, which is more powerful politically. This has encouraged significant migration from rural to urban areas. In its latest five-year plan, the government aims to encourage investment in regions that were previously given less attention and have remained underdeveloped, such as in Upper Egypt. The plan also calls for increasing fiscal and administrative decentralization and promoting public participation, preserving natural resources and the environment, and engendering development.

Economic and Political Opposition

Opposition to reform efforts has been driven by three main factors. The first factor consists of ideological considerations marked by a lack of consensus on the nature and tools of economic reform, on the one hand, and the absence of effective participation by various stakeholders in the process and implementation of reform programs, on the other hand. Underlying the second factor are socioeconomic concerns. Many reform policies have been predicted to increase the gap between the Egyptian rich and poor before the masses can feel the positive effects. With unemployment and poverty already high, this has provoked resistance to reform from Egypt's poor. Second, the consistent failure of reform efforts to address socioeconomic problems and the perception that this reform has generated more damages to society than benefits has fueled the drive to oppose the current reform efforts. Finally, the third factor driving opposition to reform efforts has been the efforts of certain members of the economic and political elite to secure their privileges in current and future economic arrangements, as was detailed above.

The position of civil society, especially political parties (apart from the NDP) and small grassroots organizations, vis-à-vis current reform agendas is totally different from the position of the business and political elite, who are often close to if not part of the regime. Though civil society members agree with the government on the need for reform, they totally disagree on the nature and tools of reform. There are three main reasons for this disagreement. The first is ideological. The idea of a market economy is rejected by many actors in civil society, based on the assumption that following market-friendly policies would

lead to empowering certain groups—the well-connected business and political elite—at the expense of the majority of the population. For example, some groups in civil society have concerns that privatized companies, when exposed to competition and profit incentives, will inevitably lay off workers. In addition, the poorer sections of the population, who are expected to suffer a decrease in subsidies, feel hostile toward economic reforms. The second reason is that the privatization of SOEs leads to selling national assets to foreign companies, which is perceived as leading to an increase in foreign influence and interference in Egypt. The third reason is related to the speed of reform, especially in opening the economy to external markets and investors. The main argument put forward in this regard is that the Egyptian economy is neither ready for such an open system nor capable of competing in the international market. Therefore, such steps would harm the economy, and especially SMEs.

The impact of this opposition on the reform agenda is limited. Such limitations are mainly related to three interlinked factors. The first is the absence of specific programs and visions that counter the current economic reform agendas. Even the economic program of the Muslim Brotherhood—which enjoys relatively better institutional capacity, compared with other secular and leftist political parties—is quite general and does not propose alternative economic policies. The discourse among these parties and the argument with the government is mainly shaped by disagreement about the accuracy of major social and economic indicators—especially for poverty, unemployment, and public debt—and accusations of corruption and lack of accountability and transparency, primarily targeting government officials and political leaders.

The second interlinked factor is the lack of sufficient political space for civil society and the government's control over many civil society institutions. Many international reports have criticized Egypt for its limited space for political parties (especially for their activities and the freedom of assembly). Recent constitutional amendments were a step backward.¹⁷ In addition, the government controls civil society institutions, and it thus mobilizes their leadership to support its agendas and programs.

The third interlinked factor includes the internal weakness and problems of civil society in Egypt. Business associations and labor unions are often run to promote the personal patronage of their leaders, and they do not enjoy autonomy from the state, which manipulates them through direct links with their leaders. Most political parties have not yet elected new leaders, and they are becoming increasingly disconnected from the population and their daily problems. In the meantime, the population itself is increasingly avoiding political activities, partially because of the severe restrictions imposed by the government on such activities, the lack of trust in political parties, and the accumulation of social and economic problems faced by the majority of the population. Together, these three factors do not give ordinary Egyptians the time and courage to be politically active.

It should be noted, however, that some civil society organizations and activists in Egypt are becoming more organized. They are advocating for their rights and confronting the problems that the groups they represent are suffering from. Traditionally, labor unions in Egypt have been controlled by the regime, because unions are bound to be part of the state-controlled Egypt Trade Union Federation (ETUF). Membership in the ETUF is mandatory. According to the International Confederation of Trade Unions' 2006 annual survey of violations of trade union rights in Egypt, "the 2003 labor law makes it legal for an employer to fire someone without giving any reason." Thus, unions have not been an effective lobby for economic reform. Instead, union leaders, who are mostly members of the NDP, have collaborated with the regime to limit the rights of public-sector workers. But as economic reform has accelerated, the country has witnessed growing independent labor activism. The December 7, 2006, Al Mahalla workers' labor strike signaled the start of widespread strikes. It represented a departure from the tradition of workers holding sit-ins while work continued, because strikes were seen as hurting Egypt's national interest. This perception changed, however, as the reform process advanced. A new feature of the most recent strikes is that they are ending peacefully, whereas in the past they would be broken by police force. Some analysts have interpreted this as a sign of the increased societal tensions around economic reform, while others have seen it as a result of increased international scrutiny. The workers arrived at an agreement whereby a share of the privatization proceeds of the Alexandria bank was used to pay off debts of textile and weaving factories and improve working conditions there. Another major strike was held at the Mansour-España garment factory, where workers occupied their factory for two months and reversed a decision by the United Bank to liquidate it. Striking workers accused union officials of working against the interests of their constituency, because the officials tried to dissuade them from their action and pressured others not to participate.

There are some signs of convergence between groups engaged in economic and political opposition to reform. Some political parties have been taking steps to support the demands of different groups affected by reform policies. In July 2007, the government declared that it planned to sell 80 percent of the Banque du Caire to a main investor. In August, sixteen professional unions declared their opposition to that step and announced the start of a popular campaign to stop the sale or to divert its path in favor of national investors, thus preventing foreigners from buying it. Opposition political groups approved this campaign. The Kifaya opposition movement announced the addition of a new "no" to its slogan, which became "no to extension, no to succession, no to selling Egypt." As a response to a recent crackdown on the Muslim Brotherhood after its promulgation of a platform, it has recently announced plans to increase pressure on the government through parliamentary means, forming a bloc of 100, including 20 independent members of Parliament. Among the issues it intends to

include in the economic agenda are the privatization of Banque du Caire and cutting energy subsidies.¹⁸

Limits to Reform Efforts

Reform efforts in Egypt have suffered from three main interlinked constraints. First, they have lacked coordination with social policies and various sectoral policies. As seen above, the reform packages implemented in Egypt have focused mainly on macroeconomic and financial reform, with little attention given to social and structural problems. In a country like Egypt where social problems, including unemployment, poverty, and regional disparities are severe, such an approach is inadequate. The result of modifying this approach has been not only a failure to address these problems but also an increase in their severity during the reform era, combined with an incapability to mitigate the negative side effects of reform in the daily life of ordinary people. This failure has been an important impediment to sustaining deep reform, because Egyptian citizens have lost trust in the reform efforts and their objectives.

The reform policies implemented in Egypt have not been synchronized with all economic sectors and have shown little sensitivity to the specific features of the Egyptian economy. The evidence presented in the previous section shows, for example, that the reform programs have failed to remove obstacles to the development of SMEs, which play an important role in the Egyptian economy. This limitation has led to increases in the cost and time of doing business and affected sectors that are closely linked to ordinary people in Egypt.

The second interlinked constraint is that Egypt has failed to create a healthy and enabling environment for conducting business and to build an economy that can compete in the global economy. At the same time, it has failed to improve economic conditions and living standards for the average Egyptian citizen. The country has introduced many laws in recent years to organize the business environment and to promote national and foreign investment, but it has failed to engage all relevant ministries in comprehensive administrative reform. It has also failed to develop effective enforcement processes to implement the new laws and regulations in a smooth and transparent way. Egypt still suffers from bureaucratic inefficiency, red tape, and wasteful government expenditures.

The third interlinked constraint is that reform efforts in Egypt suffer from a lack of a consensus about issues of timing, means, and goals. Hence, changes in the social contract, due to the reform process, have not enjoyed consensus among main parties affected by the contract: state, market, and civil society. As is shown in the next section, this has created a rift between relevant stakeholders, where people benefiting from the introduced changes or whose ideologies are congruent with the adopted approach support reform efforts while those whose interests and ideologies are not supported by the reform take a stand against it.

What makes this rift quite severe is the absence of mechanisms for debating the reform among all relevant stakeholders. Participation in policy making and policy implementation is limited to the ruling elite and their close associates in the business and political communities, without any effective participation from other stakeholders. Hence, the government has implemented the top-down reform prescribed by the international financial institutions without perceiving all stakeholders as important actors in the reform process.

These three constraints are highly linked to the prevailing institutional arrangements in Egypt. The country suffers from an institutional deficit. The institutional capacity to design and implement comprehensive reform that takes into account social policies and seeks to expand the scope of ownership has been very limited. In addition, the current institutions, both public and private, have neither been able to adapt to changes resulting from reform programs nor to mitigate the negative spillover from reform policies. This situation is, nevertheless, expected to continue in the short run before new economic opportunities arise for Egyptian citizens. So, though it could be accurately stated that the country has witnessed positive results at the macroeconomic level, it also should not be forgotten that those positive results were largely due to external factors and were combined with a failure to create a competitive environment, improve the regulations for doing business, reduce corruption, and promote transparency in state institutions and among political leaders.

The Institutional Deficit

The key questions to put forward are the following: What are the main factors contributing to this failure to create a competitive environment, improve the regulations for doing business, reduce corruption, and promote transparency in state institutions and among political leaders—and what can Egypt do to address these factors and thus meet its social and economic challenges? A thorough examination of the country's economic reform process and its current social and economic challenges indicates that the main reasons for this failure lie in the convergence between institutions and governance factors that prevented the majority of the population from enjoying the positive outcomes of reform. Though Egypt achieved positive results at the macroeconomic level—highly influenced by external factors—and little progress at the social level, microeconomic and structural challenges were not addressed, which could be attributed to the country's institutional deficit.

According to Transparency International's 2007 Corruption Perceptions Index, Egypt ranked 105 among 163 countries, with a score of 2.9, on a scale of 0 ("rampant corruption") to 10 ("least corrupt").¹⁹ In the Egyptian context, a lack of transparency was fueled not only by the drive to protect political interests but also by business interests.²⁰ The most recent *Arab World Competitiveness Report* revealed that the most problematic factors for doing business in Egypt

were access to financing (23 percent of responses), inefficient government bureaucracy (15 percent), and inadequately educated workforce (11 percent).²¹

The World Bank has commended Egyptian authorities for their serious and timely efforts to improve the business environment. In its *Doing Business 2008* report, the World Bank ranked Egypt 126 out of 178 countries in ease of doing business, an improvement over the year before, when it was 165 out of 175. The categories in which Egypt fared worse were dealing with licenses (in which it ranked 169), getting credit, (159) and enforcing contracts (157).²² A year later, Egypt was designated the top reformer in the world. Its recent reform efforts have covered different aspects of the business environment. Among the measures introduced were the reduction of the minimum capital required to start a business, from 50,000 to 1,000 Egyptian pounds, along with halving the start-up time and cost, the introduction of a private credit bureau to ease access to credit, the substantial reduction of fees to register property, and the establishment of one-stop shops at the ports, which shortened the time to import by seven days and the time to export by five.²³

The SMEs represent the business sector that is most burdened by current heavy regulatory measures and thus faces considerable obstacles to doing business. SMEs account for 75 percent of Egypt's employment, 80 percent of its GDP, and 99 percent of its nonagricultural private sector. According to the World Bank Investment Climate Survey, access to finance and the associated cost are among the top constraints impeding SMEs' investment and growth.²⁴

In addition, it has been estimated in a U.S. Agency for International Development report that 40 to 60 percent of the cost of doing business arises from the regulatory framework fueling the informal economy in Egypt.²⁵ The country's informal economy (a concept that encompasses both the informal sector, where enterprises work unregulated, and informal employment, which lacks regulation or protection) grew at an annual rate of 5.3 percent from 1998 to 2006. A recent study suggests that, in 2006, 35 percent of microenterprises and small enterprises (MSEs) did not meet the conditions for formality of having a license, being registered, and keeping regular accounts, and were thus counted as part of the informal sector, compared with 32 percent in 1998.²⁶ During this period, the share of MSEs satisfying these three conditions remained steady at 18 percent.

The reform process has also failed to adequately address the problem of protecting property rights. This not only affects the trust in Egyptian official measures and influences the decision of foreign investors but also creates political pressures on the state. Egypt has faced political pressure about the issue of protecting intellectual property rights, and there have been calls for the U.S. administration not to sign trade agreements with Egypt unless it solves the issue. In April 2007, the United States put Egypt on a "priority watch list" of twelve countries. The reasons cited included "continuing deficiencies in Egypt's [intellectual property rights] enforcement regime, problems with its judicial

system, a backlog of pending patent applications, the lack of protection against unfair commercial use for data generated to obtain marketing approval, and the lack of an effective coordination system between its health and patent authorities to prevent the issuance of marketing approvals for patent-infringing pharmaceutical products.”²⁷ The main reasons for such problems are related to the judicial system, particularly its lack of efficiency, transparency, and technical expertise.

The benefits of reform have been reaped by a limited segment of the population, mainly the business and political elite, whereas the majority of the population has paid the costs of reform. As is illustrated in the next section, the problems in Egypt’s institutional and governance arrangements have limited the country’s capacity to implement better-coordinated reform programs that are more closely linked to social policies and allow a wider scope of ownership. Hence, Egypt needs to accelerate the process of reform and implement more comprehensive reform programs that expand the scope of ownership and are better coordinated with social policies taking into account the various economic sectors in the country. The task of engaging in such a process and achieving its goals will be almost impossible unless the country builds dynamic, transparent, and effective institutions that can facilitate the process and sustain its outcomes.

The Way Forward: Toward Comprehensive Institutional Reform

As has been shown, the reform programs implemented in Egypt have been piecemeal, have lacked coordination with social policies and various economic sectors, and have not enjoyed a consensus among various stakeholders. In light of these reforms, Egypt has managed to achieve good macroeconomic outcomes—though ones largely generated by favorable external factors—while making very limited progress in facing its socioeconomic challenges and its structural and institutional problems. Egypt needs to develop a productive economy that can sustain a mode of growth less dependent on external factors while creating decent jobs for the unemployed, the underemployed, and new entrants into the labor market. This could facilitate addressing regional disparities and finding long-term solutions to major social and economic imbalances. It is obvious that achieving these objectives necessitates being engaged in a comprehensive economic reform effort that allows a wider scope of ownership than the current one and that is better coordinated with social policies pertinent to different economic sectors. Engaging in such an effort requires addressing the key factors that are impeding reform efforts and preventing the mass of the population from receiving the rewards of reform while incurring its costs.

In this paper, it has been argued that the main constraints on comprehensive economic reform in Egypt are highly linked to the prevailing institutional arrangements. On the one hand, Egypt lacks the institutional capacity to design

and implement comprehensive reform programs. On the other hand, current institutions have neither been able to adapt to changes resulting from reform programs nor mitigate the negative spillover from reform policies. Therefore, if Egypt is to meet its current economic challenges and engage in comprehensive reform, special attention should be paid to developing a set of formal and informal institutions that can define the rights and obligations for all actors in the economy and regulate the process of reform.

It should be emphasized that institutional development takes a long time. Given the nature of the Egyptian state and the main actors in the market and civil society, developing the necessary institutions and, most important, making them function properly within a short period of time seems unrealistic. Hence, Egypt should make the choice: Either start developing these institutions soon or lag behind. Building these institutions is the responsibility not only of the Egyptian state but also of the private sector and civil society. In addition, these institutions should be developed in all areas that affect economic performance and determine the nature of its outcomes.

Developing State Institutions

Three types of state institutions need to be developed: institutions that influence the work of the bureaucracy, institutions that shape politicians' behavior by punishing or rewarding certain types of behavior—*influencing the accountability and transparency of politicians*—and institutions that widen political space and participation for Egyptian citizens. The evidence presented above indicates that Egypt needs to create an enabling and competitive business environment as well as work on reducing corruption and increasing the efficiency of the bureaucracy. This goes beyond the objective of introducing new laws and regulations to organize the business environment and promote competition in the Egyptian economy or to improving the staff salaries and merit system of hiring and firing in the public sector. Egypt needs to develop new institutional capacities and to create a shift in the culture of the public sector from one of rent seeking, control, and lethargy to one with efficiency, transparency, and a results-driven orientation. Particular care should be given to improving the provision of welfare services, especially health and education, which have suffered during the reform era.²⁸

Egypt also needs to develop checks-and-balances mechanisms for holding policy makers and high-ranking politicians accountable. The Egyptian media have reported that high-ranking politicians and members of the Parliament have been accused of corruption. These cases have often been closed without giving information to the public on whether those people were found guilty of corruption or not, and what institutional mechanisms needed to be modified to limit potential corruption opportunities. Hence, Egypt should also improve the dissemination process of data and information to the public not only on such cases but also on reform programs.

Finally, the political space and public participation in Egypt are limited. As was shown above, the state controls many civil society institutions and mobilizes them according to its interests; it also imposes restrictions on the activities of political parties and labor unions. In addition, many Egyptian figures and organizations, as well as international organizations, have called for a fairer and more transparent electoral process in Egypt. As is shown below, widening the political space and promoting public participation are crucial for advancing civil society institutions and promoting an effective role for them in the process of designing and implementing comprehensive economic reform.

Rebuilding Private-Sector Institutions

Private-sector institutions can be classified in two types, both of which are large. One is very close to the regime, mainly connected to the business elite. The other is the sector of SMEs from which major sections of the population make a livelihood; this sector generally works informally.

One way in which economic reform can become more responsive to the needs of the SMEs is by introducing private-sector representative organizations where both small and big enterprises interact; because SMEs are more numerous, their bargaining power in shaping economic policy would be strengthened. In addition, the reorganization of business organizations according to the economic sector would help mitigate the side effects of the sectors' shifting importance in the economy. Indeed, in this regard, the state should focus on targeting the potential drivers of future economic growth by selecting specific high-value-added sectors and rewarding those companies that succeed while withdrawing support from those that do not. Better monitoring and enforcing of responsible corporate practices are both necessary steps, particularly in the Special Economic Zones where labor rights are most often violated.

Advancing Civil Society Institutions

Workers need to be enabled to have a stronger bargaining position vis-à-vis other social partners, who have mainly benefited from reform. Key International Labour Organization standards of freedom of association and collective bargaining should be respected. For instance, union leaders who restrict the union activities of their constituencies instead of representing them are not conducive to developing a consensus on reform. Practical steps include alleviating the restrictions on labor unions; under current restrictions, labor unions cannot operate unless part of a recognized federation and as part of ETUF. In addition, because economic policies are ultimately the result of the political process, the prohibition of civil society organizations from engaging in political activities should be abolished. Respecting and promoting the role of different civil society organizations, especially those acting as watchdogs, is necessary in this regard.

In addition, Egypt needs to widen the space for political activities. This requires two main steps: making sure that the elections are fair and transparent and

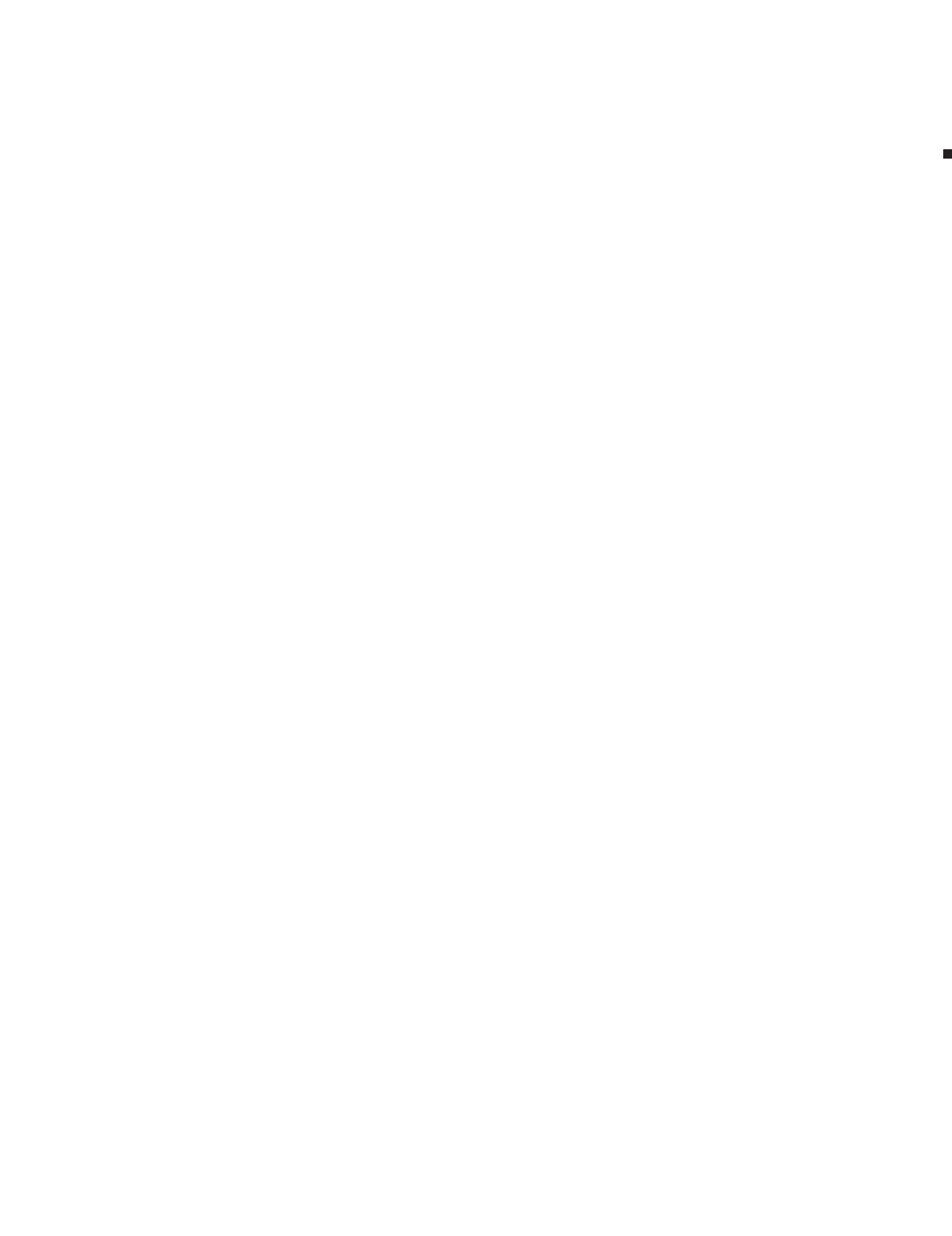
amending the regulations pertinent to the freedom of assembly and activities of political parties. Within the context of economic reform, expanding political space is important for two main reasons. First, it helps increase participation in the process of reform and it increases Egyptian citizens' chances to benefit from the upsides of economic reform. Second, it puts pressure on the political parties in Egypt to develop specific economic programs and to formulate agendas to present to the voters, which would allow Egyptian citizens to assume a more proactive role in influencing the nature of economic reform efforts.

Institutionalizing Coordination Between the State, the Private Sector, and Civil Society

Egypt's main task is to develop institutions that can achieve the desired economic reforms. In this paper, it has been argued that to make clear what the desired reforms are, certain institutional mechanisms need to be in place. Developing the institutions described above certainly does not mean that Egypt will automatically implement comprehensive economic reform with the outcomes guaranteed. It means, however, that the more concrete steps that are taken toward reaching a more inclusive social contract, the higher the potential will be for implementing comprehensive reform.

Economic reform is by nature an uneven process, with resources and human power shifting across sectors. Determining which sectors should be promoted and which methods need to be used—as well as monitoring the implementation of reforms and protecting the vulnerable groups affected by them—are significant areas that require central coordination between the state, business, and civil society.

Finally, three main issues should be taken into consideration in the process of developing new and reformed institutions in Egypt. The first is the need to avoid building technocratic institutions that are disconnected from the realities on the ground. In the process of developing the needed institutions, it is important to consider the political issues that are pertinent to these institutions and influence their effectiveness, the ideological differences among various stakeholders in society, and the issue of legal reform in Egypt. The second main issue is the need to clarify the role, obligations, and rights of each institution to minimize conflict and avoid having institutions that are nonfunctional and dominated or hijacked by one side, for example, state actors or elites. The third main issue is the need to facilitate interaction among various institutions, to foster comprehensive economic reform that takes into account social policies and leads to a wider scope of ownership.



Notes

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