Strategic Economic Directions

2000

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Strategic Economic Directions 2000

The Editor

Ahmed El-sayed El-Naggar

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Contributors to The report

Ahmed El-Sayed El-Naggar

Dr. Husseen Abedallah **Dr. Salwa El-Antary**

Mohamed Nour El-Deen

Translated and Edited by

Mandy McClure

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Introduction

The last decade of the twentieth century witnessed stormy changes on the international economic front, the historical medium in which Arab economies operate and by whose circumstances they are influenced. If the will and planning are present, Arab economies can themselves influence this environment more effectively than is currently the case. The changes of the last decade have not been mere discrete events following each other chronologically, but have coincided to form the outlines of a new international economic system. This system is still rife with contradictions, whether within some of its major organizations—for example, the World Trade Organization (WTO)—or within the model it sanctions and the values that inform it. Moreover, tension still exists between international commitments and national self-interest, which at times undermines these commitments.

The last decade's changes have also created further conflicts and tensions: between those forces pushing for the liberalization of international economic relations and those attempting to guide economic relations more strictly; between the theoretically absolute values of economic globalization and the way they are applied selectively in practice; and between the universal economic model that is being promoted globally and the individual circumstances of each country. As the necessity of resolving these tensions persists, the future promises even greater changes in the international economic situation.

International, regional, and local economic developments of the last ten years can be summarized as follows: after the end of the Cold War and the fall of the Soviet Union as a superpower, the economy and civil technology came to represent the principal axis of conflict among states and among large multinational corporations, some of which enjoy economic power that exceeds that of a large country or several small ones. As a result, regional economic cooperation began to take more advanced forms in order to reinforce the strength of the participants and their collective position in the international economy.

Although the economy has always been a major element in the total power of any state, over the last decade it has become the most important element. A country like Russia—militarily powerful, but crisis-ridden economically—occupies a lower international status than economically stronger countries such as Japan, Germany, and China, although these are all militarily much weaker than Russia.

As the rivalry between two competing economic systems came to an end, bilateral economic cooperation and conflict began to take place within the single international capitalist system. The fall of the old bureaucratic socialist regime in Eastern Europe, and after it the Soviet Union, also led to the collapse of the economic cooperative structure among these states under the auspices of Comicon. This put an end to the parallel system that had competed with the West, and Soviet-bloc countries began working within the existing organizations of the capitalist economic system, controlled by the West and, specifically, the United States.

Initially, this transformation created a state of international submission to the will of those western countries that had won the Cold War. As formerly Soviet-bloc countries witnessed political and economic change on the domestic front, they asked to be allowed entrance to the organizations of the new economic world order with no preconditions, hoping that they could negotiate from within to change the terms on which the system operated.

In such a climate, selective and partial efforts to expand the sphere of economic globalization increased. These efforts tended to coincide with the interests of advanced capitalist states, who led them towards the partial and gradual liberalization of international trade. Efforts to free international trade tended to focus on areas in which these countries possessed a high ability to compete—industrial goods, financial, insurance and banking services, telecommunications, and the

movement of capital. Liberalization was less, or controls existed more fully, in fields where they did not enjoy a competitive edge—agricultural commodities, textiles, the movement of labor. Advanced capitalist countries arrived at the General Agreement on Tariffs and Trade (GATT) to free up international trade, and they created the WTO as a third prong to the two other already existing organizations: the International Monetary Fund (IMF) and the World Bank. WTO was approved in December 1993, signed officially in Marrakech in April 1994, and came into force in 1995.

WTO is essentially an embodiment of the interests of advanced industrialized countries. The agreement liberalizes the trade in industrial commodities, while not doing so for agricultural commodities; it protects intellectual property rights and prohibits an unfair use of intellectual products, which come largely from industrialized societies, without preventing the unfair use of minds themselves. Research organizations in developed countries regularly offer enormous financial incentives to attract minds from developing countries after they have been educated in their home countries. The solution to this problem is to create a general environment conducive to knowledge and research and establishing research bodies and financial incentives for intellectuals and scientists in developing countries that would encourage them to stay at home. Agreements made to protect intellectual property rights should also compensate developing countries for the brain drain, putting a price on the movement of minds to another country that represents the expenses of educating them in their home countries.

In 1997, under the auspices of the WTO, an agreement was reached to liberalize the communications trade, followed by an agreement to liberalize financial and insurance services. Hence was the movement of capital in all its forms freed up, without allowing for a similar liberalization of the movement of labor. Aside from the principle of justice that is inherent in demands to free up the movement of labor, it is necessary economically to push multinational companies and financial organizations of advanced capitalist states to focus on pumping in direct investment to developing countries. This would encourage workers to stay in their home countries, rather than heading to advanced countries.

The WTO, along with agreements to liberalize the communications trade and financial and insurance services—and before that similar programs of the IMF and the World Bank—together form the basic pillars of economic globalization. They clearly express their nature as selective globalization, which, at its core, represents the interests of its makers and their favored economic model, regardless of the specific circumstances of developing countries. Although the economies embracing the process of globalization contribute the bulk of products and international trade in commodities and services in the world, this does not necessarily mean that the current conditions of economic globalization are fair or suitable to the circumstances and interests of all participating countries.

This imbalance calls for great theoretical and applied efforts to renegotiate the conditions of globalization and work to change them, perhaps even entailing a rejection of some of its more blatant ideological aspects which do not take heed of the particularity of circumstances of each country. One example is the economic model currently being propagated, which is based on the state giving up its role in the economy as much as possible, focusing instead on issues of defense, security, and law enforcement. This model has been adopted despite the fact that the state in the past played a prominent role in spurring on economic and social developments in advanced capitalist countries themselves, representing progressive forces in these countries, and expressing a profound realization of the need for political, social, and economic stability, whether it necessitated intervening directly in the economy or intervening strongly through financial, monetary, and socially transformative policies.

The events surrounding the WTO conference in Seattle in 1999 appeared as an expression of rifts—limited thus far—in the coalition of advanced industrialized states over the liberalization of international trade, as well as an expression of the late realization by developing countries of the need to defend their interests and reform the conditions of economic globalization such that it takes into account their interests. It was also an expression of the popular rejection of the present form of

globalization. The Seattle conference saw a US-Japanese clash after Japan, along with Canada and developing countries, insisted on reviewing US anti-dumping legislation, much of which contradicts the obligations of the US to liberalize trade in goods and services in accordance with the General Agreement on Tariffs and Trade (GATT) and other agreements to free up financial, insurance, and communications services. The US rejected the Japanese demand, showing clearly that it only upholds the absolute principle of free trade when it supports its special interests. If these interests are opposed to free trade, then free trade will be blocked by any possible means, such as with anti-dumping legislation. Japan pointed out that such laws limit the influx of its steel exports and other commodities into US markets.

Similarly, the 1999 Seattle conference saw the US, Canada, Australia, and some developing countries come head to head with the European Union (EU) over the trade in agricultural commodities. The countries of the EU offer the most extensive subsidies to farmers and agricultural exports to maintain their ability to control European markets, creating a competitive edge for their agricultural exports on world markets. This allows the EU to maintain its position as the principal exporter of agricultural goods, and particularly food commodities—in essence, a political decision. It must be pointed out that the vast majority of advanced countries, including the US, give huge subsidies to agriculture and agricultural exports, a grand total of US$350 billion annually.

The Seattle conference also saw a conflict between developing and developed countries over the liberalization of the textile and garment trade, as developed countries still put in place several conditions which obstruct free trade in these areas. Moreover, developed countries have taken no serious steps to abolish the quota system, which restricts the movement of textile exports from developing countries, although these limitations are to be completely abolished by 2005.

Developing and developed countries also clashed over the insistence of developed countries to establish environmental and labor standards for industries in developing countries. Although labor rights are constantly disregarded in most developing countries, these rights should be established through social change within these societies, or through agreements to which trade unions, businessmen's associations and international labor organizations are a party. US and European pressures in this regard are not disinterested efforts; international capitalism cannot suddenly transform itself and begin defending labor rights in developing countries. Rather, it seeks to strip industries in developing countries of one of their relative advantages: the lower cost of labor. If developed countries are truly eager to protect labor rights in developing countries, why did they refuse to include the issue of the free movement of labor on the agenda of liberalizing international trade relations, as they did with the free movement of capital and the commodities and service trade?

All of this does not mean that liberalizing international economic relations is a bad thing. On the contrary, it is a positive step, as it necessarily brings about challenges and incentives for producers to advance and develop their competitive abilities. It also protects consumers from exploitation by local capitalists. The aforementioned observations on free trade stem from its selective and unjust nature, which needs to be changed so that free trade can be based on just and coherent principles.

If Seattle saw a rift in the coalition of advanced industrialized states over free trade, it is necessary to point out that the first countries to encroach on free trade agreements—the backbone of economic globalization—are advanced capitalist countries themselves, led by the US. The US, for example, built its trade agreement with Japan in 1995 on the principle of fair trade, which obligated Japan to import a minimum limit of US goods, thus contradicting the principles of free trade.

In addition, the subsidies that developed countries give to some of their large industrial companies occasionally cause problems, such as the subsidy that European countries have given to the Airbus project, which has strengthened its competitive and financial edge and allowed it to compete more effectively with the US-based Boeing. This led the US president in December 2000 to warn of a trade war between the US and the EU, although Boeing and other US companies also receive support from the US government in obtaining foreign contracts, especially in those countries that receive US aid. US President-elect George W. Bush reiterated that his administration would invest the nation's budget surplus in certain companies in the form of tax breaks to increase their competitive edge. If European countries tread the same path to preserve the competitive abilities of their companies, these states might see a sharp decline in social programs, meaning a greater imbalance in the distribution of resources, which will lead to parallel tendencies in developing countries.

Faced with strong resistance to a continuation of these policies, some believe that economic globalization—rife with stark contradictions among the countries who carry the greatest weight in it—may engender severe consequences, pushing the international economy in different directions in the future (Dr. Ibrahim al-'Isawi, 2000). Even from within developed countries and pro-globalization forces, voices have been heard calling for a reassessment of the current shape of globalization. Head of the German Manufacturers' Union, Tyll Necker, has pointed out that "globalization leads to rapid structural transformations, and an increasing number of individuals are no longer capable of bearing its burdens." Similarly, Klaus Schwab, founder and head of the Davos economic forum, has stated that "increasingly widespread feelings of loss and fear warn of an impending, sudden reversal which cannot be controlled...It is a reactionary movement which must be taken seriously. Economic and political leaders must demonstrate that the new global capitalism will achieve a benefit for most humans, not only for business leaders and investors." (See Peter Martin, Harold Schumann, 1996.)

The gap between rich and poor countries is enormous, as it always has been, particularly in areas related to production and participation in world exports. However, the Gross National Product (GNP) of any poor state tends to be greatly underestimated, as the currencies of poorer states are generally undervalued. Commodities exported by developing states are exchanged with goods produced by developed countries on terms that are weighted against them. Figures from the World Bank's *World Development Report* (2000/2001) show that the population of poor countries—i.e., where an individual's annual income is less than US$755—reached 2417 million, or about 40.5 percent of the world's population in 1999. At the same time, the total value of all these countries' GNP did not exceed US$987.6 billion, or about 3.4 percent of the total world product in the same year. The population of middle-income countries was put at about 2667 million in 1999, or about 44.6 percent of the world's population. Their combined GNP reached US$5323.2 billion, or about 18.2 percent of the world's product in 1999. Thus, 85.1 percent of the world's population received 21.6 percent of its income, while 14.9 percent of the inhabitants of the world receive 78.4 percent of the world's income. If GNP is calculated in terms of a local currency's buying power relative the US dollar, however, the combined GNP of poorer countries increased to 11 percent of total world product in 1999. The share of middle-income countries went up to 33 percent, while the share of wealthy countries dropped to 56 percent of total world product in the same year, according to World Bank figures. This shows that low- and middle-income countries are being wronged in the calculation of their GNP in accordance with world market and nominal exchange rates. Instead, the exchange rate should reflect a local currency's buying power relative to other currencies.

The last decade also witnessed the movement of the countries of the EU towards economic unity, including the creation of a common currency with the release of the euro in 1999. Eleven European countries started using the euro when it was released: Germany, France, Italy, Spain, Holland, Belgium, Austria, Finland, Portugal, Ireland, and Luxembourg. By 2002, the currency should replace other national currencies still in use. The release of the euro comprised the first big challenge to the international position of the dollar as the international reserve currency, as the euro, too, is backed by a substantial economic power, although less powerful than the US. The combined Gross Domestic Product (GDP) of euro countries reached US$6339.1 billion in 1999, compared to the US GDP of US$8351 billion the same year. Nevertheless, the euro draws its power from a sizeable trade bloc which is far greater than the US. The total value of commodities exports for euro countries reached US$1774.3 billion in 1998, compared to about US$682.5 billion in the US in the same year. Similarly, the value of service exports from euro countries reached about US$420.3 billion in

1998, in contrast with about US$240 billion of US service exports the same year.

On the other hand, the value of commodities imports in euro countries reached about US$1644.4 billion in 1998, while the value of service imports the same year reached about US$425.9 billion. Meanwhile, the value of commodities imports in the US reached about US$942.7 billion in 1998, while service imports reached US$165.8 billion. The euro declined sharply next to the US dollar in the year 2000, hovering around US$.9, a loss in value of about 24 percent from the time it was released in January 1999, when the euro equaled US$1.18. The decline of the euro was linked to the weakness of European economic indicators in comparison to similar indicators for the US economy. The euro was also negatively influenced by the mad cow crises and its influence on the agricultural sector and agricultural exports to the countries of the EU, particularly after the disease spread in a number of countries other than Britain. The euro was also negatively influenced by the rise in oil prices, which are measured in dollars. The euro rallied at the end of 2000, reaching US$.95, due to declining US economic indicators in the fall of that year and falling oil prices.

Arab economies were affected by the decline of the euro during most of 2000, as it led to a rise in the value of Arab oil exports when calculated in euros. At the same time, the competitive edge of Arab exports in European markets declined, particularly those Arab exports pegged to the dollar, as is the case in Saudi Arabia, the United Arab Emirates, Qatar, Bahrain, Oman, Egypt, Syria, Djibouti, and Yemen. These exports rose in price compared to the euro and European currencies. At the same time, the competitive edge of European exports in Arab markets rose, although this tendency declined at the end of 2000 with the rise of the euro, which is expected to continue in 2001 in light of the decline of the US economy at the end of 2000.

The last decade also saw the establishment of the North American Free Trade Agreement (NAFTA). The economies of east and southeast Asia were speedily developing before they were hit with a monetary and economic crisis in the middle of 1997, whose negative effects lasted through 1998 before recovery began in 1999. In 2000, the pace of development again picked up in these countries. Similarly, Chinese economic power increased after 20 years of rapid and continuous development, and after several decades spent expanding and diversifying the Chinese economy while achieving average to good growth rates. The result was the appearance of China as a force to be reckoned with on the world economic field. China's GDP reached about US$980.2 billion in 1999, rising to US$1141.9 billion if Hong Kong is included. China also became a major trade power, particularly after it regained Hong Kong, an important international trade center. China started to contribute about 4.9 percent of world exports, while accounting for about 4.5 percent of world imports.

At the same time, efforts to establish an Arab economic and trade bloc increased. There are substantial obstacles to this goal, however, due to shortcomings in the project. As it is now envisioned, the Arab free trade zone would not include certain agricultural commodities, which means practically the lack of free agricultural trade. Despite these obstacles, the existence of a plan and the increased conviction in both official and popular circles of its necessity for the future of Arab economies will open the way to developing it further and reforming its current shortcomings. This is particularly true if Arab countries depend on an organized body to hold annual economic summits to steer Arab economic cooperation towards new horizons, as is the case with annual economic summit of the EU.

Arab economies are also constantly subject to price fluctuations in production and foreign trade due to fluctuations in oil prices. These economies now stand at the crossroads, with rapid economic developments taking place, along with changes in the structure of international economic power and its distribution. Arab economies will either depend on a basic commodity and bear the consequences of market fluctuations, backwardness and increasing marginalization—no matter how important the basic commodity that they produce and export is—or they will catch the boat of industrial and technological development with a strong awareness that a real jump can be made in their ability to develop and change their international economic position.

The last decade also witnessed the appearance of other regional economic and trade blocs, such as COMESA. These comprise a step toward economic cooperation in different areas of the world.

In Egypt, the economic liberalization reform program is still underway, meeting with success in some areas, while encountering obstacles and stumbling blocks in others. In 2000, the economy reached a bottleneck, raising questions on how to develop the economy further and guide economic performance domestically and in foreign relations.

In addition, a number of Arab countries have begun to implement a liberal economic reform program and adopt the economic model it entails (the state foregoing its economic role and liberalizing its foreign relations to varying degrees). This reform, however, has been dealt with on purely ideological grounds, which equates liberal reform with economic reform, such that liberal transformation has become a goal in itself. Nevertheless, the goal of any economic reform, whatever its nature, is to rid the economy of shortcomings; increase production through incentives to develop; modernize technology; increase the efficiency of resource allocation; raise the efficiency level of production and the labor force; and develop a competitive edge for the economy and local products. At the same time, economic reform should guarantee a minimum standard of living for citizens through social policies and effective domestic transformations. The importance of this type economic reform is limited to its ability to There are several definitions of economic reform; the most precise of them is also the most general. One definition claims that it is "an organized process to change the economy with the goal of lessening or erasing local or foreign imperfections through a wide variety of changes in public policy as the basis of sustainable growth," (Dr. 'Abd al-Shakkur Sha'lan, 1987). Another definition indicates that economic reform is "guiding the use of capital investments and human resources, while spurring on technical and scientific progress, developing labor productivity, and raising the effectiveness of production through improving the salary system in accordance with actual work in order to reinforce economic incentives for workers," (Maurice Debb, 1972).

The greatest economic reform of the twentieth century—perhaps in the history of the world—was built upon Keynesian thought. It is this reform that brought advanced capitalist countries out of the Great Depression that hit in the 1930s. Keynesian thought and the reform that springs from it are based fundamentally on widening the sphere of state intervention in the economy. As Keynes said: "Expanding the duties of the state is necessary to keep consumption tendencies in line with incentives to employ. It might seem to an author in the nineteenth century or to an American businessman a gross violation of the principles of individualism, but on the contrary, it appears to us that this expansion of the role of the state is the only means of avoiding a complete breakdown of current economic organizations and a condition for the success of individual efforts."

Keynes also notes: "Linking certain administrative authorities—left for the most part to private initiative—to central institutions is of the utmost importance. Concerning consumption trends, the state will always be forced to exert a guiding influence through its monetary policies, particularly the interest rate and perhaps by other means. As for employment policies, it may be that the influence of monetary policy over interest rates is enough to bring it to its ideal value. Hence, we believe that a type of aware socialism in the area of employment is the only means of insuring almost complete employment," (J.M. Keynes, *The General Theory of Employment, Interest and Money*, Arabic translation by Dar Maktabat al-Hayat, Beirut). **[There was a note here to return to the original text, which I tried to do originally. Unfortunately, I do not have access to these texts. If they are available at the center, they should be consulted.]**

Keynesian theory and the economic reform that grew out of it saved the capitalist societies of advanced countries in the 1930s and remained the starting point of its economic policies until the beginning of the 1970s. In the first half of the 1970s, however, it lost much of its intellectual currency after the spread of an inflationary recession, as Keynesian theory maintains the impossibility of simultaneous spread of high inflation and unemployment, embodied in the Phillips curve. In any case, the blow to Keynesian theory opened the field to thought of the new monetarists, led by Milton Friedman and the Chicago school, elevating their status to that previously held by Keynes. Their ideas on

economic reform revolve around the relationship of the amount of money with the production unit (Ramzi Zaki, 1980).

During the 1980s and 1990s, a number of liberal economic ideas appeared, both moderate and extreme. As a whole, they formed the basis of the liberal economic reforms that are presently sweeping the world. Fundamentally, they all revolve around the idea of the state giving up its economic role insofar as possible, while giving free rein to the private sector and market mechanisms. The idea of the guardian state, defined by the classical school since the nineteenth century, has been revived by new critics. Joseph Stiglitz, head of the US Council of Economic Advisors under President Bill Clinton, believes that there are six roles for the state: building an infrastructure in science, technology, currency, health, environment, and social services (Stiglitz, 1999). The state's fulfillment of these duties can lead to progress, he says, pointing to the US experience and that of Far Eastern countries.

At the same time, the World Bank's *World Development Report* (1997)—most of which is devoted to dealing with the role of the state—believes that the fundamental mission of the state is to instill law and stabilize the environment for policies that will entail comprehensive economic stability, as well as investing in infrastructure, social services, and the protection of the weak and the environment.

In turn, the interference of the state in economic activity as a manufacturer or trader is seen as undesirable under the terms of liberal economic reform. Indeed, this model of reform includes selling state-owned assets to the private sector. Sinita Kikeri, John Nellis, and Mary Shirley point out that privatization as a part of liberal economic reform achieves profits by increasing efficiency and innovation in those sectors that are successfully privatized (1994).

A slightly different theory maintains that decentralization measures or lessening the interference of the state is much like medicine, which, if prescribed for a general illness at the appropriate time and in the right way, can lead to positive, desirable effects. But, inappropriate timing can harm the economy more than it helps (Remy Prod'homme, 1995). This theory treats limiting the state's role in the economy in a more subjective way, without making it a sacred tenet. Indeed, it points out the necessity of ensuring the right set of circumstances to make certain that the state's withdrawal is positive and effective.

In light of the international hegemony of this model of liberal economic reform, several calls have been raised to adopt what is called the "Third Way." The Third Way is simply an amended copy of Keynesian ideas in the two countries that have most strongly adopted economic liberalization: the US in the Clinton era, and Britain under Prime Minister Tony Blair. These calls appeared in reaction to the dramatic effects engendered by freeing up market forces, particularly in the currency and stock exchange markets.

As any economic reform seeks to eliminate economic imperfections, the degree to which it succeeds should be the main indicator of the overall success of reform.

These, then are the broad outlines of the international, regional, and local economic constraints; reading these developments correctly, with a true realization of the present economic reality, is the first step to establishing effective mechanisms to act within these constraints and the changes they entail. This will increase the benefit from current developments, or at least lessen the dangers that come with them. But it is necessary to realize that fundamental steps to achieve economic modernization in any country must depend on incentives and developing social and economic efficiency in these countries.

As such, it is vitally important to issue an annual strategic economic report, or even several reports on different trends by a number of Egyptian scientific and research centers, in order to express—truthfully, scientifically, and in a way that redounds to the nation's credit—the necessities of economic progress and to express a positive, rather than passive interaction with the international economic environment in a way that achieves the interests of the Arab peoples, particularly the Egyptian people.

Why this annual report?

Although economic issues on both the theoretical and applied level have been present in one form or another in different publications coming out of the Ahram Center for Political and Strategic Studies, the

rapid local, regional, and international developments of the last decade revealed the need for an annual strategic economic report that would express the Arab-Egyptian viewpoint of current economic developments in the world, as well as suggesting how to deal with them, the aim being to serve Arab economic interests, including the interests of the Egyptian economy. In addition, a need was felt to present a scientific view of regional and local economic developments, with the aim of spurring on progress and economic modernization and strengthening the international position of Arab economies, including Egypt, in the rapidly-developing international economic environment, as this constitutes the historical framework within which Arab economies act. These economies are influenced by its constraints, and they can in turn influence them if there is sufficient Arab willpower, consensus, and coordination.

In such circumstances, Dr. 'Abd al-Mun'im Sa'id, director of the center, proposed the idea of publishing this annual Arab economic strategic report. It chooses and treats the most important economic issues and developments, particularly relevant strategic issues, and their effect on international, regional, and local economic trends in the future. Each subject is treated on several levels, from initially understanding the topic in itself, to studying its effect on Arab and the Egyptian economies, to suggesting appropriate mechanisms to deal with it in a way that will serve Arab and Egyptian interests. It is on these grounds that the specific subjects were chosen for this, the first issue of the report.

Dr. 'Abd al-Mun'im Sa'id was enthusiastic about the idea and provided the academic and administrative aid necessary to bring it into reality. The idea also garnered the full support of Mr. al-Sayyid Yasin, the real founder of the Ahram center, its current consultant, and its spiritual father, as well as the support of those contributing researchers. Similarly, the great economist Dr. Isma'il Sabri 'Abdullah gave his support and excellent advice to the project, reaffirming his role as the teacher of various generations of Egyptian economists.

Reflecting the enthusiasm of all those who contributed to the report, ambassador Muhammad Gamal al-Din al-Bayumi, assistant foreign minister, gave his distinguished view of the plan to establish a regional economic bloc, examining the relationship between it and the international economy. This is contained in a separate chapter in the report which aims to present a distinct viewpoint of one certain topic, in an attempt to establish the democratic administration of difference over important issues within the Arab cultural elite.

Dr. Husayn 'Abdullah, the former head of the Energy Planning Commission in Egypt, and one of the most distinguished Arab experts in the field of petroleum, presented an impressive study on developments in the international oil market and Egyptian strategic aims in the field of energy. Dr. Sulayman al-Mandhari, economic consultant to the Union of Stock Exchanges and the Arab Currency Market Authorities, contributed an excellent study on Arab stock exchanges, their interrelationships, and the challenges they face. Dr. Salwa al-'Antari and Muhammad Nur al-Din offered distinguished contributions to this report, whose preparation depended on the participation of different generations, as is clear form the list of contributors.

In addition to these contributions, the report also contains a study on the principal actors in the international economy, examining interactions with them in such a way that may achieve Egyptian and Arab economic interests; a review of the financial and economic crises suffered by Asian countries and their recovery; the first study on corruption and combating it in the Arab world; a study on the Arab boycott of Israel and calls to boycott the US; a distinguished examination of the Egyptian banking sector in a period of economic change in Egypt and the dangers associated with it; and an overview of the Egyptian economy, including a discussion of the contradiction between government figures and actual economic performance, the roots of the currency crisis, and an evaluation of the privatization process.

I wish to express my heartfelt thanks and gratitude to all those who participated in bringing this work to light. Above all, I would like to thank the Ahram institution, headed by Ibrahim Nafi', who lent his support to this project as a living expression of the high degree of democracy that characterizes the administration of this institution, and

as an expression of its championing of research works based on truth and science, which aspire only to be a credit to the nation.

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International Economy

The international oil market: current developments and strategic directions

The steep rise in oil prices in the year 2000 raised several questions about the nature of international oil markets and fueled speculation about whether producers were starting to control the market again after having lost control of it in the mid-1980s. The price hike also raised questions about the respective roles and relationships of the active parties in the oil market—producers, consumers, and oil companies. Finally, questions were raised concerning future trends in oil pricing and the long-term role of oil as an energy source.

Before turning our attention to these questions, it must be pointed out that the enormous changes witnessed by oil markets and oil prices in 2000 did not begin with that year, but with the dramatic decrease of oil prices in the fall of 1998, when the price of a barrel of crude collapsed to less that US$10, causing extreme negative effects on the economies of oil-producing countries. Export income and the foreign trade balance decreased and budget revenues dried up, leaving a large deficit in several of these states.

In the face of this economic crisis, oil-producing states exerted their utmost efforts to improve prices. This movement gained even more momentum when Saudi Arabia— OPEC's largest oil-producing country and the single largest source of oil in the world—joined in the efforts. As Saudi Arabia generally adopts the most conservative stance towards a dramatic increase in oil prices, its support meant in essence that there was no longer any oil-producing country that was against taking measures to raise prices. In March 1999, OPEC members and certain non-OPEC oil-producing countries, such as Mexico, reached an agreement to decrease world production by 2.1 million barrels per day (bpd), with OPEC countries decreasing production by 1.7 million bpd. The states involved agreed to maintain these levels until March 2000.

The agreement lent a boost to oil prices, particularly in the context of the general international economic improvement of 1999, when Japan and the countries of southeast Asia finally came out of the severe recession that had hit in 1998. The majority of these countries began to achieve high economic growth rates, contributing further to the general international economic improvement. The average rate of growth in gross world product was 3.4 percent in 1999, compared to 2.6 percent in 1998, spurring on new investments, increased interest in existing investments, and an increased demand for energy sources, primarily oil. Increased demand for oil combined with the fixed supply led to an improvement in oil prices in the second quarter of 1999.

These trends continued in 2000, as the average rate of growth in gross world product reached 4.7 percent, and the demand for oil increased accordingly. Oil prices reached levels not seen since the Gulf War, and the average price per barrel in 2000 was the highest since 1985. Throughout the year, OPEC raised the level of production several times in an attempt to curb prices, which fluctuated between US$22-US$28 per barrel. In OPEC's mid-year meeting in March 2000, the organization decided to raise production by 1.65 million bpd, bringing world production up to 24.7 million bpd. In June of the same year, production was raised again by 708,000 bpd, making daily production 25.4 million bpd. In September 2000, in a meeting attended by Russia, Mexico, and Oman, OPEC agreed to raise production once more by 800,000 bpd, bringing daily production to 26.2 bpd. In addition, Iraqi production reached approximately 3 million bpd.

OPEC's production increase reached a balance between supply and demand in the first quarter of 2000, but in the second and third quarters, supply began to dramatically exceed demand. According to OPEC's monthly bulletins, the world supply of oil reached 76.6-77.1 million bpd, while world demand hovered around 74.4-75.5 million bpd. Nevertheless, prices continued to rise in the second and third quarters of 2000, leading OPEC president Ali Rodriguez to comment that speculations in oil futures contracts had added US$8 to the price of a barrel of crude. At the same time, US presidential candidate Al Gore attacked oil producers and accused them of profiteering. The truth is that oil speculators and large international oil companies

played an important role in increasing prices to levels that did not reflect the balance between supply and demand.

Oil companies saw huge leaps in their profits in this period. Shell, for example, saw record profits of US$3.254 billion in the third quarter of 2000. Shell chairman Mark Moody Stewart said that such exceptional profits were the result of irregular oil prices. Exxon-Mobil, the world's largest oil company, saw similarly high profits—US$4.29 billion for the third quarter of 2000, compared to upwards of US$1.21 billion for the same period in 1999. The profits of US oil giant Chevron reached US$1.65 billion in the third quarter of 2000, compared to US$702 million in third quarter 1999. Large international oil companies, in addition to oil speculators, participated in raising prices unnaturally by controlling how much oil was pumped into the market and by creating an atmosphere of fear, which pushed prices upwards.

US policy also contributed to the rise in world demand, as it increased its oil imports and started storing imported oil in its own exhausted wells. *Oil Market Intelligence* of September 2000 stated that the commercial stock of oil in North America rose from 1.043 million barrels in February 2000 to 1.151 million barrels in August 2000.

With the rise in oil prices, interactions between exporters and importers ranged from outright clashes to accusations about who was responsible for what had happened in the international oil market; debates raged about the fair price of a barrel of oil.

Through its secretary of energy, Bill Richardson, the US exerted great efforts to convince the principal oil-exporting countries, in particular Saudi Arabia and the Gulf states, to increase production to bring prices down. The US even threatened that it would use its strategic reserves, and actually did use them for an entire month, rather than buying oil abroad.

In Europe especially, the widespread public outcry over the price increase of petroleum products led the public to look for someone on which to place the blame. In general, Europeans realized more than Americans that their respective governments were responsible for the increase in the form of huge taxes placed on the consumption of fossil fuels. A liter of diesel before taxes is approximately EU.34, EU.34, EU.41, EU.34, and EU.35 in France, Italy, Belgium, Germany, and Spain respectively; after taxes, prices rise to EU1.11, EU1.11, EU1.08, EU1.04, and EU.84 respectively. Such figures show that heavy taxes were responsible for the price increase in fossil fuel in Europe. As a result, calls to lower taxes grew more fervent, but European governments refused to submit to popular pressure, although some states, like Italy, did impose a temporary cut on fuel tax.

Aside from this, there was general agreement between European states and oil consumers that OPEC should be made to bear responsibility for the price increase. This attitude was particularly noticeable in Britain, where the prime minister declared the necessity of continuing to pressure oil-producing states to raise production in order to lower prices. Nevertheless, Italian prime minister Juliano Amato was more on target when he noted that "oil-consuming countries are the ones who brought the fuel crisis on themselves. OPEC-member states are developing countries that depend on oil sales, and developed countries did nothing for them when the price of oil fell to US$10 per barrel in the fall of 1998. In the end, they depended on themselves by lowering production to raise the price of oil."

The year 2000 saw fundamental changes in how OPEC dealt with oil-importing countries. The organization set price limits on oil, deciding that a barrel of crude should not fall below US$22 per barrel, and that the ceiling would be US$27 per barrel; after that, production could be increased in increments of one-half million bpd to put a stop to further price increases. By the same token, production was decreased when the price of oil fell below the set price.

On the other hand, the major oil-exporting countries began to feel a sense of responsibility to stabilize the price of oil, particularly evident at the Caracas summit in September 2000. This, in turn, prepared the way for serious talks between producers and consumers in November 2000 in Riyadh, Saudi Arabia, at the Seventh International Energy Forum. While the US asked OPEC states to raise production, member states focused on the role of high taxes and the limited availability of

renewable energy sources in consumer countries during the oil market crisis.

The dialogue between producers and consumers was serious this time, as both sides felt strong, yet mutually dependant on one another. Nevertheless, the forum's final resolutions were limited to recommendations on the necessity of oil-producing states to provide enough oil to meet growing needs, with a reiteration on the need for greater transparency to put a lid on price fluctuations.

These, then, are the developments of the year 2000. Given them, what are future trends likely to be in the international demand for oil, its supply, and expected prices?

Increased international demand for oil

The demand for energy is closely bound to levels of economic activity and growth rates. This relationship is referred to as the income elasticity of demand, which is reached by dividing the average change in demand for energy by the average change in Gross Domestic Product (GDP). In addition to economic growth, a number of other factors also play a somewhat important role, but they cannot be treated in this limited study.

The relevant studies show that the worldwide average GDP will grow approximately 2.9 percent annually during the period between 1996-2020, rising from about US$27.5 trillion in 1996 (taking the dollar at its 1997 value) to about US$40 trillion in 2010, to US$47 trillion in 2015, and finally reaching US$54 trillion in 2020. The average GDP varies according to region, with the countries belonging to the Organization for Economic Cooperation and Development (OECD)—North America, Western Europe, Japan, Australia, and New Zealand—averaging 2.3 percent yearly. During the same period, the countries of the former Soviet Union and Eastern Europe will average approximately 3.1 percent growth (2 percent in the former Soviet Union and 4 percent in Eastern Europe). In developing countries the average rate of economic growth will be 4.8 percent annually, with variations according to region: Asia at 5.2 percent; 3.6 percent in the Middle East; 3.2 percent in Africa; and 3.8 percent in Central and South America.

Despite the varying economic growth rates given by different studies, all agree on their assumptions concerning income elasticity. In most studies, the figure for income elasticity remained approximately .75 on the world level, meaning that every 1-percent increase in GDP is accompanied by a .75-percent increase in energy demand. This coefficient varies greatly from country to country depending on how advanced each country is in terms of energy conservation, energy efficiency, and energy intensity.

The income elasticity of demand in most countries was more than 1 percent until the late 1970s, when oil prices were rectified and the energy conservation movement began in earnest. As a result, energy efficiency rose while energy intensity declined. In Egypt, average growth rates and rates of energy consumption from 1993-1998 show that the income elasticity of demand reached approximately 1.3 percent, meaning that programs for energy conservation and efficiency must be developed in order to bring the ratio closer to the world average of .75 percent.

In light of what has been said, it is expected that energy consumption of all sources throughout the world will grow in the period 1996-2020 by 2.1 percent annually, rising from the equivalent of 187 million bpd in 1996 to 251 million bpd in 2010; 277 million bpd in 2015; and 305 million bpd in 2020.

The world demand for oil (see table 1) is expected to grow in the period from 1996-2020 approximately 1.8 percent annually. World consumption of oil will go from 71.5 million bpd in 1996 to 94 million bpd in 2010; to 102 million bpd in 2015; and reaching 110 million bpd in 2020. Thus will oil remain the world's primary energy source, accounting for 37-39 percent of total consumption during the period in question. The US Department of Energy has calculated even higher figures, putting the growth in demand for oil at 2.1 percent annually until 2020, meaning that consumption levels will reach 117.4 million bpd in 2020, compared with the current 76 million bpd.

In the face of such optimistic expectations about the future of oil, Ahmad Zaki Yamani, the former oil minister of Saudi Arabia who established the World Center for Energy Studies in 1986, has stated that there will be a sharp decline in the price of oil in approximately

five years due to the development of new technology, which will produce electricity with sources other than oil, radically affecting the demand for oil. According to Yamani, the demand for oil will decrease with each such discovery, and the world supply will push the price of oil lower.

The demand for natural gas is expected to increase in the period between 1996-2020 by 3.3 percent yearly, going from 82 trillion sq. ft in 1996 to approximately 129 trillion sq. ft in 2010; 151 trillion sq. ft in 2015; and 174 trillion sq. ft in 2020. Thus will gas consumption increase, to account for 29 percent of total energy consumption by the end of the period (as opposed to 22 percent in 1996). Gains in gas consumption will be made at the expense of nuclear energy, which will decrease by approximately 3 percent. Similarly, coal and oil demand will decrease relatively by approximately 2 percent each.

It is expected that the world demand for coal in the same period will grow approximately 1.7 percent annually, rising from 5167 million short tons in 1996 to 6381 million short tons in 2010; 6845 million short tons in 2015; and 7568 million short tons in 2020. These figures show that the percentage of coal use among energy sources will decline from 24.7 percent to 22.6 percent during the same period.

The consumption of nuclear energy is expected to drop sharply as a result of the dangers associated with its use, from 2.28 trillion kilowatts/hour in 1996 to 2.08 trillion kw/hr in 2020, a total decline of.4 percent annually. Thus, its share of total energy use will decrease from 6.4 percent to 3.5 percent in the same period.

As for new and renewable sources of energy, including hydroelectric energy, its share of total world consumption was less than 8 percent in 1996, and it is not expected to exceed that percentage by 2020, though absolute consumption is expected to increase by 2.5 percent annually during the period in question.

The concentration of the world's oil supply

As table 2 clearly shows, the world's oil production capacity in 1997 was 77 million bpd, with an actual production of 73.7 million bpd, where the difference represents energy stores reserved to face crises like that which occurred during the Gulf War, when Saudi Arabia, the United Arab Emirates (UAE), and Venezuela made up for the lack in world oil supply as production stopped in Iraq and Kuwait. The world's oil production capacity is expected to rise to 95 million bpd in 2010; 104 million bpd in 2015; and 112 million bpd in 2020.

In this framework the production capacity of OPEC is expected to rise from 29.4 bpd (actual production, including liquefied natural gas) in 1997 to 43 million bpd in 2010; 49 million bpd in 2015; and 56 million bpd in 2020. Thus will OPEC's relative contribution to meeting the world's oil needs rise from 40 percent in 1997 to 46 percent in 2010; 47 percent in 2015; and 50 percent in 2020.

In OPEC itself, there are only six countries which will have the capabilities to expand and develop their production capacity, going from 22 million bpd (actual) in 1997, to 34 million bpd in 2010; 40 million bpd in 2015; and 47 million bpd in 2020. These states include Saudi Arabia, the United Arab Emirates, Kuwait, Iraq, Iran, and Venezuela. Thus will these countries supply 36 percent of the world's oil needs in 2010; 38 percent in 2015; and approximately 42 percent by 2020. The production capacity of other OPEC-member states is not expected to exceed 9 million bpd from 1997-2020, nor is the share of any particular state expected to change significantly.

Aside from OPEC, the world's oil production capacity is expected to rise from approximately 44 million bpd in 1997 to 52 million bpd in 2010; 55 million bpd in 2015; and not more than 56 million bpd in 2020.

To sum up, oil production will tend to be concentrated even further in the near future, as the world depends more on OPEC to fill its needs—approximately half by the year 2020. Indeed, this production will be limited largely to six OPEC-member states. This essentially means a small number of countries will have the ability to determine production and export policies and, in turn, prices. The expected shortage in oil supplies which will occur as wells are exhausted in a number of countries in the near future will undoubtedly lead to an increase in prices, even without policies being formulated to that effect, whether by OPEC states or other countries.

This trend will be strengthened as oil exports are increasingly limited to a few states, even more than the expected limitations in world production and supply. Available studies show that the net

deficit of oil-consuming countries will grow with time, leading to a widening import gap. As table 3 shows, with the exception of the Commonwealth of Independent States (CIS, i.e. the former Soviet Union) and Eastern Europe, which are expected to earn oil income from the export of 4-7 million bpd from 2010-2020, the world will suffer from a net deficit in oil, requiring an almost exclusive dependence on OPEC.

The greatest oil deficit will be concentrated in the western industrialized countries of the OECD, whose oil consumption is expected to rise from approximately 42 million bpd in 1997 to 50 million bpd in 2010, and 55 million bpd in 2020. As this group of states depends on imports to fill the gap, the deficit will increase from approximately 19 million bpd in 1997 to 25 million bpd in 2010, and 31 million bpd in 2020. The US is responsible for approximately half of this deficit, with the rest spread over Western Europe and Japan.

At the same time, oil consumption is expected to rise in the rest of the world, primarily developing countries and including OPEC-member states, from 26 million bpd in 1997 to 37 million bpd in 2010, and 49 million bpd in 2020. Thus, the oil deficit in the rest of the world will increase from approximately 13 million bpd in 1997 to 21 million bpd in 2010, and 29 million bpd in 2020.

In short, the total worldwide deficit in oil—which OPEC will be expected to fill—will increase from approximately 29 million bpd in 1997 to 42 million bpd in 2010; 47 million bpd in 2015; and 54 million bpd in 2020.

Available studies also show that the world trade in oil will rise from approximately 37 million bpd in 1995 (40 million bpd in 1997) to approximately 66 million bpd by 2020. Thus OPEC's share of world oil exports will rise from 62 percent (or 23 million bpd) in 1995 to 72 percent (or 48 million bpd) by 2020. Within OPEC, the share of the six principal oil-exporting countries is expected to increase from approximately 49 percent (or 18 million bpd) in 1995 to approximately 63 percent (or 42 million bpd) by 2020. These figures clearly show the increasing concentration of supply and export in the near future.

On the flip side, the share of non-OPEC oil-exporting countries is expected to decrease during the same period, from 38 percent (or 14 million bpd) to 28 percent (or 18.5 million bpd). The experience of

1999 has proven that these states will not hesitate to cooperate with OPEC in establishing production and export policies when their national interests require them to do so. In 1999, Mexico, Russia, Norway, and Oman all froze production to support prices, which had fallen in 1998 to unprecedented levels, meaning OPEC countries alone saw huge losses—US$56 billion in that year.

In short, the concentration of the world's oil supply is not only rising, but the concentration of exports is also increasing, allowing the largest exporters a greater opportunity to shore up prices.

Oil prices in the foreseeable future

Expectations concerning oil prices in the near future vary greatly, reflecting a gap between pessimists and optimists. While we shall avoid discussing the merits of each argument, we will take a look at the arguments of those that assume lower oil prices. These pessimists base their arguments on a number of assumptions, the most important of which are the following:

1) The cost of searching for and producing oil is trending down as a result of technological improvements achieved during the last few years, the most important of which are advances in three-dimensional seismic surveys, horizontal drilling, and deep-water drilling technology. In light of these improvements, the world's oil reserves have been reassessed since the end of the 1980s at approximately 350 billion barrels, or about 50 percent more than was previously thought. Most of these new reserves were found in OPEC-member states, particularly those of the Arabian Gulf.

2) A number of international oil companies have established investment programs for locating and producing oil with the assumption that the price will remain at US$16 per barrel.

3) Natural gas must be considered a strong competitor to oil, and its competitiveness will increase in the future as a result of environmental considerations, as its use produces less pollutants—such as carbon dioxide and sulfur compounds—than do oil and coal.

4) Competition, not coordination, will reign among oil producers on the world market, as they strive to increase their share of the market. As a matter of course, oil prices will decrease dramatically.

Faced with such pessimistic arguments, we can counter with a number of reasons for optimism:

1) It is true that the investment cost necessary to increase energy production by 1 bpd in the Arabian Gulf region ranges between US$2515-US$4866, depending on the size of the field. This leads to a decrease in the cost of extraction by approximately US$1-1.50 per barrel. But this investment cost rises to about US$7610 in Indonesia and to US$10,240 in Venezuela, and it rises dramatically in difficult areas like Alaska and the North Sea.

Even assuming that the cost of oil production will decrease in the future, the cost of oil, in contrast to that of the oil processing industries, is not determined in the long run by production costs alone. It is also priced with the consideration that oil is an exhaustible primary resource—a nonrenewable source spread over a limited number of nations. It is a given as well, both theoretically and practically, that those countries enjoying oil reserves have the right to obtain their fair share of its true value, as represented by the price of refined petroleum products sold on the market to the final consumer.

2) As most studies point out, the traditional world supply of oil will become scarcer and will be concentrated in the hands of a few countries starting from the mid 2020s. The International Energy Agency has affirmed this trend, adding that at about the same time it expects the world to be nearing the point at which traditional oil production will fall short of meeting growing world demand. That will entail the exploration of non-traditional sources of oil, which are still expensive and which are not expected to get cheaper in the foreseeable future. This trend is also supported by world experts in oil geology.

With the inability of traditional oil resources to meet growing world demand, along with the cost increase of extracting petroleum products from non-traditional sources, the price of oil must rise to achieve a balance between supply and demand.

3) The assumption that competition will rule interactions on the oil market is incompatible with the increasing monopolization of oil production and export, as monopolization will necessarily impose a coordination of oil supply on world markets. If the price of a commodity is determined by the dynamic between supply and demand, the level and effects of this dynamic vary according to differences in the market structure. In the context of a market subject to absolute competition, the price might near production cost, but in a

market subject to a high degree of monopolization, the price may include financial profits above and beyond production costs.

4) The difference between the price of crude, as determined by supply and demand, and the cost of production should not be considered outright profit. It is, in fact, compensation for the exhaustion of an oil wealth that cannot be renewed. Thus, the difference is the cost of this wealth independent of the cost of production. This difference helps create financial returns that can be used to diversify sources of income, so that oil-producing countries are compensated for an exhaustible natural resource. It can similarly be invested to increase productive capacity to fill the world's growing need for oil.

5) Regional variations in the cost of oil production help to determine oil prices. In the long run and under stable conditions, the final price must cover the higher production cost of the marginal producer, as well as pay for an exhaustible natural resource and provide a profitable return on an investment that carries certain dangers. Marginal producers are not content to regain expenses with a profit on investment, but attempt to earn enough to compensate them for exhausted reserves, the search for new fields, and the dangers of producing oil. The US, for example, used to give oil companies working in its territory a depletion allowance in the form of tax breaks, allowing companies to earn enough to invest in the search for new wells.

In short, there is no guarantee that a cheap producer will price his product less than that determined by the world market to cover the total expenses of a high-cost product.

6) The assumption that natural gas will compete on the market with oil, causing the latter to become cheaper, lacks positive proof. It is true that the world consumption of natural gas will grow more rapidly than oil consumption, but the world's total energy consumption will increase as well, allowing the two sources to coexist on the market with a fractional decrease in the ratio of oil and coal use and a larger decrease in the use of nuclear energy.

In addition, natural gas is not a perfect substitute for oil. As has been shown, oil will continue to occupy the prime place in the near future, supplying approximately 36 percent of the world's energy needs. Moreover, the infrastructure of natural gas, including primary and secondary pipelines, cannot be used except in limited areas of the world, such as western industrialized nations and the CIS; in most countries of the world, particularly in developing countries in which energy is a necessity for development, building gas networks and buying gas-employing machinery—almost all of which are capital investments or advanced consumer goods—requires vast investments and several years to purchase or construct. Thus, it is not feasible for most developing nations, and oil is expected to remain the preferred energy source.

7) As for coal, despite its abundance, its polluting effect on the environment will be an obstacle to its use, with the exception of a small group of developing countries, such as China and India. Although its consumption is expected to increase between 1997-2020 by 1.7 percent annually, it is not expected to replace oil, whose consumption will increase by approximately 1.8 percent annually in the same period.

Similarly, the use of renewable energy sources, the most important of which is hydroelectric power, is expected to rise 2.5 percent annually between 1997-2020, but this is still not expected to effectively meet the world's growing energy needs. As was previously mentioned, it is not expected to comprise more than 8 percent of energy consumption in the foreseeable future.

In conclusion, we can expect the price of oil to reach at least US$27 per barrel by 2010, assuming an annual growth rate of 5 percent (a 2-percent annual growth in the demand for oil and a 3-percent rise representing the increase in its true value in the face of growth in oil-consuming industrialized countries). Thus will be the case as long as no fundamental change affects these two figures or no groundbreaking discoveries are made in finding alternate energy sources. If the price of oil keeps rising at this rate, it will reach upwards of US$40 per barrel in early 2017, the end of the current strategic economic and social development plan in Egypt. One should not be surprised by such prices—the price of oil surpassed US$40 per barrel in the late 1970s and early 1980s. Even in the second half of 1999 and the first half of 2000, its price surpassed US$25 per barrel.

Table 1

Expectations for world energy consumption according to type and area (calculated in Quadrillion (10) ^{15} Btu

Area and type of fuel	Actual consumption		Expected consumption			Annual growth
	1990	1996	2010	2015	2020	1996-2020
OECD total	182.7	202.5	240.4	251.6	262.8	1.1%
Oil	78.7	85.7	100.2	104.5	108.9	1%
Natural gas	35.5	44	60.8	67.7	73.7	2.2%
Coal	37.2	35.8	38.3	39.1	40	.5%
Nuclear energy	16.3	19.8	19.2	17	15.5	-1%
Water and renewable energy	15	17.2	21.9	23.3	24.8	1.5%
Soviet Union and Eastern Europe	73.6	52.4	61	65.3	69.8	1.2%
Oil	21	12	13.4	13.9	14.4	.8%
Natural gas	26	21.7	30.2	34	38.7	2.4%
Coal	20.8	13	11.1	10.2	9.1	-1.5%
Nuclear energy	2.9	2.8	3	3.1	2.7	-.2%
Water and renewable energy	2.8	2.9	3.4	4.1	4.9	2.3%
Developing countries	87.4	120.6	202.8	238.2	279.2	3.6%
Oil	35.2	48.1	76.8	89.2	101.3	3.2%
Natural gas	10.5	16.5	39.8	51.9	65.1	5.9%
Coal	32.5	43.9	66.6	75.5	89.2	3%
Nuclear energy	1.1	1.5	3	3.5	3.6	3.6%
Water and renewable energy	8.1	10.6	16.5	18.2	20	2.7%
Total world consumption	343.8	375.5	504.2	555.1	611.8	2.1%
Oil	134.9	145.7	190.4	207.5	224.6	1.8%
Percentage of world total	39.2	38.8	37.8	37.4	36.7	
Natural Gas	72	82.2	130.8	153.6	177.5	3.3%
Percentage of world total	20.9	21.9	25.9	27.7	29	
Coal	90.6	92.8	116	124.8	138.3	1.7%
Percentage of world total	26.4	24.7	23	22.5	22.6	
Nuclear energy	20.4	24.1	25.2	23.6	21.7	-.4%
Percentage of world total	5.9	6.4	5	4.3	3.5	
Water and renewable energy	25.9	30.7	41.9	45.6	49.7	2.5%
Percentage of world total	7.5	8.2	8.3	8.2	8.1	

*One ton oil=7.3 barrels=about 40 million Btu/1000 cubic feet gas=about 1 million Btu

Table 2

Expected development of global oil production capacities 1997-2020 (in million bpd)

Country or area	1997	2010	2015	2020
Saudi Arabia	9.09	14.1	16.2	20
Iraq	1.18	3.8	4.7	5.9
Iran	3.75	4.5	4.9	5.5
United Arab Emirates	2.48	3.4	4.2	4.9
Kuwait	2.12	3.2	4.3	5.2
Venezuela	3.44	5.1	5.4	5.8
Total of 6 major oil-producers	22.05	34.1	39.7	47.3
Percentage of world production	30%	36%	38%	42%
Rest of OPEC members	7.3	9.2	9	8.6
All of OPEC	29.35	43.3	48.7	55.9
Percentage of world production	40%	46%	47%	50%
Non-OPEC members				
U.S.A.	9.46	9	8.9	8.7
Western Europe	7.03	7	6.4	5.9
Soviet Union and Eastern Europe	7.42	10.1	12.1	13.1
Rest of the world	20.39	25.6	27.4	28.6
Total of non-OPEC members	44.3	51.7	54.8	56.3
World totals	73.65	95	103.5	112.2

Table 3
Oil consumption and production and the oil deficit in select areas 1997-2020 (in million bpd)

	1997	2010	2015	2020
U.S.A.				
Consumption	18.62	22.7	23.7	24.7
Production	9.46	9	8.9	8.7
Deficit	9.16	13.7	14.8	16
Western Europe, Japan, OECD				
Consumption	23.24	27.4	28.6	29.8
Production (North Sea, Canada, Mexico, Australia)	13.94	15.8	15.2	14.6
Deficit	9.3	11.6	13.4	15.2
Western Industrialized Countries (OECD)				
Consumption	41.89	50.1	52.3	54.5
Production	23.4	24.8	24.1	23.3
Deficit	18.49	25.3	28.2	31.2
Former Soviet Union and Eastern Europe				
Consumption	5.06	6.4	6.6	6.9
Production	7.42	10.5	12.5	13.6
Surplus	2.36	4.1	5.9	6.7
Rest of world				
Consumption (including OPEC)	26.18	37	42.9	48.7
Production (without OPEC)	13.48	16.4	18.2	19.7
Deficit	12.69	20.6	24.7	29
World total				
Consumption (including OPEC)	73.13	93.5	101.8	110.1
Oil production capacity (without OPEC)	44.3	51.7	54.8	56.3
Deficit	28.83	41.8	47	53.8
OPEC's production capacity	29.35	43.3	48.7	55.9
Total world oil production capacity	73.65	95	103.5	112.2

Production capacity includes shut-down or reserve capacities

Arab Economy

The Aqsa Intifada and the Arab boycott of Israel and the United States

The Aqsa Intifada flared up at the end of September 2000, after the second Camp David negotiations failed to lead to a final settlement between Israelis and Palestinians, and immediately following an attempt by Israeli Likud party leader Ariel Sharon to desecrate the courtyard of al-Aqsa Mosque. The uprising raised the question of a revival of the Arab economic boycott of Israel, as a form of punishment for its violent aggression against the Palestinian people in the occupied territories and even in Israel proper. The calls for a return of the second- and third-degree boycotts intensified after they were dropped in 1994 in light of progress being made towards a final settlement of the Arab-Israeli conflict and under heavy American pressure towards this end. A call also went up to boycott American products, as a form of punishment for the constant and clear favoritism exhibited by the US towards Israel. This was increasingly resented by Arab peoples considering Israel's aggression towards the Palestinians during the Aqsa Intifada.

The final resolution of the Arab Summit held in Cairo on October 21-22, 2000, came as a show of official support for popular sentiment in this regard and built upon it. Arab states decided not to resume any official or unofficial multilateral activities with Israel; to halt economic cooperative activities with Israel on the regional level; to stop participating in such activities until tangible progress could be made towards a fair and comprehensive peace; and to cut all relations with any country that moves its embassy to Jerusalem or recognized it as the capital of Israel. First Oman, and soon after Tunisia and Morocco, cut their economic relations with Israel; Qatar hesitated to do so until it was forced to officially announce the closure of the Israeli Trade Office in Doha under pressure from Saudi Arabia and Iran, who announced that they would not attend the Islamic Summit in Doha until Qatar closed the office. Nevertheless, the Israeli deputy foreign minister stated that Qatar had not officially closed the office and that there had been no communication with his ministry concerning the affair, adding that the office had been closed by the Israelis after they had heard the Qatari foreign minister's statement on television. He stated that the office had been closed for security reasons and could possibly be reopened with the coordination of the responsible Qatari parties, except in the event that Qatar asked officially that it be closed.

In Egypt, the largest Arab state, the boards of directors of the Association of Investors in Ubur City and Association of Investors in Sixth of October City made the decision to cut all economic relations with Israel and boycott Israeli products. The board of directors of the Association of Investors in Ubur City added that the city contained no Israeli workers, and the Goldsmiths' Syndicate decided to boycott Israeli gold. The United Egyptian Chambers of Commerce, comprising 3.5 million merchants, decided to impose a full boycott on Israeli products. The head of the chamber said that if the Palestinian uprising and Israeli oppression continued, Arab markets would be closed to any country that stood against Arab rights, whether in Europe or the Americas. He added, however, that there was no objection to Jewish or Israeli investment in Egypt, as such companies would be considered Egyptian, whatever the nationality of the capital that had established them.

The board of directors at the Egyptian Tour Guide Syndicate also decided in its meeting of October 2000 to boycott international trade conferences held in Tel Aviv, and the board's statement warned Egyptian tour guides against traveling to Israel or legal action would be taken against them. Statements were issued by the General Union for Art Syndicates, the Cairo Pharmacists' Syndicate, and the Egyptian Universities' Teaching Staff Committee in Support of the Palestinian and Lebanese Peoples, all calling for a boycott of Israel and its products. Some, such as the Pharmacists' Syndicate and the Committee for Teaching, even called for a boycott of US products.

At the same time, calls to boycott products imported from the US spread through Egypt, extending even to products and restaurants considered American symbols. The General Egyptian Committee for Boycotting American and Zionist Companies and Products was formed, its founders including the Egyptian Committee to Resist Normalization, the Popular Movement to Resist Zionism and Boycott Israel, the

National Egyptian Universities' Teaching Staff Committee to Combat Zionism, the Arab Committee in Support of the Islamic Resistance in Lebanon and Palestine, the Egyptian Committee for Dialogue and Culture, and the Popular Committee in Support of the Palestinian People's Uprising. The General Egyptian Committee for Boycotting American and Zionist Companies and Products published lists containing the names of businessmen supporting normalization and their companies, as well as the member list of the Egyptian-Israeli Friendship Organization. The committee also published several statements, many of which were inaccurate and harmed its credibility. For example, its boycott statement said that Egyptian imports of Israeli gold, which the Department of Gold Workers had decided to boycott, annually totaled about US$100 million. This is patently untrue, as Egyptian imports of all Israeli products did not exceed US$22 million in 1999, according to Egyptian sources, or US$55 million according to Israeli sources (see *IMF, Direction of Trade: Statistics Yearbook, 2000*). Any popular committee that wants to maintain its legitimacy must depend on accurate information, and it must have clear goals it works to achieve methodically, not through good intentions alone.

Supporting popular anger and the increasing calls for a boycott of Israeli and American products, Dr. Nasr Farid Wasil, the high mufti, issued a *fatwa* declaring it impermissible to consume products imported from the US and Israel. The *fatwa* declared importers of such commodities to be committing a grave sin. Concomitantly, Sheikh of al-Azhar Muhammad Sayyid Tantawi called for a boycott of all foreign goods whose profits supported Israel. He added that boycotting the products of any country that supported Israel, whether American or not, was a grave necessity and constituted a means of supporting the Palestinian struggle.

In the face of calls to boycott Israel and the US, there were some who opposed such a measure, particularly as it related to the US.

In Lebanon, the National Authority for Resisting Normalization, the Permanent Conference to Oppose the Israeli Cultural Invasion, and the National Arab Club in Lebanon called for a boycott of inessential US products as a measure of support for the Palestinian uprising and a means of denouncing America's biased support of Israel. A call went out to every citizen asking them to avoid purchasing American products.

In Jordan, professional syndicates and opposition parties organized an intense, wide-ranging campaign to boycott US products and commodities in an assembly held by the secretaries-general of opposition parties, the heads of professional syndicates, and a number of independent political figures. The board of professional syndicate heads also published a list with the names of Jordanians supporting normalization with Israel, containing 200 political and economic figures, organizations, and companies that dealt with Israel. Similarly, the head of the Association of Investors in the Industrial City of Amman called on Jordanian manufacturers in all industrial areas to halt any dealings with Israel, emphasizing the necessity of foregoing Israeli products in Jordan. He proclaimed joint Israeli-Jordanian projects in north Jordan useless, adding that the value of total investments was US$300 million, concentrated largely in garment manufacturing and services which depended on raw materials and components produced by Israel.

In Saudi Arabia, the head of the Chamber of Commerce and Industry in Riyadh said that any boycott must be aimed specifically at Israeli products, which, in any case, are not found in Saudi Arabia, adding that the idea of boycotting countries that supported Israel hurt the cause rather than helped it.

Despite the differences in individual positions, it is clear that Arab countries as a whole saw a rising call to boycott Israel and products imported from the US. We should thus discuss these demands in the context of the current international economic situation. What are the goals of an Arab economic boycott of Israel, and to what extent were they achieved? Are there acceptable reasons to boycott American products? What are the profits and losses involved in such a boycott? Is it possible for the Palestinians to boycott Israel in one way or another and loosen the ties that bind the Palestinian economy to that of Israel?

I. International double standards in boycotting

The international economic environment is characterized by clear double standards in the application boycotts in international economic

relations. At the same time that world economies are merging in terms of goods, service, and the movement of capital, a number of obstacles inhibit the movement of workers between countries. Similarly, the trade in agricultural goods has not yet been freed. While countries of the West, particularly the US, are staging a ferocious attack and exerting violent pressure to put an end to the Arab boycott of Israel in all its manifestations, in general any western country, particularly the US, uses the tool of boycott to punish countries that disagree with it. If it does not succeed in imposing a boycott through the UN Security Council, it imposes one unilaterally or in agreement with other countries. Currently, the UN Security Council has imposed complete sanctions on Iraq based on the concept of boycott. Although there has been no reason to continue the sanctions since Iraq withdrew from Kuwait in the winter of 1991, the US insists on imposing punitive sanctions against the Iraqi people.

The US has used the policy of economic boycott against countries it considers hostile to its interests more than 70 times since World War II. It still imposes a complete economic boycott on Cuba to this day. Begun in 1961, the boycott was made more stringent in 1996 with the passing of the Helms Law, which obligates the US government to isolate Cuba, increase its blockade of Cuban sugar exports, and punish any countries, companies, or individuals who invest in Cuba.

The US also currently imposes economic boycotts of varying degrees on Libya, Iran, North Korea, and Sudan. The US itself participated in bringing down the racist regime of South Africa by participating with other western countries in imposing an economic boycott on the country from 1985 until the early 1990s, when the regime began to collapse. The US also led the process of imposing an economic boycott on Yugoslavia as a means of pressuring the ruling party before finally leading direct military interventions against it. It is currently using the threat of an economic boycott and promises to lift it to force change in the regime in Belgrade.

The overwhelming propensity of the US to use sanctions and economic boycotts against other countries is illustrated by proposals from the US legislature to use economic sanctions in cases in which no one else would dream of using them as an effective means of pressure.

For example, in 1997 the US threatened to impose economic sanctions on South Africa because it intended to export electronic systems to Syria that would allow greater accuracy in tank fire, night vision, and improved aim at moving targets. In doing so, the US managed to impede the deal. Similarly, in October 2000, the US Congress asked the president to impose economic sanctions on Russia and block its entry into the World Trade Organization if it did not release a former American intelligence officer, currently a businessman, it had detained on charges of military espionage. Although he had been sentenced to 20 years in prison, Russia released the man after the presidential decree.

The contradictions are clear. On one hand, there is increased international economic cooperation in certain areas, while on the other hand, clear obstacles exist to such cooperation in other areas. At the same time, certain countries make heavy use of the boycott card and economic sanctions while at the same time asking other countries not to use such measures, touted as a relic from the Cold War era. This odd split, clearly embodied in positions taken by the US in particular, comprise an international base from which to support the position of those calling for an Arab boycott of Israel that would also include the US. It gives no significant international foundation to those who reject the policy of an Arab boycott of Israel and the US. More important, however, is whether or not there is a justification, or even the necessity of an Arab economic boycott of Israel.

II. Is there justification for a boycott?

The Arab boycott of Jewish products began in Palestine before World War II and continued after the war when several ordinances were issued preventing Jewish imports coming from Palestine, whether directly or indirectly. The ordinances also prohibited exporting primary materials to the Jews in Palestine, even before the Arab boycott of Israel was initiated after the founding of the Zionist state, at which point the breaking of the boycott by any Arab became equivalent to high treason.

The Palestinian economic boycott of Jewish products was imposed during the British Mandate in Palestine, particularly after the Arab

revolt of 1936. An Arab boycott of Jewish products was imposed in December 1945 under the auspices of the Arab League soon after its establishment, expressing Arab rejection of the rape of Palestine by the Jews with the protection of Britain and the West in general. The boycott was implemented as an attempt to lay economic siege to Zionist organizations in Palestine, with the ultimate goal of weakening them and thus preventing the loss of Palestine.

That boycott was not based on scientific studies, as at that time what Palestine needed was positive effort in the form of political, financial, and military aid to the Palestinians. Nevertheless, the economic boycott of the Jews was not effective as Jews in Palestine depended largely on an influx of Jewish capital from Europe and the US and on western support, exemplified in the Haavara Agreement made with Nazi Germany in 1933. The agreement allowed the transfer of machinery and equipment valued at BLE8.1 million, according to the *Encyclopedia Judaica*, or approximately BLE60 million according to calculations based on the text of the agreement itself and the number of Jews who immigrated. This machinery and equipment provided the foundation of modern Jewish industry in Palestine at a time when the total amount of currency in circulation in Palestine was no more than LE5 million. The Zionists also depended on Britain, which supported Jewish military industry in Palestine through regular demands for its products during World War II. This is in addition to the financial support coming from the US as a nation and from resident Jews. The economic boycott of the Zionist presence in Palestine during the British Mandate was a natural step taken in the face of attempts to wrest away Palestine, but its effect was negligible, as preventing the loss of Palestine required much more than boycotting the Zionist presence.

After the establishment of the state of Israel, the boycott continued, taking on a new dimension after the Arab League decided to establish boycott offices in May 1951 under the supervision of the president's office in Damascus. The main boycott office and its subsidiaries were responsible for planning and executing the Arab boycott of Israel. Thus was the boycott used as a means of pressuring Israel by depriving it of the numerous advantages that would accrue if economic relations were established between it and Arab countries. Such benefits included first and foremost the reduction of transportation and insurance costs for the trade in commodities and for individual movement. The boycott also prevented Israel from investing in the prime geographical location of Palestine: with its position in the heart of the Arab world and its long coastline on the Mediterranean coast, Palestine could otherwise be a center of regional transit trade. The percentage of Arab imports that passed through Palestine reached 1 percent, 2 percent, 4 percent, 9 percent, 8 percent, and 4 percent of all Arab imports in the years of 1939, 1941, 1942, 1943, 1944, and 1946 respectively. The percentage of Arab exports that passed through Palestine in the same period was .3 percent, 1 percent, 2 percent, 1 percent, 4 percent, and .4 percent. (See Mikha'il Shifir, "Nata'ij al-muqata'a al-'arabiya 'ala al-iqtisadayn al-'arabi wa al-isra'ili," in *Min al-fikr al-sihiyuni al-mu'asir*, Palestinian Books, Research Center, PLO, Beirut: 1968, p. 509.)

The justification for the Arab economic boycott of Israel after its establishment—withholding the economic privileges of dealing with neighboring Arab markets and depriving it of the historical role that Palestine had played as a center of Arab transit trade—was a logical attempt to lay siege to Israel, pressure it, and weaken it economically as part of the comprehensive battle on all fronts. It was also an attempt to raise the price the West would bear to preserve Israel's existence.

In this stage also—that is, directly after the establishment of the state of the Israel—the economic boycott of Israel, though necessary, was not the primary economic act that was required to support the Palestinian people, cut off the Zionist state, and weaken it. Israel accommodated the closure of Arab markets by linking its economy to the West, both Europe and the US. It regularly received technological facilities and trade privileges in bringing its commodities to the markets in these countries, as well as financial and other material aid. More pressing than an economic boycott at this stage was the necessity of establishing a strong agricultural, service, and industrial economic base in the remaining parts of Palestine—that is, in the West Bank, East Jerusalem, and the Gaza Strip. At the same time, Palestinian refugees expelled from their homes in 1948 by Israel, or those that left in fear of Zionist terrorism and oppression, should have returned to the West Bank, Jerusalem, and the Gaza Strip and been absorbed economically

through agricultural, industrial, and service projects funded by Arab states.

But this did not happen. It was not even seriously considered, despite the existence of a strong current of Arab nationalism in most Arab countries in the 1960s. Arab countries' adoption of the economic boycott policy was made without taking the larger step of building a strong Palestinian economy capable of absorbing the Palestinian people economically and funding the struggle with Israel. It was, instead, the adoption of the easier policy, which cost Arab countries nothing. This policy reflects both the lack of clear planning in opposing Israel on the economic front and the lack of readiness by Arab countries to make financial sacrifices to build what was left of Palestine after 1948, thus preserving its independence and supporting its ability to defy Israel. In short, after Israel was established as a state, Arab countries were content to pursue a policy of boycott, which cost them nothing, rather than adopting a more effective policy, albeit more expensive. In turn, this reveals that the imposition of a boycott was not a positive act of struggle as much as it was connected to the desire of Arab states to be unadulterated by any dealings with the Zionist state and to mollify Arab popular opinion; economic enmity with the Zionist state was reinforced without having to take any losses, in the belief that Israel alone would suffer from the Arab boycott. It would lose the privilege of dealing with neighboring countries—economically the cheapest trade option—and it would lose the competitive edge such geographic proximity could bring its exports. Arab countries would not be influenced by such factors, as every country could establish economic relations with other Arab states or countries situated on the borders of the Arab world, benefiting from the relative advantage of geographic proximity. The Arab world did not suffer after removing Israel from its circle of foreign economic relations.

After 1991, when a comprehensive political settlement to the Arab-Israeli conflict began to be discussed, the Arab economic boycott of Israel was used as a trump card in negotiations. The justification for continuing the boycott was to pressure Israel to continue its pursuit of a political settlement, as any breakdown in negotiations meant that Israel would be barred from Arab markets, which absorb more than US$160 billion in commodities exports annually. If Israel pursued negotiations, it would receive the huge reward of having Arab markets opened before it.

Despite the importance of continuing the boycott in this stage, even more important was pumping money into Palestine to build the economy and keep the Palestinian labor force on its own land, rather than having it migrate to Israel or other Arab countries. Thus would all Palestinians remain on the land and be capable of economic resistance in the long battle with Israel.

When initial progress was made on the political front of the Arab-Israeli conflict, the US pressured those Arab countries with which it had close ties, particularly the Gulf countries, to end the boycott in all its degrees (The first degree involves a boycott of Israeli products; the second a boycott of those companies that deal directly with Israel; the third, a boycott of those companies that deal with companies that deal with Israel). The US secretary of state officially and publicly asked the six Gulf countries to quickly end their economic boycott of Israel and put a halt to any money given to Palestinian organizations opposed to a settlement. US pressure to end the boycott found a positive response among a number of Arab countries, who lifted the second- and third-degree boycotts.

Despite the official persistence of the first-degree Arab boycott—with the exception of Egypt, Jordan, and the Palestinian territories occupied in 1967—some Arab countries quickly developed economic relations with Israel, unnecessary by any standards. Qatar, Oman, Tunisia, and Morocco exchanged trade officers, although a final, comprehensive settlement to the Arab-Israeli conflict had not been reached. Most of these countries, however, with the exception of Qatar, have officially broken their economic ties with Israel in accordance with the final resolution of the Arab summit held in Cairo in October 2000 following the eruption of the Aqsa Intifada.

The lack of coordination of the boycott policy with other, perhaps more important, economic policies, the fluctuations of Arab positions on the boycott, and the willingness to give up part of it with no real justification undoubtedly reflect the true nature of Arab official policy on the boycott. As mentioned previously, the boycott is a means of

absolving Arab states from the sin of dealing with Israel, a way of pleasing the Arab public without being part of a comprehensive, strategic policy to support Palestine and weaken Israel. In some cases, certain Arab countries adopted the boycott policy solely in consideration of the competitive advantages it would give them in regional markets.

There are several justifications for imposing a boycott on Israel: the Zionist attack on Palestine; the establishment of the Israeli state in 1948 on Palestinian land and Israel's hostile expansion of its borders; and the continued Israeli occupation of Palestinian and Arab lands. Nevertheless, the boycott's effectiveness will not be complete unless it is accompanied by positive steps to shore up the Palestinian economy by any means and link it to Arab economies. Palestinians must also be maintained on their land and absorbed economically to strengthen Palestinian capabilities to face Israel.

III. Revealing the boycott accounts

Despite the importance of the Arab economic boycott of Israel, rarely have any Arab studies been conducted concerning its actual effects on the Israeli economy, reflecting the true nature of this policy, as has been pointed out. There has been no official monitoring of the effectiveness of the policy and the extent to which it has accomplished its desired goals, as any other policy or strategy would be evaluated. Rather, the policy was put in place and left to work spontaneously with no development, despite the role of the boycott office subsidiary to the Arab League, which at times did not find a suitable reception in some Arab countries.

Under such circumstances, it was easy for the policy to be eaten away and weakened under US pressure and Israeli attempts to enter Arab markets through a third country—or even through Arab countries, such as Jordan, where the value of direct Israeli investment is at least US$300 million—or at times by not revealing the source of the commodity. The economic boycott was also eroded as more Arab businessmen began cooperating economically with their Israeli peers under US auspices, at times reaching unprecedented levels. In the

Israeli-Jordanian free trade zone, for example, products are exempted from customs charges when entering the US market.

Despite the scarcity of studies on the economic boycott and lack of evaluation as to its success or failure, there is one study of the Arab boycott office of the Arab League which states that Israeli losses as a result of the boycott in all its forms and degrees have reached approximately US$92 billion since the Israel's establishment.

In contrast, a report issued by the United Israeli Chambers of Commerce states that Israeli losses stemming from the imposition of the Arab boycott in the period 1952-1993 totaled US$45 billion, including US$1 billion in Arab investments that could have been directed to Israel were it not for the boycott. The remainder of the losses are due to possible Arab-Israeli trade which was not carried out and tourism revenues. Losses were also garnered as many international companies refused to cooperate with Israel when the second-degree boycott was still effectively in existence.

As shown by both Arab and Israeli evaluations, the boycott has been relatively effective, insofar as Israel has suffered huge losses, making western support of the state extremely expensive. Nevertheless, the boycott needed, and still needs, complementary policies that would shore up the Palestinian economy and reinforce its ability to withstand Israel.

IV. Feasibility of an Arab boycott of US goods

We pointed earlier to the rising popular calls for a boycott of consumer products imported from the US, or even commodities produced through US investments in some Arab countries. These calls find true justification in the perpetual favoritism exhibited by the US towards Israel and against the Arabs in general and the Palestinian people specifically. This bias reached provocative levels even for Arab leaders, not only Arab peoples, during the Camp David negotiations between Palestinians and Israelis, particularly when concerned with the Arab holy places. US bias was at its highest after the eruption of the Aqsa Intifada, with which Washington dealt as if it involved acts of violence on both sides, asking Palestinians to stop the violence. It is perfectly logical that US bias for Israel against the Arabs should lead to

increased Arab popular anger at the US. Boycotting its products is a means of expressing this anger and an attempt to demonstrate to what extent US bias towards Israel might harm US interests in the area.

Calls for a boycott of US products also have another important justification: the US uses the boycott policy more than any other country in the world against those countries that disagree with it, even if they are unable to threaten it or its interests. The US is also the first country to ignore the GATT agreement, trends to liberalize international trade, and agreements of the World Trade Organization if they are contrary to its own interests. For example, in its trade negotiations with Japan in 1995, the US proclaimed what it called the principle of fair trade, while Japan insisted on the principle of free trade. This US logic gives Arab countries the right to call for a boycott of US products in light of US bias towards Israel, in addition to its firm and absolute support of Israel, its guarantee of Israel's military superiority, and its standing with Israel in any battle against the Arabs.

These calls for an Arab boycott of US products are, in one form or another, an attempt by Arabs to alert American society, companies, and administrations to the interests that tie it to the Arab world. The Arab world consumes three times as many US products as does Israel, and it exports oil to the US, the lifeline of its economy. These interests call on the US to revise its absolute support for Israel at the expense of the Arabs.

As the calls for an Arab boycott of US products came from popular, rather than official, circles, official Arab imports have not been included in the boycott up until now. Until official circles are influenced by popular stances, Arab government imports of non-military commodities will continue to form an important percentage of the total Arab imports coming from the US. However, the greater part of US non-military imports head directly to the market, and the majority come through the private sector.

According to the IMF in its *Direction of Trade Statistics Yearbook 2000*, the value of Arab imports of US non-military commodities reached approximately US$21,148 million in 1998, comprising approximately 3.1 percent of all US consumer exports that year. The markets of Saudi Arabia, Egypt, the United Arab Emirates, Kuwait, Morocco, Algeria, and Lebanon are the most important Arab markets receiving US exports (see table 1). In the same year, the US earned profits on trade with the Arab world in the amount of US$6667 million as a result of the sharp decrease of oil prices that year, which averaged US$11.84 per barrel, compared to US$17.43 per barrel in 1997. Oil prices rose in 1999 to reach US$17.32 on average, then rose even more in 2000, to an average price per barrel of US$27.30 for the first nine months of that year. It is noteworthy that the US oil trade deficit was, for a long period since the 1970s, largely responsible for bringing the US trade balance from positive to negative, and it is still an important component of this deficit today (see table 2).

In 1999, Arab imports from the US fell to approximately US$18.1 billion, or approximately 2.6 percent of all US exports, after the primary Arab importers of US goods took severe steps to decrease in exports when oil prices dropped drastically in the fall of 1998 and early 1999.

As Saudi Arabia, the largest Arab importer of US commodities, did not take the position of boycotting the US even in popular form, the effectiveness of any boycott of these goods is considerably weakened. Saudi imports of US goods reached approximately US$10,525 million in 1998, comprising approximately 49.8 percent of the total Arab imports from the US that year. In 1999, Saudi imports of US commodities fell to US$8287 million, or about 45.8 percent of the total Arab imports from the US.

Thus, the influence of a partial popular boycott of US exports will be marginal, as Arab imports comprise only a limited amount of US exports. In turn, the message Arabs hope to send by boycotting US commodities will be largely symbolic, rather than effective. On the other hand, US projects or those in which Americans participate in Arab countries—which have been met with a strong popular desire to boycott—are the ones that will be harmed as they depend on local marketing. The message here will be effective, not merely symbolic.

It is nevertheless important to note that the US companies which would be affected by such a boycott are the same companies that pump investment into Arab countries. Accumulated US investment in Egypt, for example, reached approximately LE2869 million or US$755 million

at mid-1999. Moreover, some of these companies may be among those that have no dealings with Israel in any case. Thus, it is necessary to choose precisely which US companies will be boycotted, in order to punish those companies that cooperate with Israel and reward those that do not. More feasible in this case is reviving the popular and official second- and third-degree boycotts on Israel, boycotting those companies that deal with Israel and companies that deal with them in turn, whether they are US companies or not. The goal must be clear: pressuring Israel, laying siege to it economically, and punishing those that cooperate with it no matter what their nationality. This is a reaction to Israel's occupation of Arab lands, its repression of Arab peoples under occupation, and its accumulation of both traditional and nuclear weapons with which to threaten Arab countries.

In addition to non-military commodities, Arab imports of US weapons, particularly in the Gulf, comprise a central cog in the wheel of the US military-industrial complex. Although these are largely imports that find their way to warehouses where they sit until they become obsolete, it is impossible to stop their flow in light of the strong military ties between a number of Gulf countries and the US and considering the US forces located in the Gulf. Moreover, the US feeds the sense of regional fear among Gulf countries, leading to the purchase of more weapons and the planting of more US forces in the Gulf, in accordance with the needs of the US and the western media in general.

There are enormous actual and potential interests between the US and Arab countries in the fields of oil, trade, investment, and tourism. These interests should force the US to reevaluate its stance towards regional issues to protect its strategic interests with Arab states, which have not attacked the US but have taken defensive measures to face US favoritism towards Israel. The current situation could open the door on more clashes in Arab-US relations and lead to increased popular calls for the boycott of US commodities. It is enough that the US understand that even if Arab countries do not implement a boycott, they possess the principle source of the world's oil, which will allow them to inflict painful costs on the US if the price of oil were to be raised dramatically.

In short, the American people have interests that coalesce with those of Arab peoples. The US administration must respect these shared interests by reassessing its absolute and unacceptable bias towards Israel.

V. A Palestinian boycott of Israel: feasibility and possibilities

Following Israel's occupation of the West Bank, Jerusalem, and the Gaza Strip in 1967, there were two opinions in Israel on how to deal economically with the occupied Palestinian territories. The first was adopted by then Israeli minister of defense Moshe Dayan and the hawks in the government of Levi Eshkol. They supported what they called "economic integration" between the economy of Israel and that of the occupied territories: essentially joining the economy of the occupied territories to the Israeli economy so that it would become a market for Israeli goods and help solve the foreign markets crisis for Israeli exports. The territories would also become a source of cheap labor, to become irrevocably dependant on the Israeli economy.

The second strategy was adopted by the father of the Israeli economy and minister of finance Pinchas Sapir, who was not enthusiastic about lifting the curtain between the economy of Israel and that of the occupied territories. In contrast, he attempted to prevent the entrance of its labor force into Israel. It was clear that Sapir and his supporters wanted to deal with the Israeli occupation of the West Bank and Gaza as if it would not be permanent. As such, there was no need to have it merge with the Israeli economy. Nevertheless, the traditional colonial mentality won out and with it the opinion of Dayan and his supporters. The occupied territories were integrated into the Israeli economy through two types of colonial bonds. The first was making the Palestinian labor force and industry dependant economically; the second involved direct colonial subjugation in the fields of water, agriculture, and trade.

Concerning labor, Israel strove to arrest the development of the Palestinian economy, which weakened its ability to absorb Palestinian workers, who were in turn forced to seek work outside the occupied territories. Part of these workers headed to Arab states, while others

went to work in the Zionist state in blue-collar jobs in construction, sanitation, agriculture, and certain hazardous industries, such as weaving and dying. Before the outbreak of the first Intifada in December 1987, the number of Palestinian laborers in Israel had reached more than 150,000. Israel attempted to manage without Palestinian labor on those days it enforced a blockade on the West Bank and Gaza, or days on which workers went on strike. Nevertheless, the alternatives were not encouraging. Workers coming from eastern and southern Europe helped spread prostitution and crime, while workers from Asia contributed to the rise in drugs and prostitution. The number of Palestinian laborers in Israel remained at 33,000 official workers, and approximately three times that many unofficial laborers. Prior to the Aqsa Intifada, Palestinians were forced to work in Israel because the Palestinian economy—controlled for years by colonial Israeli policies—could not economically absorb the Palestinian labor force. Returns of Palestinian laborers in Israeli reached approximately 14 percent of Gross National Product (GNP) in 1998.

In industry, Israel worked to compensate for growth in this sector by stipulating that any industrial project must first get Israeli government approval, which many Palestinian industrial projects were unable to attain. The Israeli state also imposed higher taxes on Palestinian manufactured goods, weakening their ability to compete. And, although Israel obtained enormous taxes from Palestinians, it was not interested in establishing basic infrastructure in the West Bank and Gaza, except for that necessary for Israeli settlers and military purposes. In general, these policies deprived Palestinian industry and the economy of the basic conditions for growth and development: the existence of a developed infrastructure.

In addition, Israeli authorities allowed the establishment of non-necessary industries, such as sweets, leather, textile, and shoe production, along with garment and construction materials manufacturing. In general, these industries depend on Israeli equipment and machinery, and in some industries, Palestinian production was only a stage in essentially Israeli industry, particularly in the areas of textile and garment manufacturing. In 1997, primary and processing industries and the water sector in Gaza and the West Bank (not including

Jerusalem) absorbed about 15.3 percent of the actual Palestinian labor force, while the construction sector absorbed approximately 25.6 percent of the work force. The industrial sector, including primary and processing industries, water, and gas, accounted for about 20 percent of Palestinian Gross Domestic Product (GDP) in 1997, while the construction sector accounted for 10 percent in the same year.

In the water and agricultural sectors, Israel clearly knows that water is a decisive limit to the growth of the agricultural sector and its ability to absorb new immigrants. Since the 1967 occupation, it has engaged in a methodical process of stripping water resources from the West Bank especially, continuing previous policies. Israel has destroyed a large number of Palestinian pumps on the Jordan River and prohibited the farming of lands close to the Palestinian-Jordanian border, justifying these measures with security concerns. It has also dug deep wells in close proximity to Arab wells to divert the water from them, salinizing the well or in some cases even drying it up as water is diverted to Israeli settlers in the occupied territories or into Israel proper. Israel also confiscated approximately half the lands of the West Bank and Gaza.

As a result of these policies, only 4 percent of the agricultural lands of the West Bank—the principal source of water in Palestine before 1948—are farmed with irrigation systems; the remaining agriculture is dependent on rainwater, and these are less-productive alternating crops. In contrast, Israel farms 45 percent of the agricultural land under its control since 1948 with irrigation systems largely dependent on the water it plunders from the West Bank and water resources shared with the surrounding Arab countries. (See *The Middle East and North Africa 1999, Europa Publication Limited, London, p. 672.*) According to the same source, 120,000 Israeli settlers in the West Bank and Gaza consume 56 cubic meters of water in agriculture, whereas 3 million Palestinians consume 152 million cubic meters for the same purpose. That is, each Palestinian consumes approximately 50 cubic meters of water for agriculture, while each Israeli settler consumes 466 cubic meters, or about 9.3 times as much.

One result of Israeli water policies in the occupied territories is that the percentage of salinized subterranean water in the Gaza Strip—poor

in water resources at any rate—has reached three times the level declared safe by the World Health Organization. It is hazardous to the health as well as to agriculture as a result of Israel's diversion of water resources for settlers. This is especially grave in light of the frightening population density of the Gaza Strip, where there are 2808 people per square kilometer in the main cities and 483 people per square kilometers as a whole—the fourth largest population density in the world, after Hong Kong, Singapore, and Bangladesh.

In addition, Israel has used the pretext of security concerns to destroy Palestinian horticulture, weakening further the Palestinian agricultural economy's ability to absorb the work force and produce the agricultural commodities necessary for residents. Israel has also put tough limits on the development of fishing in the Gaza Strip, also under the pretext of security concerns, although there are enormous possibilities to develop this sector and increase its share in national production, which would absorb more of the Palestinian labor force.

In trade, Israel controls foreign trade in the West Bank and Gaza in line with the worst colonial traditions, turning the markets of the occupied into a market for goods of the occupier. It also controls the country's import structure for security reasons. As a result, more than 87 percent of imports to the West Bank, Gaza, and Jerusalem come from Israel. In 1997, the value of Israeli imports into Palestine reached US$1803 million. The lands occupied in 1967 are considered the second most important market for Israeli goods after the US and before any European country. Similarly, 75 percent of Palestinian exports go to Israel, which imported Palestinian goods worth US$358 million in 1997. As is clear, there is a large, persistent Palestinian trade imbalance with Israel, which reached US$1445 million in 1997, according to *The Middle East and North Africa, 1999*.

It is clear that the Palestinian economy is dependant on that of Israel, capable of being exploited and oppressed by the occupier. This relationship was put in place under pressure from the occupier and with arbitrary regulations that completely ignored the international laws that are supposed to rule the relationship between an occupied country and its occupier. According to a Palestinian study published by Institute of Political and Economic studies in late 2000, since its occupation of the

Gaza Strip, East Jerusalem, and the West Bank, Israel has established production and economic foundations and structures to produce goods to meet Palestinian demand and has protected and subsidized these commodities to encourage further growth and development. This is negatively reflected on the possibilities for development and growth of alternate Palestinian economic structures, especially in light of the protective measures Israel has taken to prevent such development.

In any case, there is no disagreement over the colonial nature of the uneven economic ties that Israel has established with Palestinian lands occupied in 1967. Judging from the current situation, these ties are likely to remain as they are, even if trade between the two sides is liberalized, due to the uneven balance of power. There will be no opportunity to create ties based on justice, even if the Palestinian Authority wanted to do so, without first undoing the present economic ties between the two sides. Palestinians must begin a comprehensive program to build the foundation of economic independence for the future Palestinian state, reassessing the structure of its foreign relations on all levels to serve this goal. In order to undo the present economic ties, a clear and decisive political step is required. As we will now try to show, funding such a process is completely within the realm of possibility.

VI. Undoing Palestinian-Israeli economic ties: justifications and possibilities

Considering the Palestinian economy's dependence on and exploitation by the Israeli economy, liberating the Palestinian economy from these ties has every justification. It is necessary, indeed urgent, to achieve true Palestinian national independence on all fronts. Such independence does not mean isolation, but replacing exploitative, dependent ties with a colonial nation for ties with Arab and European states and others based on balance and justice.

Nevertheless, breaking these ties is a complicated, but feasible process, though ties in areas of land, water, and fishing will remain as they are as long as the Israeli occupation continues. Thus, at the present time, it is necessary to focus on undoing the Israeli-Palestinian economic relations in the areas of industry, labor, and trade, until

Palestinian independence is obtained and all Israeli-Palestinian ties can be undone.

As the Palestinian economy lacks great agricultural possibilities, there is an urgent need to build a Palestinian industrial economy separate from Israel, although such a separation has an economic price. Those industries that depend on equipment, raw materials, or primary components that come from Israel, or those that only comprise a stage in Israeli production, will bear different costs as the price for breaking their ties with Israel and creating alternate relations with economic organizations and Arab or European markets. Although there is no difficulty in the availability of machinery, raw materials, primary components, or markets, replacing Israeli equipment with new equipment in some Palestinian industries will constitute a one-time large expense. The expense can be lessened by exchanging older equipment, while newer equipment can remain in use until it has run its course. Spare parts can be manufactured locally using reverse engineering—i.e., deriving the form of the part from the existing machinery—or can be imported, as long as they are not from Israel, whenever possible. Machinery can be replaced by new non-Israeli machinery as the price of building an independent Palestinian economy. It is obvious that raw materials can be immediately imported from any other country besides Israel with no appreciable losses. In addition, there are three principal directions that Arabs and Palestinians can take to build the Palestinian economy and support its ability to face Israel.

I. Opening Arab markets to Palestinian commodities

Opening up foreign markets to Palestinian goods is one of the most important means of developing the Palestinian economy. Arab markets must be opened to Palestinian exports to absorb those exports that would otherwise go to Israel. The value of total Palestinian exports to Israel that need to be diverted did not exceed more than US$358 million in 1997, and these are all products imported by several Arab countries, including vegetables, citrus fruits, flowers, marble, sweets, leather, and shoes. On the other hand, Palestinian imports coming from Israel totaled US$1803 million in 1997. When Palestinian-Israeli economic ties are broken, a large part of Palestinian import demands will be met by Arab products.

Arab states must lift all barriers—be they customs, quotas, or seasonal barriers—to Palestinian exports, in order to truly support the Palestinian economy and the process of building its independence. Opening US markets to Israeli products was an important factor in encouraging the growth and development of the Israeli economy, particularly after the two signed a free trade agreement in 1983, which allowed Israeli exports into the US with no barriers. At the same time, US exports have not been given a similar reception on Israeli markets, and the US administration has complained to Israel of administrative and other barriers that act as obstacles to the free flow of US goods to Israel. (See George W. Paul and Douglas B. Paul, *Emotional Ties: American's Involvement with Israel Since 1948 Until Today*, New York: W. W. Norton, Arabic translation by the General Information Authority, Cairo, in the series of translated works, #820, p. 257.) If 35 years after its establishment, Israel needed to free its export movement to the US to strengthen and develop its economy, Palestine is even more in need of Arab countries opening their markets without barriers to Palestinian exports, in order to build a strong Palestinian economy and reinforce its independence.

In order to encourage Palestinian industry to break its ties with the Israeli economy, Arab markets must open up to those Palestinian commodities which contain no Israeli components and which were manufactured with no Israeli equipment or machines. Those products that employ Israeli equipment and machines already available can also benefit from the opening of Arab markets for a period of five years, on the condition that all interaction with Israel be stopped immediately. Within those five years, the manufacturer should exchange its obsolete or broken machinery with new equipment from Arab countries, or any other source but Israel.

It is obvious that the means of undoing the industrial ties between Palestine and Israel also involves undoing trade relations. Every commodity imported by Palestine from Israel has an alternative in Arab, European, or other countries. As long as the Palestinian Authority has the freedom to determine the source of its imports, it is

necessary to completely stop the influx of Israeli imports. It is unthinkable for Palestinians to import Israeli commodities and thus contribute to the growth of the Israeli economy and, in turn, its overall capacities, which are used to strengthen its occupation of Palestinian and Arab lands and to fund repressive operations against the Palestinian people.

In terms of labor, breaking Palestinian and Israeli economic ties means providing work for the approximately 33,000 Palestinian laborers who legally work in Israel, and about three times that many who work unofficially in Israel. Thus will a large section of the Palestinian people stop depending on the occupying state to provide a source of income, as this dependence contradicts the necessity of achieving independence from the occupier.

If labor ties between Palestine and Israel are broken without providing alternative jobs for Palestinian workers, it will drastically raise the level of unemployment in Palestine. The Palestinian work force was approximately 600,000 in 1998; of these about 419,600 had jobs, while 180,400, or 30 percent, did not (see *Bayanat al-taqrir al-iqtisadi al-'arabi al-muwahhad*, 1999, p. 331). Considering that the total number of Palestinians who work in Israel, both legally and otherwise, is approximately 130,000, breaking labor ties means that the Palestinian economy must provide new job opportunities for about one-fifth of its labor force to prevent them from becoming unemployed and raising the level of unemployment. This would also negatively impact Palestinian GDP and the standard of living in Palestine.

For workers, two options are available to treat the effects of a break in economic ties. The first is sending Palestinian workers to those Arab countries who require a larger labor force, but this is a negative choice considering the necessity of building a Palestinian state and economy that can act as a main pillar of its overall capacities. Such a choice would mean sending even more Palestinians abroad, while achieving Palestinian independence requires maintaining them on the land and their participation in the struggle to achieve independence in all its forms, including working to build a strong Palestinian economy.

The second choice is funding industrial and service projects in the Palestinian territories occupied in 1967 to absorb the Palestinian labor force that would otherwise head to work in Israel. This would also absorb new entries into the Palestinian labor market and lessen widespread unemployment among Palestinians. This choice is more difficult as it poses the question of how to fund such projects. This choice, however, is the one that will build a Palestinian economy independent of Israel. Thus the question arises of how this might take place.

II.Arabs and Palestinians abroad: building an independent Palestinian economy

A strong Palestinian economy is one that would be able to meet the basic necessities of the Palestinian people, achieve a high standard of living for citizens, absorb the Palestinian labor force by providing enough job opportunities to employ workers who would otherwise head to Israel, and absorb the already unemployed as well as new entries into the work force. This issue is decisive in achieving comprehensive independence from the occupying state, i.e., Israel, whether it takes place before or after political independence.

In considering how to fund the construction of a Palestinian economy that would employ Palestinians and ensure a high enough standard of living to keep them on their land, there is an important example to follow: the process of funding and building the Zionist economy in Palestine during the British Mandate and the ways in which it was strengthened after the state of Israel was established.

The process of building the Israeli economy in Palestine, as well as developing a military force and attracting immigrants, began completely through outside funding. Indeed, it was the pivotal point in establishing a Zionist state in Palestine. In the period between 1904-1914, approximately 40,000 Jews immigrated to Palestine. Some settled in Palestinian cities, while one-quarter established themselves in 47 settlements set up on an area of 420,000 dunams, most of which was purchased by the Jewish Baron Edmond de Rothschild. The cornerstone of the Jewish agricultural economy in Palestine was formed, funded, and expanded by the World Zionist Organization and the United Jewish Fund. It was increased several times over with the outcome of the 1948 war.

Israeli industry began in earnest in the 1930s with the signing of the Haavara Agreement with Nazi Germany in 1933. Under the terms of this agreement, German Jews immigrating to Palestine were able to transfer their capital in the form of German goods to Palestine, in increments of at least BLE1000. Under this agreement about 60,000 Jews left Germany and Austria.

There are substantial differences concerning the amount of money which was poured into Palestine as a result of the Haavara Agreement. Primary calculations would indicate that the immigration of 60,000 Jews, each transferring at least BLE1000, would mean an influx of German products valued at no less than BLE60 million. However, the *Encyclopedia Judaica* puts the number at only BLE8.1 million, while Arab estimates place it at more like GM140 million. Even taking the lowest estimate of BLE8.1 million, it is an enormous amount compared to the size of the Palestinian economy in the 1930s. In 1938 the total amount of Palestinian currency in circulation did not exceed LE5 million.

In any case, Jewish transfers in the form of goods from Nazi Germany into Palestine allowed German Jewish immigrants to fund the establishment of industry through this capital, most of which was taken in the form of investment commodities, that is, machinery necessary for industry.

It was no accident that Jewish military industry in Palestine began in 1934, one year after the beginning of the Haavara Agreement, which acted as a decisive point in the history of Jewish industry in Palestine. Industry in general, even after the establishment of the Jewish state, focused on military industry, which still continues to occupy a leading place in Israel's industrial economy.

During World War II, the British army depended on Jewish military industry in Palestine to manufacture some of its military needs. Between 1942-1944, Jewish factories in Palestine produced about 3.6 million anti-tank mines and 7.9 million hard steel containers. The net value of products from Jewish factories in Palestine made for the British army during the war reached about BLE33 million.

British permission to establish a Jewish military industry in Palestine before World War II, followed by its activation of the sector by creating demand for its products during World War II, is one of the most decisive factors in the establishment and development of this industry. It was also an important element in the Zionists' ability to take Palestine.

Since its establishment in 1948 through 2000, Israel has received enormous foreign aid in the form of loans, valued at approximately US$171.5 billion. Compensations received by Israel in the same time period reached approximately US$137.5 billion (putting the dollar at its current value), including US$64.5 billion in US grants, US$10 billion in Jewish donations, and approximately US$60 billion in German reparations from 1953-1996, according to statements by then German foreign minister Klaus Kinkel. Add to that about US$3 billion in German compensations from 1997-2000 according to the average annual rate of compensations, estimated at US$743 million in 1994 according to the Israeli Statistics Office.

The loans Israel received from 1948-1998 total US$34 billion, most of which were granted by the US, which has given loans to Israel totaling US$2105 million, in addition to the US$10 billion obtained after the first Bush administration guaranteed loans at financial institutions for Israel. The US has also given US$11413 million in military loans, bringing the total value of loans given to Israel by the US to about US$23518 million. (See Ahmad al-Sayyid Naggar, *Dawr al-musa'idat al-kharijiya li-Isra'il min 1948-1996 bi-bina' dawla*, published by the Ahram Center for Political and Strategic Studies, Cairo: 1998, p. 38.)

The value of these loans and grants has been raised by current prices, as a large portions of them went to Israel immediately after its establishment, or were distributed over the years from1948 until 2000. Thus, their value in terms of current dollar prices is increased several times over.

In addition to sizeable loans and grants, Israel has received much direct foreign investment, although it has remained in a state of war from its establishment until the present time. It is thus clear that these investments have been directed to Israel due to political, rather than economic, considerations, as the most important factor in determining the flow of capital in investments, both direct and non-direct, to any

country is the extent to which that country enjoys political stability, internal security, and stable political and military relations with its neighbors. The value of foreign assets in Israel reached about US$23.4 billion in 1994, all of which is Jewish capital or that of Israeli sympathizers.

Given the above, it is clear that the Zionist economy in Palestine during the British Mandate and the building of the Israeli economy after the establishment of a state in 1948 took place through substantial US aid, German reparations, and the influx of capital from wealthy Jews all over the world.

Similarly, the building of a strong Palestinian economy capable of guaranteeing a high standard of living for its people, absorbing them economically, and funding the struggle against Israel will not be achieved except through pumping investment into the West Bank, Gaza, and Jerusalem. This can come from both wealthy Palestinians living outside the occupied territories, as well as wealthy Arabs. Indeed, investments belonging to Arabs both inside and outside the Arab world reached US$1 trillion in 2000; Saudi Arabian businessman Prince al-Walid Ibn Talal alone had investments totaling US$24 billion in 2000. He has donated US$5.3 million to support Palestinian workers unemployed due to the Israeli blockade of the occupied territories. Such good spirits must be extended to include direct investment or joint ventures with Palestinians in the West Bank and Gaza, and it must be extended to other Arab businessmen, including Palestinians living abroad, so that there is an effective collective effort from Arab businessmen to build the Palestinian economy and strengthen its ability to free itself from the Israeli economy.

A number Palestinian businessmen living abroad have formed the Palestine Development and Investment Company (Padico), dedicated to investing in the occupied territories. The company has concentrated on large projects, such as the industrial area in Gaza, whose total investment stands at US$40 million. It has also invested in tourist projects in Jerusalem, specifically in holy areas, in the amount of US$25 million. Similarly, the company participated with the Arab Bank, the Palestinian Authority, and the United Contractors Company in an electricity project to meet the needs of Palestinians, enabling them to break away from Israel in this sector. Padico also joined forces with the Palestinian Authority to establish the Palestinian Communications Company, enabling it to be independent of Israel in the communications sector as well. The Palestinian Arab Investment Company has invested about US$18.5 million in the National Aluminum Production Company and about US$5 million to establish freezer storage for agricultural produce.

Nevertheless, according to the Palestinian minister of planning and international cooperation, the total investment pumped into the occupied territories by Palestinians abroad has not exceeded US$1.5 billion. This is a trifling amount that does not do justice to the large financial resources of Palestinians abroad. But as much as economic independence requires increased funds from Palestinians abroad, it also requires wealthy Arabs, particularly from the Gulf, to invest in the development of the Palestinian economy in such a way that would achieve profits for investors as well.

III. An Arab fund for developing Palestine

Leaving aside the Palestinian and Arab private sector, Arab states have not shown any awareness of the importance of positive support to build the Palestinian economy since the beginning of the Arab-Israeli conflict. Even when the Arab Summit was held in Cairo in October 2000 after the outbreak of the Aqsa Intifada, its resolutions concerning financial support to the Palestinian people were limited to establishing an Aqsa fund in the amount of US$800 million, in order to preserve the identity of Jerusalem and free the Palestinians from dependence on the Israeli economy, and an Intifada fund in the amount of US$200 million, for the families of martyrs. After the amounts were disbursed over member states, the amount allocated for both funds did not exceed US$683 million, most of which had not actually been paid by the end of 2000.

Despite official Arab awareness of the need to support the Palestinian people economically, the Palestinians themselves are not in need of one-time aid disbursements, but a steady flow of annual aid provided largely by the wealthy Gulf states. Hence, we call for the establishment of an Arab Fund to Develop Palestine, whose resources

would be earmarked for establishing industrial and service projects to absorb the Palestinian labor force and create a strong Arab Palestinian economic base. The fund could also be used to provide long-term loans to Palestinians living in the occupied territories, with no-interest or low-interest loans (no more than 3 percent), like those given by the World Bank to the poorest countries. The loans could thus be used to fund productive projects in the occupied territories and to put an end to Israeli-Palestinian economic ties and replace them with Arab ties.

A fund to develop Palestine would require approximately three times as much money as that set aside by both the Intifada and Aqsa funds in order to be effective in achieving its goal. The money required for the fund is easily found, even if over the course of two years, in the Arab oil states, who have achieved exceptionally high revenues for the last two years as a result of the increase in oil prices. Exports in Saudi Arabia, for example, went up from US$38.7 billion in 1998 to US$48.5 billion in 1999, and are estimated at no less than US$75 billion for the year 2000.

Both Arab countries and Palestinian people failed to prevent the taking of Palestine, either because they were colonized, ruled by regimes subservient to colonizers, or unaware of the seriousness of the Zionist threat to Arab rights, land, and aspirations. These same countries now have the historic mission of repairing the situation, at least partially, by bearing their responsibility to build an independent Palestinian economy as the basis for the maximum capacity and total independence of occupied Palestine.

Table 1
Arab trade with the U.S. (in $ million)

Country	U.S. exports							U.S. imports						
Year	1993	1994	1995	1996	1997	1998	1999	1993	1994	1995	1996	1997	1998	1999
Algeria	895	1191	775	632	695	650	470	1711	1664	1807	2270	2646	1799	1987
Djibouti	13	7	10	8	7	20	18	--	--	--	--	--	1	--
Mauritania	19	14	43	15	18	19	26	7	4	7	7	--	--	1
Morocco	602	405	522	476	438	553	525	201	211	256	275	328	368	410
Somalia	31	30	8	4	3	3	3	--	--	--	--	--	1	--
Sudan	53	55	44	50	37	7	7	12	37	24	20	13	3	--
Tunisia	232	327	215	189	251	197	283	43	59	67	81	67	65	67
Bahrain	653	443	253	244	406	295	358	109	165	146	124	126	170	236
Egypt	2763	2844	2985	3146	3840	3060	2982	664	594	655	714	695	699	659
Iraq	4	1	--	3	82	107	20	--	--	--	--	317	1361	4266
Jordan	363	288	333	345	402	353	303	20	31	31	26	26	17	31
Kuwait	1009	1175	1416	1979	1394	1479	1069	2003	1598	1469	1782	1998	1471	1551
Lebanon	377	443	590	628	551	514	380	28	26	36	43	80	85	53
Oman	252	219	220	215	342	303	198	305	497	321	448	261	230	226
Qatar	166	162	223	207	360	354	155	72	87	99	163	168	237	291
Saudi Arabia	6666	6011	6085	7295	8451	10525	8287	8432	8307	8898	9443	10353	7169	8734
Syria	186	99	223	226	181	161	170	145	72	65	16	30	48	95
U.A.E.	1811	1593	1994	2527	2606	2370	2680	775	479	486	538	965	708	737
Yemen	318	178	185	256	154	178	163	110	199	44	31	18	43	20
Total	16413	15485	16124	18445	20218	21148	18097	14637	14030	14420	15981	18091	141475	19364

Table 2
Oil imports, the U.S.-Arab oil trade deficit, and the overall U.S.-Arab trade deficit 1974-2000

Year	Oil imports (in million bpd)	Oil trade deficit (in $ million)	Overall balance of trade (in $ million)
1974	6.1	-23876	-3884
1975	6.1	-24289	9551
1976	7.3	-31228	-7820
1977	8.8	-41093	-28353
1978	8.4	-37965	-30205
1979	8.5	-54801	-23922
1980	6.9	-75803	-19697
1981	6	-72963	-22267
1982	5.1	-54511	-27510
1983	5.1	-48659	-52409
1984	5.4	-52454	-106703
1985	5.1	-45768	-117712
1986	6.2	-31503	-138279
1987	6.7	-38363	-152119
1988	7.4	-35094	-118526
1989	8.1	-44683	-109999
1990	8	-54682	-102496
1991	7.6	-44396	-66723
1992	7.9	-44805	-84501
1993	8.6	-44831	-115568
1994	9	-45167	-150629
1995	8.8	-48047	-158801
1996	9.5	-64038	-170214
1997	10.2	-62560	-180522
1998	10.7	-43690	-229758
1999	10.9	-60055	-328821
2000*	10.8*	-50994*	-199326*

*Figures for 2000 cover only the first six months of the year

Corruption and anti-corruption efforts in the Arab world

The year 2000 saw a number of Arab countries put the fight against corruption among their most important priorities. In some cases, this was a genuinely felt position, while in others it was simply an empty claim or related to a settling of political accounts. The official position in a number of Arab states coincided with popular demands to fight corruption and similar demands made by the cultural elite, who believe that combating corruption is necessary to achieve progress and social, political, and economic development in Arab countries. Despite the existence of effective anti-corruption institutions in some Arab states, most anti-corruption campaigns in the Arab world revolved around exposing individual cases rather than treating the roots of corruption. These states did not advance to the stage of refining the controls that actually prevent corruption, nor did they work to create institutions that enjoy true independence and the right to information connected to state affairs and domestic and foreign contract, so that a war could truly be waged against corruption. However, certain states did throw a stone in the pond of corruption, whose waters had stood stagnant for many years. The important thing now is to follow up on these efforts and further them through a public dialogue in order to protect and develop Arab societies and to develop the foundations of stability and the political and economic systems of Arab states.

Combating corruption in Arab states is of the utmost importance, as corruption has a destructive effect on all social, economic, and political levels, particularly when it goes from being an exceptional phenomenon to a general state of affairs endemic to the economic, political, and social structures.

This study will examine corruption in Arab states and the steps taken to combat it. It will also review the position of certain Arab states in the context of worldwide corruption according to the corruption index of Transparency International (TI), a Berlin-based, non-governmental organization (NGO) established in 1993 with the mission of working to stamp out corruption. First, however, corruption itself must be defined, to distinguish it from the black market, for example. It is also necessary to describe the general causes of the appearance, growth, and spread of corruption and the effects it leaves on the economic, social, and political structures. Finally the current international climate towards corruption must also be examined, as this is the historical milieu in which corruption and anti-corruption efforts are undertaken in Arab countries.

I. Defining corruption

Corruption, and the wealth derived from it, are considered part of the black market, which includes all illegal and illicit activities, such as the drug traffic, prostitution, unauthorized gambling, and the illegal arms trade, as well as the trade in human organs, children, and currency, and other activities. If the black market economy seeks to make a profit and amass wealth outside of legal frameworks, corruption is an aspect of this illegal economy that depends on the abuse of influence and privileges by high-level civil servants and political and economic officials who seek to attain profit and wealth unlawfully. As corruption gains currency, it extends to low-level civil servants who have the authority to grant official documents or licenses. There are certain systems which are corrupt by their very nature, such as state systems based on the control of one tribe or family over all political authority and natural resources. The ruling family or tribe is thus free to exploit political power to take possession of the people's wealth. States in which ruling families or tribes leave the administration of the state to parties and political forces that have the trust of the people and turn over the administration of natural resources to specialists and professionals—only receiving expenses to cover the general needs of the ruling family—are not by definition corrupt systems. Corruption occurs when a family or tribe puts its grasp simultaneously on power and wealth and unjustly expropriates a large portion of the national wealth.

Some researchers at the World Bank believe that corruption is a symptom of poor organization and administration. (See Daniel Kaufmann, Aart Kraay, Pablo Zoido-Lobaton in the International Monetary Fund's [IMF] *Finance and Development*, June 2000.)

Although these two elements are necessary for the spread of corruption, corruption itself is the expression of a desire to own and possess wealth and authority. When this desire is not accompanied by a legal means to attain it, it creates the incentives and psychological motives necessary to break the law in order to amass wealth illegally—in other words, it breeds corruption. A condition for corruption is some degree of poor organization and administration which allow for the breaking of the law and the circumvention of legal channels. In order to spread and grow, corruption requires the absence of transparency and accountability, which create particular problems in countries where there is no regular circulation of political power.

Thus, corruption, in one form or another, is a process of fraud which seeks to illegally amass property and wealth from state transactions. It is also the attempt to avoid paying state revenues. Bribery is the primary form of corruption, taking place primarily on the borders or the meeting points of the private sector and the state, and involving civil servants, political officials, and businessmen.

II. Causes of corruption

There are several causes for the appearance, growth, and spread of corruption in any state, which can be summarized as follows:

1. **The lack of transparency and the right to information related to state affairs and finances** enables government employees and high-level civil servants to break the law and shirk their professional obligations. They are thus able to profit illegally without being forced to share information that might implicate them. In such cases, information related to state enterprises is shared only selectively, meaning that it is not revealed at the same time to all parties and businessmen involved—in other words, there are some who know before others. As a result, information has a price, which those lucky enough to be in the know will pay; it also brings a financial return to civil servants who manipulate information about state enterprises.

2. **The weakness or absence of real and effective means to monitor state officials and their administration, police and security officials, and local administrations and authorities.** In such cases,

there is little or no deterrent to corruption, and it will grow and spread as the possibility of being subject to official investigation is little to none. The chances that corruption will spread increase the more central authority is transferred to local and provincial administrations, where oversight may be totally absent.

It should be noted that the weakness or absence of effective monitoring is often linked to those systems where popular political participation is either weak or absent altogether, as is popular oversight over government enterprises and officials. Effective oversight is also weaker or absent in absolute monarchies which are based one family or tribe's control over all political power and natural resources.

3. **A lower pay scale for civil servants and workers in public administration, the police, and local administrations and authorities compared to private-sector employees, and an income for public-sector employees that is too low to guarantee a decent life.** This creates a motive for some workers to use their authority to illegally amass wealth through bribes, which they receive as a condition for facilitating the work over which they have authority.

At the same time, a low pay scale means that government administrations, the police, and local authorities lose the most skilled and honest workers, who go to the private sector, self-employment projects, or abroad to obtain a better income that can guarantee a decent standard of living without resorting to corruption.

The opportunities for corruption increase if a state has a complex bureaucratic system that must be navigated to complete a job or obtain a license or an official document. The same is true if the state has conflicting laws as a result of economic and political transformations that introduced new laws to reflect a new reality while simultaneously maintaining outdated laws untouched. Thus does corruption become a back-door means of overcoming this bureaucracy and the contradictions inherent in the law.

4. **Allowing state officials and those in the public sector wide-ranging authority to grant licenses and official documents and manage the public sector without effective official or popular oversight, and without establishing a clear principle of transparency.** This leads to the appearance of corruption embodied in

the bribes government employees receive in exchange for licenses and official documents. It is also seen in the bribes given to prominent directors in the public sector who then grant benefits to preferred clients and amass wealth through manipulating purchases and inventory and through selling products and depreciable assets.

5. **Unclear tax and customs systems combined with the existence of wide-ranging authority for customs and tax officials without any effective oversight or precise monitoring of their personal finances.** This often allows officials to solicit bribes from taxpayers in the private sector and from commodities importers, particularly large businessmen, in return for reducing their tax burden or eliminating it completely, or in exchange for facilitating the entry of imports without collecting the proper customs payments.

6. **The absence of strict laws which act as an effective deterrent to corruption, in addition to the absence of an independent judiciary that faithfully applies the laws of the state on state officials themselves.** In such situations, the forces of corruption are freed from the fundamental deterrent force, allowing them to grow and spread.

7. **The transitional phase from one political, social, and economic system to another** often witnesses the appearance and growth of corruption, particularly when the transition is unexpected and unorganized, or when a conflict still exists between the forces of the old and new regime. Such a situation can create the rise of sudden wealth and lead to the spread of organized crime networks that include high state officials and civil servants. As they work to break the *ancien regime* and transfer the center of state finance to businessmen of the new regime, an important part of the nation's wealth is also transferred to their private accounts and those of organized crime members. Russia in the age of Yeltsin is the prime example of this kind of state at its worst.

8. **The program of selling the public sector to the private sector, or privatization, greatly helps the spread of corruption.** Susan Rose-Ackerman, professor of economic and privatization studies, says in her study of corruption and anti-corruption mechanisms that transferring state assets to private-sector ownership can create in and of itself

incentives for corruption. Selling a large government company is similar taking bids for a large infrastructure project; thus, the incentives for professional misconduct are correspondingly large. She points out that the privatization process in Argentina, for example, at one point aided those who had access to inside information and connections. Similarly, the privatization process in Thailand included extortion and paying commissions. The same thing is true in Eastern Europe, where the privatization process came to include corrupt transactions. (See Susan Rose-Ackerman, "The Political Economy of Corruption," in *Corruption and the Global Economy*, translated by the Ahram Center for Translation and Publication, Cairo, 2000.)

9. **Poor oversight over foreign economic transactions, particularly government transactions with foreign companies, whether in service or commodities imports or in contracts with foreign companies hired to implement projects inside the country in question.** Poor oversight leads to the spread of bribery, as foreign companies pay local officials to win contracts they would otherwise lose in a fair, free competition. Corruption connected with foreign transactions increases as popular and official supervision over foreign contracts decreases. Moreover, popular supervision over foreign contracts and high-level state employees and political officials cannot be achieved except within a truly democratic system in which political power on all levels is regularly circulated. This transfer of power comprises one of the most important guarantees of combating corruption connected to political influence, one of the most serious forms of corruption as a whole.

10. **Poor popular and official oversight over the banking sector, the stock exchange, and the financial sector in general.** This provides the opportunity for the appearance, growth, and spread of corruption, embodied by the tendency of high-level banking officials to take bribes in return for granting loans with insufficient or no collateral. It also enables stock exchange officials to disregard violations by brokerage firms, market-setting companies, and companies listed on the exchange in return for commissions. Infractions by these companies or by favored clients are disregarded at the expense of small and medium investors, although the latter are actually the true generators of a rise in

any stock exchange, comprising the most stable element for transforming the stock exchange into a mechanism for financing new investments and pumping liquidity into the private sector and the state—the two primary positive roles of the exchange. Other activities on the exchange may in fact have negative effects, such as speculations by local and foreign investors that create quick profits, by both legal and illegal means, at the expense of economic stability and the interests of small and medium investors.

Similarly, poor oversight over the insurance sector can lead high-level insurance officials to collude with clients to defraud insured companies or firms undertaking maintenance on machinery, equipment, and durable goods.

11. **Favoritism, particularly appointing relatives of political officials to important economic and administrative posts for which they are not qualified.** Favoritism is a symptom of the spread of corruption in undemocratic states, and even in some semi-democratic countries, such as Japan, South Korea, and Mexico, according to Kimberly Ann Elliot, a researcher at the Institute for International Economics. (See *Corruption and the Global Economy*, Ahram Center for Translation and Publication, Cairo, 2000.) While favoritism in its various forms is one symptom of corruption, it also causes it to spread on a wider basis. Those appointed to posts by dint of their political connections are not subject to oversight, even in its lesser forms, and thus there is ample opportunity for them to abuse their authority in order to profit illegally from their position. Even worse, they create an example of corruption to be followed by high-level state officials who participate in corruption.

12. **A generally sluggish political life resulting from long-term oppression and tyranny over the people, crackdowns on the opposition, and the marginalization or lack of popular political participation.** This can weaken or even temporarily put an end to deterrents to corruption. In such a state, the growth and spread of corruption is held in check only by oversight mechanisms within the ruling system; if these mechanisms are weakened, or if the system and its leaders are involved in corruption, the state becomes a breeding

ground for the worst sorts of corruption, with no official or popular supervision.

13. **Huge gaps in the income levels of the upper class on one hand and the middle and lower classes on the other** empowers the financially strong upper classes and high-level state officials and gives them the ability to justify their behavior with the finances and assets of the state. They are able to buy the media and use it to their own ends, while the low and middle classes are too weak to combat corruption. Indeed, one way of coping with the situation is through participating in corruption on the small scale enjoyed by low- and middle-level civil servants. This, in turn, leads to a general acceptance of corruption, a serious state of affairs that can only be remedied by exceptional efforts.

II. The fruits of corruption

Although corruption is immoral, examining its effects on the economy and the political system needs to be an objective process, starting from a true assessment of its role and effects on the economic, social, and political systems. There are those who believe that a certain level of corruption comprises an important mechanism for accumulation, as it places property and assets that would have been distributed over a great number of citizens into the hands of one person or a group of corrupt individuals who can then use it to institute projects and spur on economic growth. Machiavelli believed that corruption had its purposes and benefits for both individual and society. The American political scientist Samuel Huntington believes that an inflexible, centralized, but honest bureaucratic system is worse than an inflexible, centralized yet corrupt system, in terms of the effect both have on economic growth. The latter, despite its corruption—or perhaps because of it—allows for a growth in enterprise. (See Robert Klitgaard, "Subverting Corruption," *Finance and Development*, IMF, June 2000.)

But this ultra-pragmatic view only justifies an understanding of corruption, and perhaps a tolerance for it as well. The accumulation of wealth with a group of corrupt individuals who can leave the national economy and flee abroad to escape investigation can funnel off national resources—resources that were amassed illegally and immorally in the

first place. Corruption in a centralized, inflexible bureaucratic system can have a detrimental effect on all incentives to growth in the long term, as its centralized hegemony cows the private sector and frustrates new investments. Similarly, the wealth created as a result of corruption often finds its way abroad, outside the national economy, where it is safe from investigations and any political changes that might occur inside the country. It is hence destructive economically.

Corruption is truly achieved when it undermines the system of economic incentives, particularly those incentives for investment and growth, and destroys legal institutions and the right of ownership. In turn, it inhibits economic growth in the long term and skews the distribution of income, creating a huge gap. By its very nature, corruption increases the wealth of the rich and the prominent while simultaneously impoverishing the lower and middle classes. Similarly, corruption can lead to political instability when its spread and impact spark a wave of popular anger against the political system that embraced corruption in the first place.

The most important negative consequences of the spread of corruption can be summarized as following:

1. Corruption destroys the principle of equality among citizens: whoever has political influence can use it to attain special, undeserved benefits, thus depriving the rightful recipients of benefits granted according to objective criteria. Those with money can obtain benefits and preferential treatment through bribery, while friends and relatives of influential people can receive contracts and prominent positions for which they are not qualified. This means that citizens outside this circle—that is, most people—are barred from the circle of privilege and are not treated fairly in comparison to those who have connections. In turn, this transforms the vast majority of citizens into second-class citizens, thus establishing the principle of inequality in reality and negatively affecting all social, political, and economic levels. The principle of equality in any society is the basic principle upon which to establish any democratic system, i.e., a system of equal opportunity.

2. Corruption and the use of influence and bribery that comes along with it lead to a disrespect of the laws and regulations of the state, as

these are transgressed on a regular basis by those in authority, their relatives, and others with financial influence. This creates a general state of disregard for the law. In such cases, the strongest and most influential people in the political and financial spheres become stronger than the law itself, and breaking the law becomes the rule, rather than the exception. It is impossible for any state to create a lasting means to achieve social, economic, and political progress without also creating a system of laws and regulations that are equally applied to all citizens.

3. Corruption facilitates crime, particularly when it permeates the very structures whose job it is to fight crime, such that important segments within these structures begin to protect and facilitate criminal activity in exchange for bribes and other compensation. This is extremely serious because it creates in the collective consciousness a link between authority and its apparatuses, on one hand, and crime and violations, on the other. At this point, chaos and a social tolerance of crime can be bred. Are not the authorities themselves lawbreakers?

4. Corruption creates an inefficient public administration as appointments to important positions are often based on favoritism rather than merit. In addition, the more the political system leaves the impression of being associated to corruption, it gradually loses its popular legitimacy and acceptance. In turn, this creates a general state of rejection that permeates society, manifesting itself silently as a state of political stagnation and lack of popular participation. Rejection, however, can be transformed into a rebellion, or even an unorganized, destructive revolution, depending on the circumstances and the domestic and foreign powers that support it, as was the case in Romania and Indonesia for example.

5. Corruption in the financial and banking sector can have disastrous effects in the financial and economic sectors, particularly when it includes granting credit to preferred borrowers with insufficient collateral, leaving bad debts, or even a deficit which may in turn lead to a financial crisis, bankruptcies, or the collapse of a bank. If corruption engenders a general lack of confidence in the banking sector and economic transactions, it can even lead to a comprehensive financial crisis. Similarly, the spread of corruption in the banking sector especially can turn it into a money laundering operation for wealth

made through criminal means, which will both encourage crime and allow criminals to use this wealth to establish businesses and enterprises that act as fronts for further criminal activity. As criminal culture begins to exercise a hegemony over economic activities, it may cause problems and perhaps even serious economic tremors.

The spread of corruption in a stock exchange without strong deterrents can lead to enormous breakdowns that echo throughout the real economy and can cause a serious crisis in the entire national economy, not merely the financial sector. The extended crisis from which the Tokyo Stock Exchange is suffering is a prime example of a breakdown caused by corruption and fraud in the stock market. The Nikkei 225 Index, the benchmark index of the Tokyo Stock Exchange, reached a high of 38,000 points in Spring 1990, but later collapsed when Japanese stock prices bottomed out as a result of fraudulent transactions conducted by certain large stockbrokerage for their own advantage or that of preferred clients. At the top of the list was Nomura Securities, the largest market-making company on the Japanese market and in the world. Corruption in the huge Japanese banking sector caused debts of US$600 billion in 1998, and Japanese politicians were linked to several instances of corruption in the stock market, causing the most serious crisis in the Japanese economy since World War II. As a result, unemployment reached record levels and the negative effects reverberated throughout the economy, in addition to the changes wrought on the Japanese political map, which might prove to be negative or positive. It is certain, however, that the financial and economic crisis—which exploded in large part due to corruption—was an important factor in these changes.

6. Corruption comprises a principal mechanism for the accumulation of wealth, which is then often smuggled abroad to be laundered, to escape the possibility of investigation, or to be enjoyed abroad. This ultimately means that national resources are drained from the economy as financial gains made from corruption are transferred abroad.

7. Corruption weakens the national economy, opening it to the influences of foreign parties and multinational corporations, who easily use bribery as a means of controlling the economy and preserving their

monopolies, while involving themselves politically and manipulating the social structure, as is the case in certain African countries.

8. Given corruption's tendency to weaken incentives for growth, it can paralyze economic, social, and political development.

9. Corruption can create the conditions necessary for an increase of tension and instability on the social and political levels, which can, in turn, lead to the disintegration or destruction of the entire political system if steps are not taken to combat corruption and eradicate it.

IV. The international environment: from concealing to combating corruption

Since the end of the Cold War, the international stage has seen extremely important developments concerning corruption, as the tendency of large countries—and especially those that were hegemonic in the Cold War—to conceal corruption has changed. During the Cold War, corruption from within was concealed in order to project a positive image abroad in the context of the great conflict between capitalism, led by the US, and socialism, led by the Soviet Union. Since the end of the Cold War, this strategy has been replaced by a more objective and open treatment of corruption in large countries. This position, however, is still applied selectively, and certain corrupt regimes are still tolerated if Western countries have a political and economic interest in maintaining these regimes. Such was the case of the regimes of the former Soviet Union, which saw unprecedented levels of corruption during their transitional phase, and which nonetheless received the support of the West as a balance to the forces of the old socialist guard.

Nevertheless, the general result of these international transformations was to expose a huge segment of corruption in these countries. It also exposed cases of corruption in countries which were traditionally considered immune from corruption, such as Germany, where an investigation into the Opel Company ended with 65 of its executive officials being tried for taking bribes. The German attorney general has said that the German construction industry regularly paid about GM10 billion annually in bribes to officials.

It was no coincidence that TI was created in 1993—that is, after the Cold War, and after the international environment (particularly advanced capitalist societies) became more receptive to advocacy by NGOs.

Although every country has some sort of laws—be they lax or strict—to fight domestic corruption, the US was the first country to establish laws to combat corruption at home and abroad. In 1977, the US Congress passed the Foreign Corrupt Practices Act, prohibiting US companies from offering bribes to officials in other countries in order to facilitate contract bids and business deals. Most other advanced capitalist countries, however, did not follow in their footsteps for the next two decades, continuing to allow their companies to offer bribes abroad in order to obtain contracts and close deals, assessing them as a tax deductible expense.

Since 1977, US companies have complained that they lose large contracts due to their legal obligations not to offer bribes, while other foreign countries obtain contracts through bribery. Thus the US began to exercise constant pressure on its partners in advanced capitalist countries to pass laws preventing bribery abroad as a means of winning civil contracts. Nevertheless, the US's share in the international trade in electrical generators (21 percent) and its larger share of the international trade in aircraft and aircraft parts (40 percent) suggest that US companies may have been involved in giving bribes abroad in these two sectors, making US demands to prevent bribery abroad less credible and less popular.

In the official US *National Export Strategy* report, figures indicate that US companies lost contracts worth US$45 billion in 1995 for not submitting bribes as did their competitors. (See Kimberly Ann Elliot, "Corruption as an International Political Problem: General Survey and Recommendations," in *Corruption and the Global Economy*, translated by the Ahram Center for Translation and Publication, Cairo: 2000.)

It appears, however, that domestic pressures in advanced capitalist countries in conjunction with US demands led the Organization for Economic Cooperation and Development (OECD) in late 1994 to recommend putting an end to illegal payments, although it did not definitively prohibit them outright.

In other areas, the communications and internet revolution undermined systems designed to hide information, leading to an increase of information about corruption in developing countries, which were no longer capable of suppressing information as they had in the past. As a result, some developing countries admitted to a degree of corruption and announced their intention to combat it in order to mollify domestic opinion and attract foreign investors. The seriousness of such efforts, however, cannot be judged except in democratic countries where it is possible to determine the true scope of corruption and in turn evaluate the seriousness of efforts to eliminate it.

In any case, over the last decade the international environment has seen an increase in information about the scope of corruption, particularly given the dizzying developments in communications and the freedom of information allowed through the internet. After the Cold War ended, the international environment also saw a decrease in organized attempts to conceal corruption, and it witnessed the establishment of NGOs specializing in tracking corruption. It also witnessed a slow, indecisive tendency in advanced capitalist countries to limit bribes given abroad, which play a substantial role in corrupting officials in developing countries. The World Bank estimates that corruption reached US$80 billion worldwide in 1996, or about 13.3 percent of the wealth produced from crime and corruption yearly, about US$600 billion in 1999 (see Rose-Ackerman). The OECD's money laundering working group has indicated that there are a number of countries which actively participate in laundering illegally gained money. Israel was at the top of the list, along with Russia, the Liechtenstein Principality, the Philippines, Panama, and the Bahaman Islands and other Caribbean and Pacific Islands. The one Arab country appearing on the list was Lebanon.

V. Corruption and anti-corruption efforts in Arab countries

Corruption is connected to illegal activities undertaken by certain political and economic officials and high-level civil servants—even low-level civil servants when corruption becomes widespread. As such, there is a lack of reliable figures concerning corruption, not only in Arab countries, but across the entire world, and estimations of the size of corruption will always be characterized by some degree of impressionism. As a result, assumptions can be made that the system in one country is more corrupt than another simply because there are more cases of corruption brought before the courts in one country than another. This conclusion may not be correct, as one country may simply be tougher on corruption, while the other may have the same levels but is not seriously interested in combating it. Indeed, the ruling system could be entirely corrupt. Hence, impressionistic judgments can be misleading in many cases.

In its annual report for the year 2000, TI included only four Arab countries on its Corruption Perceptions Index (CPI): Tunisia, Morocco, Jordan, and Egypt. While there are no figures on corruption for other Arab countries, this does not necessarily mean that corruption exists only in these four countries, and is non-existent in the rest of the Arab world. On the contrary, these four countries are more open in comparison to other Arab countries, and are perhaps the best in terms of efforts to fight corruption.

The corruption index designed by TI reflects the views of businessmen, risk analysts, and public opinion about the extent of corruption in any one country. The highest score is 10, representing the lowest possible level of corruption, while the lowest score is 0, meaning that a country is afflicted with the worst sort of corruption. The index is severely constrained in its dependence on a relatively small number of surveys and impressions which may be subjective and may reflect personal experience rather than a general state of corruption or integrity. In any case, we will take a look at the index.

Among the 90 countries measured by the CPI in 2000, Tunisia occupies spot 32 on the list, ahead of most countries in Eastern Europe and ahead of two countries in the EU: Greece and Italy. Tunisia received a 5.2 on the scale of 0-10. However, only four surveys were undertaken in Tunisia, and the standard deviation from the average of 5.2 was high, meaning that Tunisia's score could change fundamentally if a greater number of surveys were conducted and the results showed a greater or lesser degree of corruption.

Morocco came in at number 37 on the list, ahead of Italy and most Eastern European countries. It received a 4.7 on the CPI based on the four surveys undertaken. Although this is same number as Tunisia, the standard deviation from the average for Morocco was less than half that of Tunis. This means that Morocco's rating may change, but in a limited fashion, if more areas are surveyed in Morocco.

As for Jordan, it came in at number 40 on the list, with a score the same as Italy at 4.6, although Italy received this score based on a greater number of surveys than did Jordan. The margin of error was also greater for Jordan. In any case, Jordan performed better than did most states in Eastern Europe.

Egypt came in at number 63 on the list, registering a 3.1 on the corruption index scale along with China. But the number of surveys was seven for Egypt, while for China it was 11. Nevertheless, Egypt's standard deviation did not exceed .7, while China's was 1.

Despite our appreciation of TI's efforts, the index is ultimately impressionistic and not a precise academic study. Moreover, it does not take into account corruption involved in military contracts, as most are confidential and are negotiated between governments, even if the production companies involved are privately owned. The possibilities for corruption are high in secret or closed deals, and if TI took this area into consideration in its corruption index, perhaps countries such as Israel, the US, France and Britain—the primary arms exporters—would fare more poorly on the list, as would the main importers of weapons.

Given this, it is perhaps more realistic to attempt to follow efforts to combat corruption in Arab states in order to build a reliable pool of results concerning the extent of corruption and the seriousness of efforts to combat it in the Arab world.

Algeria

To mark the end of the academic year, Algerian President 'Abd al-'Aziz Bouteffiqa gave a speech on July 8, 2000, at the University of Hawari Boumedien for Sciences and Technology, in which he made what are considered the most indicative statements of the level of corruption in Algeria: "Corruption has dissolved the bonds of the state, bloodied the values of rule, confounded the march towards social and

economic development, and corrupted the work ethic and concepts of integrity, labor, and self-sacrifice; in the end it has created the phenomenon of terrible, destructive terrorism."

In May 2000, during a meeting with Algerian immigrants in Montreal, Canada, Bouteffiqa promised to fight the corruption widespread in Algeria, saying that he was prepared to sacrifice his life for the sake of it.

Former Algerian Prime Minister Sayyid Ahmad Ghazzali also announced that corruption had reached dizzying levels in Algeria, and as prime minister he accused Minister of Petroleum Bulqasim Nabi of stealing US$40 billion from the state treasury (*al-Ahram*, 1/14/92). Similarly, former prime minister 'Abd al-Hamid al-Ibrahimi revealed the involvement of several government officials and former ministers in corruption and bribery cases that amounted to US$26 billion (*al-Ahram*, 1/22/92). Revelations of such startling figures—issued from the highest levels of the executive—were not followed by judicial proceedings to root out corruption and corrupt officials who have wasted the wealth of the Algerian people.

As a great part of corruption in Algeria takes place though local administration, the National People's Assembly, and the State Council, President Boutefliqa, who does seem predisposed to fight corruption, stressed to local governors the necessity of working to make public service truly a service and eliminating the abuse of power and influence. He also stated that combating corruption requires long-term efforts and varied methods. Boutefliqa took the initiative by removing those he perceived to be corrupt, including his own officials and particularly those who were appointed by state authorities, ministries, and state administration in the time of his predecessor al-Amin Zarwal.

As is clear, corruption exists on a widespread scale in Algeria, as the president himself admitted. Combating it continues to rely on concerted efforts by the president. These, however, are administrative rather than political and organizational efforts. Thus far, the available information does not indicate that those accused in prominent cases of corruption have been tried before a court. The question, then, is will the president be able to stem corruption, which has spread for so long and in so many areas of the state, its organizations, and its central and local administrations.

It is extremely difficult for the president to achieve victory over this sort of corruption, and it requires a long-term, continued battle which treats the root causes of corruption, in addition to stamping out corruption and bringing corrupt officials to fair trials. Whatever the power and position of the Algerian president, the matter requires something greater than he is, as is the case in all Arab countries. We shall deal with this point in the final recommendations in this chapter, which can be applied to Algeria as well as other Arab states.

Lebanon

The economic role of the state has always been limited in Lebanon, and the economy has always been a free economy uncontrolled by the state bureaucracy. As a result, corruption has never been widespread in Lebanon. On the flip side, however, substantial black-market activities in all forms has always existed.

In any case, what concerns us here is corruption. Suzanne Rose-Ackerman says in her study that a survey of Lebanon revealed that loans are largely granted through the payment of bribes, which points to the existence of corruption in the Lebanese banking sector.

In addition, Lebanese parliamentary elections in the summer of 2000 saw former Prime Minister ‘Umar Karami accuse Minister of Public Works and Transportation Najib Miqati of stealing US$700 million from the state treasury. However, the matter stopped there and no investigations into the accusation were carried out, nor did Karami raise a case against Miqati. It is thus impossible to judge the truth or falsity of the accusation. Lebanon is a complex country rife with sectarian and political sensitivities, which reached their peak in the long civil war the country witnessed from the mid-1970s to the early 1990s. These complications and sensitivities put boundaries on efforts to fight corruption if indeed it exists.

Syria

For a long time, no information came out of Syria that would either confirm or deny the existence of corruption among officials and high-

level civil servants and public-sector employees, although there is no country completely free of corruption. Suddenly, an enormous change occurred during the illness of the late Syrian President Hafiz al-Asad, particularly beginning from March 2000 as he was preparing to transfer power to his son Dr. Bashar al-Asad. Corruption scandals exploded in Syria, although doubts surfaced among the Syrian political opposition concerning the relationship of corruption scandals to differences of opinion within the reigning political elite over the succession of Bashar al-Asad to the presidency. These doubts were bolstered as those accused of corruption by the Syrian authorities were long-time symbols of the state, including a prime minister, his deputies, other ministers, a head of state intelligence, and even a party leader. When they were accused, they were all former officials—that is, they were removed from their posts before being accused. Doubts were also raised in connection to accusations later made against high-level civil servants. These doubts, however, can neither be confirmed nor denied.

Prominent officials targeted by the anti-corruption campaign included the head of general intelligence, retired General Bashir al-Najjar, who was sentenced to 12 years in prison. His possessions and those of his wife and children were sold at public auction to meet his debt of one billion Syrian lira, allegedly taken from the public treasury.

Mahmud al-Zu‘bi, prime minister from 1987 to March 7, 2000 (when he either resigned or was removed) was subjected to house arrest on May 10, 2000, after he was brought to the court on charges related to corruption. He was expelled from the ruling Arab Socialist Ba‘th Party on May 13, 2000, before the Syrian government announced that he had committed suicide on May 21, 2000. His suicide was allegedly discovered when the head of the Damascus police force went to his home to issue him a subpoena to appear before a military judge on charges based on the recommendations by regional leaders of the ruling party. The banned Muslim Brothers organization in Syrian cast doubts on al-Zu‘bi’s suicide in a statement that was distributed to some newspapers. Did al-Zu‘bi commit suicide or did he not? Al-Zu‘bi’s sons—Muflih and Hamam—were also detained on charges of abusing their influence, and the moveable and non-moveable property of al-Zu‘bi, his wife, and his sons and daughter was sequestrated.

While al-Zu'bi was being arrested and investigated on corruption charges, Minister of Transport under al- Zu'bi, Mufid 'Abd al-Karim, was arrested on charges linked to corruption and bad debts. Soon after, Dr. Salim Yasin, undersecretary of economic affairs in al-Zu'bi's government, was arrested, a sequestration order was issued against 'Abd al-Karim's property and that of his wife and children, and Yasin and his wife and children. Muhammad Haydar, former underminister of economic affairs and a prominent member of the Ba'th Party, was informed through official statements published in the press that he should return to Damascus—he was abroad—where he would stand trial for trying to weaken national sentiment.

Later, Syrian authorities announced that the charges of corruption directed at al-Zu'bi, Yasin, and 'Abd al-Karim were related to the 1996 purchase of six French Airbus planes for the Syrian national airlines worth US$250 million. The authorities said that the purchase agreement contained conditions contrary to Syrian laws and incurred the loss of millions of dollars for Syrian airlines and the Ministry of Transport. It did not go unnoticed that the charges against al-Zu'bi, 'Abd al-Karim, and Yasin were brought by a regional and national leader of the Ba'th Party in a case more than three years old.

In addition to these prominent officials, the minister of supply and internal trade decided in May 2000 to remove six high-level employees from his ministry as part of a government campaign to fight corruption. The government also removed a number of customs employees and directors of public-sector industrial organizations for reasons related to corruption, and it issued an order to sequestrate the property of retired general 'Umar Rida, former director of Syrian Airlines, on the charge of squandering millions of dollars on maintenance for two jumbo jets. Similarly, six directors of Ministry of Transport offices in the provinces were dismissed—in Homs, Tartus, al-Haska, Aleppo, al-Riqqa, Damascus, and suburban Damascus—all due to alleged mismanagement.

The authorities also arrested the assistant director of the Damascus International Fair—also the director of the Syrian lottery—on charges of corruption, after his aides drafted checks in the names of his relatives for winning lottery tickets that had not been sold. He was transferred to

the economic security court. The financial director of the Damascus International Fair was also charged with squandering public money and corruption.

Syrian authorities took severe steps to prevent the smuggling of subsidized Syrian mazut to Turkey, and the property of 23 officials in the Department of Fuel in the city of al-Riqqa was sequestrated, along with the property of the director of the Department of Fuel in suburban Damascus. Syrian authorities said that they had cost the state about 218 million Syrian liras and about 190,000 canisters of gas.

On the whole, the opening of the corruption file in Syria is a very positive development, although it must be ascertained that efforts to combat corruption are not motivated by a desire to settle political accounts. Only then will anti-corruption efforts in Syria enjoy the utmost degree of legitimacy and fairness. A number of steps must be taken here to disprove claims of partiality or account settling; these will be presented in the conclusion of this study as general recommendations applicable to all Arab states, enabling them to effectively fight corruption with the utmost fairness.

Iraq

In an emergency session of the Iraqi Ba'th Party headed by Iraqi President Saddam Husayn, 80 leaders were expelled from the party after being charged with corruption and tarnishing the party's image. The expelled leaders were described as corrupt elements that abused their positions at the expense of party ideals to close huge business deals, mentioning the abuse of their influence over public and private economic organizations. Despite these charges, the steps taken against the accused were limited to expelling them from the ruling party and did not include a confiscation of property or legal proceedings.

As is clear, charges of corruption in this case came from the ruling party and not from the state authorities, as there is no distinctions between the two in Iraq.

It is impossible to know the true extent of corruption in this case. Even before Iraq can reveal the extent of corruption and combat it, the state must take a number of measure that we mention in the conclusion of this study.

Kuwait

Although it has been almost ten years since the corruption scandal broke that ultimately destroyed Kuwaiti investments in Spain, the negative consequences are still being felt. According to the Kuwaiti State Accounting Diwan, losses incurred by Kuwaiti investment in Spain might exceed the total amount of invested capital in the country, about US$4763 million. The fallout from the crisis left outstanding Kuwait debts to Spanish banks of more than US$400 million. The problems faced by the Kuwaiti Investment Office began before the second Gulf War during Shaykh Ali al-Khalifa al-Sabbah's tenure in the Ministry of Finance, when he placed Shaykh Fahd al-Muhammad al-Sabbah at the head of the investment office from 1984 to 1992. During the latter's tenure, he managed the office poorly and in cooperation with financially disreputable people, such as Charles H. Keating, who was imprisoned in the US on charges of fraud.

In August 2000, the General Authority for Investment in Kuwait won a court battle against Shaykh Fahd al-Muhammad al-Sabbah, getting a commercial court in the Bahamas to dissolve one of his stock portfolios worth US$177 million, with the proceeds going to the Spanish Torres company, a subsidiary of the General Investment Company in Kuwait. If it were not for the collapse of Kuwaiti investments in Spain, corruption may not have been exposed and probably would have continued to thrive.

The former director of the Kuwaiti Investment Office in London, Fu'ad Ja'far, also participated in fraud in the context of financial transactions he had conducted in Spain since the end of the 1980s. Spain asked Britain to turn him over to the Spanish authorities in September 2000.

In addition to this ongoing case, in the year 2000 the parliamentary committee for the protection of public monies presented a report that included a number of observations and accusations of impropriety and violations in the General Authority for Investment, which also directs the Future Generations Reserve, valued at about US$45 billion. The report was given to the attorney general to determine the extent of criminal activity by the accused officials.

Similarly, the gas leak at the Shu'ayba refinery and the death of two Kuwaiti engineers inspired a debate over corruption in the Kuwaiti petroleum sector. Although the government formed an official committee to investigate the accident, parliamentarians assigned their own health affairs committee to investigate as well, granting them wide-ranging authority on the basis of article 114. Other deputies raised the issue of corruption among leaders in the petroleum sector, and one MP, Salim al-Hammad, said that the minister himself was unable to dismiss even one of these corrupt leaders. It is understood from this statement that these officials enjoy a direct relationship with those above the minister and the government—i.e., the royal family. Parliamentary discussions also raised the issue of specifications infractions by contractors, implicitly directing accusations of corruption against those officials who gave projects to unqualified contractors.

As a whole, the participation of members of the royal family in the general financial administration of the state, or as leaders in the petroleum sector, has weakened the effectiveness of follow-up efforts and investigations, allowing corruption to spread in some Kuwaiti investment offices abroad and in the petroleum sector. Nevertheless, the Kuwaiti parliament's treatment of corruption cases was much more positive than is the situation in a number of Arab countries.

Palestine

The Palestinian Authority (PA) faced charges of financial and administrative corruption and misuse of funds received as aid from other countries, while the PA itself directed charges of corruption to one former prominent PA official.

In November 1999, number of members of the Palestinian legislature—a total of eight—signed a statement termed the "statement of 20," (signed by 20 Palestinian leaders) in which they accused the PA of tyranny and corruption. One parliamentarian and signatory to the statement—MP Husam Khidr—said that corruption is not a fleeting issue, but a living reality from which the Palestinian people and its institutions suffer. Indeed, these institutions have almost collapsed due to corruption. Dr. Kamal al-Sharafi, head of the human rights and oversight committee in the Palestinian legislature, pointed to repeated demands to refer those charged with corruption to the courts, with no response by the PA. No corrupt official has been brought before a court, while those who attack corruption are subject to punitive measures and investigation.

At about the same time, in November and December 1999, mutual accusations between the PA and former head of the Palestinian National Fund, Juwayd al-Ghasin, became particularly fierce. The PA raised a case against al-Ghasin, who lives in Abu Dhabi, demanding that he repay a loan of US$6.5 million with interest, which, according to the laws of Abu Dhabi where the suit was filed, could amount to as much as US$13 million.

In return, al-Ghasin accused the PA of to use the case against him to cover up corruption within its own ranks, saying that there were hundreds of people around Yasser Arafat who had become millionaires at the expense of the revolution.

The truth is that the PA was born within other organizations, which existed and moved throughout other states. Even when it returned to the Occupied Territories in 1967, it was still subject to Israeli occupation. In such circumstances, the material and cash assets of the revolutionary Palestinian organizations were maintained in the names of individuals. It is thus logical to expect some cases of corruption, which could have been limited and exterminated or could have grown to include every institution of the PA. This situation will continue until there exists an independent Palestinian state with a comprehensive structure that allows it to change the system of depositing public monies in individual accounts. Until that time, fighting and preventing corruption depends on the presence of transparency, accountability, and checks and balances, as well as punishing corrupt officials in areas related to public finances at least.

In its 1997 report, the Palestinian Oversight Organization accused the Palestinian self-rule authorities of corruption and misappropriating public monies, saying that US$326 million of public money was misused in 1996. Five ministers in the PA were involved in the scandal. The report also revealed the loss of US$50 million in customs duties after a number of automobiles were not assessed properly. The report also proved the involvement of several Palestinian officials granting

contracts to companies in which they had a personal interest. It also mentioned the loss of US$67 million in misappropriated funds. Despite the examples of corruption included in the report—issued by an official Palestinian body—the publication of such a report in and of itself is a positive step reflecting a realization and official recognition of corruption. Nevertheless, combating corruption is still an important issue, as is maintaining the independence of Palestinian oversight institutions and facilitating their mission by strengthening their authority to access information and investigate any individual, whatever his position in the PA or in society.

In 1999, a case was also raised involving the chairman of the board at the Palestinian International Bank, 'Isam Abu 'Isa, whom the PA accused of financial violations totaling US$15 million.

In any case, Palestine, like other Arab countries, must establish institutions and mechanisms to fight corruption and end the causes for it in order to build a true state.

Jordan

Although there has been an Accountability Office in Jordan for many years, in 1996 a special office for fighting corruption was established, reinforcing the importance of increasing anti-corruption efforts. The anti-corruption office is linked to general intelligence. Despite its relative youth, the anti-corruption office had already rooted out 605 corruption cases two years after it was formed, saving about US$56 million and sending 323 civil servants to the courts in cases involving misappropriation of funds and embezzlement.

Despite these positive efforts to combat corruption, a true awareness of the extent of corruption and the ability to effectively fight it require a high degree of transparency and a free flow of information to the national and local legislatures as a mechanism of popular oversight over civil servants and their administrations. It also requires giving a high degree of independence to the anti-corruption office while granting it the authority to investigate any person regardless of his position or family connections.

Yemen

After Yemen signed the International Land and Sea Borders Agreement with Saudi Arabia on June 12, 2000, the Yemeni president announced that his country had entered a new phase. The important thing in the coming phase, according to the president, was combating corruption on all levels of the state and society, and he spoke strongly of the need to put an end to favoritism in government institutions and stop the decay of the administration and judiciary. He empowered the oversight and accountability departments and the security and government apparatuses with compiling files and in preparation for a campaign to rid state institutions of corruption. He also empowered political security to participate in preparing the information upon which the anti-corruption campaign would be based, which raises several questions and opens the door to doubts.

In any case, during the first two months of the anti-corruption campaign, 155 cases connected to financial corruption were transferred by the state and its administrations to the attorney general and the financial comptroller. The civil servants accused in the cases were low- and mid-level, not leaders in state administration.

In the beginning of the efforts to fight corruption in the government, judiciary, and administrative branches of government, the Yemeni president implicitly acknowledged the existence of corruption on a wide scale. Nevertheless, the result of the "campaign" against corruption was trying a number of mid-level employees, which means that statements of intention to fight corruption have not yet been begun to be implemented on a wide scale. In addition, the participation of the political security branch of government in the "campaign" casts shadows of doubt on the real intentions behind it.

Libya

When at a public meeting Libyan President Mu'ammar al-Qadhdhafi ripped up the state budget for the year 2000, it was an indication of his anger at the head of the popular finance committee (the Libyan finance minister), Muhammad Bayt al-Mal. Only a few months passed before Bayt al-Mal was removed along with the head of the Libyan Central

Bank, Tahir al-Juhaymi. Bayt al-Mal and 22 other banking leaders were subsequently subject to an investigation concerning their involvement in granting loans without collateral to certain individuals, including army officers, causing the loss of about US$4 billion of the Libyan people's money. The purging committees formed by al-Qadhdhafi, composed of junior army officers and elements from the revolutionary committees, began to investigate the minister and banking leaders for squandering state monies. Press reports indicated that Libyan authorities would undertake a comprehensive review of the industrial river project and its component parts as millions of dollars had been embezzled with the involvement of high-placed officials supervising it, who allegedly accepted commissions and bribes from foreign companies participating in the project.

The planning stages of the industrial river project began in the early 1980s, and in 1983, an agreement was made with the South Korean Kong Ah Company, which won the tender to implement the first phase of the project, estimated at US$3300 million. There are three additional stages planned, which include digging wells and building pumping stations and water lines which will eventually run over 4040 kilometers with a capacity to pump six million squares meters of water daily. The project also includes establishing farms and agricultural villages. The total cost is estimated at US$25 billion. The French Dumex Company won the main contract for the third phase of the project.

There was no official Libyan announcement concerning the details of the corruption case in the Ministry of Finance, although authorities did leak some information. Thus, the picture is not complete enough for a fair and objective evaluation. Similarly, turning the investigation over to the revolutionary and purging committees gives it a political cast, as these committees are political rather than judicial.

If there is a consensus that fighting corruption is a noble cause and must enjoy moral, social, political, and economic legitimacy, then it must be fought fairly and strictly, whether in Libya or other Arab countries. The conditions for such a campaign will be set forth in the conclusions of this study.

Morocco

In 2000, Morocco joined a wave of Arab countries that saw the explosion of several large corruption cases, the most important of which for Morocco was that involving four prominent Moroccan banks. During an audit of the National Fund for Agricultural Loans (the Agricultural Bank)—a public-sector bank—international conglomerate Price Waterhouse discovered unexplained financial improprieties and substantial non-guaranteed loans that had been used to finance non-agricultural sectors. Audits in three other Moroccan banking establishments—the National Fund for Property and Tourist Loans, the People's Bank, and the Social Insurance Fund—revealed similar findings.

In light of the violations uncovered by audits of these institutions, the Moroccan government began preliminary investigations into corruption, while admitting that grave violations had been committed. It turned the cases over to the judiciary in May 2000, and ultimately 32 former officials of the National Fund for Agricultural Loans were charged with squandering public funds through granting non-agricultural loans to relatives and politically connected clients. The total amount of loans granted with insufficient collateral in this case was estimated at US$190 million. Other charges were brought up in a case involving loans to build docks—an area outside the Agricultural Bank's field of specialization. Defendants were also charged with embezzlement in transactions to build luxury palaces and to acquire property and equipment for the bank at inflated prices.

The total amount of money lost through bad loans and financing non-agricultural activities was subsequently estimated at US$660 million, later reaching US$1.2 billion.

The Moroccan parliament formed a committee to investigate the National Fund for Property and Tourist Loans—owned principally by the Central Bank and the Deposit and Management Fund—when losses reached US$450 million and unaccounted debts totaled US$900 million. The government was thus forced to pump in US$500 million to save the bank from collapse after it lost its base capital.

Similarly the National Social Insurance Fund, which has deposits evaluated at about US$1 billion in the Deposit and Management Fund

(the principle shareholder in the National Fund for Property and Tourist Loans), was also the site of financial indiscretions in its accounting. The Moroccan parliament formed a committee to investigate corruption within the bank, and the committee prepared a report and submitted it to the head of parliament.

The People's Bank also saw related corruption cases in which the bank financed the purchase of luxury properties in Europe by former political officials.

In addition, an army officer working in the fuel storeroom on an Air Force base in al-Rashidiya revealed a case of corruption and the embezzlement of fuel and public monies at the base. Investigations led to the punishment of the head of the fuel storeroom along with a number of military officials. However, the officer himself (Colonel Mustafa Adib) was brought to trial and sentenced to five years in prison because he submitted a detailed report of the case to the French daily *Le Monde*, which published it. This behavior was considered violation of military law.

The year 2000 also saw a corruption scandal in which certain regional leaders and officials in the Ministry of Information abused their influence to set up fake investments in exchange for bribes. The investments were made without the knowledge of the central administration. A number of consultants and local leaders were implicated in fake investments in Casablanca, Tanja, Esfa, and other cities, leading the Ministry of Interior to launch a campaign in most provinces to root out financial violations and other illegal activities undertaken by officials.

On the whole, Morocco saw several attempts to fight corruption, making it one of the most laudable Arab states in this field. Efforts to combat corruption were organized and were characterized by acceptable levels of fairness. It is also noteworthy that Morocco used private companies to conduct audits, and that when indiscretions were found, it undertook preliminary government investigations before transferring the matter to the judiciary. However, Morocco employed a foreign company to conduct its audits, which, given the existence of local skilled companies, is somewhat unfathomable, unless there were fears that corruption could be further buried in return for bribes if audits were done locally. Even so, it is necessary to experiment; if a Moroccan auditing company hushed up a case of corruption, it should be considered a party to it and it should be punished and prohibited from practicing professionally again. But participation by Moroccan companies in auditing practices is necessary in order to develop local competence to spot and stop corruption, and in order to facilitate the mandate of the people, the parliament, the government, and the judiciary in combating corruption.

If there are any recommendations for Morocco, they will be included in the general recommendations for Arab countries found in the conclusion to this study.

Sudan

In summer 2000, differences within the Sudanese government over anti-corruption issues ultimately froze all attempts to open the corruption file in Sudan. After Sudanese President 'Umar al-Bashir empowered Minister of State at the Ministry of Justice Amin Banani to move forward with anti-corruption efforts, the latter tried to obtain the information necessary to pursue an investigation in the banking sector and the Central Bank. His request was rejected, however, and in August 2000 he announced that the Central Bank was reluctant to provide information and that it was hiding violations in the banking sector and refused to take punitive measures recommended by investigative bodies against the perpetrators. The matter did not stop here. Banani was subject to a joint attack from Minister of Justice 'Ali Muhammad 'Uthman Yasin and Minister of Finance Muhammad Khayr al-Zubayr, who issued a statement denying Banani's accusations. The minister of justice proceeded to use his authority to remove Banani from his supervisory position on the anti-corruption investigative committee, taking over the position himself.

The timing of al-Bashir's attempts to open the corruption file indicates that perhaps they were linked to political differences from within. The difficulties in the subsequent attempts to deal with corruption also indicate that differences between government bodies can put obstacles in the path of any effort, whether it was truly intended to combat corruption or to settle political accounts. If Sudan really

wants to fight corruption in an organized fashion, there are a number of measures that must be followed; these are mentioned at the conclusion of the study.

Egypt

Egypt is at the forefront of Arab countries in terms of the number of corruption cases that have gone to the courts in the last few years. As much as this points to the existence of corruption, it shows that Egypt is a large and venerable country with institutions capable of rooting out and combating corruption. It is also evidence of a clear tendency to fight corruption in Egypt on official levels, as it is considered an utmost necessity to preserve the political system, its stability, its liveliness, and its ability to evolve. Of course, combating corruption is a constant popular demand because, in the end, corrupt officials squander the wealth of the people and incur losses on public assets. Anti-corruption campaigns are also a joint demand of important parties in the Egyptian political opposition. It is thus possible to say that there is a consensus or social and elitist strategic trend towards combating corruption. Nevertheless, the mechanisms for fighting corruption and the punishments imposed on corrupt officials are perhaps the point of debate or controversy.

In 2000, the most important corruption cases in Egypt revolved around the banking sector, including embezzlement and granting non-guaranteed loans to favored clients with financial or political influence or to relatives in the banking sector. In some cases, clients fled the country after receiving substantial loans through transactions involving bribery and the misuse of authority. Corruption cases in Egypt also included tax and customs evasions and bribery in all forms, including commercial violations in collusion with corrupt government officials, facilitating the illegal seizure of state lands and property, and abetting antiquities smuggling.

The most important anti-corruption event in Egypt in 2000 was the verdict issued against the so-called "loan deputies" in June, more than three years after the case had been transferred to the judiciary—it began on April 8, 1998. The case involved four deputies from the People's Assembly and 32 banking officials and businessmen who made away with loans worth LE1250 million, without providing collateral or after providing false collateral. The sentences were sufficiently stiff so as to act as a future deterrent: three defendants were sentenced to 15 years in prison and. removed from their posts; fourteen defendants were sentenced to ten years in prison, seven of whom were removed from their posts; one defendant was sentenced to five years in prison; seven defendants were sentenced to three years in prison, one of whom was removed from his post, although the sentence was suspended; and six defendants were sentenced to one year in prison, four of whom were removed from their posts. In its brief, the court stated that the defendants had formed a gang for the purpose of defrauding banks, forming small companies and then taking out loans over LE1 billion with insufficient or fake collateral. The court reiterated the necessity of insuring bank deposits against the dangers represented by banking investment policies. It also pointed out the necessity of instituting controls through the Central Bank requiring commercial banks to appoint officials of guaranteed repute. It further recommended harsher punishments for all those found guilty of squandering the money of banks.

It is noteworthy that the extended trial period—three years—is due to a year-long period of inactivity by the district attorney to whom the case was originally assigned, and who had a close relationship with one of the witnesses. This reinforces further the need for fairness and impartiality in such cases, where measures must be carried out fairly in accordance with the highest possible judicial practices.

The court also sequestered the property of Mahmud 'Azzam, a former MP and one of the loan deputies, along with his wife Aliya al-'Ayouti, who fled the country. He received credit lines worth LE119.5 million from the Nile Bank with the help of his wife, vice-president of the bank, through unauthorized banking practices and without thorough credit studies. The original loans were not repaid, although other loans followed. Assets of 'Azzam and al-'Ayouti that were sequestered were estimated at LE92.1 million.

In the context of banking corruption, there were a number of cases, for example that of businessman Mustafa al-Beleidi, who borrowed LE148 million from the Bank of Cairo and refused to pay it back,

causing the bank substantial losses. He had not submitted sufficient collateral to allow the bank to recoup its losses, and then he fled the country. The socialist public prosecutor decided to sequestrate his assets and those of his three children, their wives, and their children, both adults and minors. The total amount of assets affected was about LE128.6 million.

The property of Egyptian-American businessman Mahmud Ahmad Muhammad Wahba, his wife, and children was also frozen after he proved unable to pay his debts to the National Bank and the Bank of Cairo, valued at LE387 million, and after he fled to the US after selling some of his holdings in Egypt.

Assets of a number of other businessmen were also sequestered when they proved unable to meet their debts to a number of banks. Muhammad Hasan al-Gharib, owner of the Mahalla Commercial and Investment Company had his assets sequestered after he received credit worth LE27 million from the Societe Generale Bank and American Express and could not meet his payments. Similarly, the assets of Samir Ahmad Musa, owner of the Pharaohs Company for Schools and his sister Magda Ahmad Musa, owner of SM Company, had their assets frozen after they received credit in the amount of LE46 million with false collateral and could not repay the loans.

Authorities sequestered the assets of businessman Muhammad 'Abd al-Fattah, owner of al-Fath Import Company, and his deputy Muhammad Riyad after they received loans totaling LE19 million from the National Development Bank and the Mohandes Bank and could not pay them back.

Four employees from the Bank of Cairo (Roxy Branch) and the Faisal Islamic Bank were sentenced to life in prison after they abetted a merchant in obtaining LE6 million in loans with false collateral. The merchant fled to Cyprus soon after with the money.

The last two years in Egypt have also seen cases such as the flight of Hatim al-Hawari, who left debts of almost LE1 billion with several banks, including the National Bank, the Bank of Cairo, the Suez Canal Bank, the Mohandes Bank, and the Cairo Barclay's Bank. He received these loans with property collateral evaluated at four times its value, and by forming front companies in the name of a number of prominent figures who then received loans for al-Hawari in return for sizeable commissions. There had always been problems in banking transactions with al-Hawari and his father, 'Izzat al-Harawi, who fled Egypt for Brazil in 1984 after his debts reached LE90 million. They were subsequently re-financed and paid off by his son in 1990. Even in the mid-1990s, the issue of Hatim al-Harawi's debts to Egyptian banks and to the Nasr Import and Export Company was raised.

Banking corruption in Egypt in the past few years has also included cases of embezzlement, such as the director of client services at the Saudi Finance Bank, who embezzled more than LE22 million from clients' accounts by forging documents. The case was exposed in September 1998.

The main problem for banking corruption in Egypt is not found in the absence of laws and controls, as these are actually present, but in the tendency to break these laws. One defendant in the loan deputies case—Khalid Mahmud—indicated that 70 percent of loans granted by Egyptian banks are done so without collateral, which is also backed up by a report by the Central Bank presented to the Economic Committee of the People's Assembly. This reflects shortcomings in the oversight structure of the Central Bank, despite its legitimate jurisdiction in this regard. It also reflects the weakness of the banking mechanisms that assess collateral before granting loans—one of the most serious weak links in the Egyptian banking sector, and a point that has been dealt with in detail in the section devoted to the Egyptian economy (see "The Banking Sector and the Dangers of the Transition Period").

The year 2000 also saw a corruption case involving the misuse of authority to smuggle antiquities. A police general, Rida Ahmad 'Alwan, former director of security at Nuzha Airport, was caught trying to abet the smuggling of 150 antique pieces to Germany on behalf of Hamdi 'Abed al-Ru'uf, director of the Import Export Company. Another active police officer was also implicated in the case, which came to include a gang of 10 individuals from a number of Egyptian provinces who specialized in stealing and smuggling antiquities.

Abetting tax evasion and soliciting bribes in the tax authority to facilitate tax evasion was another issue. General Hitler Tantawi, head of the Central Oversight Authority, denied a study by the World Bank

that indicated that 67 percent of tax commissioners in Egypt were involved in this sort of crime. At the same time, the finance minister indicated that there was a high frequency of tax evasion, and that outstanding taxes owed the state had reached LE17.8 billion, although he attributed the problem to the high tax rate.

There were a number of relatively small corruption cases involving tax evaders. The owner of one company was arrested after evading a payment of LE9 million, while the head of a cinema production company was brought to trial for evading LE6.1 million in back taxes. Nevertheless, because those that have money and assets are prime candidates for tax evasion, they are usually financially and perhaps politically influential as well. Thus it is necessary to institute a more effective system for monitoring and supervision, and to develop the tax system itself, lessening the tax burden such that it would be more acceptable to taxpayers, which may in turn lessen tax evasion.

In this regard, Egypt suffers from a bizarre contradiction: there are excessive tax breaks for investors in the new industrial zones and megaprojects, while the tax rate is excessively heavy once it is actually implemented. It would be preferable to lower the tax breaks while also easing the tax rate in order to make it fairer and more acceptable to taxpayers. At the same time, steps should be taken to strictly enforce tax collection and punish tax evaders.

In the area of stealing state monies, three officials in the Alexandria Antiquities area were transferred to a court in October 2000 after taking bribes in exchange for granting 45 feddans of land from the Antiquities Authority to a Yemeni businessman. In addition, seven officials in the Agricultural Properties Administration in Suez and the Agricultural Reform Authority were transferred to the High Disciplinary Court in November 2000 on charges of fraud, after a report by the Administrative Oversight Authority implicated them of scheming with a leading member of the ruling National Democratic Party to purchase 15 feddans of land next to the Suez Canal for less than one-tenth of its actual value. In May 2000, six civil servants and two citizens in the governorate of Matruh were tried based on a report by the Administrative Oversight Authority in Marsa Matruh, which said that three civil servants in the deed office in Marsa Matruh and one civilian had helped steal 21 feddans of land owned by the Matruh local council.

In other areas, the minister of culture's secretary was brought to trial on charges of abusing his position and authority for illegal gains, amassing a fortune of more than LE3 million according to a report by the Administrative Oversight Authority. If the secretary to the minister was able to abuse his influence to this degree, what about those in more important positions of power?

In November 2000, sessions began in the retrial of Dr. 'Abd al-Hamid Hasan, the former governor of Giza, who was given a one-year prison sentence in 1990, to be deferred for three years. He was also fined LE99,000 for abusing his position and illegally profiting from it.

The most infamous case in this regard was that of 'Abd al-Wahhab al-Habbak, who was sentenced in 1999 to ten years in prison and fined US$24 million. He was also forced to return LE4 million and other amounts acquired illegally by his wife and children. He had abused his position as the head of a number of companies between 1975 and 1996: he was the head of the Nasr Company for Philips Electrical and Electronic Appliances; the chair of the Public Authority for Engineering Industries; and the head of the Holding Company for Engineering Industries. During this period he profited illegally by betraying his position and the trust that those in positions of power had granted him.

The year 1999 also saw the trial and sentencing of businesswoman Mona al-Shafi', along with four high-level employees at the Nasr Import and Export Company. The four employees were charged with abetting al-Shafi' in stealing LE47.75 million in exchange for bribes. Each defendant was sentenced to ten years in prison, and they were fined a total of LE48 million. One year before that, the verdict came out in the corruption case against Misr Foreign Trade, in which two defendants were sentenced to 15 years in prison, one was sentenced to 10 years in prison, and a fourth defendant received three years. All were removed from their positions. Other defendants in the case were sentenced to one year in prison, while six defendants were required to return LE24.4 million to the company.

Over the last few years, several corruption cases have come to the surface, some even affecting the press. Six journalists at *Akhbar al-Yawm* submitted a complaint with the public prosecutor in 1999 against the chair of the institution, Ibrahim Sa'da, who had agreed to sell a 10,000-meter piece of land owned by the paper in Ramla in Bulaq on the Nile Corniche for LE62 million. (The land in this area is valued at several times that amount.) Moreover, the paper received no payment for the sale as the buyer was granted a three-year grace period, after which payment would be completed in two years. The case ended when the prosecutor suspended the investigation against Sa'da.

In the year 2000, one of the most important cases of corruption in Egypt was exposed: that connected to the practices of Palestinian businessman Muhammad 'Ali Yusuf al-Safadi. The Egyptian prime minister said that al-Safadi had obtained a license to import and refine 100,000 tons of sugar. He soon began to exceed his limit, meaning that he was essentially smuggling sugar. He also imported refined and half-refined sugar as raw sugar, taking advantage of lower customs duties. His sugar imports eventually reached 500,000 tons, and ultimately18 cases were brought against him for smuggling and commercial fraud.

Since 1995 al-Safadi had also exploited his ties with officials at the Public Authority for Supply Commodities and the heads of the Egyptian Company for Food Commodities and the Public Company for Chemicals and Trade to win tender bids and sign contracts to import raw and fine white sugar. He was paid for the contract in advance and did not comply with the importing schedule, costing these companies substantial losses. He also received commercial and private credit lines without submitting proper collateral. His debts to banks amounted to about LE287.5 million at the beginning of 2000, including debts to the National Development Bank and the Port Said National Development Bank. The loans were written off after al-Safadi fled the country in 2000. Moreover, his Arab Brothers Group was the victim of a fire in 1994 and received LE16 million in compensation from the insurance company. In light of the serious questions concerning his responsibility for the fire, the insurance company asked him to sign a waiver releasing them from responsibility to compensate him for any future accidents. (See *al-Ahram al-Iqtisadi* 2000/10/2.)

In addition to these cases, some of the deals concluded in the context of Egypt's privatization program provoked controversy over the likelihood of corruption (see the section on the Egyptian economy). The Egyptian Stock Exchange was also the subject of some debate. Despite its venerable heritage, it was activated in the 1990s after more than three decades of stagnation, and is thus still considered a developing stock market. As such, it is not free of violations, as is the case with any stock exchange. Nevertheless, it may be more widespread in some developing stock exchanges given a lack of investment experience and the absence of administrative and oversight institutions.

On the whole, the main avenue for corruption in Egypt is the weakness of transparency, even if the situation is better than some Arab and non-Arab developing countries. Other aids to corruption include granting high-level state employees and civil servants wide jurisdiction in granting licenses and official documents in the administration of the public sector combined with a low pay scale that does not allow for an honest life in many cases. The confusion in the tax system and the combination of excessive tax breaks and excessive tax burdens also contributes to the problem, as does granting tax employees wide-ranging authority. Moreover, the transition period towards a free market economy and concomitant activities, such as privatization and legal changes, create conditions for corruption to grow. The abuse of political influence to profit illegally was also one cause of corruption in some cases, such as the loan deputies case. These problems are exacerbated by poor choices for influential positions in banks and public-sector holding companies—for example, al-Habbak—and even on parliamentary economic committees—for example, 'Abd al-Rahman Baraka, the former director of the Ahram Bank and the vice-president of the economic committee in the People's Assembly before the elections of 2000. Baraka has been accused and convicted of corruption and smuggling foreign currency abroad in 1985, and his assets were sequestered.

As for anti-corruption efforts, as was mentioned previously there is a consensus among the people, the government, and the opposition on the importance and necessity to fight corruption for the sake of the political

system and social and economic development in Egypt. Egypt is lucky to be a well-established state with varied institutions to regularly monitor and fight corruption, but these institutions need more independence and authority to gain access to information and investigate officials on the highest levels. Egypt is also distinguished by the presence of a political opposition and party and independent papers, which increase the pressure to fight corruption. Nevertheless, eliminating corruption in Egypt requires further measures, recommended in the conclusion to this study.

Corruption in other Arab countries

There are no figures on corruption for the rest of the Arab countries not mentioned here. This does not mean that they are free of corruption—there is no state on the face of the earth completely free of corruption—but in the absence of information, the level of corruption in these states cannot be accurately assessed. We cannot answer questions such as whether these countries suffer from intense corruption or not, organized or incidental corruption. Such judgments cannot be made except based on reliable figures, which are not available. Nevertheless, the environment in a number of these countries is ripe for corruption, considering that political and economic power are controlled in such a way that it is difficult even to investigate the matter effectively. Although there are no indicators of corruption in the Gulf countries or Tunisia, for example, these indicators cannot be formed with a clean conscience until figures about corruption become available as a result of preliminary steps towards transparency and accountability.

VI. A general view of the mechanisms to advance anti-corruption efforts

It is clear that anti-corruption efforts in Arab states or in any state in the world must start by putting an end to the varied causes of corruption. This must be a long-term strategic decision. In the short term, the process of fighting corruption must be done by taking serious measures, particularly in those cases where it has spread such that it threatens the legitimacy and stability of the political and social order.

It must be clear that discussing any general plan to combat corruption does not mean that this is a prescription or a ready-made recipe to establish priorities in every country; even if these steps on the whole cut down on corruption, it must be realized that the causes of corruption differ from state to state. In turn, anti-corruption efforts in each state need to focus in general on treating the most important causes for its spread.

Before turning to suggested means of fighting corruption, it also must be pointed out that an effective campaign against corruption in any country requires first and foremost an admission that corruption exists. There must also be a general consensus between the government, opposition, and the people over the importance of fighting corruption at all levels, whether that means involving those with financial and political influence and high-level state employees, or only low-level civil servants.

In any case, the mechanism for developing anti-corruption operations in Arab countries can be summarized as follows:

1. As the absence of transparency and accountability are considered major factors in the spread of corruption, it is necessary for the state to force its administration and institutions to conform by law to the principle of transparency in all areas related to the economic and financial transactions of the state, including contracts, tender bids, auctions, domestic and foreign imports, and the sale of public lands and assets. It also requires the state to legally force political officials, high-level state employees, administrative leaders, those with financial influence and regular citizens to be subject to investigations into corruption charges.

In order to achieve this, a consensus must be forged among the political elite, including the government and the opposition, and it must be supported clearly and forcefully on the highest levels of state, whether this is represented in the president, the king, the prince, or the prime minister. High-level state authorities must affirm the principle of transparency and accountability, and it must be implemented with the utmost calmness and firmness. Anti-corruption must be treated as an issue of developing the state's infrastructure and social values. Moreover, anti-corruption cases should be used towards political ends as little as possible, based on an agreement between the government

and the opposition, in order to ensure political and social stability and to support the campaign against corruption in the long term. It is clear that these steps requires a democratization of the political system in any given country. Although it does not prevent corruption, democracy allows more opportunities to catch it, publicize it, and strengthen the deterrents against it.

2. Independent institutions to fight corruption must be established, or existing institutions must be made more independent so that they can investigate corruption on the highest levels of government. The members of these institutions must be independent, reputable individuals who are appointed—if it is a public body—for a definite, non-renewable period of time. They cannot be subject to dismissal, and they must have the force of law behind them, the ability to access information connected to domestic and foreign state matters, and the legal mandate and authority to investigate any government official.

3. State institutions, the judiciary, local and central legislatures, and the relevant independent authorities must all be involved in the battle against corruption: exposing it, monitoring it, and waging war against it. Thus will battling corruption become a general type of behavior and a public duty, rather than the mission of one particular institution.

4. Mechanisms for exposing and following up on corruption must be developed by supporting information-gathering bodies from within those institutions or those that work with them, as well as in banks and their clients. Research and investigations into corruption must be developed as well by monitoring the wealth of those who occupy positions that allow them to profit through corruption. Their assets must be compared with their salaries and their legal income.

5. Bureaucratic measures must be loosened as much as possible in licensing and obtaining documents, making the process clear and easy. The authority of state employees in granting and revoking licenses must also be restricted in order to guarantee that objective conditions obtaining licenses are met. The conditions must be as simple as possible.

6. The salaries of civil servants in the state, its administration, and its institutions must be raised to guarantee a honorable life for them and their families and to lessen their need to accept bribes and involve themselves in corruption to increase their income. Salaries must provide a fair standard of living at the entry level, and there must be an

opportunity advance economically. These measures must take place within the comprehensive context of improving the distribution of wealth in society through wage policies and social transformations.

7. The legal punishments for corruption must be reinforced to increase the deterrents to corruption, so that one will think twice before embarking on it. Both the one who pays and receives bribes must be punished, as was the case in the past before the revolution moved to release the payer of a bribe from punishment if he informed on the person who took the bribe and helped to prove the charge against him. Simply paying a bribe is itself participating in corruption.

8. The oversight role of the Central Bank must be strengthened and it must be given a high degree of independence and the authority to question bank employees and clients, even if these be political or economic officials.

9. The independence of the judiciary must be reinforced so that the conditions are met for the greatest possible degree of integrity in the fight against corruption.

10. There must be a distinction made between the ruling party and its institutions, on one hand, and the state, on the other, as the state and its institutions should have their own general structure that includes all citizens regardless of their political affiliations. This would naturally facilitate the prevention of corruption. In cases where the ruling party controls government administrations, the public sector and other state institutions, the opportunities for the appearance, growth, and spread of corruption are greater, while combating corruption is more difficult. Moreover, the ruling party can use what it terms anti-corruption operations as a cover for punishing its internal opponents or the opposition.

11. The tax system must be evolved to clearly define tax rates and limit them to acceptable levels that meet the financial abilities of taxpayers in order to reduce the causes of tax evasion.

12. Favoritism must be fought in the appointment of public officials and in transactions involving imports, tender bids, and government and public-sector auctions, through preventing the appointment of relatives at the fist and second levels of the same institutions and by thoroughly screening relatives and friends of political officials when they apply for jobs in the public sector. As for those import and government enterprises, relatives must be completely removed from the process in

the beginning, as they can obtain information not available to competitors through their relatives in the government or public-sector, thus creating unfair conditions for competition and making it easier to wrongfully win contracts.

13. Strict oversight should be instituted over the privatization process, which comprises one of the primary avenues for corruption in Arab and non-Arab states during the transition from a controlled economy to a market economy. ‘Abd al-Rahman al-Suhaybani, assistant secretary general of economic affairs at the Arab League, has said that 20 percent of the proceeds of privatization end up going as bribes to those who work in supervisory positions in the government. (See ‘Abd al-Rahman al-Suhaybani, “al-Khaskhasa fi al-buldan al-‘arabiya: qadaya mu‘asira, a working paper presented to the privatization committee in Amman, Jordan, 4-6 May 1998.)

14. The preventative controls against corruption in Arab stock exchanges must be further developed through building institutions and reinforcing the principle of transparency and equal information on market conditions to all participants. Corruption in the stock exchange must be met with strict penalties so that it acts as a deterrent to others who would manipulate markets or profit illegally at the expense of small and medium investors.

15. A blacklist needs to be drawn up of multinational companies that offer bribes in their dealings with foreign countries, including the Arab world, to prevent them from participating in contracting, tender bids, or auctions in Arab countries. This measure is important in that it blocks an important avenue of corruption in one of its most destructive forms—one that weakens the national economy and puts it at the mercy of multinational corporations. It also penalizes international companies that use bribery and tolerate it while giving greater opportunities to those companies that do not resort to corruption as a means of getting work.

These, then, are the general outlines of anti-corruption methods to be used in Arab countries. It must be said that embarking on anti-corruption efforts represents a decisive step to develop any political and economic system and to strengthen its legitimacy and its ability to lead society towards comprehensive progress.

Table 1
World Corruption Index

Country rank	Country	Corruption index	Number of surveys undertaken	Deviation from the average	High and low range of the corruption index for the surveys undertaken
1	Finland	10	8	.6	10.4/9
2	Denmark	9.8	9	.8	10.6/8.6
3	New Zealand	9.4	8	.8	10.2/8.1
4	Sweden	9.4	9	.7	9.9/8.1
5	Canada	9.2	9	.7	9.9/8.1
6	Iceland	9.1	7	1.1	9.9/7.3
7	Norway	9.1	8	.7	9.5/7.6
8	Singapore	9.1	11	1	9.7/6.2
9	Netherlands	8.9	9	.6	9.9/8.1
10	United Kingdom	8.7	9	.6	9.7/7.3
11	Luxembourg	8.6	7	.7	9.3/7.4
12	Switzerland	8.6	8	.3	9.1/8.1
13	Australia	8.3	10	1	9.3/6.7
14	U.S.A.	7.8	10	.8	9.2/6.2
15	Austria	7.7	8	.7	8.5/6.2
16	Hong Kong	7.7	11	1.2	8.6/4.3
17	Germany	7.6	8	.8	8.4/6.2
18	Chile	7.4	8	.9	8.4/5.7
19	Ireland	7.2	8	1.9	8.5/2.5
20	Spain	7	8	.7	8/5.9
21	France	6.7	9	1	7.7/4.3
22	Israel	6.6	8	1.3	7.9/4.3
23	Japan	6.4	11	1.3	7.8/4.3
24	Portugal	6.4	9	.9	8.1/5.3
25	Belgium	6.1	9	1.3	8.8/4.3
26	Botswana	6	4	1.6	8.2/4.3
27	Estonia	5.7	4	1.6	8.1/4.4
28	Slovenia	5.5	6	1.1	7.3/4.1
29	Taiwan	5.5	11	1,4	7.2/2.5
30	Costa Rica	5.4	4	1.9	8.1/3.8
31	Namibia	5.4	4	.8	6.1/4.3
32	Hungary	5.2	10	1.2	8.1/3.9
33	Tunisia	5.2	4	1.5	7.1/3.8
34	South Africa	5	10	.9	6.6/3.8
35	Greece	4.9	8	1.7	8.1/3.7
36	Malaysia	4.8	11	.6	5.9/3.8
37	Mauritius	4.7	5	.8	5.6/3.9
38	Morocco	4.7	4	.7	5.6/4.2
39	Italy	4.6	8	.6	5.6/4
40	Jordan	4.6	5	.8	5.7/3.8
41	Peru	4.4	5	.5	5/3.8
42	Czech Republic	4.3	10	.9	6.2/3.3
43	Belarus	4.1	3	.8	4.9/3.4
44	El Salvador	4.1	4	1.7	6.2/2.1
45	Lithuania	4.1	4	.3	4.4/3.8
46	Malawi	4.1	4	.4	4.8/3.8
47	Poland	4.1	11	.8	5.6/2.8
48	South Korea	4	11	.6	5.6/3.4
49	Brazil	3.9	8	.3	4.5/3.6
50	Turkey	3.8	8	.8	4.5/2.1
51	Croatia	3.7	4	.4	4.3/3.4
52	Argentina	3.5	8	.6	4.5/3
53	Bulgaria	3.5	6	.4	4.3/3.3
54	Ghana	3.5	4	.9	4.7/2.5
55	Senegal	3.5	3	.8	4.3/2.8
56	Slovak Republic	3.5	7	1.2	6.2/2.2
57	Latvia	3.4	3	1.3	4.4/2.1
58	Zambia	3.4	4	1.4	5.1/2.1
59	Mexico	3.3	8	.5	4.1/2.5
60	Columbia	3.2	8	.8	4.5/2.5
61	Ethiopia	3.2	3	.8	3.9/2.5
62	Thailand	3.2	11	.6	4/2.4
63	China	3.1	11	1	4.3/.6
64	Egypt	3.1	7	.7	4.1/2.3
65	Burkina Faso	3	3	1	4.4/2.5
66	Kazakhistan	3	4	1.2	4.3/2.1
67	Zimbabwe	3	7	1.5	4.9/.6
68	Rumania	2.9	4	1	4.3/2.1
69	India	2.8	11	.7	4.3/2.3
70	Philippines	2.8	11	1	4.7/1.7
71	Bolivia	2.7	4	1.3	4.3/1.7
72	Ivory Coast	2.7	4	.8	3.6/2.1
73	Venezuela	2.7	8	.7	4.3/2.1
74	Ecuador	2.6	4	1	4.3/2.1

75	Moldavia	2.6	4	.9	3.8/1.8
76	Armenia	2.5	3	.6	3.5/2.4
77	Tanzania	2.5	4	.6	3.5/2.1
78	Vietnam	2.5	8	.6	3.8/2.1
79	Uzbekistan	2.4	3	.9	3.7/2.1
80	Uganda	2.3	4	.6	3.5/2.1
81	Mozambique	2.2	3	.2	2.7/2.4
82	Kenya	2.1	4	.3	2.7/2.1
83	Russia	2.1	10	1.1	4.1/.6
84	Cameroon	2	4	.6	3/1.6
85	Angola	1.7	3	.4	2.5/1.6
86	Indonesia	1.7	11	.8	3.2/.5
87	Azerbaijan	1.5	4	.9	2.5/.6
88	Ukraine	1.5	7	.7	2.5/.5
89	Yugoslavia	1.3	3	.9	2.4/.6
90	Nigeria	1.2	4	.6	2.1/.6

Source: Transparency International, www.transparency.org, 12/17/2000

The Egyptian economy

the gap between statements and performance, the roots of the currency crisis, and the necessity of reassessing privatization

The year 2000 was a contradictory one for the Egyptian economy. By the government's own admission, the economy faced a real crisis, described as one of "liquidity." At the same time, there was a crisis in the currency market; its root causes and the measures taken to treat it both led to the plummeting of the Egyptian pound next the US dollar. Stepping up the process of selling the public sector to the private sector in the framework of the privatization program led to a fierce debate about the program, its feasibility, and its strategic effect on the Egyptian economy. Yet at the same time that the government was pointing to a crisis in 2000, the main indicators of the economy's performance as announced by the government—growth rates, inflation rates, and unemployment rates —completely belied its existence. These indicators were all positive, even excellent, and reflected no such crisis. If the role of economic indicators is to embody the state of the economy, the contradiction between government-issued indicators and the crisis requires some explanation, as it is, at heart, irreconcilable.

According to statements by the Ministry of Economy and Foreign Trade, the rate of real growth in Gross Domestic Product (GDP), excepting the tourism and oil sectors, reached 6.5 percent in fiscal year 1999/2000 compared to the previous year (see the ministry's monthly bulletin, November, 2000). The tourism sector registered an excellent performance in the same year, as Egypt's tourist revenues rose to US$4314 million in 99/00 from US$3235 in fiscal year 98/99. As a result of the rising price of oil and Egypt's increased exports, the oil sector also improved, bringing in US$2273 million in 99/00, compared to about US$1000 million in 98/99. Given these figures in the petroleum and tourism sectors, the real rate of growth in Egypt's GDP was more than the announced 6.5 percent, reaching 6.8 percent according to economic statements published by the National Bank of Egypt (see vol. 53, no. 2, 2000). The IMF in its *World Economic Outlook* of October 2000 predicted that the actual rate of growth in Egypt's GDP would reach 5 percent in the year 2000. As the IMF's projections include the petroleum and tourism sectors—the fastest growing as a result of the increase in oil prices and the excellent performance of the tourism sector—that means that growth in other economic sectors was much less than the 6.5 percent announced by the Ministry of Economy.

Government statements also indicated that the unemployment rate had declined to 7.4 percent in fiscal year 99/00, from 7.9 percent the previous year. In its *International Financial Statistics Yearbook 2000*, the IMF does not report unemployment figures in Egypt after 1995, when unemployment was up to 11.3 percent, despite the availability of Egyptian government figures for the following years.

Egyptian government reports also stated that the yearly rate of inflation had also declined to 2.8 percent in 99/00, down from 3.8 percent the previous year. These figures do not differ radically from those published by the IMF in its yearly report on the world economy (*World Economic Outlook*, October 2000), where the average rise in consumer prices in Egypt is put at 2.9 percent for 2000, down from 3.8 percent in 1999.

Government statements point to a rise in overall domestic savings—the statements actually concern national savings, and not domestic as the statements say—to LE55.7 billion in 99/00, compared to LE47 billion the previous year, bringing up its share in the GDP to 16.4 percent, compared to 15.6 percent the previous year. Local investments also rose to LE67 billion in 99/00 from LE60 billion the previous year. Local investments accounted for about 19.8 percent of GDP in 99/00, compared to 19.9 percent the previous year. Foreign direct investment in Egypt reached US$1656 million in 99/00, up from US$711 million in 98/99.

These Egyptian economic indicators, then, were all positive and did not express a state of crisis. Even domestic savings and investments—some of the lowest in the world—seemed stable; the former improved slightly in 99/00, while the latter only marginally decreased in the same year. This contradiction between the indicators and talk of a crisis require official explanation.

If the liquidity crisis that Egypt witnessed in 2000, particularly the first half, came as a result of the surplus in commodities and real estate

and the accumulation of unsold imports, where did the huge growth in the GDP come from? Normally, a commodities surplus and a sluggish real estate market lead to stagnation in the property sector and those industries linked to it, as well as in those sectors producing surplus commodities. Similarly, surplus imports negatively affect the movement of external trade. Government delay in paying its debts to the private sector impedes movement for part of that sector, delaying funds needed for further investments and thus increasing stagnation. How, then, could real growth in GDP have reached 6.5 percent in 99/00, even without the tourism sector, the best performing of the said year, and the petroleum sector, which saw a great increase in prices and in revenues from exports?

There are figures that clearly point to the existence of an economic crisis, in particular in the financial sector. The indicator expressing the movement of stock prices circulating on the bourse was down 39 percent in mid-December 2000 from the levels seen in early 2000. If Egyptian stocks are calculated in dollars, the figures are even worse, with prices falling 45.9 percent in mid-December 2000 compared to levels in January of the same year. The decrease is a result of the decline in stock prices, as well as the loss of value in the Egyptian pound next to the US dollar. (See *The Economist: Emerging Market Indicators*, London, December 16-22, 2000.)

Even in terms of the real economy, statements released by the General Authority for Investment showed that the number of corporate bankruptcies increased from 27 during all of 1999 to 42 in the first 8 months of 2000, according to monthly bulletins published by the Ministry of Economy and Foreign Trade. Similarly, foreign and domestic trade balances point to a real crisis. The general deficit reached 3.7 percent of GDP in fiscal year 99/00, although the government aimed to reduce the deficit to only 1 percent of GDP. In addition, the trade and accounts deficits reached worrying levels, as we shall soon see.

We will discuss the Egyptian government's explanation of the economic crisis of 2000, along with other underlying, chronic causes. We shall also examine the main developments and their causes in the currency market, and we shall touch on the privatization program and its role in the crisis.

I. An analytical reading of government explanations of the economic crisis of 2000

The government gave a number of reasons to explain the crisis that hit the Egyptian market recently, and it built a method of facing the crisis based on these reasons. Egyptian Prime Minister Dr. Atef Ebeid concentrated on a number of causes, the main one being excess production and surplus goods that found no markets. This led to particular anxiety as production and goods are largely financed through loans. (See Dr. Atef Ebeid's conversation with the editors-in-chief of Egyptian papers on the current economic situation in *al-Ahram*, 8/29/2000.)

This explanation of the crisis, however, contradicts the enormous size of the deficit in the Egyptian trade balance, which reached US$12.5 billion in fiscal year 98/99, and approximately US$11.5 billion the following year. (See the Central Bank of Egypt's monthly bulletin, October 2000.) This deficit indicates that local production of commodities does not even come close to meeting local demand. The deficit was not created in that year alone, or even in the past few years, but is a chronic feature of the Egyptian trade balance. However, it has increased dramatically since 1996 (see table 1).

The accumulated Egyptian trade deficit from 1990 to mid-2000 equals about US$85.5 billion, while the trade deficit of the last two fiscal years (98/99 and 99/00) reached US$12,563 million and US$11,474 million respectively. Thus, it is difficult to locate the problem of the Egyptian economy in overproduction, as there is a persistent shortage in local supply equivalent to the trade deficit. This situation is evidence either of weak productive capacity, in both the private and public sector, or of a weakness in applying these capacities, or possibly both, which is the most likely explanation. In the same context, the surplus of medium-range and high-end housing is linked to the failure to market these units due to excessive pricing by both private and public companies in an attempt to achieve exceptional

profits. This surplus is juxtaposed to excess demand in lower-income housing and a concomitant increase in pricing in these units.

Finding the source of the crisis in an oversupply of commodities will create a climate inhospitable to investment in Egypt; as long as there is a crisis due to a surplus of goods on the Egyptian market, any Egyptian, Arab, or foreign investor will think twice before establishing any new investments in Egypt. Thus, the government's imprecise prognosis of the causes of the economic crisis in Egypt in 2000 may be just as damaging as the crisis itself.

A clear line must be drawn when speaking of the roots of the crisis. On one hand, there is a decrease in Egyptian production of capital, intermediate, and consumer goods, leading to an enormous trade deficit. The deficit itself is an expression of the true dilemma of the Egyptian economy: it produces and exports much less than it consumes and imports. This is quite different from, on the other hand, an excess supply of certain unsold, imported commodities, which is ultimately an expression of the inadequacy of trade policies, a weak government role over this sector, and a lack of coordination between the private sector and its institutions and the government economic administration in fixing imports to levels needed by the local market—in short, regulating imports.

The inability to produce a large number of capital, intermediate, and consumer goods, coupled with an oversupply of certain number of marginal commodities is indicative of weaknesses in the structure of production—i.e., that it does not meet demand. This is ultimately the cause of Egypt's enormous trade deficit, which currently exceeds the total revenues that Egypt gets from the service industry and remittances from workers abroad. This situation led the government to spend a significant portion of its hard currency reserves, which reached their height in fiscal year 96/97 when reserves averaged out at US$20.3 billion, sometimes exceeding US$21 billion. Reserves began to recede as they were withdrawn to meet the exaggerated needs of importers, until reserves fell to US$14.6 billion in July 2000, according to figures from the Central Bank of Egypt (CBE), and then to US$13.4 billion in August 2000. (See *The Economist: Emerging-Market Indicators*, London, December 16-22, 2000.) Thus was one of the most important achievements of Dr. Atef Sidqi's government eroded: the creation of a large reserve of hard currency. The substantial reserves raised Egypt's credit worthiness and gave it financial leverage, which would have been more properly used to restructure the economy and achieve development, rather than hemorrhaging it to meet the needs of importers of consumer goods or importers working in the assembly industries, assembling automobiles for example, which does not represent a true addition to the Egyptian economy.

The large trade deficit is the source of the violent pressure exerted on the Egyptian pound next to the US dollar, leading to an unstable currency market for almost a year. The government is still following its policy of injecting foreign currency into the economy to meet the needs of importers and the general demand for the dollar, without considering the experiences of other countries. Similar policies in Mexico in 1995, Thailand in 1997, and the rest of southeast Asia—with the exception of Malaysia—led to a draining of foreign reserves. These countries later declared bankruptcy and sought refuge with the IMF, where they submitted to all its conditions in order to obtain new loans with the support of the principal member countries. Egypt is not guaranteed to receive the same support should its economy reach that point. Even an industrialized, technologically advanced country like England nearly spent most of its foreign reserves when the Bank of England stepped in to meet the high demand for foreign currency in September 1992. Hence, it is necessary to review the policy of currency pricing completely, in order to benefit from the experiences of southeast Asian countries in facing their economic crises. China, for example, has managed to avoid the crisis by maintaining a stable currency, raising domestic savings and depending on itself to achieve development and increase its ability to compete. As a result, it has achieved a substantial surplus in the trade balance and accounts.

When Malaysia was exposed to the winds of crisis in the second half of 1997, it stabilized currency prices, postponed certain infrastructure projects, and regulated imports to ameliorate the trade deficit. It succeeded in reducing it dramatically, from about US$79.1 billion in 1997 to about US$58.3 billion in 1998. By depending on itself, Malaysia was able to overcome the economic crisis without the help of

the IMF and without having to succumb to its conditions. Most of the country's economic indicators were subsequently excellent. Growth was put at 5.7 percent in 1999 and is expected to reach 6 percent in 2000, compared to a negative growth rate of 7.5 percent in 1998. It has achieved a substantial surplus in its trade balance of US$16.7 billion in only 12 months, ending October 2000, after having registered a trade deficit every year from 1994-1997. The surplus in running accounts reached US$11.3 billion in the year ending June 2000, and foreign currency reserves rose to US$30.1 billion in October 2000, compared to US$20.8 billion in 1997. As a result, the country's credit rating has improved immensely.

The Egyptian government adds that one of the reasons for the current economic crisis is several years of government spending on projects funded with debt, along with the private sector's increasing dependence on loans. (See the dialogue between the prime minister and editors-in-chief of Egyptian papers in *al-Ahram*, 8/29/2000.)

The truth is that public spending is not the cause of the crisis, but rather the type of public spending, which has been concentrated in infrastructure projects on which about LE275 billion have been spent over the 1980s and 90s. Spending has been conducted without establishing productive enterprises that would complement it. The total issued capital of private investment companies—Egyptian, Arab, and foreign—which were established and began working in Egypt in the mid-1970s until mid-2000 does not exceed LE56644 million. In other words, the issued capital of these companies from the mid-70s until mid-2000 only accounts for 20.6 percent of the public spending on infrastructure projects throughout the last two decades. If we include the capital of those investment companies in the process of being established, the total comes to LE118,952 million for the same period.

Such a situation compels the state to review its spending patterns in order to set aside an important portion for establishing directly productive ventures in capital industries, intermediate industries, or high-tech industries to meet the needs of society for these commodities and to export, particularly as private investments—local, Arab, and foreign—have not responded properly to the huge development in infrastructure which was funded by the people in the form of state expenditures. Achieving a general economic boost with the participation of government investment, and without touching the general framework which allows the utmost freedom to the private sector, will motivate both the local and foreign private sector to pump investments into the Egyptian economy. The private sector often looks for a successful developing country where it can participate in that success, but it doesn't often bear the industrial cost of getting that success off the ground. If the government feels that owning new ventures contradicts its current economic policy of shedding a direct economic role, it should sell these ventures with controls that would guarantee a fair price. The important thing is that it establish them.

It was recently reported that Japan is abandoning the implementation of more than 200 large public works projects totaling more than US$25 billion in light of doubts of the feasibility of infrastructure projects, which create extraordinary pressure on the economy. Instead of these projects, new high-tech ventures will be pursued. In other words, even for a highly developed country like Japan, cutting down on infrastructure projects is possible, particularly when this infrastructure is already relatively high, as is the case in Japan.

Egypt currently has a very good infrastructure in comparison with the level of economic activity and average income. This justifies cutting down expenditure on it and putting the money instead into productive ventures that the economy needs. Moreover, it is possible to concentrate on establishing new infrastructure projects, particularly those related to cities and new industrial areas, using the buy-operate-transfer system (BOT) to lessen the burden on the state and open new areas to the private sector.

As for the negative effects of increasing loans to the private sector, the problem is not with the policy itself. When banks receive savings deposited by families, they do not do so in order to lock them up, but to use them in loans to the private sector to encourage investment and growth and obtain a return that will cover the interest and make a profit. The problem, rather, is in granting loans without collateral and the propensity of some high banking officials to not abide by existing regulations. The problem also lies partly in how the private sector uses

the loans, which in turn determines their ability (or inability) to pay them back.

In any case, it is very important to locate the true causes of the crisis which currently plagues the Egyptian economy in order to determine how to end it. Leaving aside issues of supply and demand, Egypt's economic performance and the general economic environment have been negatively affected by several cases of corruption—the al-Habbak case, the so-called loan deputies cases—and several cases of businessmen fleeing abroad after obtaining sizeable bank loans, whether this was due to the banks' failure to verify the client's collateral, or because high-placed bank officials gave loans in return for a commission, or because of the financial collapse of some who received loans. Similarly, the level of government administration and complicated bureaucratic measures continue to act as a deterrent to the growth of private investment, and they create outlets for corruption. In general, all this impinges on opportunities to encourage the new investments necessary for growth.

The Egyptian economy's performance also suffered after freeing up the movement of foreign capital in non-direct investment in the Egyptian stock market, coupled with the lack of controls to prohibit this foreign capital from becoming 'hot money', which moves quickly and can destabilize the Egyptian stock market. This is especially true after mid-1996, when the 2-percent tax on capital gains made on the stock market was cancelled. Foreign capital operations made on the Egyptian stock market comprised 43 percent of the total value of all transactions in the first seven months of 2000, up from 44 percent in 1999, 40.7 percent in 1998, and 38.7 percent in 1997. This indicates their increased ability to affect the market according to their own interests, regardless of Egyptian economic interests. In the end, their profits are transferred abroad.

The prime minister's program for dealing with the economic crisis included paying off government debts to the private sector; proposing new public works projects in the amount of LE20 billion to establish 500 schools, complete potable water lines, raise the capacity of main roads and transform them into 250-km state roads, add 700,000 new telephone lines, and continue to enlarge the telephone network;

Egyptianizing government purchases by making sure local products are purchased whenever; combating smuggling to protect local products; and privatizing certain state holdings to put the returns back in the market. (See the interview with the prime minister and editors-in-chief of Egyptian newspapers, *al-Ahram*, 8/29/2000.)

If schools, water lines, and combating smuggling are necessary measures with which no one disagrees, the current economic circumstances in Egypt require limiting spending—even if temporarily—on roads and new phone lines, and concentrating effort instead on direct investments in production to meet local demand and to raise the level of competitiveness in export. It also requires social expenditures and improving social services to combat poverty.

Continuing with the privatization of the public sector during a "liquidity crisis," as the government describes it, is equally strange, as it means that public companies will be put up for sale when there is no demand for them. Hence will the asking price be less than the company's true value. Moreover, the companies will be sold largely to foreigners. This is unacceptable, especially considering that the privatization process engenders a trend towards economic recession by creating a shortcut for possible private investments that could otherwise spur on economic growth. Finally, the assumption that injecting the proceeds of privatization into the market will help ease the current crisis is unsubstantiated. The money with which the private sector will buy public companies is already present in the market, whether in the private sector or in the bank that will loan it. Thus, privatization will add nothing, but will only transfer the money from the private sector to the state. We shall deal with the Egyptian privatization program in further detail below.

There must be a workable, methodical program for raising the level of domestic savings, considered among the lowest in the world—it did not exceed 16.4 percent of GDP in 99/00, according to Egyptian government figures. The level of domestic savings in Malaysia and China reached 47 percent and 43 percent respectively of GDP in 1998, according to the World Bank report on world development. Clearly, raising the level of domestic savings requires financial and monetary measures and a development of popular culture to redirect

expenditures, particularly those that go abroad, such as expenditures on travel, which reached US$1028.3 million in fiscal year 99/00.

It is also necessary to revise monetary policy, whether it means unpegging the pound from the dollar and examining linking the pound to a basket of currencies, or reexamining the idea of a controlled float, which will be discussed below.

Similarly, imports must be strictly regulated so that the crisis does not deepen and we are led in the end to forced regulations. The achievement of a balanced trade should be the highest goal of economic policy, such that the success or failure in meeting that goal becomes the basis for judging the success or failure of economic policy as a whole in a country being eaten away by a huge trade deficit. Perhaps policymakers in Egypt will be inspired by the Malaysian example, where the trade deficit became a trade surplus within one year after imports were effectively limited and exports stimulated.

Controls must also be placed on the movement of foreign capital, particularly indirect investments on the Egyptian stock market, with the aim of slowing down their movement through taxes on profits. A minimum time limit could be set for holding stock before trading it and laws could be implemented requiring foreign capital to invest part of their profits in the Egyptian market.

If achieving balanced economic relations with the outside world is important, balancing the budget is of the utmost importance. This is quite possible through combating tax evasion and comprehensively revising the tax system to be less of a burden, but more strictly applied.

II. The currency market: a chronic crisis with protracted roots

The Egyptian currency market was exposed to severe disruptions in 2000, creating pressure on the Egyptian pound next to the US dollar. These disruptions and pressures magnified the rumblings experienced in the currency market over the last two years due to the increased Egyptian demand for US currency. The government dealt with the crisis by pumping its hard currency reserves into the Egyptian market, leading to the consumption of more than one-third of the reserves from 1997-2000. Although there are contingent factors for the fluctuations seen in the Egyptian currency market, the market acted essentially on a number of long-range factors that have influenced the exchange rate and the market in general.

Before taking up the causes of the crisis and suggesting a strategy for dealing with it, it must be said that the ideal price of the Egyptian pound is that which reflects its buying power in the Egyptian market compared to the buying power of the US dollar in the US market. Accordingly, the US dollar should be no more than LE1.44, according to calculations based on World Bank figures in its report on world development 2000/2001. The report indicates that Egypt's Gross National Product (GNP) in 1999 reached US$87.5 billion based on current exchange rates, whereas it reached US$206 billion based on buying power equivalency with the dollar.

As is clear, there is a large gap between the ideal price of the Egyptian pound (LE1.44 per US dollar in 1999) and the actual price of the pound (LE3.41 per US dollar in 1999). This gap could increase even more with the plummeting price of the Egyptian pound in 2000, which reached on average LE3.75 per dollar, and sometimes went as high as LE3.95 per dollar. The reason for the difference between any currency's ideal price and its actual price is found in the foreign trade balance of the country in question, local and international impressions of its economy and currency, the level of speculation and illegal activity that goes on in the market, and other factors. It is also necessary to point out that the stability of a currency's price is not sacrosanct; the important thing is that the currency price of any country serves to achieve its economic policies and goals, stimulate development, encourage local investment, stimulate exports, achieve a balanced foreign trade balance, improve the ratio of international exchange, and guarantee a stable level of inflation. If achieving these goals calls for lowering the price of local currency by a studied amount, it should not be dealt with as if it were a national tragedy or the collapse of the local currency. If the price of the local currency should be raised, it should also be done in a studied manner. In short, the Egyptian political and cultural elite, businessmen and Egyptian society as a whole, need to get rid of the idea that maintaining the price of the

local currency is in itself the highest goal; the currency price should serve to achieve the state's economic goals instead.

I. Causes of fluctuations in the market and currency price

The huge Egyptian trade deficit comprises the most important factor for pressure on the Egyptian pound and, in turn, for fluctuations in the Egyptian currency market. The deficit has been growing exponentially since 1997 due to the enormous increase in imports coming from southeast Asia, whose financial and monetary crises led to a devaluation of their currencies next to the US dollar and other currencies pegged to it, such as the Egyptian pound. This meant that the price of exports from these countries decreased for Egyptian importers, spurring them on to increase imports. Rather than limit themselves to the commodities needed by the Egyptian market, importers overstocked in the belief that the price of these commodities would soon go up.

Figures from the IMF based on statements from the CBE indicate that the deficit in the Egyptian trade balance jumped from US$9620 million in 1997 to US$13,284 million in 1998, US$12,427 million in 1999, and US$5588 million in the first six months of 2000. The total trade deficit from 1990 to mid-2000 is approximately US$85,501 million (see table 1). Thus the trade deficit for that 10-year period comprises about 53.5 percent of the total value of Egyptian foreign commodities trade in the same period—US$159,688 million, according to Egyptian sources.

IMF figures based on statements from Egypt's trade partners indicate that the trade deficit reached US$10,621 million in 1996, US$12,740 million in 1997, and US$14,283 million in 1998, before slightly decreasing to US$14,190 million in 1999. The total accumulated Egyptian trade deficit from 1990-1999 is put at US$97,872 million (see table 1). Accordingly, the trade deficit for the ten-year period comprised about 46.4 percent of the total value of Egyptian foreign commodities trade, or US$210,906 million, according to Egypt's trade partners.

Whether using Egyptian figures or those of its trade partners, the trade deficit is by any standards enormous, both in terms of its total value and its percentage of foreign commodities trade. If the deficit shows that Egypt produces and exports much less than it consumes and imports, it also reveals the danger of such high levels of consumption. Not only does local demand exceed imports, but there is a low ration of domestic savings, which, according to the World Bank in its report on world development 2000/2001, reached only 14 percent of GDP, much less than the level of local investment, which reached 23 percent the same year. (Egyptian government figures show that for fiscal years 98/99 and 99/00 domestic savings accounted for 15.6 percent and 16.4 percent respectively of GDP, while the level of investment in the same two years reached 19.9 percent and 19.8 percent respectively of GDP.)

In any case, the level of domestic savings is trifling, and there is a gap between it and the level of investment, although the latter, too, is low given Egypt's developing status. This gap is bridged with loans or foreign investment, which is still limited despite the concessions Egypt gives to foreign investors, often allowing them and their home nations to benefit from the investment more than Egypt.

The World Bank report previously mentioned indicates that the world average rate of domestic savings was 23 percent of gross world product in 1999. The same year, that figure reached 45 percent and 48 percent in the less developed countries of Congo-Brazzaville and Angola respectively. In Algeria, domestic savings were 30 percent of GDP, 24 percent in Tunisia, and 18 percent in Syria and Morocco. In a number of newly industrialized countries, such as Singapore, Malaysia, China, and South Korea levels of domestic savings to GDP reached 52 percent, 45 percent, 42 percent, and 34 percent respectively. In fully industrialized capitalist countries, such as Japan, Holland, Finland, Austria, and Germany, the figures were 30 percent, 27 percent, 26 percent, 25 percent, and 23 percent respectively of GDP in 1999 (see table 2).

Of all these countries, Egypt's rate of domestic savings is the lowest. This low rate and its consequences—loans and attempts to attract foreign investors with more than generous incentives—in the end puts more pressure on the Egyptian pound. This means that raising the level of domestic savings and curbing consumption and its culture are necessary, not only to lessen the pressure on the Egyptian pound, but to fund development and economic growth more securely by depending

on the self. In the context of supervising spending to increase savings, it is necessary to reduce the levels spent on traveling and tourism abroad, which reached US$1104 million and US$1028.3 million respectively in fiscal years 98/99 and 99/00.

In addition, currency smuggling connected to illegal activities such as loan default or the drug trade increased demand for the dollar, as money was taken out of the country only after being turned into hard currency. Similarly, the loss of confidence in the stability of the Egyptian pound and the rumors that accompanied it generally lead to transferring a portion of domestic savings in pounds to dollars, also creating a higher demand for the dollar and encouraging speculation, which puts pressure on the Egyptian pound. Thus, the currency price in the market does not reflect the actual relative buying power of the Egyptian pound in the Egyptian market or the US dollar in the American market.

In short, among the long-term factors sparking fluctuations in the Egyptian currency market is the large and persistent trade deficit, which has reached levels that cannot be bridged by Egypt's service economy and receipts from abroad. Also included are illegal activities, particularly the drug trade, where drugs are imported with hard currency, and smuggling currency abroad. These chronic conditions can lead to a crisis when they are triggered by any new factor, or when one reaches high enough levels to choke the currency market. This happened in 1997 when the large increase in imports and the trade deficit combined with the strong reduction in tourist revenues in 1998 after the Luxor massacre in November 1997. It also happened with the large decrease in oil prices and the corresponding value of Egypt's petroleum exports in 1998, which led to a deficit in Egypt's petroleum trade balance in 1999.

II. How can the currency market be stabilizing?

Fixing the currency market does not mean fixing the price of the Egyptian pound—these are two different things. In many cases, lowering a currency's price is one method used to treat the problem, or a means of creating a balance between the currency's price and the changing factors that influence it. In the case of the Egyptian market, the large increase in tourist revenues and petroleum exports in fiscal year 99/00 compared to the previous year could contribute ease the crisis in the currency market and minimize the pressures exerted on the Egyptian pound next to the US dollar. Nevertheless, we should not forget that the increase in oil export revenues in 2000 is not guaranteed to continue, whether due to severe fluctuations in the price of oil or because Egypt cannot export oil indefinitely. Similarly, Egyptian tourist revenue depend on foreign parties who are influenced by the western media, and they are affected by breaches of security that might not spark a similar reaction in another country. The truth is that the strategic factors which cause tremors in the currency market from time to time still exist, even if they are minimized. These factors include primarily the huge trade deficit and illegal activities, particularly the drug trade and smuggling currency abroad.

Thus, treating instability in the currency market requires dealing with both the strategic and transitory factors that lead to upsets, particularly the chronic and large trade deficit. Here it is possible to benefit from the experiences of southeast Asian countries such as South Korea and Malaysia. Both countries suffered from trade deficits from 1994-1997, and neither did anything substantial to stop the problem from growing, until with other factors involved, the monetary crisis hit both of them, almost at the same time. Both countries exerted tremendous effort to improve the balance of trade and to improve external accounts generally. One of the most important remedial measures taken by both countries was to drastically reduce the level of imports, quite possible in the short term, whereas increasing exports generally takes much longer. South Korea reduced its imports from US$144.9 billion in 1997 to US$93.4 billion in 1998. At the same time, the value of its exports fell from US$136.4 billion in 1997 to US$132.7 billion in 1998. But the greater decrease in imports changed its trade balance from a deficit of US$8.5 billion in 1997 to a surplus of US$39.3 billion in 1998. In 1999, South Korea was able to raise its exports effectively, reaching a value of US$143.7 billion. Although imports were also increased to US$119.7 billion, South Korea continued to register a large surplus in its trade balance—US$24 billion in 1999.

Malaysia registered a trade deficit of US$200 million in 1997. It reduced its imports decisively from US$79.1 billion in 1997 to US$58.3 billion in 1998. Its exports also decreased from US$78.9 billion in 1997 to US$73.5 billion in 1998. The result was a transformation of the balance of trade, from a limited deficit in 1997 to a large surplus that reached US$15.2 billion in 1998. In 1999, Malaysia was able to effectively increase its exports to US$84.6 billion. Its imports also went up to US$65.5 billion, although the larger increase in exports left a surplus of US$19.1 billion in the foreign trade balance in 1999. (See the IMF, *Direction of Trade Statistics: Yearbook 2000*.)

Judging from the experiences of Malaysia and South Korea, facing Egypt's chronic trade deficit—which has caused a loss of more than one-third of the nation's hard currency reserves, put pressure on the price of the Egyptian pound, and created tremors in the Egyptian currency market—requires restricting imports in the short term while working effectively to permanently increase exports. It should be noted that the sudden increase in the value of Egyptian exports as a result of high oil prices is not guaranteed to remain as such. Hence, primarily industrial exports are capable of ensuring an increase in export revenues, whether in Egypt or any other country.

Similarly, the situation in the currency market must be treated, and it is necessary to reevaluate the policy of pegging of the Egyptian pound to the US dollar, which has caused enormous losses for Egypt in the past few years. This was one important factor in restricting the development of Egyptian exports to European Union states—a more important trade partner to Egypt—as the rise of the US dollar, and with it the Egyptian pound, in comparison to European currencies led to a price rise in Egyptian exports to Europe when evaluated by local currencies. Thus the competitive capacity of Egyptian exports on European markets decreased. In turn, the price of European commodities fell in comparison to the US dollar and the Egyptian pound, which raised their ability to compete in Egyptian markets. It also increased imports rapidly, leading to a dramatic growth of the trade deficit with countries of the EU (see table 3).

According to the IMF's *Direction of Trade Statistic Yearbook 2000*, based on Egyptian government figures, Egyptian exports to EU states sunk by 23.3 percent between 1996-1999, while EU figures show that Egyptian exports fell by 30.5 percent in the same period. Egyptian figures show that the trade deficit with the EU rose from US$3098 million in 1996 to US$4491 million in 1999, or 45 percent. EU figures for the same period indicate that the Egyptian trade deficit rose from US$3512 million in 1996 to US$5735 million in 1999, or a jump of 63.3 percent.

In short, the policy of pegging the pound to the dollar put extra pressure on the Egyptian pound, which led to an increase in imports and a trade deficit with Europe, Japan, and the countries of southeast Asia, which were affected by economic crises and saw the value of their currencies plummet compared to the dollar and the pound. It is necessary to increase the methods of fighting illegal activities which take foreign currency out of Egypt, particularly the drug trade and currency smuggling.

III. Privatization: an attempt at an objective evaluation

When the idea of privatization was first broached in Egypt, the goal was to sell unprofitable public-sector companies. It was thought that the loss incurred by some companies reflected poor management and that selling it to the private sector—which always strives for maximum profit—could turn these companies into profitable ventures. This version of privatization was a means of ensuring popular support for the idea, although years passed before it was put into practice. When the process started, the best companies and profitable hotels were put on the block, and the earlier conception was forgotten, as it had only been circulated to convince citizens of the idea in the first place. Privatization was not discussed except in a perfunctory way, taking advantage of the international climate after a wave of privatization in Britain, the US, and other western countries, and after the dissolution of the former Soviet Union and the fall of the old regime.

In short, with the privatization process the Egyptian people and its cultural elite submitted to the blackmail of prevalent world opinion. More specifically, this blackmail took place through Egypt's creditors and the IMF, whose most important role has become to act as an agent on behalf of creditor countries in their dealings with debtor countries.

Privatizing the Egyptian public sector was set as a condition by the IMF and Egypt's creditors to revising the country's debt schedule and dropping part of it.

All of these conditions gave rise to an arbitrary way of dealing with the issue, and it seemed at times as if the public sector were a sin or a nightmare that had to be cast off before the economy could take off. This was despite the fact that the public sector played an important role in industrialized capitalist countries in the past, as they faced the Great Depression of the 1930s, when the state intervened to restore economic equilibrium and raise the level of employment through public works. The public sector was also important in these countries after World War II, when it was necessary for the state to intervene to rebuild the economy that the war had destroyed, along with several vital economic areas and areas national security. Moreover, in developing countries, the public sector was largely established as a result of the inability of the private sector to implement the necessary investments to achieve economic progress and to fill the gap between developing and advanced economies. The public sector in many cases stepped in to build an economic base capable of interacting with the international economy from a position of strength. Hence, the public sector played, and still does play, and important role in the economies of developing countries in particular.

Industrialized capitalist countries adopted the ideas of John Maynard Keynes on increasing the state's economic role to allow it to come out of its depression in the 1930s, and they depended on these ideas after World War II to rebuild the economies destroyed by the war. Indeed, they continued to depend on them through the early 1970s without it at all affecting the private sector. These states have now become capable of relinquishing a direct economic role, while maintaining control over financial and monetary economic policy and supervising the economy in general. They have achieved a high level of economic development and socioeconomic efficiency; its companies have developed locally and internationally; they have established shared interests and a coherent traditional capitalist class that realizes its social responsibilities and turns this realization into reality, exemplified in the taxes they pay, something Egypt strongly lacks. (The minister of finance indicated in April 2000 that taxes owed to the state had reached LE17.6 billion.)

Hence, there were no negative effects on the economies of these countries (Britain, the US, and other developed countries) when they privatized a large chunk of their public sector. Moreover, the governments in these countries continue to spend a substantial portion of GDP—in 1998, 47.7 percent, 46.6 percent, 44.6 percent, 44.6 percent, 42, 8 percent, 37.8 percent, 40.5 percent, and 33 percent respectively in Holland, Belgium, Italy, France, Sweden, Britain, Austria, and Germany, according to the World Bank. Such a huge level of spending makes the state capable of exerting a direct, effective influence on the economy.

Rather than privatizing the Egyptian public sector, it could have been restructured and developed, its performance and profits improved, and it could have been made to submit to true popular monitoring to ensure that corruption did not spread. However, Egypt's acceptance of privatization took place under pressure related to the debt crisis and the economic retardation of the late 1980s and early 1990s. The current economic situation in Egypt allows for a fresh discussion of the issue to evaluate the privatization program and its effects on the Egyptian economy.

Firstly, one cannot equate privatization with economic liberalization. One cannot possibly claim that the British economy before Thatcher led the privatization process, or the US economy before Reagan did the same, were socialist economies or even based on the public sector. There were, in contrast, the two most liberated economies in the world insofar as the private sector was given free rein in all areas and foreign economic relations were highly liberalized. The move towards privatization in these two countries took place as the state was renouncing its role in the economy for an economic reason, namely, the surplus capital that resulted from a poor distribution of income and a general rise in income. This surplus capital was transformed into hot money, which caused disruptions in the stock and currency markets. The ideal conditions for such speculation were met in the early 1970s, specifically after the US abolished a law allowing dollar to be converted to gold on August 15, 1971. The collapses that followed led

in the end to the total floating of the primary free currencies. The chaos caused by the huge capital surplus in European and American stock and currency markets was made intensified by the influx of a large surplus resulting from oil revenues and Japanese trade, which increased the amount of capital moving in the US market especially. This in turn created a pressing need to open world markets to US capital, whether through direct or indirect investments. The surplus of local capital and its influx from abroad to the US and British economies fueled inflation and became a factor of general economic instability. The two countries thus had to treat this long-term phenomenon.

Looking at table 4, we can see the huge increase in foreign investment that flowed into the US since the mid-1970s until the present in light of several factors, starting with the oil surplus and the Japanese and Asian trade surplus and ending with wealth migrating in from developing countries, whether legally or not.

The policy of privatization in industrialized, advanced capitalist countries—particularly the US and Britain which suffered more than others from a surplus of hot money—was a means of reining in unruly hot money by linking it to stable assets. As public assets in these countries are limited and are not enough to ensure the use of surplus domestic capital and the influx of foreign capital, the industrialized, advanced capitalist countries began their call to privatize the public sector in developing countries. The call was accompanied by strong pressures to free up the movement of capital, whether in direct or indirect investments, to ensure the availability of assets in developing countries before the surplus capital from developed countries. This is clearly embodied in the sudden debt crises felt by several heavily indebted developing countries, particularly in Latin America in the early 1980s. Every country that could not pay its loans and hence requested support from the IMF and creditor countries was forced to grant foreign capital unfettered access to its economy. In some cases, countries were also made to exchange debts for public assets. A similar thing occurred with the countries of southeast Asia when the financial and economic crisis hit in mid-1997, continuing through 1998 until it began to recover in 1999.

The trend of transferring western hot money abroad was strengthened after this capital contributed to a rise in share prices in the stock markets of these countries, pushing them to levels higher than their true value. This was another factor in the outbreak of the great crisis that hit these markets in 1987, considered the biggest stock market crisis since Black October in 1929.

In any case, the use of the privatization policy in western industrialized nations was not a move to liberalize these economies, as they were already free. Rather, it was an attempt to marginalize the direct economic role of the state in the interest of increasing the hegemony of the private sector after it had proved its ability to achieve the economic goals of the state both at home and abroad. It was also an attempt to increase economic power, a main component of the state's comprehensive power, and a means of requiring the private sector to take on public burdens, principally through paying taxes.

Nevertheless, while the state was minimizing its direct economic role—its role as a direct producer of commodities and services—it maintained, and even increased, its indirect role in the economy through public expenditure and the formation of general economic policy. We have already indicated the high percentage of public expenditure to GDP in these western industrialized countries that adopted privatization.

Egypt, in contrast, does not suffer from a surplus a capital that must be curtailed by selling public assets. On the contrary, it suffers from a lack of capital. The average ratio of domestic savings and investment are low when compared to the rest of the world, as we have pointed out. Thus, the objective reasons for adopting privatization in the West has no foundation in Egypt, and, as a result, this policy must be reconsidered in light of Egypt's economic and social circumstances—not in light of what the IMF and Egypt's creditors demand.

It must be pointed out that privatization naturally inhibits the implementation of new private-sector investments: the capital used by the private sector to buy public-sector assets is, in the end, the same capital that would have wholly or partially been used to fund new investments. Instead, it is used to circulate already existing assets. This can push the economy towards stagnation, and even recession, except

in the case that the state uses the proceeds of privatization to build new productive ventures, even if they will be sold to the private sector in the future, and except in the case that the private sector uses the profits of its acquired ventures to fund new capital improvements that will ensure economic growth.

That the public sector is a center of government corruption is also no justification for privatization—privatization itself can open the door to even greater corruption, particularly in the process of appraising assets and selling them. As a result, isolated instances of corruption in the economy can become an innate feature of that economy, particularly if privatization takes place in the absence of strict control by government and legislative oversight bodies. Popular oversight can only be achieved within a truly democratic system.

There are two primary methods of appraising the public-sector assets to be sold. The first is arbitrary, as when a governmental, local, or foreign agency is authorized by the government or its representatives directly to undertake the evaluation process. When a committee of governmental or non-governmental experts empowered by the sate appraise the companies to be privatized, there is the possibility that members of the committee will undervalue the assets in the interest of an investor or a group of investors in exchange for bribes or commissions. Similarly, government committees might overvalue the price of public-sector companies that the government actually does not want to sell, in order to justify the fact that they have not been privatized to the IMF and Egypt's creditors.

The second method of evaluating public assets up for privatization is a market assessment that derives from the dynamic between supply and demand, conducted through auctions, tender bids, or by gradually selling the company's shares in the stock market.

It can be argued that selling through an auction or a tender bid does not necessarily constitute a market transaction, as the government can exercise control over supply by determining which companies will be sold at a particular time. The sale may also be delayed or cancelled if the auction or tender bid does not reach the market price. In addition, large investors can agree to set the price of companies at certain levels that serve their own interests, and, as a result, the sale of these companies will not reflect a free interaction between supply and demand. It will instead reflect the interaction of monopolizing tendencies on the forces of demand, represented by the investors, on the forces of supply, represented by the state.

Selling companies by offering shares on the stock market must be done properly, through a strong market that has a wide base of small, medium, and large investors, contains companies that create markets, and that has controls to prevent it from becoming an arena for speculators and professional traders.

The assistant secretary-general of the economic affairs committee in the Arab League, Abd al-Rahman al-Sahibani, says in his study, "Privatization in Arab Countries," that in those countries that have recently turned from a controlled to a market economy, approximately 20 percent of the value of companies privatized is paid in bribes and commissions to members of supervisory agencies in the government.

I. The initial evaluation and the final proceeds of selling the public sector

Those public-sector or joint-venture companies that have been sold so far—214 in all—have been assessed at radically different values. At times, the difference was a result of the methods used to assess their value—some were assessed according to market value, some by book value and others by nominal value. In *al-Ahram* of 4/20/1990, Ibrahim Nafie stated that the value of public-sector assets was approximately LE100.84 billion, or US$50.42 billion according to the average price of the dollar in 1990 (LE2, according to the IMF's *International Financial Statistics Yearbook 1995*). In 1991, deputy prime minister and minister of planning Dr. Kamal al-Ganzuri said that the public enterprise sector controlled investments worth LE124 billion, or about US$37 billion according to the price of the pound in 1991. He was most probably referring to the book value of companies in the public enterprises sector, rather than the market value. In 1993, the vice-president of the National Investment Bank said that the true value of companies in the public sector was more than LE500 billion, or about US$150 billion according to the 1993 price of the pound.

After a substantial portion of the public sector has been sold, the returns seem shockingly meager in comparison to these initial evaluations of the value of the public sector. From the beginning of the privatization process through late July 2000, 138 companies were sold either completely or partially. According to the Ministry of Public Enterprises, the returns on these sales reached LE15,622 million. When 135 companies had been sold, Dr. Mukhtar Khattab, minister of public enterprises, indicated that returns totaled LE14.8 billion, while the value of companies still owned by the state was LE10 billion, plus LE4 billion for the total value of state stock in companies that had been privatized (see *al-Ahram*, 6/8/2000). In order words, the total value of the public sector had become LE28.8 billion in 2000, less than US$8 billion.

The danger of the minister's statement lies in the undervaluation of the remaining public-sector assets, to say nothing of the undervaluation of those assets that have been sold. There were several cases in which the price of the land upon which a company was established was alone much higher than the final price for which the company was sold, as we will soon see. In such cases, it would have been wiser to sell the company's equipment and trade name, while giving the purchaser land in new industrial areas to move the company to once it was privatized. In such a way, the state could have taken the land and used it to the benefit of the people, particularly when these companies were established on property in the city or on its outskirts.

We shall now deal with certain examples of privatization in Egypt.

1) The Pepsi-Cola deal: sold for less than the price of the land

The deal to sell the Egyptian Bottling Company (Pepsi-Cola Egypt) is considered one of the most important privatization deals in Egypt up until now, and the evaluation process and the final price it fetched are considered a practical example of the problems associated with appraisals.

The Pepsi-Cola deal began on February 3, 1993, with a government order to sell the company and widen its ownership base. The particulars of sale were distributed to prospective buyers in March amid attempts to market the company. The US-based Cooper and Lerand took on the evaluation process and appraised the company at about LE76 million, but the Holding Company for Food Industries thought the price undervalued. It refused the results of the appraisal and ask for a reassessment, stressing that the company would be sold to the investors who offered the highest price and best conditions. As the company owned a huge slice of land on Mustafa Kamil Street in Alexandria—approximately 5000 meters—the company's value increased when the value of the land was calculated as property that could be used for any purpose, not merely permanently occupied land.

When Pepsi-Cola was reevaluated, the consultant office of the Holding Company for Food Industries put the top market price at LE140 million, suggesting that the company be sold for between LE100-140 million. Pepsi-Cola Egypt owned 8 bottling factories, some of which were in major cities like Cairo; 18 production lines with the capacity to produce 50 million cases; and a fleet of trucks which distributed its products all over Egypt. The Bank of Cairo oversaw the marketing of the company and the sale process.

Interested businessmen and companies began to compete for the company. The most prominent competitors who submitted purchase offers were Egyptian businessman Muhammad Nusayr in partnership with Pepsi-Cola International; Coca-Cola International; and Mahmud Wahba, head of the Egyptian-American Businessman's Association, who offered to buy the company in partnership with a number of Egyptian-American businessmen. Although some Arab businessmen, such as Shaykh Fahd Ibn Salman from Saudi Arabia and Bashir al-Dakali from Libya, expressed interest and bought the particulars of sale from the Bank of Cairo, they did not submit a bid for the company. Serious offers were limited Muhammad Nusayr in partnership with Pepsi-Cola International and Saudi Arabian businessman Muhammad Buqshan, and to the Egyptian Masrub Company.

Muhammad Nusayr, along with his partners, commissioned a private company to evaluate the Egyptian Bottling Company's assets, which put them at LE56 million, then later raised them to LE74 million. With the existence of an offer by the Masrub Company in the amount of LE103 million, including LE23 million in contested land, Nusayr and

his partners raised their evaluation of Pepsi-Cola Egypt to LE129 million.

In the end, Nusayr's offer was chosen, as it featured the highest price and offered the best conditions, as stipulated by the Holding Company for Food Industries in the privatization of any of its subsidiaries. Once the choice was made, the holding company began negotiations with the buyers in an attempt to raise the price of the deal. Negotiations lasted four months before an initial agreement was signed to sell the Egyptian Bottling Company-Pepsi-Cola Egypt to Alcan Company (Muhammad Nusayr), Pepsi-Cola International, and Buqshan Investments.

Contradictory government statements

There are real discrepancies concerning the final price sale. Reports from the Ministry of Public Enterprises indicate that the company was sold in April 1994 for LE156 million. The same ministry later published another report putting the price at LE131.1 million, including LE123.2 million from the private sector and LE7.9 million from the workers' union.

In any case, shares in the company were divided among the principal investors. The Alcan Company (Nusayr) and Buqshan Investments each held 49 percent of the company, with the remaining 2 percent being held by Pepsi-Cola International. Nusayr held the right of administration, and his son after him. Among the conditions of the sale was that 10 percent of the company would be distributed to workers, while 30 percent would be offered on the stock market within 2 years. The buyers were also obliged to maintain the workers at the company for at least 3 years. The total number of workers at the factor was 4160 when it was sold in April 1994, although Nusayr indicated when he and his partners bought the company that they would need no more than 1860 permanent workers, in addition to 600 seasonal workers for the summer when the demand for soft drinks increased. Although he did keep on the larger than necessary labor force, he indicated that their wages were extremely low and that enabled him to keep them on at minimal cost for the required three years.

In 1995 Nusayr sold about 40 percent of his stake in the company to the Buqshan Investments, bringing his share down to about 28 percent, while Buqshan's holdings rose to 70 percent. Nusayr justified the sale of a large portion of his shares to his Saudi partners saying that it would allow him to fund the necessary new investments to establish a number of new bottling factories, which would in turn raise the company's share of the Egyptian soft drink market.

In 1999, Pepsi-Cola International announced that it had bought 77 percent of the Egyptian Bottling Company for US$400 million, or about 9 times the price the entire company had been sold for by the public sector (see *al-Ahram*, 5/2/1999). Nusayr had sold a majority share to his Saudi partner first, which was later sold to Pepsi-Cola International.

The deal garnered much criticism in the opposition press. One report quoted the former chair of the Egyptian Bottling Company to the effect that the two factories of Minya and Port Said had been assessed at LE150 million alone. How, then, could 8 factories with 18 production lines and a fleet of distribution vehicles be sold for the price of only two factories?

Aside from reservations concerning the price of the factories, production lines, and vehicles, the evaluation of the land owned by the company was extremely controversial. For one thing, the appraisal did not take into consideration the possibility that the land might be used for some purpose other than building a factory or a warehouse—for example, for real estate development or some other purpose. The sale only stipulated that the land not be used for any other purpose for five years after the property was sold to the private sector. The company owned, for example, land on Mustafa Kamil Street in Alexandria, as well as land on Pyramids Road in Cairo. If these lands are appraised according to the market price for land lots, it exceeds the total price of the original sale to the private sector.

2) The Nasr Boilers deal: wasting a strategic company

This deal is considered one of the most controversial of the entire privatization process, and here also, there are inconsistencies in statements published by the Ministry of Public Enterprises. The ministry initially stated that he company was sold for LE58 million;

one year later it issued another statement saying the company had been sold for LE15.6 million--a substantial discrepancy to say the least.

The company occupies 31 feddans (about 130 sq. meters) in Manyal Shiha, directly on the Nile across from Maadi. Five offers were made to buy the company when it was put up for sale, all of which came from foreign companies, including the US, Canada, France, Italy, and Japan.

Before it was privatized, the company employed 1100 workers. It produced anywhere from 1-12-ton pressurized containers capable of producing as much as 1300 tons of steam in per hour. It also produced steam generators, liquid gas canisters, water purifying and water-desalinization units, and other products. The company registered a profit until 1991, when it undertook investment expansions funded by bank loans, which put the company in the red until it was sold. There is no justification for these new investments in a company that is preparing to be sold, especially ones that would land it in a debt crisis, except if these losses were necessary to sell it. However, this company was one of the most important of Egyptian companies, falling in the framework of what might be called the heart of Egyptian industry: it manufactured investment goods. Before it was privatized the company was subsidiary to the Holding Company for Technical Industries, headed by Abd al-Wahhab al-Habbak, who later stood trial (see below in the section on corruption and fighting it in the Arab world).

The evaluation process was left to a US consulting firm subsidiary to real-estate giant Bechtel. The company was valued at about US$24.16 million, much less than the price of the land on which the company stands. If evaluated as a building lot, the price per meter of land directly on the Nile opposite of Maadi would go for no less than LE3000, meaning the price of the land would be at least LE390 million, or about US$115 million. Thus, it is clear that Bechtel based its low assessment of the price of the company in the interests of possible buyers, primarily the interested US company.

Although workers protested the privatization of the company, the process went forward as planned. On December 13, 1994, the company's board obtained the permission of the General Assembly of the Company for Technical Industries to sell the company's real assets for US$11 million and its stock for US$6 million, bringing the final price of the company to US$17 million, according to press reports, although there are inconsistencies with the Ministry of Public Enterprises, as was mentioned. The company was sold to the US-Canadian firm Babcock and Wilcox without stipulating that the buyer pay the company's back taxes and other debts. The final price is similar to the highest price mentioned by the ministry in its initial bulletin, but it is more than three times the final price released by the same ministry.

3) Asyut Cement

Asyut Cement was put up for sale in the wave of cement company privatizations that included Beni Sueif Cement and Alexandria Cement. All were sold to foreign companies such that the entire cement sector in Egypt became to a large degree controlled by foreigners.

Before its privatization, Asyut Cement produced 3.9 million tons of cement annually, with 3300 workers. According to statements from the Ministry of Public Enterprises, net profits for fiscal year 98/99, immediately before its privatization, reached LE136 million. The company acts as the prime source of cement for the Toshka project, as it is the closest geographically to the Toshka site when compared to other Egyptian cement companies. The company's stock totals 32 million shares.

After the company was put up on the block, the envelopes were opened and the company went to the Mexican cement company Cemex, which clinched the deal in November 1999, getting 77 percent of the company's stock, along with the farm and the rest rouse subsidiary to it. The deal was completed in June 2000 when Cemex obtained 13 percent more of the shares that were with the holding company. Thus Cemex held 90 percent of the company's holdings, while the remaining 10 percent were held by the workers' union.

The Ministry of Public Enterprises stated that the 90-percent stake in Asyut Cement was sold for LE1268 million, while the workers' union maintained a stake worth LE112.6 million. The contract of sale stipulated that the buying company modernize the factory and its production lines, and raise production to 4.5 million tons annually.

In the final analysis, there was no reason for the company to be sold. Since Egypt imports cement, the local or foreign private sector could

have established new cement factories. It would have been better for there to be new investments in the sector rather than taking available capital and putting it in established assets and an existing producer. Moreover, Asyut Cement made net profits in 98/99 of about 42.5 percent of its book capital and more than 10.6 percent of its selling price.

4) Meridian Hotel

The Meridian Hotel is located at the northern tip of Manyal Island, appearing as a peninsula in the Nile in a unique and distinguished location. It spans 21,000 sq. meters that were owned by the governorate of Cairo. When the hotel was put up for sale in 1993, the price of land per square meter in this spot was no less than LE30,000 per meter—that is, the total value of the land alone equaled LE630 million, or more than US$185 million at 1993 prices (see "Iqhtiyal funduq tarikhi," *al-Ahram*, 15/11/1997).

The hotel was sold to a Saudi prince for US$75 million, approximately 40 percent of the value of the land alone. Similar things have been seen in the sale of other hotels, such as the Sheraton Cairo (LE350 million) and the Sheraton Hurghada (US$16 million): examples of unjustified sale, as the assets generated profits and brought in revenues to the public treasury.

B. The uses of privatization returns

Concerning the use of the revenues from the privatization process, available statements cover the period from the beginning of the process though August 19, 1999. For that period, the Ministry of Public Enterprises has indicated that privatization has garnered LE10,008 million. The revenues have been used thus: LE3610 million towards meeting bank debts, or about 36.1 percent; LE1930 million for early retirement funds, or 19.3 percent; LE331 million for the mine workers fund and to meet salaries at losing companies, or 3.3 percent; and LE4137 million transferred to the Ministry of Finance, or 41.3 percent.

This method of utilizing the proceeds from privatization is unacceptable by any economic logic. It is not acceptable for 36.1 percent of assets to be sold to meet bank debts. Rather, officials who let the public sector get to such a state should have been made to answer for their actions. But the matter passed without a reckoning as if the public sector—built with the people's money—belonged to no one. The use of 19.3 percent of privatization profits to fund early retirement for workers simply means that one-fifth of the assets sold were done so to pay for sending a number of workers into the ranks of the unemployed. As one's income drops when taking early retirement, those who obtained the pension likely used it on either household expenses or one-time special expenses, such as those related to marrying sons. This, in turn, means that the pension funds were not used in small private enterprises, particularly as employees leaving the public sector had no previous experience in this area and were not trained to start small enterprises in any case. Thus, the vast majority of them ended up among the unemployed.

Using even a small percentage of privatization returns to pay the wages of unprofitable companies is not supportable economically. Why are the most favored, profitable companies sold to be used to support the wages of workers in losing companies?

C. Conclusions concerning the privatization process in Egypt

Summarizing the most important results of the privatization program in Egypt, the following points come to the fore:

- Privatization does not mean a liberalized economy. Liberalizing the economy means providing a legal framework in which the private sector can move freely in all areas, while doing away with bureaucratic obstacles and developing the social and cultural environment to support work in the private and small business sectors.
- The privatization program as applied in Egypt has consumed the country's assets, built by previous generations and governments, for the purpose of funding the current government's expenses. This could lead to a huge increase in the domestic budget deficit after the public sector is sold.

- There are inconsistencies in statements by the Ministry of Public Enterprises concerning the sale of public-sector companies, which raise doubts and require an explanation.
- The privatization process has hindered the implementation of new private investments that the economy needs. The capital used by the private sector to buy public-sector assets is, in the end, money that could have been wholly or partially put into building new investments. Instead, it was put into an exchange of currently existing assets. Privatization in advanced capital-exporting economies, such as Britain, the US, and France, formed an important means to regulate excess capital, transferring a large part of it into the ownership of assets instead of maintaining it as hot money in the currency and stock markets. The situation arose initially because these countries had large surpluses of capital, which they also exported. In Egypt on the other hand, privatization was not funded by cash surpluses in the private sector, but redirected private-sector capital that would have been used for investment. In some cases, loans were used to finance the process, which robbed the Egyptian economy of an important means of encouraging development. Instead, it contributed to the liquidity crisis in hard currency and the continued recession in 2000.
- A large segment of state-owned assets and profitable companies were sold, while the proceeds were not used to build new productive assets. This led to the shrinkage of the public sector and an increasing inability by the state to undertake its defined role in the Egyptian economy, as a developing economy that needs to be pushed forward.
- The privatization process contributed to consolidating the Egyptian capitalist class as a class that lacks initiative. Privatization involves selling already productive ventures, most of which achieve profits and already have a market share. It thus requires no risk. Hence, buying the private sector does not build important investment experience for the private sector, but reinforces routine performance and weakens the aggressiveness of the Egyptian capitalist class. It also reinforces the worst investment culture among this class, particularly the tendency to focus on buying at the cheapest price,

while avoiding the risks associated with establishing productive new assets. Rather, these sorts of calculated risks are the main method of developing the private sector's skills in production and marketing.

- Many of the public-sector companies that are located in big cities or on their outskirts—such as Pepsi-Cola, Coca-Cola, Nasr Boilers, Ahram Beverage Company, and others—could have been sold on the condition that they be moved to the new industrial areas as much as was possible. Thus, the state would have maintained the land, whose value in many cases exceeded that of the value of the company, particularly when assessed as residential property. The state then could have used these lands to establish residences, parks, or other necessary public facilities. This idea was not lost on the government, but was suggested in a totally unsuitable context, specifically in the privatization of the public-sector department stores, Omar Effendi, Ben Zion, Sednoui, Haneaux, and Manufactured Goods. The Ministry of Public Enterprises proposed that these holdings be held in usufruct—i.e., that only the right of use be sold, not the land the stores stand on—in order to substantially lower the price, although the ministry did not indicate how long a company might enjoy such a concession. Using this method in this case, however, wastes the state's chances of getting a fair price for prime real estate in the heart of Cairo and other large cities. Similarly, long-term usufruct normally prevents the state from using the property in any other way. It would be preferable to break the department stores into individual stores developed within a shopping mall, then sell the stores individually based on the market price for shops in similar areas. Such a method would open the door for small and medium investors, widening the base of possible interested parties, and would ensure that these companies are sold piece by piece at fair prices. This would widen the ownership base as well.
- The privatization process almost everywhere from Germany to Egypt has led to the appearance of corruption, although the scale varies from one country to the next. Several Egyptian privatization deals raised much controversy in this regard, such as the sale of Nasr Boilers and certain hotels.

Based on the above, economic logic dictates bringing the privatization process to a halt at the current time, particularly when the government is speaking of a liquidity crisis, which means that the sale of public assets now will bring a depressed price. With no liquidity in Egypt, the buyers are likely to be foreign parties.
Stopping the privatization process must be accompanied by moves to increase economic freedom, to allow the private sector to work in favorable conditions. The state must give growth incentives, the first of which is creating demand, rather than financial incentives which do not constitute true encouragement of long-term investors. If any public-sector assets are privatized, the proceeds should be used directly to build new productive assets in an area necessary to meet existing demand, or to embark on high tech projects, even if these assets are later sold to build even newer assets. The public sector was built with the money of the people in order to achieve an economic leap, and it does not need to be sold to pay for current state expenditures. This is an economic catastrophe in a developing country like Egypt.

Public-sector administrations must also be developed to ensure efficiency, while making them accountable to strict government and popular oversight bodies in a climate of true transparency to prevent corruption. Popular oversight cannot be truly effective except in a democratic climate where power can be shared.

The public sector and the economy of the state will be the subject of future studies in this report.

Table 1

Egyptian imports, exports, and the balance of trade according to Egyptian sources and according to Egypt's trade partners (in $ million)

Year	Imports, exports, and trade balance according to Egyptian sources			Imports, exports, and trade balance according to Egypt's trading partners		
	Exports	Imports	Trade balance	Exports	Imports	Trade balance
1990	2585	9216	-6631	5424	12185	-6761
1991	3659	7862	-4203	4560	12455	-7895
1992	3050	8293	-5243	5440	12257	-6817
1993	3110	8188	-5078	5547	12871	-7314
1994	3448	9452	-6004	5933	13453	-7520
1995	3441	11739	-8298	6082	15813	-9731
1996	3534	13019	-9485	6561	17182	-10621
1997	3908	13168	-9260	6370	19110	-12740
1998	3195	16479	-13284	5369	19652	-14283
1999	3535	15962	-12427	5231	19421	-14190
2000*	3629*	9217*	-5588*	--	--	--
Total	37093	122595	-85501	56517	154389	-97872

Source: IMF, *Direction of Trade Statistics Yearbook 2000*

*Figures for 2000 cover only the first half of the year (data from the Central Bank of Egypt, monthly bulletin, October 2000)

Table 2

Domestic savings as a percentage of GDP in Egypt and selected countries

Country	1990	1999
Egypt	16%	14%
Angola	30%	48%
Republic of Congo	24%	45%
China	38%	42%
Malaysia	36%	45%
South Korea	37%	34%
Thailand	34%	32%

Table 3

Egypt's commodities trade with the E.U. 1996-1999 according to Egyptian and European figures (in $ million)

Year	Egyptian imports, exports, and trade balance with the E.U. according to Egyptian figures			Egyptian imports, exports, and trade balance with the E.U. according to European figures		
	Egyptian exports to the E.U.	Egypt's imports from the E.U.	Trade balance	Egyptian exports to the E.U.	Egypt's imports from the E.U.	Trade balance
1996	1613	4711	-3098	3643	7155	-3512
1997	1621	5031	-3410	3202	7571	-4369
1998	1196	5978	-4782	2562	8199	-5637
1999	1237	5728	-4491	2531	-8266	-5735

Source: IMF, *Direction of Trade Statistics Yearbook 2000*

Table 4

Direct and indirect investment from and to the U.S. 1974-1998 (in $ million)

Year	Direct U.S. investment abroad	Direct foreign investment in the U.S.	Indirect U.S. investment abroad	Indirect foreign investment in the U.S.
1974	4.95	3.33	1.82	1.71
1975	13.98	2.56	6.23	11.31
1976	11.66	3.25	8.87	12.84
1977	11.26	2.9	5.45	29.49
1978	14.72	5.85	3.63	10.73
1979	25.37	8.7	4.7	5.37
1980	19.23	16.93	3.57	14.15
1981	9.62	25.19	5.7	21.15
1982	-.98	12.47	7.98	17.49
1983	7.74	10.47	6.78	8.53
1984	12.35	24.76	4.77	29.73
1985	14.06	20.01	7.5	76.04
1986	19.02	35.64	4.33	85.78
1987	28.35	58.22	5.25	66.93
1988	16.18	57.28	7.98	73.86
1989	36.83	67.74	22.07	95.71
1990	29.95	47.92	28.77	22.02
1991	31.38	22.01	45.67	57.54
1992	42.66	17.94	49.17	71.98
1993	77.95	48.99	146.25	110.98
1994	75.21	44.59	60.31	139.40
1995	96.65	57.65	100.07	237.48
1996	81.07	77.62	115.8	367.63
1997	121.84	93.45	87.98	383.51
1998	131.93	196.23	89.35	268.13

Source: IMF, *International Financial Statistics Yearbook 1999*, pp. 923, 929

The banking system and the dangers of the transition period

The year 2000 saw a number of events which cast long shadows of doubt over the health of the Egyptian banking sector. There was the sentencing of the so-called loan deputies, the announcement that several large bank clients had defaulted on their loans and fled the country, and the publication of lists in the press that indicated the huge indebtedness of other big businessmen, which didn't seem to fit with their strong financial positions. Businessmen accused banks of putting a lid on new loans, causing a liquidity crisis which harmed their business interests and threatened to stop production and send workers into the streets. Indeed, businessmen did threaten to lay off workers if banks actually started to take legal steps against loan defaulters.

These events raised a number of questions among the public about the efficiency (and honesty) of bank credit officials, the extent of controls on credit, and the supervisory and oversight role of the Central Bank of Egypt (CBE). Some asked that protection for depositors be put in place through a system of deposit insurance, while the issue of privatizing commercial public-sector banks again came to the fore.

The controversy over loan default in Egyptian banks was not in itself a new phenomenon—since the 1990s it has been one of the main subjects that pops up every time bank reform is mentioned. Most of the time, however, talk concerned those overdue debts owed by public-sector companies and agencies. Creditor banks would demand that some of the proceeds from the privatization of public companies be used to rectify these debts, while partisans of privatization used debt as evidence that decisions to grant credit in public-sector banks were subservient to political aims and government administrations, far removed from economic fundamentals or healthy banking norms.

This is completely different from the controversy now raging over loan default, which has taken on new dimensions. This time it is directed essentially at the debts of the private sector to the banking system, including commercial public-sector banks, joint-venture banks, or even offshore banks, as some are afraid that depositors' monies will be smuggled out of the country as doubts are raised about the health of the banking system as a whole.

Any discussion of the Egyptian banking system must begin by dealing with the size of the problem, its roots, its negative effects, and the position of the CBE, which is what we shall now take up.

I. The size of loan default in the banking system

It must be said at the outset that there are no figures regarding the total amount of loan default in the banking system in Egypt, or its sectoral distribution. Nevertheless, estimates of the IMF and the Ministry of Economy make it clear that the percentage of uncertain loans dropped from 14.7 percent of total credit in June 1996 to 12.3 percent in June 1997, and 11.7 percent in June 1999. Liability reserves covered 82.2 percent of bad loans in June 1999. Judging from these indicators, and taking into account that the total amount of loans as of June 1999 was about LE204.1 billion, total loan default can be calculated at approximately LE23.9 billion.

In addition, the available information indicates that the total uncollected interest on unpaid debts in the banking sector as a whole increased from LE19.6 billion in March 1999 to LE23 billion in March 2000. About 76.5 percent of that interest was from loans granted to the private sector. During the same period, the construction sector was responsible for about 22 percent of the total uncollected interest on unpaid debts; about 48 percent of that was associated with loans to the private sector.

Considering the absence of figures, the only available indicator concerning the relative position of different banks is the percentage of uncollected interest on unpaid debts to the total amount of money loaned. In March 2000, uncollected interest comprised 11 percent of the loan portfolio in commercial public-sector banks, 10.1 percent in joint and private commercial banks, 7.5 percent in investment and business banks, and 7.7 percent in specialized banks.

This indicates that the problem of loan default palpably exists in all of Egypt's banking sector, and that an important part of it is associated

with those loans granted to the private sector, which, in turn, has come to comprise the primary client of the banking system, as we shall see.

II. Roots of the problem

The 1990s saw a clear transformation of the loan structure of the banking sector to the benefit of the private sector, which became the main client of the banking system and a primary recipient of its loans. Loans to the private sector increased from LE28.9 billion in June 1992 to LE150.4 billion in June 2000, compared to LE44.5 billion for the government and public sectors. Hence, private loans comprised 66.3 percent of all loans (compared to 64.6 percent at the end of last year), or 81.5 percent of the increase in loans granted in one year.

Direct financing given by the banking system to the private sector in the form of joint-venture projects rose from LE3.7 billion in 1992 to LE6.66 billion in June 1997, to LE11.8 billion in June 1999, to LE12.5 billion in June 2000. (These figures are calculated from CBE reports submitted to the People's Assembly.) These figures indicate that the total amount of loans and direct financing of capital that went to the private sector reached LE162.5 billion in June 2000, or about 365 percent of financing given to the government and the public sector.

In addition, the private sector is the main beneficiary of credit facilities offered by the banking system, such as documentary credit and letters of credit, which the bank must cover fully when they fall due. The non-guaranteed part of the note can thus turn into a *de facto* loan if the client does not cover it at that point. The private sector (including the cooperative and investment sectors), was the beneficiary of about 58.9 percent of all credit lines and 73.1 percent of letters of guarantee in all banks in March 2000.

This change in the loan structure did not come about only as a result of the expansion of the private sector's role in the economy, but is in part attributable to new banking regulations which were put in place in the early 1990s. Egyptian banks were required to implement regulations concerning the itemization of assets and the calculation of appropriations as directed by the World Bank as part of its guidelines. Banks were required to set aside allocations in increasing proportions if the client was late with debt payment, applying the same standards to clients in the public sector.

At the same time, the permissible ceiling banks could loan to clients was unified, regardless of whether to the private or public sector (see Banking and Credit Law 37/1992, article 37.) They were also required to settle outstanding debts with public agencies and public-sector companies and inform the CBE of unguaranteed government loans as long as these were not accompanied by permission from the minister of finance. (See the periodic bulletins issued by the CBE, no. 317, June 21, 1991.)

These developments led to an increased growth of the private sector's role in economic activity and a transformation of the loan structure in Egyptian banks, as the private sector received a larger share of loans.

The change in the loan portfolio to the benefit of the private sector was supposed to lead to increased efficiency in financial offices in accordance with the principles of financial liberalization. When the principal client is the private sector, banks are more careful to conduct thorough feasibility studies, monitor loans, regulate the business activities of the debtor, and offer more efficient means of balancing payments. The public sector, in contrast, might be financed on executive directives not necessarily based on sound financial principles.

Nevertheless, the Egyptian experience indicates that this transformation in the loan structure to the benefit of the private sector was accompanied by a number of phenomena that, as a whole, represented a high degree of risk for the banking sector. These phenomena include:

1) Increased concentration in the loans granted. At the end of March 2000, 343 clients had received 42 percent of the total credit facilities granted to the private sector. The largest 28 clients received about LE26.7 billion, representing 13 percent of total credit given to the private sector and about 135.5 percent of the total value of shares owned by stockholders in the banking sector. Indeed, 8 clients received about LE12.4 billion of these credit facilities, or LE1551 million each. This number represents about 60

percent of the total value of shares owned by stockholders in the Egyptian banking sector.

2) A sizeable portion of loans to the private sector were concentrated in fields characterized by a high degree of risk, such as the construction sector, which received about LE7.2 billion, or 11.5 percent of total private loans in March 2000, compared to 10.8 percent the previous year. This represents about 99 percent of the total value of shares held by stockholders in the banking sector.
3) There was a huge jump in the amount of loans granted to private-sector clients in foreign currency, a phenomenon that partially reflected the desire of the private sector to benefit from a lowering of the interest rate on foreign currency as compared to loans in Egyptian pounds. Foreign currency loans comprised about 58 percent of total foreign currency deposits in June 1997, but rose to about 68 percent in 1998. This forced the CBE to intervene, issuing orders to bank to "take care that local loans made in foreign currency are given to projects capable of producing revenues in this currency." (See CBE report to the People's Assembly 1997/98, p. 13.) Despite this, private-sector loans in foreign currency continued to rise in 1999, reaching 69.9 percent of all foreign currency deposits that year.
4) The private sector received an important share of its loans—about 53 percent—without producing any material collateral. In accordance with accepted banking practice, the means of repaying any loan is located in the proposed venture itself, and the principal guarantee of the loan is the financial strength of the venture. Hence, the various forms of collateral used to guarantee a loan should not be a substitute for meeting the conditions of credit competence, determined by detailed credit studies. Material collateral, then, is considered in banking practice as a supplementary guarantee, to meet the risks associated with loan extensions and the difficulties of precisely predicting the factors that may influence the credit competence of the borrower. It is also possible for the borrow to hide pertinent information related to his true ability to meet the loan, known as a situation of asymmetric information between the two parties.

Judging from these changes that occurred in the loan structure to the benefit of the private sector, it is clear that they were accompanied an increased degree of risk that might constitute a threat to the health of the loan portfolio.

Undoubtedly, these phenomena can all be explained in the context of banking principles used in the first stages of financial liberalization, which often lead banks to accept a higher degree of risk, whether to increase profits or as a result of a lack of the experience and technical skills allowing a proper evaluation of credit risks and a precise monitoring of the loan through its course.

But these two factors, in our opinion, only constitute part of the picture of the Egyptian experience, which is completed by adding the relationship of businessmen to state policymakers and bank officials.

In official statements, the state always reiterates its dependence on the private sector to undertake the mission of developing the economy. In practice, this has been accompanied by an increased political role for businessmen, who have begun to appear in official delegations accompanying political leaders on foreign tours and in the annual meetings of the World Economic Forum. They are also found on the US-Egypt Presidents' Council, and state officials join businessmen on their yearly trips abroad and on door-knocking tours. They have channels through which to influence policymakers and economic policy, whether through professional organizations—such as the growing businessmen's associations, industry unions, and chambers of commerce—or through think that express their own interests and that are charged with examining at economic policy, or though membership in the consultative bodies of research centers in universities, to say nothing of their presence in the press and media.

In addition, the 1990s saw a strong representation of businessmen in the banking sector, whether as the principal buyers of bank shares up for privatization or as members of the administrative boards of banks established under the Investment Law. According to the annual banking reports, the most important representatives in this regard are the following:

Misr Exterior Bank: where Unsi Nagib Sawirus serves as a members of the administrative board with Abdullah Tayil—also head of the economic committee in the People's Assembly—who serves as the chairman of the board and an appointed member. Muhammad al-Garhi, one of the businessmen who fled the country, is a principal shareholder in the bank.

African Arab Egyptian Bank: represented by Muhammad Lutfi Mansur, Yasin Ibrahim Lutfi Mansur, Ahmad Amin al-Maghrabi, and Muhammad 'Akif Amin al-Maghrabi.

Al-Watani Bank of Egypt: represented by Abd al-Mun'im Sa'udi and Safwan Ahmad Thabit.

Egyptian British Bank: represented by Ibrahim Abu al-Aynayn Kamil and Sa'id al-Tawil.

Egyptian Gulf Bank: represented by the recently deceased Salah al-Din Muhammad Mahmud and Muhammad Gamal Mahmud.

In our opinion the increased political influence of large businessmen and their relationship with state and banking policymakers comprises a factor for pressure, and in many cases it was one of the primary reasons banks granted credit to big businessmen or participated in joint ventures with them or guaranteed their bonds. It is worth pointing out that a decree from the minister of economy (no. 42 of 1999) allows private-sector companies—with the approval of the stock exchange authority—to issue bonds whose value exceeds the company's net assets, even if it suffers from an unsuitable credit rating, or even if its rating is less than its proven ability to meet the bond obligations.

The past year has also revealed interesting news about businessmen who are members of private bank administrative boards obtaining large loans from their own banks, contrary to what is stipulated in the Banking and Credit Law, where article 39 stipulates that "commercial banks are prohibited from granting loans, advances, credit allowances, or guarantees of any sort to members of the bank's board or to any establishment where a member of the board is a partner or a member of the board." The same phenomenon was seen with large stockholders, at times sparking the resignation of bank officials in protest over such practices.

Aside from the dangers such a situation poses, it is interesting to note that the offending banks have not been brought to task. The CBE has only pointed out that "the situation must be amended in which loans are granted to parties linked to bank officials in accordance with the legal prohibition of granting loans to members of the bank's administrative board." It added: "Although the regulations do not put fetters on loans to large stockholders, it is necessary to take into consideration the negative effects this could have on the bank's financial status."

III. The negative consequences of the problem

The year 2000 saw a number of businessmen accuse banks of putting a lid on new loans, causing them a crisis of liquidity. The liquidity of any society—that is, local liquidity, or the money supply in its widest meaning—is represented by the number of methods of payment that the society allows. This differs from one place to the next depending on how widespread banking culture is, the extent to which checks are used, how developed the cash market is, and what sorts of tools and agencies have been developed to cope with it. There are two main factors that influence liquidity. The first is net foreign assets, reflecting the state of the balance of payments; there is a expansive effect when there is a surplus in the balance of payments (an increase in revenues coming from abroad) and a recessionary effect when there is a deficit. The second factor is net domestic credit, which exercises an expansive effect when there is a surplus and a recessionary effect when there is a deficit.

The truth is that banks themselves have suffered from a liquidity crunch over the past two years as the cumulative effect of a number of factors, the most important of which is the huge expansion in granting credit to the private sector and defaults on debt payments.

One must first understand the nature of the problem. According to standard banking practice, liquidity means maintaining a sufficient amount of assets that can be converted into cash with little or no reduction in value to meet withdrawal demands by depositors and other obligations such as these or to respond to demands for loans.

The extent to which banks maintain their obligations is represented in the level of cash reserves and liquidity as determined by monetary authorities. This is an important indicator of the financial health of banks and their ability to meet their obligations. It also comprises one of the primary limitations on their ability to grant credit, as the bank is not free to direct its resources to loans except after meeting the reserve and liquidity requirements determined by the central bank.

The performance of banks working in Egypt over the last two years reveals a gradual eating away of the liquidity surplus as the result of a number of a factors, including:

1) Several government agencies took an important part of their accounts in private-sector banks and transferred them to accounts at the CBE.
2) The banking system, particularly public-sector commercial banks, largely bore the burden of covering government bond subscription issued during this period.
3) An increasing amount of local currency was used to buy foreign currency from the CBE to meet the gap in bank resources.
4) Private-sector companies expanded their bonds holdings.
5) More loans were given, the largest part to the private sector. Table 1 indicates that the increased loans given by banks in fiscal year 98/99 registered record figures, reaching LE31.7 billion, of which the private sector took about LE26.6 billion, or 83.9 percent.
6) Instances of loan default increased, particularly in light of economic stagnation and sluggish stock, to say nothing of the oversupply in the luxury housing market and tourist resort developments. This means that a large part of the money loaned by banks was not returned to be used again as resources that could be pumped into new loans.
7) Deposits did not increase adequately to cover the expansion in loans. Deposits inflows did not exceed LE16.3 billion in 97/98, compared to loans of LE20.2 billion. Hence, loans accounted for 123.9 percent of deposits. The same phenomenon occurred in 98/99, when deposits increased only LE19.3 billion compared to

loans of LE31.7 billion, meaning loans accounted for 164.2 percent of deposits.

That was the state of liquidity in the various banks in Egypt over the past two years. According to the monthly budgets prepared by commercial and investment banks, it becomes clear that:

- The level of liquidity and local currency reserves declined at investment banks. Commercial and investment and business banks must maintain non-interest-bearing cash reserves at the CBE not less than 15 percent of its deposits in Egyptian pounds. They are required to keep liquid local reserves of at least 20 percent and liquid foreign reserves of at least 25 percent. These banks were unable to meet these requirements throughout 98/99, excepting March 99, and they were unable to maintain these levels more than once through 99/00.
- There was no liquidity surplus among commercial banks, which barely managed to meet the cash reserve minimum in 98/99, failing to meet in completely during some months of 99/00.
- There was pressure on the resources of commercial public-sector banks to cover the liquidity gap at private banks. This, in addition to the expansion of credit and the transfer of a portion of public deposits to the CBE, led to a destabilization of the liquidity situation at these banks, and prohibited some from meeting the minimum cash reserve requirement.

In order to counter the liquidity shortage, banks employed the following strategies:

1) Increasing the interbank loan rate, which pushed the interbank interest rate at times higher than the interest on clients' loans. The average interbank interest rate in 98/99 was 13.8 percent, compared to 12.8 percent on client loans. It reached record levels in 99/00, occasionally hitting 17 percent, compared to an average of 13.11 percent for commercial loans.

2) Increasingly turning to the CBE to provide the required short-term liquidity (5-14 days) through repossessing treasury bills, which reached a net total of LE209 billion in 99/00, compared to LE61 billion and LE7.7 billion the previous two years.
3) Working to attract more deposits and becoming more inventive in offering new means of savings, which banks had stopped doing throughout the 1990s.
4) Regulating loans. Loans decreased in 99/00 to LE22.7 billion, compared to LE31.7 billion the previous year, such that for the first time in three years, loans was less than the increase in deposits, which reached LE23.7 billion (see table 1).

With the regulation in loans, particularly in the first half of 2000 (see table 2), the increase of loans in local currency was limited to LE8.7 billion, compared to LE15.7 billion in the second half of 1999. Loans in foreign currency registered a decline in 99/00 by about 1.7 billion.

But as table 2 makes clear, the private sector continued to get the largest portion of new loans throughout the year. Indeed there was a clear movement towards the private sector from January to June 2000 in local currency loans. The total value of new loans obtained by the private sector, minus those that were paid, reached LE9.2 billion, compared to LE8.6 billion for all other sectors combined. This means that payments made by other sectors were used to give new loans to the private sector.

IV. Controls on bank credit and the oversight function of the CBE

The problem of loan default by big businessmen, the increased concentration of loans in the private sector, and the size of their collateral raised several questions about the extent of controls over credit and the role of the CBE in supervising and overseeing banks. In light of current regulations and laws, systematic controls over the financing activities of banks are represented in the following:

1) Minimum reserve limits

Since 1991, commercial and investment and business banks have been required to maintain with the CBE no-interest-bearing cash reserves not less than 15 percent of its deposits in Egyptian pounds. Correspondingly, the maximum amount of those deposits available for use is 85 percent. For foreign currency deposits, banks are required to maintain a portion at the CBE in the form of interest-bearing deposits at a rate equivalent to the average LIBOR rate over 6 months. The required reserve level was reduced from 15 to 10 percent as of December 31, 1993.

2) Liquidity limits

Commercial and investment and business banks are required to maintain a minimum of 20 percent of liquid local currency, and 25 percent of foreign currency. The components of the liquidity minimum are represented by the total liquid assets maintained by banks to meet possible withdrawals of deposits by bank clients, in addition to a portion set aside for contingent liabilities.

Hence, the bank is not free to direct its resources to finance investments—whether new or an expansion of existing productive capacities—or a undertake a regular financing of working capital, except after meeting these two minimum requirements in the amount determined by the CBE.

3) Capital requirements

Banks in Egypt follow the capital requirements in accordance with the unified system approved by the Basel Committee (subsidiary to the Bank for International Settlements in Basel, Switzerland), which links the bank's capital and its probable assets as determined by the degree of risk. The ratio of bank capital to these assets should be no less than 8 percent, meaning that a bank can loan a maximum of 12 times its capital. The more a bank supports its capital base, the greater its ability to finance activities in various sectors.

4) Maximum financing for individual clients

The CBE stipulates that banks working in Egypt cannot exceed a set limit on financing given to one company, whether represented in credit facilities or joint ventures. The limit is set at 30 percent of the bank's capital base, but the CBE has reduced this burden, set by the law, to 25 percent.

5) Controls related to financing certain activities or according to certain currencies

These are perhaps the most outstanding controls set by the CBE over the past three years, presented in its report to the People's Assembly concerning the state of cash and credit in fiscal year 97/98. They include the following:

- Limiting the role of banks in the field of money for hire to holding shares in companies that work in the field. Shareholding should be well within the acceptable limits laid out by the Banking and Credit Law.
- Taking care not to expand property loans from commercial and investment and business banks.
- Requiring the approval of the CBE, as well as the stock exchange authority, before allowing any banks to guarantee company bonds.
- Limiting local loans made in foreign currency to those projects capable of supplying revenues in the same currency.
- Prohibiting loans in local currency from being guaranteed by foreign currency deposits (from October 2000) in an attempt to regulate activities in the foreign currency market and to combat speculation in the price of the Egyptian pound.

These are the controls related to banking credit. What about the oversight powers of the CBE?

Actually, measures to liberalize banking transactions and raise the level of competition in the 1990s were accompanied by a reinforcement the oversight powers of the CBE. According to Law 37/1992, article 30, the CBE has the right to intervene with any bank facing financial problems to take a number of measures, from demanding that the bank reinforce its capital base, to issuing an order to merge the bank with another, to shutting down the bank completely. The CBE also has the authority to approve the basic system of any bank, as well as administrative contracts that are made between another party and the bank's administrative board (article 21).

In addition, the governor of the CBE has the right to object to any member of a bank's administrative board, to its general director, and to its directors of credit, investment, and foreign transactions. (See article 24 of the Banking and Credit Law 163/1957, modified by Law 37/1992.)

According to the same law, banks must choose outside account auditors from a list accredited by the CBE and the Central Accounting Office. The governor of the CBE can also seek recourse with a third auditor to undertake limited activities when necessary (article 25). The main objective of accounts auditors is to evaluate the quantity of allocations and the health of the bank's internal oversight system. Depending on the reports of accounts auditors, the CBE can force a bank to withhold shareholder profits and direct them to supporting its allocations until they reach the necessary levels.

The CBE also has the authority to recognize or reject any request to register a bank before it begins any activity, and to demand that a bank halt all transactions. It is also now necessary to get the approval of the administrative board of the CBE before one can obtain more than a 10-percent share of the capital in any one bank.

Thus, it is clear that the CBE is not lacking officially in the authority necessary to undertake its oversight and regulatory role over the banking system. Nevertheless, the question remains as to the extent to which this authority is used in practice.

Off-site oversight

Although banks are required to submit regular reports requested by the CBE concerning their activities, that does not necessarily mean that the CBE has an early warning system that gives a signal to intervene before crisis hits.

We can give the example of the Central Administration for Collecting Bank Credit Statistics, which was established in the 1950s and to which banks must submit detailed information concerning client loans that exceed LE40,000. Quarterly reports by this body over the last few years show that there is a high level of concentration in granting credit to clients in the private sector and in the proportion of this credit to the combined capital of banks.

Despite the danger and persistence of the phenomenon, no alarm was raised at the oversight bodies in the CBE as long as the facilities given to each client in each bank fell within the set limit (less than 30 percent of the bank's base capital). No questions were raised as to whether the client was financially solvent or whether his cash inflows could service all his debts in the banking sector as a whole.

Standard banking practice requires evaluating a client's risk by taking combined loans into consideration, in accordance with the one obligor total rule. The CBE has also warned banks of the importance of "studying the position of the client and those parties in a close relationship with him as a whole." Nevertheless, in reality the CBE limits itself to monitoring a bank's adherence to the set limit for establishing credit risk for individual companies, rather than taking into consideration the net situation of several related companies. This is particularly important for those clients who have several economic activities or several companies—where it might be proven that these exist on paper only, as the court brief in the loan deputies case showed—or projects which are essentially part of other family endeavors.

The CBE's response to the concentration of credit and the dangers associated with it did not begin in earnest until several large clients defaulted on their bank loans in 1999.Only then were banks required to submit detailed periodic reports to the CBE concerning those debts that exceeded LE100 million so that they could be closely monitored.

On-site oversight

The limited human capabilities of the CBE still prevent forcing all banks working in Egypt from undergoing regular periodic audits. Hence, the CBE has concentrated on a group of commercial public-sector banks which still represent the largest part of economic activity, with the ultimate goal to cover all banks once every three years. Certainly, this policy represents a large step forward in comparison with the situation of the 1970s and 80s, when some private-sector banks were never audited by the CBE. Concentrating on banks that comprise the largest part of the banking sector is something that oversight authorities in many countries do, to greater or lesser degrees, including France and the US.

Regular publications coming out of the CBE indicate that insofar as on-site auditing operations have taken place in banks, these operations have revealed "a lack of compliance by some banks with the regulations and foundations of healthy credit practices in giving credit to clients. This could cause increased credit risk followed by negative effects." Audits also revealed an inattention to the regulations on extending credit to the private sector which were issued in 1987. These laid out the measures necessary to determine the strength of collateral and its healthy administration, the importance of getting thorough information, and the necessity of meeting all the required conditions before credit is extended.

Perhaps the most pertinent breach is that which led the CBE to recommend in its report to the People's Assembly on fiscal year 99/00 that new companies be established specializing in evaluating collateral presented to banks by clients seeking loans. The CBE also recommended improving the skills of those who compile client credit histories; establishing an independent body to provide information about bank clients; strengthening the system of information in independent banking units; linking the primary banking centers with their branches in a system which would allow better communication to facilitate the flow of information; and strengthening the role of the primary banking centers in overseeing the operations of their branches.

Undoubtedly, these recommendations indicate the lack of ability (or lack of honesty) in some banks' evaluation of loan collateral, as it also points to the existence of real shortcomings in the information-gathering facilities in a number of banks.

In conclusion, it must be reiterated that the CBE does not lack the authority necessary to implement supervision and oversight over the

banking system, but the main issue remains the importance of exercising this authority in full in practice and training the professional cadre necessary and capable of undertaking competent off-site monitoring and thorough, regular on-site audits on all components in the banking system.

There is also a need to reinforce the early warning system which helps to uncover and deal with practices that threaten the health of banking activities. Perhaps the need for such controls is what has led some specialists to call for placing an auditor of the CBE on the administrative board of every bank, to avoid the time lag between the origin of the problem and its discovery.

V. A look at the future

In light of the previous exposition, the question now is to what extent should we take advantage of the flexibility of monetary and credit policies to increase the efficiency of the banking system and better direct credit? How far can Egyptian banks go in responding to the demands of the coming period, in which the state aims to increase economic growth to about 7 percent annually, which entails raising domestic savings and the level of investment?

In other words, to what extent can we expect the adoption of monetary and credit policies that lead clearly to growth? To what extent can we anticipate a healthy banking system that performs well and pays close attention to providing the necessary financing to industrial, agricultural, and service projects that will absorb the unemployed and workers returning from the Arab oil states over the next few years, along with the recent graduates who are being put on early retirement under privatization policies?

In turn, what credit policies can be adopted to push small banks to merge or support their financial positions, if the goal is for all banks working in Egypt to enjoy a sound financial status? Only then will they be able to face competition from abroad, which will increase dramatically over the next few years. Can we establish short-term incentives for the new banks that grow out of mergers? The experience of the last few years prove that small banks will not go willingly towards mergers—the CBE intervened more than once to save small banks and announced that it would not allow the state to foreclose a bank. In addition, officials believe that mergers are a decision to be made by the shareholders in these small private banks, not the prerogative of the state and the CBE. The issue requires a reassessment and a decision that works to the benefit of society as a whole.

Here we must point to the relative position of the banks working in Egypt as compared to the international banks that have begun to examine the possibility of entering the Egyptian market over the last few years. According to the annual list published by *The Banker* in July 2000, the capital of nine banks working in Egypt (according to the standards set out by the Basel Committee qualifies them to be counted among the largest 1000 banks in the world on the basis of their capital. The National Bank of Egypt is at the head of the list, occupying rank 299 worldwide, with a capital of US$1040 million and net assets worth US$20 billion. The net capital of all banks working in Egypt as of June 30, 2000, reached LE21 billion, or US$6 billion. If all Egyptian banks merged into one bank, it would occupy spot 70 on the international list, coming after the Belgian bank Dexia. These numbers reveal the weakness of the capital base in Egyptian banks, particularly as the law before 1992 established no minimum limit for a bank's capital. In 1992, it was stipulated that the capital of licensed banks be no less than LE100 million, with paid-in capital of LE50 million. Branches of foreign banks working in Egypt were required to have allocated capital of no less than US$15 million. In comparison, the largest bank in the world in terms of capital is City Group, whose capital is more than US$47 billion and whose assets come close to US$717 billion. The latter figure is about seven times as much as the combined net assets of all banks working in Egypt as of June 2000.

It appears that those banks that will merge in the near future include a merger between the Egyptian British Bank with the International Credit Bank, after their ownership has effectively passed into the hands of one financial group. The assets of the new bank total about LE4.5 billion, a still modest number even by local standards.

Another important issue related to mergers is the issue of privatizing Egyptian banks. Current economic policy views it as a means of completing what it began in 1974: to achieve the gradual withdrawal of

the state from direct economic activity, leaving the economy to the mechanics of free market forces. The banking sector was one of the first that was opened to foreign private capital, in 1974, by allowing banks to be established owned entirely by foreign capital at an early stage in the *infitah*. These were in the form of branches of foreign banks, who were limited to foreign currency transactions until 1994. The early *infitah* policies also allowed the establishment of joint-venture banks, in which public banks and state companies and agencies held shares in select foreign banks. These banks were allowed gradually to practice banking activities and compete with the banks of the public sector in offering banking services. Local capital has been able to establish banks since 1977. These developments led to many changes, the most important of which for our discussion is that the share of public-sector commercial banks grew gradually less over 25 years, to be limited to 52 percent of banking activity in 1999/00.

It cannot be said that the public-sector banks around today are those that were present in 1974, as many government restrictions have been lifted since the issuance of Law 120/1975, in terms of the CBE and the banking system. This has allowed these banks to compete with the foreign and joint-venture banks that have been established. These banks were also able to consolidate their capital by withholding shareholder profits and introducing different means of development. This is in addition to their ownership of a large network of branches that covers all the cities in Egypt.

Over the last ten years, the issue of privatizing public-sector banks in Egypt was raised, especially with the growth of the privatization process in the industrial, commercial, agricultural, and service sectors. It was clear that the government wanted to postpone the privatization of the financial sector until a substantial number of privatizations had already taken place in other sectors, in order to prepare public opinion for the privatization of this influential and important sector. Researchers raised questions such as which bank to begin with, a small bank or larger public banks? Should privatization take place by selling a share of the capital or by increasing the capital and selling the increase as a subscription to the private sector or individuals? Should the sale be limited to Egyptians or should it also be open to foreign individuals and companies by subscription? What size stake should be sold in order to truly privatize the bank such that the state no longer has the authority to directly influence or control banking decisions? Should the bank to be privatized undergo fundamental reforms before it is sold or should that be left to the new administration? This is in addition to wide-ranging discussions about the appraisal of these banks and who could conduct a reliable evaluation based on its assets—including outstanding loans to the government and public-sector companies and authorities—and its subsidiary branches, buildings, and lands. How long should such an evaluation take, and after that, reviewing, discussion, and confirmation?

Before waiting to answer these questions and others, Law 155/1998 was issued to organize shareholding by the private sector in the capital of public-sector banks. The law allowed the private sector—both Egyptian and foreign—to own "shares" in the capital of banks owned entirely by the state, without setting a maximum limit to such ownership excepting the general regulations—i.e., that it is necessary to get the approval of the CBE before owning 10 percent or more of the capital of one bank.

The prime minister indicated recently that the process of privatizing commercial public banks would not take place except after undertaking detailed studies about the best way to sell them, to ensure that privatization will take place in the most suitable manner possible. Similarly, a number of officials stated that privatizing a public commercial bank is an important and decisive step—this is a strategic decision made by the government from which there is no return—but choosing the appropriate moment requires time and serious study to ensure a proper evaluation of assets and prepare public opinion to accept the privatization.

Nevertheless, the World Bank and international financial organizations—including active international banks, estimating authorities, investment companies and banks, and other organizations involved in the privatization process and the international financial market—have demanded that the state begin immediately by privatizing at least one public-sector bank. The World Bank believes that the time is suitable to privatize public-sector banks and that the

matter is pressing, given its importance in developing and modernizing the financial sector in Egypt. It also believes that this will be reflected in the better distribution of resources, the goal which, theoretically, privatization hopes to achieve. The World Bank has established a set of measures necessary in this regard:

1)Achieving a greater degree of transparency in the banking sector
2)Guaranteeing the rights of stockholders
3)Establishing training programs
4)Providing greater financial resources to legal institutions
5)Increase the salaries of workers in oversight bodies—namely, the CBE—in order to attract efficiency and prevent losing these workers to private banks.

There are clearly many reasons for postponing the privatization of the four commercial public-sector banks, including political considerations and the ability to choose the proper time politically, socially, and economically. But there is another factor not often taken into account or even mentioned: the problem with the loan portfolio of public banks. This is not only a matter of outstanding debts by the government and its various agencies, or the public sector in general, but includes many debts owed by the private sector, which increased its borrowing over the last few years without presenting—and in many cases, without being asked to present—serious, faithful studies of the projects and activities being financed. This is in addition to the mistakes made (or the negligence) in properly evaluating the collateral presented for loans to the private sector. The World Bank points to this as an obstacle impeding the timely privatization of public banks, but public-sector banks possess, in the opinion of many, several merits, the most important of which are the following:

1)A huge network of already existing branches spread over the entire country, in addition to several branches abroad. This means that potential capabilities can be drawn upon to collect savings, widen the sphere of services offered, and present new banking services, taking off from already prepared ground. The public-sector banks have more than 1200 branches. This brings up an issue that has been raised in the past: the possibility of following more than one method of privatization with public-sector banks, such as selling some of the branches.

2) As a rule, many assets belonging to public banks are assessed at less than their value, particularly when loose accounting procedures are used to depreciate the value of buildings, property, and other assets owned by the banks by assigning them an accelerated rate of depreciation. It is thus imperative to re-evaluate these assets, a sensitive process fraught with difficulty.

3) The high degree of trust by individuals in public banks, particularly depositors. The total deposits with the four commercial public banks reached about LE150 billion as of June 30, 2000, compared to LE70 billion at private commercial and joint banks, and LE30 billion at business and investment banks, including foreign banks. This indicates that public-sector banks still enjoy the confidence of depositors, with about 50 percent of total bank deposits. Undoubtedly there are historical and psychological factors that must be taken into account, particularly since one of these banks was faced several years ago with a huge deposit withdrawal after the local press published a report about its impending privatization.

4) The low wages of workers in these banks due to their long-time subjection to inflexible regulations, bringing the wage structure closer to its peers in the government and public sector. Despite successive adjustments made to the system of wages and salaries in these banks since 1975, the level of salaries in them—and in the CBE as well—are much less than their peers in the private sector. This entails an increase in the expected revenues from banking activities, even if wages were raised considerably.

Privatization would also include the shares of public banks in joint-venture banks, as well as in other projects established since the beginning of the *infitah,* to which banks have directed a not inconsiderable portion of their resources. Several years ago, public-sector banks embarked on the process of selling these shares in the context of the privatization program, which often involved selling shares owned by the public banks with those owned by the holding company. Public banks also began renouncing their ownership in joint-

venture banks, where its holdings sometimes reached 51 percent. Table 3 clarifies the current holdings of public banks in joint-venture banks (18 as of June 2000).

The Ministry of Economy and Foreign Trade agreed to sell public stakes in three banks: Misr America International Bank, the International Islamic Bank, and Misr Iran Development Bank. The public stake in Misr America International Bank was transferred to the Kuwaiti National Bank and the Egyptian Kuwaiti Holding Company in a deal worth LE398 million. As for the International Islamic Bank for Investment and Development, where public-sector banks held a 20-percent stake as part of the state's interventions to shore it up, offers have been made by the al-Rajhi Company, the Kuwaiti Brokerage House, and another Gulf institution, although a decision has not yet been made to sell it. The Iranian government has offered to buy Egypt's share in the Misr Iran Development Bank—79 percent, divided between the Bank of Alexandria and Misr Insurance—so that it will possess sole ownership.

With the transition to the era of the World Trade Organization and free international trade in commodities and service, it is important for Egypt to benefit from the time span allotted to arrange its affairs in certain sectors and activities. This raises the question of the role credit policy can play in this arena. Should it be left to each bank to unilaterally decide to finance a certain industry or sector based on its own studies to determine the future capabilities of various sectors? Or does the matter require a more coordinated effort, as the discussion revolves around the future of a number of important sectors (such as pharmaceuticals, weaving, cinema, computers, and automobiles), along with a number of special services (such as transport, cargo, and communications), in addition to producing cereals, food commodities, and fertilizer. Is it possible to adopt credit policies that would support these activities in the transitional period, in coordination with other policies to preserve their position in the local market and to raise the level to which they meet domestic needs? This is in addition to supporting their ability to penetrate world markets. There is conceivably a role here for the Union of Egyptian Banks with the Union of Industries, the United Chambers of Commerce, and the commodities assemblies that have recently been created. Together they can offer banks studies and practical, healthy ideas from which banks can choose or consider.

As long as the subject is the future and horizons, it is necessary to show how credit policies and the Egyptian banking system can contribute to the attainment of society's general economic goals. This includes setting a limit on the increasing problem of unemployment, raising the skills of the unemployed, encouraging small industries, establishing industrial activities outside cities, putting a lid on pollution, establishing a domestic base of technology, exploiting imported technology, increasing nontraditional exports, and establishing industries with a heavy labor base. Do these economic goals deserve special attention from credit policies, particularly in establishing concessions or incentives to banks that take the initiative in granting credit to such activities? What would happen if it was decided to decrease the level of cash reserves with the CBE by an amount equal to the credit given by banks to technology development projects? Can the possible losses and gains of such a decision be calculated?

As it is banks that grant credit in all its forms, and banks that are exposed to credit risks, what is the minimum level of coordination necessary to avoid the maximum amount of market risk as a whole? What types of information should banks agree to exchange? Is it possible to increase the amount of joint loans and joint promotion of substantial, large-scale projects that one bank alone cannot possibly finance? Could this lead to strengthening the position of banks working in Egypt to face new arrivals coming in the context of liberalizing commercial financial services, on the assumption that the newcomer might simply be a service offered from afar?

The present time is witnessing an increasing tendency to property and financial investments—which at their root constitute a type of speculation—in addition to a tendency to finance imports of consumer or intermediary commodities in quantities that will meet the needs of Egypt for several years to come. Naturally, banks that grant credit for such activities are aiming to increase their profit margin, but at the same time they are exposing their resources and the money of investors to great risks, no matter what the collateral taken from clients. It also represents a waste of society's energies and that part of its resources that should be put into activities that will comprise a source of profit in the medium and long term, not merely in the short term.

Table 1
Loans granted from banks (in LE billion)

	1996/1997		1997/1998		1998/1999		1999/2000	
	Amount	Increase over previous year	Amount	Increase over previous year	Amount	Increase over previous year	Amount	Increase over previous year
Loans to the private sector	83.1	18.5	105.3	22.2	131.9	26.6	150.4	18.5
Total loans	152.2	23.4	172.4	20.2	204.1	31.7	226.8	22.7
Total deposits	200.2	25.3	216.5	16.3	235.8	19.3	259.5	23.7
Share of the private sector of all loans 1:2	54.6%	79.1%	61.1%	109.9%	64.6%	83.9%	66.3%	81.5%
Percentage of loans to deposits 2:3	76%	92.5%	79.6%	123.9%	86.6%	164.2%	87.4%	95.7%
Percentage of private sector loans to deposits 3:1	41.5%	73.1%	48.6%	136.2%	55.9%	137.8%	57.9%	78.1%

Source: computed from figures from Central Bank annual reports and fiscal reports presented to the People's Assembly 1999/2000

Table 2
Net totals of loans July 1998-June 2000

Loans in local currency (in LE million)			
Period	All sectors	Private Sector	Percentage
July-December 1998	15796	11609	73.5%
January-June 1999	13950	12297	88.2%
July-December 1999	15738	10705	68%
January-June 2000	8643	9245	107%
Loans in foreign currency			
July-December 1998	711	701	98.6%
January-June 1999	1295	2003	154.7%
July-December 1999	(1407)	(947)	68.3%
January-June 2000	(324)	(496)	153%

Source: compiled from Central Bank of Egypt monthly bulletins

Table 3
Public-sector bank stakes in joint-venture banks

Bank	Public-sector bank stake	Other public stakes	Private stake
Alexandria Commercial	--	52	48
Bank of Commerce and Development	59	27	14
Export Development	45	40	15
Housing and Development	--	63	37
Islamic Investment	80	--	20
Misr America	33	67	--
Misr Iran	38	37	25
Cairo Paris	22	--	78
Cairo Barclay's	40	--	60
Cairo Far East	29	20	51
Egyptian American	35	--	65
Egyptian Gulf	--	24	76
Egyptian Saudi	24	13	63
Egypt International	25	4	71
Egypt Rumania	33	--	67
Egyptian Commercial	10	--	90
Commercial International	20	--	80
International Credit	20	--	80
African Arab Egyptian	--	18	82
Misr Exterior	20	--	80
National for Development	--	12	88
Societe Generale	18	--	82
Suez Canal	5	12	83

Source: Carana Corporation, *Privatization in Egypt*, quarterly review, April-June 2000

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This Report

As the most recent publication from the Ahram Center for Political and Strategic Studies, the annual *Strategic Economic Directions* is an expression of the vital importance accorded to the economy by the center and the Ahram organization as a whole. The economy is one of the most important components of any state's comprehensive power in the present day, and it has played a decisive role in determining the overall position of any country since the end of the Cold War. Inasmuch as this report expresses an Arab viewpoint, it is open to contributions from Arab economists. Indeed, such contributions are seen in this, the first edition of the report, so that the process of producing the report will be truly an Arab effort, not only Egyptian. Contributing researchers to the report also span several generations, as interactions between the newer and older generations is a necessary mechanism for reviving Arab economic thought.

The report presents analytical studies of some of the most pressing issues today that exercise great influence on the global economy, as well as the Arab and Egyptian economies. The report contains a special viewpoint section open to present a vision on a certain topic that may or may not differ with the general tendency of the report. This was done to ensure that the report reflects the intellectual diversity of the Arab research community. The rest of the report—including sections on the international economy, the Arab economy, and the Egyptian economy—reflect a consistent line of thought held by the contributors to the report on the issues discussed here.

The report discusses specific regional and international issues by first looking at the dimensions of an issue and determining its impact on Arab economies, including the Egyptian economy. It then provides a vision for dealing with the relevant developments in such a way as to achieve Arab interests. In those issues pertaining to the Arab and Egyptian economies, the report depends on facts and figures for its analysis, striving for objectivity and attempting only to serve the interests of the nation. In looking at the global economy and Arab economic relations, the report starts from the belief that it is imperative that Arab economies, including the Egyptian economy, be integrated into the global economy; the challenges that will present themselves must be met with responses designed to improve the performance of the Arab economy and particularly its competitiveness. At the same time, integration does not mean submitting to the currently selective shape of economic globalization, but rather working to change its conditions in coordination with other countries that also have vested interests in such a change. Nor does integration into the global economy mean tearing down all walls between Arab economies and the rest of the world. Rather, the report believes it is necessary to place appropriate controls on every country, so that the integration of Arab economies into the global economy will be achieved to serve Arab interests.

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